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NEWS RELEASE

Impact of “Dutch disease” on manufacturers smaller than feared



Montreal – Although the resource boom has been widely blamed for the woes in the manufacturing sector and cited as a textbook example of the so-called “Dutch disease,” this diagnosis requires a second opinion, according to a new study published by the Institute for Research on Public Policy.

In *Dutch Disease or Failure to Compete? A Diagnosis of Canada's Manufacturing Woes*, authors Mohammad Shakeri, Richard Gray and Jeremy Leonard find that while a booming energy sector in Canada has indeed contributed to the strong Canadian dollar, only one-quarter of total manufacturing output has been adversely affected by the dollar's increased strength.

The authors examine the linkages between energy prices, the exchange rate and manufacturing output in Canada for 80 different manufacturing industries. They use an empirical model that accounts for changes in global demand and competitive pressures, as well as energy-induced strengthening of the dollar.

They found that the Dutch disease most strongly affects small, labour-intensive industries such as textiles and apparel. Larger industries, such as food products and metals and machinery, are less adversely affected. Contrary to popular belief, the automotive sector does not show symptoms of the disease. Rather, its weakness stems from cyclical changes in demand and increasing international competition, according to Shakeri, Gray and Leonard.

The authors conclude that Canada has a mild case of the Dutch disease, but argue that trying to weaken the dollar directly would be impractical and counterproductive. Rather, part of the windfall federal tax revenues from the energy boom should be used for infrastructure and other activities to help shore up the competitive position of manufacturers.

In addition, they recommend that resource-rich provinces adopt policies to ensure they do not become too dependent on wealth generated from resource extraction. “We need to ensure that the resource blessing enjoyed by some regions does not become a curse for the country,” they conclude.

Dutch Disease or Failure to Compete? A Diagnosis of Canada's Manufacturing Woes, by Mohammad Shakeri, Richard Gray and Jeremy Leonard, can be downloaded free of charge from the Institute's Web site (www.irpp.org).

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