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## **Improving Productivity for the Prosperity of Canada**

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**September 2015  
IRPP/University of Toronto  
Canadian Priorities Agenda  
Award-winning student paper**

The IRPP's *Canadian Priorities Agenda* project is the inspiration for the capstone seminar in the master's in public policy program of the School of Public Policy and Governance at the University of Toronto. The course is offered in an intensive format as a core requirement in the final semester of the two-year program. *A Canadian Priorities Agenda: Policy Choices to Improve Economic and Social Well-Being* is the basic text for the course. It is supplemented by readings chosen by the instructors and guest presenters. The students take the role of judges, and for their final assignment they write a 5,000-word paper modelled on the judges' reports in the original project, in which they have to make the case for an agenda comprising five policies selected from options presented in the course. Every year the instructor selects the best student paper, and the IRPP posts it on its website.

# Improving Productivity for the Prosperity of Canada

Creig Lamb

“Productivity isn’t everything, but in the long run it is almost everything. A country’s ability to improve its standard of living over time depends almost entirely on its ability to raise its output per worker.”

— Paul Krugman, *The Age of Diminished Expectations*, 1990

## Introduction

In the long run, productivity<sup>1</sup> is the most important driver of a country’s economic growth, prosperity and overall living standards.<sup>2</sup> Despite its significance, productivity has been declining in Canada relative to international comparators. According to the OECD, from 1995 to 2012, Canada’s average annual productivity growth rate ranked 26th of 35 countries.<sup>3</sup> This trend is even more pronounced when comparing Canada’s productivity to its closest trading partner — the United States. Between 1985 and 2000, business sector productivity growth in Canada lagged behind that of the United States by an average of 0.8% per year. Between 2001 and 2011, this productivity gap doubled to 1.6%.<sup>4</sup>

Addressing Canada’s poor productivity performance will become increasingly important in the near future. Currently, Canada faces a number of economic challenges that will inhibit future growth. To overcome these challenges, the country will need to raise its productive capacity to maintain real wages and income.<sup>5</sup> This proposed policy agenda is designed to cost-effectively improve Canada’s productivity to ensure the country can continue to thrive and prosper in the long run.

In the near term, Canada has relatively favourable economic prospects.<sup>6</sup> However, the two main contributors to Canada’s recent economic success — rising commodity prices and strong employment growth, are in decline.<sup>7,8</sup> First, it is unlikely that commodity prices will experience the 300% growth that occurred during the 2000s.<sup>9</sup> The recent decline in global oil prices, which saw the price of a barrel of oil drop 60% in 2014-15, is a clear indication of

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<sup>1</sup> Productivity, broadly speaking, is a measure of how efficiently the inputs into production are utilized to produce a given amount of output (<http://www.oecd.org/std/productivity-stats/40526851.pdf>).

<sup>2</sup> Harris, R. G. (1999). *Determinants of Canadian Productivity and Growth: Issues and Prospects*. Simon Fraser University. Industry Canada Research Publications Program. Page 3.

<sup>3</sup> OECD. (n.d. b). *Labour Productivity Growth in the Total Economy*. Retrieved from <http://stats.oecd.org/Index.aspx?DatasetCode=LEVEL>

<sup>4</sup> Government of Ontario. (2014). *Ontario’s Long-Term Report on the Economy*. Ministry of Finance. Page 121.

<sup>5</sup> Harris, R. G. (1999). *Determinants of Canadian Productivity and Growth: Issues and Prospects*. Simon Fraser University. Industry Canada Research Publications Program. Page 3.

<sup>6</sup> Rao, S. (2011). *Cracking Canada’s Productivity Conundrum*. IRPP Study. Page 3.

<sup>7</sup> Macdonald, R. (2008). *The Terms of Trade and Domestic Spending*. Statistics Canada. Government of Canada. Page 12.

<sup>8</sup> Rao, S. (2011). *Cracking Canada’s Productivity Conundrum*. IRPP Study. Page 4.

<sup>9</sup> Rao, S. (2011). *Cracking Canada’s Productivity Conundrum*. IRPP Study. Page 5.

this.<sup>10</sup> Second, Canada's population is rapidly aging. This has resulted much slower labour force growth.<sup>11</sup> According to Statistics Canada projections, the labour force participation rate is expected to drop from 67% in 2010 to between 59.7% and 62.6% in 2031. This would be the lowest participation rate since the 1970s.<sup>12</sup>

Based solely on labour market projections, if Canada's productivity fails to increase, real GDP growth will "slow to less than two-thirds its historical pace over the 2017–2050 period."<sup>13</sup> In this scenario, per capita income would be \$24,900 or 30% lower than it otherwise would be without population aging.<sup>14</sup> Slower GDP growth also means a shrinking revenue base for governments at all levels.<sup>15</sup>

The opportunity costs of not addressing Canada's productivity are high. Using data from two separate models, closing the average annual productivity gap between Canada and the United States would:<sup>16</sup>

- Raise per capita income by 28% or \$18,900, by the year 2050,<sup>17</sup>
- Increase annual real GDP by \$399 billion by the year 2030,<sup>18</sup>
- Generate an additional \$65.3 billion in revenue for the federal government, \$91 billion for provincial governments, and \$18.7 billion for municipal governments by the year 2030.<sup>19</sup>

## Selection Criteria

The goal of this policy agenda is to improve Canada's productivity to ensure the long-run economic prosperity of the country. The primary selection criteria used were:

- (1) **Fiscal Sustainability:** The policies chosen should cost-effectively improve Canada's productivity. They should also generate revenue and create short- and long-term economic impacts.
- (2) **Efficiency:** The policies should address market failures and distortions to allow for a more efficient allocation of scarce resources.

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<sup>10</sup> Economist. (2015, Feb. 21). *The Saudi Project, Part Two*. Retrieved from <http://www.economist.com/news/finance-and-economics/21644198-oil-price-has-been-rising-again-but-will-it-last-saudi-project-part-two>

<sup>11</sup> Library of Parliament. (2011). *41st Parliament Current and Emerging Issues*. Page 161.

<sup>12</sup> Martel, L., Malenfant, É. C., Morency, J.-D., Lebel, A., Bélanger, A., & Nicolas, B. (2012). *Projected Trends to 2031 for the Canadian Labour Force*. Statistics Canada. Retrieved from <http://www.statcan.gc.ca/pub/11-010-x/2011008/part-partie3-eng.htm>

<sup>13</sup> Department of Finance. (2012). *Economic and Fiscal Implications of Canada's Aging Population*. Retrieved from <http://www.fin.gc.ca/pub/eficap-rebvpc/report-rapport-eng.asp#ftn4>

<sup>14</sup> Department of Finance. (2012). *Economic and Fiscal Implications of Canada's Aging Population*. Retrieved from <http://www.fin.gc.ca/pub/eficap-rebvpc/report-rapport-eng.asp#ftn4>

<sup>15</sup> Department of Finance. (2012). *Economic and Fiscal Implications of Canada's Aging Population*. Retrieved from <http://www.fin.gc.ca/pub/eficap-rebvpc/report-rapport-eng.asp#ftn4>

<sup>16</sup> This would involve increasing Canada's productivity by 0.7% per year above the base case.

<sup>17</sup> Department of Finance. (2012). *Economic and Fiscal Implications of Canada's Aging Population*. Retrieved from <http://www.fin.gc.ca/pub/eficap-rebvpc/report-rapport-eng.asp#ftn4>

<sup>18</sup> Dungan, P. (2002). *The Impact of Productivity on Social Well-Being: The Cases of Government Fiscal Balances and Environmental Sustainability*. Canadian Centre for the Study of Living Standards. Page 107. This figure is extrapolated from a model that simulates a 0.3 percent productivity increase above the base case between 2004 and 2030 with public sector real wage response.

<sup>19</sup> Dungan, P. (2002). *The Impact of Productivity on Social Well-Being: The Cases of Government Fiscal Balances and Environmental Sustainability*. Canadian Centre for the Study of Living Standards. Page 107.

- (3) Appropriate Role for Government: The policies should not exceed the appropriate scope of government action or intervention.

## Policy Proposals

Option 1: *Pass provincial legislation to allow municipalities to opt into a 1% sales tax increase dedicated to transit and infrastructure.*

### *Background*

Canada is increasingly becoming an urban society. The country's urban population has expanded at an astounding rate — growing 114% from 1961 to 2011. This compared to the 14% growth in the rural population during the same period.<sup>20</sup> Canada's urban population is also highly concentrated in a few key areas. In 2013, 35.2% of Canadians lived in one of the country's three largest census metropolitan areas (CMAs) (Toronto, Montreal and Vancouver).<sup>21</sup>

Beyond population expansion, cities in Canada are also growing in economic significance. In 2009, approximately half of Canada's GDP was produced in the country's six largest CMAs.<sup>22</sup> When people and economic activity are concentrated, urban areas become hubs of productivity growth and innovation. Studies show that this agglomeration allows for businesses to take advantage of labour market pooling, talent, knowledge spill-over and market access.<sup>23</sup> This results in greater productivity and increasing rates of return for businesses in larger cities.<sup>24,25</sup>

At the same time, however, cities in Canada also suffer from aging infrastructure, inefficient transit and substantial congestion issues, and these problems will significantly inhibit the productive capacity of Canada's cities in the future. The current municipal infrastructure deficit in Canada is an estimated \$123 billion.<sup>26</sup> To appropriately address this growing deficit, it has been recommended that public infrastructure investments be increased by 62%.<sup>27</sup> Studies show that over the next 50 years, infrastructure underinvestment could lower Canada's real GDP growth by 1.1% per year. This would cost the average Canadian anywhere between \$9,000 and \$51,000 annually.<sup>28</sup> In the Greater Toronto and Hamilton

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<sup>20</sup> Statistics Canada. (2011). Population, Urban and Rural, by Province and Territory (Canada). Retrieved from <http://www.statcan.gc.ca/tables-tableaux/sum-som/l01/cst01/demo62a-eng.htm>

<sup>21</sup> Statistics Canada. (2013). Canada's Population Estimates: Subprovincial Areas. Retrieved from <http://www.statcan.gc.ca/daily-quotidien/140226/dq140226b-eng.htm>

<sup>22</sup> Statistics Canada. (2009). Metropolitan Gross Domestic Product: Experimental Estimates, 2001 to 2009. Retrieved from <http://www.statcan.gc.ca/daily-quotidien/141110/dq141110a-eng.htm>

<sup>23</sup> Brown, M. (2010). Urban Productivity: Who Benefits from Agglomeration Economies? Statistics Canada. Pages 6-7.

<sup>24</sup> Brown, M. (2010). Urban Productivity: Who Benefits from Agglomeration Economies? Statistics Canada. Page 6.

<sup>25</sup> Behrens, K., Duranton, G., & Robert-Nicoud, F. (2014). Productive Cities: Sorting, Selection, and Agglomeration. *Journal of Political Economy*, 122 (3), 507-553. Page 508.

<sup>26</sup> Mirza, S. (2007). Danger Ahead: The Coming Collapse of Canada's Municipal Infrastructure. Federation of Canadian Municipalities. Page 2.

<sup>27</sup> RCCAO. (2010). Public Infrastructure Underinvestment: The Risk to Canada's Economic Growth. Page 7

<sup>28</sup> RCCAO. (2010). Public Infrastructure Underinvestment: The Risk to Canada's Economic Growth. Page 5.

Area (GTHA) alone, congestion is estimated to cost the region \$6 billion annually in lost productivity and wages.<sup>29</sup>

To explain how this happened, it is important to understand broad trends in infrastructure financing. Over the past 50 years, the primary responsibility for financing infrastructure has slowly shifted from the federal government to municipalities. From 1955 to 2003, the federal government's share of total capital investments dropped from 34% to 13%, while the municipal share increased from 27% to 48%.<sup>30</sup> This has resulted in a funding structure where the level of government least equipped to make large capital investments is charged with building and maintaining the largest portion of the country's infrastructure.<sup>31</sup> Municipalities currently own "52 percent of public infrastructure, but collect just eight cents of every tax dollar."<sup>32</sup>

### *Solution*

To address this issue, it is recommended that provincial governments pass legislation to allow municipalities to opt into a 1% sales tax increase dedicated to transit and infrastructure. Under this option, the provinces would be responsible for developing the new legislation, which would likely specify the size and capacity requirements for municipalities to qualify for this program. The onus would then be on the municipalities to propose and vote on the policy. For efficiency purposes, the tax should be added onto existing provincial sales tax receipts. The revenue generated would then be transferred to municipalities and earmarked for transit and infrastructure projects.

### *Impact*

Infrastructure investments can have significant positive impacts on productivity. A recent study showed that, between 1962 and 2008, half of Canada's total-factor productivity could be attributed to investments in infrastructure.<sup>33</sup> Another study found that infrastructure spending in Ontario between 2006 and 2014 increased the province's productivity by 2.1%.<sup>34</sup>

Infrastructure investments can also have substantial economic multipliers. The Conference Board of Canada discovered that, for every \$100 million invested in infrastructure, real GDP is increased by \$114 million. This investment also generates roughly 1,670 person-years of employment. The study also found that the federal and provincial governments recouped roughly 31% of infrastructure investments through increased tax revenue.<sup>35</sup>

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<sup>29</sup> Metrolinx. (2008). Costs of Road Congestion in the Greater Toronto and Hamilton Area: Impact and Cost Benefit Analysis of the Metrolinx Draft Regional Transportation Plan. Page 2.

<sup>30</sup> Metrolinx. (2008). Costs of Road Congestion in the Greater Toronto and Hamilton Area: Impact and Cost Benefit Analysis of the Metrolinx Draft Regional Transportation Plan. Page 2.

<sup>31</sup> Mackenzie, H. (2013). Canada's Infrastructure Gap: Where It Came From and Why It Will Cost So Much to Close. Canadian Centre for Policy Alternatives. Page 8.

<sup>32</sup> Broadhead, J., Darling, J., & Mullin, S. (2014). Crisis and Opportunity: Time for a National Infrastructure Plan for Canada. Retrieved from <http://canada2020.ca/crisis-and-opportunity-time-for-a-national-infrastructure-plan-for-canada/>

<sup>33</sup> Gu, W., & MacDonald, R. (2009). The Impact of Public Infrastructure on Canadian Multifactor Productivity Estimates. Statistics Canada. Page 7.

<sup>34</sup> Conference Board of Canada. (2013a). The Economic Impact of Ontario's Infrastructure Investment Program. Page 10.

<sup>35</sup> Conference Board of Canada. (2013a). The Economic Impact of Ontario's Infrastructure Investment Program. Page 10.

## *Revenue*

According to KPMG, a 1% increase in sales tax in the GTHA would generate \$1.3 billion in revenue (\$197.7 per capita) annually.<sup>36,37</sup> Using these estimates, if this program were universally adopted by all the municipalities in Canada's six largest CMAs (Toronto, Montreal, Vancouver, Calgary, Edmonton, Ottawa-Gatineau), it would generate \$3.28 billion annually in additional revenue for transit and infrastructure.<sup>38</sup> This is \$1.08 billion more per year than the federal government's 10-year municipal infrastructure commitment through the Gas Tax Fund.<sup>39</sup> Based on Conference Board of Canada estimates, this investment would boost real GDP in Canada by \$3.74 billion annually.

## *Evaluation*

This proposal would increase municipalities' ability to address growing infrastructure and transit needs. It would require no major expenses, but could significantly improve the productive capacity of Canada's major urban centres.

Increasing municipal tax revenue for transit and infrastructure is also becoming increasingly prevalent in Canada's policy discourse. This may improve the political feasibility of this option. Metrolinx has formally recommended a 1% increase in the HST in the GTHA to generate revenue for its second phase of transportation projects.<sup>40</sup> In Vancouver in 2015, a referendum took place to vote on the proposed Metro Vancouver Transit Tax, which would have led to a 0.5% increase in provincial sales tax receipts in the region.<sup>41</sup>

Other jurisdictions have already taken a number of strides to broaden municipal revenue bases. Municipalities in France, Japan, Korea and the United States receive over 20% of their revenue from sales taxes. In the Netherlands, over 50% of municipal revenue comes from sales taxation.<sup>42</sup>

While increasing taxation presents political challenges, from an international perspective, Canada has a very low tax burden. When compared to other OECD countries, Canada's total tax revenue as a percentage of GDP ranked 21st overall in 2013.<sup>43</sup> Consumption taxes are also one of the most efficient forms of taxation since they are easy to administer and do not

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<sup>36</sup> KPMG. (2013). *Big Move Implementation Economics: Revenue Tool Profiles*. Metrolinx. Page 187.

<sup>37</sup> Based on 2011 Statistics Canada Census Profiles of Hamilton, Halton, Peel, Toronto, York and Durham.

<sup>38</sup> Statistics Canada. (2014d). *Population of Census Metropolitan Areas*. Retrieved from <http://www.statcan.gc.ca/tables-tableaux/sum-som/l01/cst01/demo05a-eng.htm>

<sup>39</sup> Cautilla, C., Zon, N., & Mendelsohn, M. (2014). *Rebuilding Canada A New Framework for Renewing Canada's Infrastructure*. Mowat Centre. Page 8.

<sup>40</sup> Metrolinx. (2014). *Investment Strategy*. Retrieved from [http://www.metrolinx.com/en/regionalplanning/funding/investment\\_strategy.aspx](http://www.metrolinx.com/en/regionalplanning/funding/investment_strategy.aspx)

<sup>41</sup> CBC News. (2015, Feb. 1). *Metro Vancouver Transit Tax Would Raise Local Provincial Sales Tax*. Retrieved from <http://www.cbc.ca/news/canada/british-columbia/metro-vancouver-transit-tax-would-raise-local-provincial-sales-tax-1.2939826>

<sup>42</sup> Federation of Canadian Municipalities. (2012). *The State of Canada's Cities and Communities 2012*. Page 15.

<sup>43</sup> OECD. (n.d. e). *Revenue Statistics — Comparative Tables*. Retrieved from <http://stats.oecd.org/index.aspx?DataSetCode=REV>

distort decisions related to savings and investment.<sup>44</sup> They have also been found to impact productivity and economic growth much less than taxes on income.<sup>45</sup>

However, there are risks associated with this option. First, consumption taxes are regressive since they disproportionately impact people with lower income.<sup>46</sup> Second, an increase in regional sales taxes can have small impacts on the competitiveness of the region by marginally reducing consumption and comparatively increasing the costs of goods and services.<sup>47</sup>

*Option 2: Create an Industrial Research and Innovation Council (IRIC) with a clear business innovation mandate.*

### *Background*

Innovation is one of the most significant determinants of productivity growth.<sup>48</sup> Not surprisingly, Canada has a relatively weak innovation climate. The Conference Board of Canada recently ranked Canada 13<sup>th</sup> out of 16 countries in terms of innovation performance.<sup>49</sup> Studies also show that Canada's weak business innovation is largely responsible for the country's low productivity performance.<sup>50</sup>

Investments in research and development (R&D) are important for developing business innovation.<sup>51</sup> Canada, however, also lags behind many international competitors in terms business investments in R&D, new technology and equipment.<sup>52</sup> In 2013, Canada's annual business expenditure on research and development (BERD) as a percentage of GDP ranked 20<sup>th</sup> out of all OECD countries.<sup>53</sup> This annual expenditure is also heavily weighted to a small number of large firms. In Canada, 25 firms make up roughly one-third of all BERD.<sup>54</sup>

The current federal support for R&D in Canada is highly fragmented. Besides the well-regarded Scientific Research and Experimental Development (SR&ED) tax credit and the Industrial Research Assistance Program (IRAP), there are 60 federal R&D programs dispersed throughout a variety of government departments.<sup>55</sup> A recent poll found that many of these federal funding programs experience low take-up rates from Canadian firms.<sup>56</sup> The most commonly cited reason was a general lack of awareness of federal support for R&D.<sup>57</sup>

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<sup>44</sup> Rosen, H. S., Wen, J.-F., & Snoddon, T. (2012). *Public Finance in Canada* (fourth ed.). McGraw-Hill. Page 399.

<sup>45</sup> Conference Board of Canada. (2012). *Reinventing the Canadian Tax System: The Case for Comprehensive Tax Reform*. Page 6.

<sup>46</sup> Rosen, H. S., Wen, J.-F., & Snoddon, T. (2012). *Public Finance in Canada* (fourth ed.). McGraw-Hill. Page 400.

<sup>47</sup> KPMG. (2013). *Big Move Implementation Economics: Revenue Tool Profiles*. Metrolinx. Page 190.

<sup>48</sup> Rao, S. (2011). *Cracking Canada's Productivity Conundrum*. IRPP Study. Page 1.

<sup>49</sup> Conference Board of Canada. (2013). *Innovation*. Retrieved from <http://www.conferenceboard.ca/hcp/details/innovation.aspx>

<sup>50</sup> Government of Canada. (2011). *Innovation Canada: A Call to Action*. Page 2-4.

<sup>51</sup> Government of Canada. (2011). *Innovation Canada: A Call to Action*. Page 2-4.

<sup>52</sup> Rao, S. (2011). *Cracking Canada's Productivity Conundrum*. IRPP Study. Page 1.

<sup>53</sup> OECD. (n.d. c). *Main Science and Technology Indicators*. Retrieved from [https://stats.oecd.org/Index.aspx?DataSetCode=MSTI\\_PUB](https://stats.oecd.org/Index.aspx?DataSetCode=MSTI_PUB)

<sup>54</sup> Government of Canada. (2011). *Innovation Canada: A Call to Action*. Page 2-7.

<sup>55</sup> Government of Canada. (2011). *Innovation Canada: A Call to Action*. Page E-7.

<sup>56</sup> Government of Canada. (2011). *Innovation Canada: A Call to Action*. Page 5-8.

<sup>57</sup> Government of Canada. (2011). *Innovation Canada: A Call to Action*. Page 5-7.



## Solution

To address Canada's business innovation problem, the federal government should create an Industrial Research and Innovation Council (IRIC). This agency would provide funding and consolidate all federal support for businesses accessing R&D grants or taking an idea or product to market.<sup>58</sup>

This agency would have three primary functions. First, it would administer the existing IRAP, which is considered to be the federal government's strongest program for providing direct support and commercialization services for businesses.<sup>59</sup> The IRIC would also deliver the federal government's pilot voucher program. This three-year pilot program was introduced in 2014 to help facilitate the movement of ideas to the marketplace by promoting industry collaboration and connecting businesses to established providers of commercialization services.<sup>60</sup>

Second, the IRIC would establish a "concierge service" and web portal to serve as a single access point for businesses seeking federal R&D support. As a common platform, the agency would provide advice and assistance for businesses looking to navigate the complex federal R&D landscape. The IRIC would also work to generate public awareness to improve the overall uptake of public R&D programs.<sup>61</sup>

Third, the agency would work in collaboration with provincial and territorial governments to develop an innovation and talent strategy. This strategy would help businesses to attract and retain highly qualified and skilled personnel to help drive innovation.<sup>62</sup>

### *Evaluation and impact*

The costs of this agency are expected to be relatively small. Initially, the IRIC would require some overhead expenses. However, these costs can be offset through the shifting of personnel from current federal programs.<sup>63</sup> A significant portion of revenue could come from the reallocation of existing funds. This includes the \$5 billion in annual revenue dedicated to federal R&D support.<sup>64</sup> It would also involve the reallocation of the additional \$110 million committed annually to the IRAP and the \$20 million allocated to the pilot voucher program over three years.<sup>65</sup>

The costs associated with the IRIC would likely be offset by expected increases in economic activity. Studies suggest that a 1% increase in business R&D (as a percentage of GDP) would raise the per capita GDP of Canada by 12%.<sup>66</sup>

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<sup>58</sup> Government of Canada. (2011). *Innovation Canada: A Call to Action*. Page 5-10.

<sup>59</sup> Government of Canada. (2011). *Innovation Canada: A Call to Action*. Page 5-12.

<sup>60</sup> Government of Canada. (2011). *Innovation Canada: A Call to Action*. Page 5-12.

<sup>61</sup> Government of Canada. (2011). *Innovation Canada: A Call to Action*. Page 5-14.

<sup>62</sup> Government of Canada. (2011). *Innovation Canada: A Call to Action*. Page 5-14.

<sup>63</sup> Government of Canada. (2011). *Innovation Canada: A Call to Action*. Page 5-12.

<sup>64</sup> Government of Canada. (2011). *Innovation Canada: A Call to Action*. Page E-7.

<sup>65</sup> Canada's Economic Action Plan. (2013). *Industrial Research Assistance Program*. Retrieved from <http://actionplan.gc.ca/en/initiative/industrial-research-assistance-program>

<sup>66</sup> Nicholson, P. J. (2003). *The Growth Story: Canada's Long-run Economic Performance and Prospects*. Page 11.

*Option 3: Use the Trans-Pacific Partnership (TPP) negotiations to update NAFTA and diversify Canada's trade with Asia.*

### *Background*

As a small open economy, Canada is highly dependent on trade. In 2013, Canada's total two-way merchandise trade was worth \$947.58 billion — approximately 55.6% of GDP.<sup>67,68</sup> However, unlike many other small open economies, Canada's international trading relationships are highly concentrated in a few select markets. In 2013, 85% of Canadian exports were sent to the United States, Mexico and Western Europe. Only 11% of Canadian exports were sent to the Asia-Pacific region.<sup>69</sup>

This current trade focus is problematic since growth in major advanced economies is much slower than that in the developing world. Real GDP growth in the United States declined from 2.8% in 2012 to 1.9% in 2013.<sup>70</sup> Real GDP growth in the Eurozone (France, Germany, Italy, Spain) was -0.5% in 2013. Meanwhile, the real GDP of developing Asia (China, India, Indonesia, Malaysia) grew by 6.5% in 2013. Real GDP growth in China was an astounding 7.7% in 2013.<sup>71</sup>

Canada can no longer afford to focus its trade efforts on slow-growing economies. Over the past decade, Canada's position as a global exporter has been steadily declining. Between 2000 and 2010, Canada's export growth was 5% slower than the global average. During the same period, Canada's share of the global export market declined from 4.5% to 2.5%. This decline made Canada the second-worst performer in the G20.<sup>72</sup>

### *Solution*

To help improve Canada's trade prospects in developing economies, Canada should leverage the existing Trans-Pacific Partnership (TPP) negotiations to update NAFTA to diversify trade with Asia.

Entering into the TPP negotiations would provide Canada with its first major access to high-growth, emerging Asian economies. The TPP would help to remove trade barriers to ensure a free flow of goods and services between Canada and many dynamic Asian countries.<sup>73</sup> The combined GDP of the countries currently involved in the TPP negotiations exceeds \$27 trillion. This represents almost 35% of global GDP.<sup>74</sup>

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<sup>67</sup> Foreign Affairs, Trade and Development Canada. (2014b). *International Commerce — By Country*. Retrieved from [http://w03.international.gc.ca/Commerce\\_International/Commerce\\_Country-Pays.aspx?lang=eng](http://w03.international.gc.ca/Commerce_International/Commerce_Country-Pays.aspx?lang=eng)

<sup>68</sup> Statistics Canada. (2014e). *Real Gross Domestic Product, Expenditure-Based, by Province and Territory*. Retrieved from <http://www.statcan.gc.ca/tables-tableaux/sum-som/101/cst01/econ50-eng.htm>

<sup>69</sup> Foreign Affairs, Trade and Development Canada. (2014a). *International Commerce — By Country*. Retrieved from [http://w03.international.gc.ca/Commerce\\_International/Commerce\\_Country-Pays.aspx?lang=eng](http://w03.international.gc.ca/Commerce_International/Commerce_Country-Pays.aspx?lang=eng)

<sup>70</sup> Foreign Affairs, Trade and Development. (2014a). *Canada's State of Trade: Trade and Investment Update 2014*, Page 5.

<sup>71</sup> Foreign Affairs, Trade and Development. (2014a). *Canada's State of Trade: Trade and Investment Update 2014*, Page 5.

<sup>72</sup> Carney, M. (2012). *Exporting in a Post-Crisis World*. Retrieved from <http://www.bis.org/review/r120403e.pdf>, Page 3.

<sup>73</sup> Dawson, L., & Bartucci, S. (2013). *Canada and the Trans-Pacific Partnership: Entering a New Era of Strategic Trade Policy*. Fraser Institute. Page 11.

<sup>74</sup> Dawson, L., & Bartucci, S. (2013). *Canada and the Trans-Pacific Partnership: Entering a New Era of Strategic Trade Policy*. Fraser Institute. Page 1.

The TPP negotiations would also present Canada with a new platform to make necessary updates to NAFTA. NAFTA requires updating since the negotiations took place before the rise of e-commerce, digital media and third-party logistics.<sup>75</sup> Since all other NAFTA signatories are involved in the TPP negotiations, any TPP commitments that exceed those made under NAFTA would take precedent. Therefore, Canada can use the TPP negotiations to simultaneously make improvements to NAFTA and diversify trade with Asia.<sup>76</sup>

### *Impact*

Entering the TPP would have significant impacts on Canada's economic prosperity. In a 2012 study, it was estimated that the TPP would increase Canada's GDP by \$9.9 billion and boost exports by \$15.7 billion.<sup>77</sup>

There are also significant productivity benefits associated with trade. According to Statistics Canada, manufacturing firms that exported experienced 0.6% higher labour productivity growth than firms that did not.<sup>78</sup> These productivity increases are associated with exposure to international competition, product specialization and increased investments in R&D and training.<sup>79</sup> Trade diversification can also have significant impacts on productivity. Export variety is estimated to account for over 10% of provincial productivity variation in Canada.<sup>80</sup>

### *Evaluation*

Entering into the TPP negotiations would be cost-effective and administratively feasible. Most of the costly trade reforms the United States will be looking for under the TPP have already been established by Canada as a part of NAFTA.<sup>81</sup>

However, there are risks associated with this option. The TPP may require Canada to make significant supply management concessions in certain agricultural sectors.<sup>82</sup> Many of Canada's agricultural industries would resist since they would face increased competition and are often not equipped to trade internationally.<sup>83</sup> Canada may need to compensate these industries for any concessions that are made, as was the case for Canada's domestic cheese

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<sup>75</sup> Dawson, L., & Bartucci, S. (2013). Canada and the Trans-Pacific Partnership: Entering a New Era of Strategic Trade Policy. Fraser Institute. Page 8.

<sup>76</sup> Dawson, L., & Bartucci, S. (2013). Canada and the Trans-Pacific Partnership: Entering a New Era of Strategic Trade Policy. Fraser Institute. Page 9.

<sup>77</sup> Dawson, L., & Bartucci, S. (2013). Canada and the Trans-Pacific Partnership: Entering a New Era of Strategic Trade Policy. Fraser Institute. Page 1.

<sup>78</sup> Baldwin, J. R., & Gu, W. (2004). Trade Liberalization: Export-market Participation, Productivity Growth and Innovation. Statistics Canada. Page 5.

<sup>79</sup> Baldwin, J. R., & Gu, W. (2004). Trade Liberalization: Export-market Participation, Productivity Growth and Innovation. Statistics Canada. Page 5.

<sup>80</sup> Chen, B. (2013). Trade Variety and Productivity in Canada. Review of Development Economics, 17 (3), 414-429. Page 414.

<sup>81</sup> Dawson, L., & Bartucci, S. (2013). Canada and the Trans-Pacific Partnership: Entering a New Era of Strategic Trade Policy. Fraser Institute. Page 13.

<sup>82</sup> Dawson, L., & Bartucci, S. (2013). Canada and the Trans-Pacific Partnership: Entering a New Era of Strategic Trade Policy. Fraser Institute. Page 14.

<sup>83</sup> Simpson, J. (2015, Jan 23). The Winds Don't Favour Supply Management. Globe and Mail. Retrieved from <http://www.theglobeandmail.com/globe-debate/the-winds-dont-favour-supply-management/article22589256/>

industry during the Comprehensive Economic and Trade Agreement negotiations.<sup>84</sup> The current presence of Japan in the TPP negotiations may alleviate some of these concerns, since Japan has significant domestic rice protection policies.<sup>85</sup> However, even Japan has made concessions on three out of five protected agricultural industries.<sup>86</sup>

Option 4: *Fix the Investment Canada Act (ICA)*.

### *Background*

For the past 40 years, there has been a dramatic rise in global foreign direct investment (FDI).<sup>87</sup> From 1970 to 2013, global inward FDI rose from US\$13.3 billion to US\$1.5 trillion.<sup>88</sup> As a small open economy, Canada has been no stranger to these trends. Canada's stock of inward FDI grew from US\$5.8 billion in 1980 to US\$67.6 billion in 2013.<sup>89</sup> This represents roughly 4% of Canada's GDP.<sup>90</sup>

At the same time, Canada's relative attractiveness for large foreign investments has declined. Canada's inward stock of FDI as a percentage of global inward FDI dropped from 15.7% in 1970 to 3.4% in 2007.<sup>91</sup> One explanation for these trends is Canada's restrictiveness toward FDI. In 2013, Canada ranked third highest out of all OECD countries in the Regulatory Restrictiveness Index.<sup>92,93</sup> A recent study suggested that if Canada were to reduce these barriers, the inward stock of FDI would increase significantly.<sup>94</sup>

Currently the *Investment Canada Act (ICA)* governs all FDI in Canada. The act requires that foreign investments over a certain threshold prove the investment will be a net benefit for Canada.<sup>95</sup> The test is, in theory, an effective and standardized assessment tool to ensure that Canada reaps the rewards of global capital movements. However, in practice, it has been criticized for its lack of transparency, ambiguity and reliance on subjective discretionary

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<sup>84</sup> Globe and Mail Staff. (2013, Oct 18). *Explainer: Why the Canada-EU Trade Deal Will Affect Almost Every Industry*. *Globe and Mail*. Retrieved from <http://www.theglobeandmail.com/news/politics/explainer-why-the-canada-eu-trade-deal-will-affect-almost-every-industry/article14937574/>

<sup>85</sup> Dawson, L., & Bartucci, S. (2013). *Canada and the Trans-Pacific Partnership: Entering a New Era of Strategic Trade Policy*. Fraser Institute. Page 14.

<sup>86</sup> Simpson, J. (2015, Jan 23). *The Winds Don't Favour Supply Management*. *Globe and Mail*. Retrieved from <http://www.theglobeandmail.com/globe-debate/the-winds-dont-favour-supply-management/article22589256/>

<sup>87</sup> Assaf, D. H., & McGillis, R. A. (2013). *Foreign Direct Investment and the National Interest: A Way Forward*. IRPP. Page 5.

<sup>88</sup> United Nations Conference on Trade and Development (UNCTAD STAT). (2013). *Inward and Outward Foreign Direct Investment Flows, 1970-2013*. Retrieved from <http://unctadstat.unctad.org/wds/tableView/tableView.aspx?ReportId=88>

<sup>89</sup> World Bank. (2015). *Foreign Direct Investment, Net Inflows (BoP, current US\$)*. Retrieved from <http://data.worldbank.org/indicator/BX.KLT.DINV.CD.WD>; United Nations Conference on Trade and Development (UNCTAD STAT). (2013). *Inward and Outward Foreign Direct Investment Flows, 1970-2013*. Retrieved from <http://unctadstat.unctad.org/wds/tableView/tableView.aspx?ReportId=88>

<sup>90</sup> Statistics Canada. (2014e). *Real Gross Domestic Product, Expenditure-Based, by Province and Territory*. Retrieved from <http://www.statcan.gc.ca/tables-tableaux/sum-som/l01/cst01/econ50-eng.htm>

<sup>91</sup> Hejazi, W. (2010). *Dispelling Canadian Myths about Foreign Direct Investment*. IRPP. Page 13.

<sup>92</sup> This index is measure of how open or closed an economy is to foreign investment.

<sup>93</sup> OECD. (n.d. d). *OECD FDI Regulatory Restrictiveness Index*. Retrieved from <http://stats.oecd.org/Index.aspx?datasetcode=FDIINDEX#>

<sup>94</sup> Ghosh, M., Syntetos, P., & Wang, W. (n.d.). *Impact of FDI Restrictions on Inward FDI in OECD Countries*. Retrieved from <https://www.ic.gc.ca/eic/site/eas-aes.nsf/eng/ra02055.html>

<sup>95</sup> Assaf, D. H., & McGillis, R. A. (2013). *Foreign Direct Investment and the National Interest: A Way Forward*. IRPP. Page 9.

powers.<sup>96,97,98</sup> The current structure also places the burden on the potential investors to prove that the transaction would be a net benefit to Canada, which can be a costly and uncertain exercise.<sup>99</sup>

### *Recent history*

In 2008 and 2010, Canada issued its first FDI rejections under the ICA — the rejections of MacDonald Dettwiler and BHP Billiton, respectively.<sup>100</sup> During these rejections, the phrase “strategic asset” was used by a number of key officials as a basis for rejecting foreign ownership.<sup>101</sup> The phrase is not mentioned in the ICA and its consideration has been denied by the federal government.<sup>102</sup> However, the term continues to drive uncertainty, especially since Industry Canada also failed to publicly provide sufficient information regarding the basis for the decisions.<sup>103,104</sup>

In 2009, the federal government introduced a national security review to the ICA. This provides the legal framework to allow Industry Canada to solicit information from investors that may pose a national security risk. However, this provision fails to clearly define what constitutes a national security risk, further contributing to the ambiguity of Canada’s FDI review process.<sup>105</sup>

The rise of FDI from State-Owned Enterprises (SOEs) has added more complications to Canada’s already complex FDI regulations. In 2007, Industry Canada released guidelines to ensure that SOEs attract additional scrutiny when applying the net benefits test.<sup>106</sup> Following the 2012 acquisition of Nexen by a Chinese SOE, these guidelines were revised.<sup>107</sup> Industry Canada then announced that foreign state control of Canadian oil sands corporations would pass the net benefits test only on an “exceptional basis,” but provided no further clarification about what was meant by the phrase “exceptional basis.”<sup>108</sup>

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<sup>96</sup> Assaf, D. H., & McGillis, R. A. (2013). Foreign Direct Investment and the National Interest: A Way Forward. IRPP. Page 23.

<sup>97</sup> Collins, S. (2011). Recent Decisions under the Investment Canada Act: Is Canada Changing its Stance on Foreign Direct Investment? Northwestern Journal of International Law & Business, 32 (1), 141-164. Page 147.

<sup>98</sup> Dobson, W. (2014). China’s State Owned Enterprises and Canada’s FDI Policy. University of Calgary: School of Public Policy. Page 20.

<sup>99</sup> Bergevin, P., & Schwanen, D. (2011). Reforming the Investment Canada Act: Walk More Softly, Carry a Bigger Stick. C.D. Howe Institute. Page 9.

<sup>100</sup> Assaf, D. H., & McGillis, R. A. (2013). Foreign Direct Investment and the National Interest: A Way Forward. IRPP. Page 10.

<sup>101</sup> Assaf, D. H., & McGillis, R. A. (2013). Foreign Direct Investment and the National Interest: A Way Forward. IRPP. Page 11.

<sup>102</sup> Assaf, D. H., & McGillis, R. A. (2013). Foreign Direct Investment and the National Interest: A Way Forward. IRPP. Page 13.

<sup>103</sup> Assaf, D. H., & McGillis, R. A. (2013). Foreign Direct Investment and the National Interest: A Way Forward. IRPP. Page 14.

<sup>104</sup> Assaf, D. H., & McGillis, R. A. (2013). Foreign Direct Investment and the National Interest: A Way Forward. IRPP. Page 12.

<sup>105</sup> Assaf, D. H., & McGillis, R. A. (2013). Foreign Direct Investment and the National Interest: A Way Forward. IRPP. Page 11.

<sup>106</sup> Assaf, D. H., & McGillis, R. A. (2013). Foreign Direct Investment and the National Interest: A Way Forward. IRPP. Page 18.

<sup>107</sup> Assaf, D. H., & McGillis, R. A. (2013). Foreign Direct Investment and the National Interest: A Way Forward. IRPP. Page 19.

<sup>108</sup> Assaf, D. H., & McGillis, R. A. (2013). Foreign Direct Investment and the National Interest: A Way Forward. IRPP. Pages 19-20.

### *Solution*

To ensure that Canada continues to benefit from inward FDI, it is recommended that amendments be made to the ICA. First and foremost, the net benefits test should be revised to increase transparency. Based on best practices in Australia, the ICA should publish the specific factors that are taken into account when assessing FDI. The minister should then publicize the justifications for the decision.<sup>109</sup> Second, Canada can also make the process more attractive to potential investors by shifting the burden of proof for the net benefits test away from the investor toward Industry Canada.<sup>110</sup>

Third, the federal government should further clarify that “strategic assets” are not part of the review process. Canada can assure investors that FDI assessments are based entirely on the potential for long-lasting benefits for the country.<sup>111</sup> Fourth, based on best practices in the United States, Canada should provide guidance to potential investors on what might be considered in the national security review.<sup>112</sup> Fifth, the federal government should make explicit the specific review process for SOEs as well as the meaning of “exceptional circumstances” regarding SOEs’ acquisition of oil sands corporations. It is recommended that this should not result in a universal prohibition of SOEs in the oil sands, given their increasing role in the development of Canada’s resource sectors.<sup>113</sup>

### *Impact*

Inward FDI can have significant impacts on productivity. Studies show that inward FDI helps to decrease production costs and raise productivity in most Canadian industries.<sup>114</sup> Foreign-controlled firms have been found to be generally more productive and have significant performance advantages over domestic firms in Canada.<sup>115</sup> These firms also innovate and conduct R&D more in all sectors, which can lead to significant R&D spillover benefits for domestic firms.<sup>116,117</sup>

A study published by the Conference Board of Canada revealed a positive and statistically significant relationship between the inward stock of FDI and labour productivity in Canada.<sup>118</sup> Baldwin and Gu (2005) discovered that foreign-controlled plants contributed

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<sup>109</sup> Dobson, W. (2014). China’s State-Owned Enterprises and Canada’s FDI Policy. University of Calgary: School of Public Policy. Page 20.

<sup>110</sup> Bergevin, P., & Schwanen, D. (2011). Reforming the Investment Canada Act: Walk More Softly, Carry a Bigger Stick. C.D. Howe Institute. Page 9.

<sup>111</sup> Assaf, D. H., & McGillis, R. A. (2013). Foreign Direct Investment and the National Interest: A Way Forward. IRPP. Page 31.

<sup>112</sup> Assaf, D. H., & McGillis, R. A. (2013). Foreign Direct Investment and the National Interest: A Way Forward. IRPP. Page 15.

<sup>113</sup> Assaf, D. H., & McGillis, R. A. (2013). Foreign Direct Investment and the National Interest: A Way Forward. IRPP. Page 30.

<sup>114</sup> Gera, S., Gu, W., & Lee, F. (1999). Foreign direct investment and productivity growth: the Canadian host-country experience. Industry Canada. Page i.

<sup>115</sup> Baldwin, J. R., & Gellatly, G. (2007). Global Links: Multinationals in Canada: An Overview of Research at Statistics Canada. Statistics Canada. Page 7.

<sup>116</sup> Baldwin, J. R., & Gellatly, G. (2007). Global Links: Multinationals in Canada: An Overview of Research at Statistics Canada. Statistics Canada. Page 8.

<sup>117</sup> Gera, S., Gu, W., & Lee, F. (1999). Foreign Direct Investment and Productivity Growth: The Canadian Host-Country Experience. Industry Canada. Page 1.

<sup>118</sup> Conference Board of Canada. (2015). Inward FDI Attraction: Is Canada Attracting Its “Fair” Share of Inward FDI? Retrieved from <http://www.conferenceboard.ca/hcp/hot-topics/inwardfdi.aspx>

65% of labour productivity growth in Canada's manufacturing industries between 1980 and 1999.<sup>119</sup>

Canada's restrictions toward SOEs may also significantly inhibit growth in Canada's resource sectors. Chinese SOEs alone saw their assets grow from \$US 360 billion in 2002 to \$US 2.9 trillion in 2010.<sup>120</sup> These enterprises are often attracted to large-scale natural resource investments in countries like Australia and Canada.<sup>121</sup> The Heritage Foundation's Investment Tracker ranked Canada as China's third top destination for investments.<sup>122</sup> At current levels, China could provide 40% of the funds necessary to optimally develop Canada's oil sands.<sup>123</sup> Any restrictions placed on these organizations may dissuade them from continued investments in Canada's resource sectors, which could slow growth considerably.

### *Evaluation*

Making the necessary adjustments to the ICA is a cost-effective solution to improve Canada's productivity performance. However, there are a number of associated risks. Shifting the burden of proof of the net benefits test would require additional administrative capacity. There is also considerable public concern regarding FDI and its potential to "hollow out" Canada's industries. Many believe that by increasing FDI, Canada may become a branch economy, with high-paying jobs and profits going to foreign countries.<sup>124</sup> While this sentiment is widespread, it is not evidence-based. Foreign-controlled firms have a long track record of developing high-paying, head office jobs in Canada.<sup>125</sup> These concerns can be partially mitigated by effectively communicating the benefits of FDI to the Canadian public.

*Option 5: Increase the intake of immigrants to Canada to 1% of the population.*

### *Background*

As natural increase slows, immigration's role in maintaining Canada's labour supply will become increasingly important.<sup>126</sup> In 2006, immigration was responsible for two-thirds of Canada's population growth. By 2030, it may be Canada's only source of growth.<sup>127</sup> While immigration alone cannot fully address the issues associated with Canada's shrinking labour

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<sup>119</sup> Baldwin, J. R., & Gu, W. (2005). *Global Links: Multinationals, Foreign Ownership and Productivity Growth in Canadian Manufacturing*. Statistics Canada. Page 8.

<sup>120</sup> Assaf, D. H., & McGillis, R. A. (2013). *Foreign Direct Investment and the National Interest: A Way Forward*. IRPP. Page 18.

<sup>121</sup> Dobson, W. (2014). *China's State-Owned Enterprises and Canada's FDI Policy*. University of Calgary: School of Public Policy. Page 13.

<sup>122</sup> Dobson, W. (2014). *China's State-Owned Enterprises and Canada's FDI Policy*. University of Calgary: School of Public Policy. Page 12.

<sup>123</sup> Dobson, W. (2014). *China's State-Owned Enterprises and Canada's FDI Policy*. University of Calgary: School of Public Policy. Executive Summary.

<sup>124</sup> Assaf, D. H., & McGillis, R. A. (2013). *Foreign Direct Investment and the National Interest: A Way Forward*. IRPP. Page 7.

<sup>125</sup> Baldwin, J. R., & Gellatly, G. (2007). *Global Links: Multinationals in Canada: An Overview of Research at Statistics Canada*. Statistics Canada. Page 8.

<sup>126</sup> Kustec, S. (2012). *The Role of Migrant Labour Supply in the Canadian Labour Market*. Citizenship and Immigration Canada. Page 10.

<sup>127</sup> Statistics Canada. (2014c). *Population Growth in Canada*. Retrieved from <http://www.statcan.gc.ca/pub/91-003-x/2007001/4129907-eng.htm>

supply, a growing immigrant workforce can help to mitigate the impacts of significant labour shortages.<sup>128</sup>

As immigrants continue to grow as a portion of the labour supply, Canada must also make concerted efforts to improve the labour market outcomes of recent immigrants. Studies show that recent immigrants to Canada face a number of hurdles in the job market. In 1980, income-earning recent immigrants (men) earned just 85 cents for each dollar earned by their Canadian-born counterparts. By 2005, this figure had declined to 63 cents to the dollar.<sup>129</sup> During the same time period, the proportion of recent immigrants in poverty increased from 24.6% to 36%.<sup>130</sup> Immigrants in Canada are also finding it increasingly difficult to land highly skilled jobs, regardless of their skill level. In 2009, Canada ranked 25<sup>th</sup> of 29 OECD countries in terms of immigrants' skills matching.<sup>131,132</sup>

### *Solution*

To address these issues, it is recommended that Canada increase the annual intake of immigrants to 1% of the Canadian population. It is also recommended that this increase come primarily from the Provincial Nominee Program (PNP). Based on 2014 immigration targets and the 2014 Canadian population, this increase would result in approximately 100,000 new immigrants each year.<sup>133,134</sup>

To explain the potential impact of this option, it is important to provide some background information on the PNP. The PNP was introduced in 1988 to provide provinces with the tools to respond to local labour demands and skills shortages. The program allows participating provinces to nominate immigrants based on identified local needs.<sup>135</sup>

While the PNP is growing, other immigration streams remain much larger. Between 2005 and 2009, the Federal Skilled Worker (FSW) program accounted for 76.2% of all economic immigrants to Canada. The PNP accounted for only 17%.<sup>136</sup> Despite the smaller numbers, provincial nominees have much better labour market outcomes. Between 1999 and 2012, the mean income of principal FSW applicants remained stagnant at \$23,000. Meanwhile, the mean income of principal PNP applicants more than doubled from \$15,200 in 1999 to

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<sup>128</sup> Kustec, S. (2012). *The Role of Migrant Labour Supply in the Canadian Labour Market*. Citizenship and Immigration Canada. Page iii.

<sup>129</sup> Kustec, S. (2012). *The Role of Migrant Labour Supply in the Canadian Labour Market*. Citizenship and Immigration Canada. Page 16.

<sup>130</sup> Dungan, P., Fang, T., & Gunderson, M. (2013). Macroeconomic Impacts of Canadian Immigration: Results from a Macro Model. *British Journal of Industrial Relations*, 51 (1), 174-199. Page 175.

<sup>131</sup> Highly skilled immigrants in highly skilled jobs as a percentage of highly educated immigrant employees.

<sup>132</sup> OECD. (n.d. a). *Indicators of Integration*. Retrieved from <http://www.oecd.org/migration/integrationindicators/keyindicatorsbycountry/name,219003,en.htm>

<sup>133</sup> Government of Canada. (2014). *Government of Canada's Immigration Planning Story*. Retrieved from <http://www.cic.gc.ca/EnGLish/departement/ips/index.asp>

<sup>134</sup> Statistics Canada. (2014a). *Canada's Population Estimates: Age and Sex, 2014*. Retrieved from <http://www.statcan.gc.ca/daily-quotidien/140926/dq140926b-eng.htm>

<sup>135</sup> Citizenship and Immigration Canada. (2011). *Evaluation of the Provincial Nominee Program*. Evaluation Division. Page ii.

<sup>136</sup> Citizenship and Immigration Canada. (2011). *Evaluation of the Provincial Nominee Program*. Evaluation Division. Page 20.



\$39,000 in 2012.<sup>137</sup> The vast majority (90%) of provincial nominees found employment in the first year. Three years after landing, between 91% and 97% of provincial nominees declared employment.<sup>138</sup> Over 70% of provincial nominees believe their job matches their skills.<sup>139</sup>

The PNP also allows for better dispersion of skilled immigrants throughout Canada. In 2011, 94.8% of immigrants settled in Ontario, Quebec, British Columbia and Alberta. Most of them landed in large urban areas. Toronto, Montreal and Vancouver combined accounted for 63.4% of the country's total immigrant population and 62.5% of all recent immigrant arrivals.<sup>140</sup> While these trends can have positive benefits, studies also show that immigrants who live in large cities earn less and face greater hurdles in terms of locating adequate work and housing than immigrants living outside of Canada's three main urban centres.<sup>141</sup> The existing FSW program largely contributes to this concentration of immigrants: 95% of FSW were found to settle in Ontario, British Columbia or Alberta. In contrast, only 36% of provincial nominees ended up in those provinces.<sup>142</sup>

### *Impact*

Increasing immigrant intake and improving labour market outcomes can significantly increase Canada's productivity. Dungan et al. (2013) discovered that, by increasing immigration by 100,000 (to 1% of the population) and closing the wage gap between new immigrants and domestic workers, we could raise productivity growth 0.6% above the base case by 2021.<sup>143,144</sup> In this scenario, government balances would also be \$22 billion higher by 2021.<sup>145</sup>

### *Evaluation*

Increasing immigration with a focus on provincial nominees once again presents a cost-effective solution to improve Canada's productivity and long-run economic growth. However, there are risks associated with this option. Increased immigration may result in added fiscal pressures should these immigrants fail to integrate properly into the labour market. The federal and provincial governments may also be reluctant to increase the

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<sup>137</sup> Statistics Canada. (2015). Table 054-0001: Income of Immigrants, by Sex, Landing Age Group, Immigrant Admission Category, Years since Landing and Landing Year, 2012 Constant Dollars. Retrieved from <http://www5.statcan.gc.ca/cansim/a26?lang=eng&retrLang=eng&id=0540001&pattern=054-0001..054-0003&tabMode=dataTable&srchLan=-1&p1=-1&p2=31>

<sup>138</sup> Citizenship and Immigration Canada. (2011). Evaluation of the Provincial Nominee Program. Evaluation Division. Page 37.

<sup>139</sup> Citizenship and Immigration Canada. (2011). Evaluation of the Provincial Nominee Program. Evaluation Division. Page 44.

<sup>140</sup> Statistics Canada. (2014b). Immigration and Ethnocultural Diversity in Canada. Retrieved from <http://www12.statcan.gc.ca/nhs-enm/2011/as-sa/99-010-x/99-010-x2011001-eng.cfm>

<sup>141</sup> Baglay, S. (2012). Provincial Nominee Programs: A Note on Policy Implications and Future Research Needs. Journal of International Migration and Integration, 13 (1), 121-141. Page 123.

<sup>142</sup> Citizenship and Immigration Canada. (2011). Evaluation of the Provincial Nominee Program. Evaluation Division. Page 51.

<sup>143</sup> Dungan, P., Fang, T., & Gunderson, M. (2013). Macroeconomic Impacts of Canadian Immigration: Results from a Macro Model. British Journal of Industrial Relations, 51 (1), 174-195. Page 186.

<sup>144</sup> This is significant, since a productivity growth increase of 0.7% would effectively close the productivity gap between Canada and the United States.

<sup>145</sup> Dungan, P., Fang, T., & Gunderson, M. (2013). Macroeconomic Impacts of Canadian Immigration: Results from a Macro Model. British Journal of Industrial Relations, 51 (1), 174-195. Page 189.

provincial role in immigration. This may decrease the political feasibility of the option.

### **Assessing the Options**

In the past it was possible to for Canada to prosper despite its low productive capacity. In the near future, however, Canada must address its poor productivity performance to ensure continued economic growth and high living standards. Using the selection criteria of efficiency, fiscal sustainability and the appropriate role for government, each of the policies were selected to help increase Canada's productivity for as low a cost as possible. This policy agenda rejects the notion that significant impacts require large government expenditures. Those policies that do require additional resources were selected based on their ability to stimulate economic activity, generate revenue, and create a net benefit for the country as a whole.

This policy package addresses a number of key priority areas that will be necessary to raise the country's productive capacity. The first option focuses on enhancing the capacity of Canada's urban centres to become hubs of productivity and innovation, The second option will provide Canadian businesses with better, more efficient access to R&D support to improve business innovation. The third and fourth options will help ensure that Canada benefits from the productivity gains associated with trade. The final policy option will help the country to build a more productive workforce by simultaneously increasing its immigrant labour supply, while also improving the labour market outcomes of recent immigrants.

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