



**Canadian
Manufacturers &
Exporters**

Canada's Leading
Business Network

**Manufacturiers et
Exportateurs du
Canada**

Le réseau d'affaires
par excellence du Canada

January 11th, 2007

Mr. Lynton Ronald "Red" Wilson, O.C.
Chair
Competition Policy Review Panel
280 Albert Street
10th floor
Ottawa, ON
K1A 0H5

Dear Mr. Wilson,

Canadian Manufacturers & Exporters (CME) welcomes the opportunity to address some of the issues raised in the Competition Policy Review Panel's consultation document *Sharpening Canada's Competitive Edge*. The questions raised by the document are of critical importance for the future of Canada's manufacturers and exporters, and your panel's recommendations should play a key role in shaping that future.

Given the scope of the mandate you have been assigned and the number of policy issues you have been asked to examine, CME has decided to provide input on two specific issues, namely Canada's ability to attract and retain foreign investment, particularly in its manufacturing sector, and the improvement of Canadian firms' ability to invest in global markets.

Improving Canada's performance in attracting investment depends on improving the country's competitiveness as an investment location. Doing so will require more than modernizing Canada's competition and investment laws. Building an attractive tax environment for business investment, coordinating efforts made by different levels of government in encouraging business investment, eliminating unnecessary regulatory differences, streamlining regulatory requirements, reducing regulatory compliance costs, expediting and coordinating investments in border, security and transportation infrastructure based on a national logistics strategy, responding to the skills shortages faced by Canadian industry, and ensuring that Canadian industry has access to reliable and cost competitive energy suppliers are all factors that play a determining role in Canada's attractiveness as an investment location.

Of all these factors, the need to improve Canada's regulatory environment is one we believe your panel should explicitly address in its recommendations to government. Modernizing and streamlining government decision-making and regulatory processes is essential to improve Canada's performance in attracting investment.

Creating a National Competition Commission based on the Australian model would help ensure that Canada's competition, investment and productivity performance be reviewed on an ongoing basis.

Being able to invest abroad is another success factor for manufacturers and exporters as they compete in world markets. Establishing on-site operations through direct investment, joint ventures and partnerships is a key condition for success as firms are trying to take advantage of global sourcing opportunities and access export markets, especially in emerging economies. The creation of a Canadian Development Finance Institution, a facility that exists in every other G8 country, would help promote private investment in foreign markets by providing risk capital for project development.

CME aims to maintain a world-class manufacturing and exporting sector in Canada that will enable Canadians to continue to enjoy strong economic growth and high-value, high-paying jobs. We trust that your recommendations to government will contribute significantly to achieving this goal.

Sincerely,

A handwritten signature in black ink, appearing to read "Jayson Myers". The signature is fluid and cursive, with a long horizontal stroke at the end.

Jayson Myers
President
Canadian Manufacturers & Exporters



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CME's Comments on Sharpening Canada's Competitive Edge

**Submission to the Competition Policy Review
Panel**

January 11th, 2008

Introduction

Canadian Manufacturers & Exporters (CME) welcomes the opportunity to address the questions raised in the Competition Policy Review Panel's consultation document entitled *Sharpening Canada's Competitive Edge*. The document raises issues of critical importance for the future of Canada's manufacturers and exporters and the panel's recommendations to government will play a key role in shaping that future.

Canadian Manufacturers & Exporters (CME) represents the largest business sectors of the Canadian economy. Together, Canada's manufacturing and exporting sectors directly account for more than 20% of Canadian GDP and offer high-paying, full-time employment to 2.3 million Canadians.

The indirect contributions that manufacturers and exporters make to the Canadian economy are also significant. Every dollar in value added by manufacturers generates an estimated \$3.05 in total economic activity – the largest economic multiplier of any business sector. One in every three jobs in Canada depends on our export success. Being responsible for two-thirds of Canada's goods and services exports and three-quarters of all private sector research and development activity in the country, manufacturers and exporters are at the cutting edge of international competition and innovation.

The importance of these two critical sectors of the Canadian economy should be kept in mind because each are now facing challenges that are fundamentally changing the nature of their business, and will consequently have an impact on the wealth-creating capacity of the Canadian economy as a whole. We are entering into a period of extensive restructuring that will affect all sectors of the North American economy. The restructuring that will take place over the next five to ten years will be driven by five factors:

1. The intensification of competitive pressures from lower cost, knowledge-intensive countries like China, Brazil, India, and South Korea, which are rapidly developing into manufacturing powerhouses with their sights set on exporting into the developed markets of North America, Europe, and Japan;
2. A profit squeeze generated by intense downward pricing pressures for most final goods producers (aggravated in Canada's case by the appreciation of the Canadian dollar which acts like a 60% price cut on export sales) and rapidly rising business costs, including energy, labour costs and materials, as well as the cost of mandatory overheads in the form of taxes and regulatory compliance costs;
3. The continuing globalization of enterprise as companies relocate operations or source products, services, technologies, skills and knowledge from around the world, and increasingly demand that their suppliers compete with the world's best in terms of cost, value, quality, design, engineering, and service capabilities;
4. Demographic changes that over the next decade will mean that Canadian businesses will experience a wave of retirements, and a loss of highly skilled and experienced personnel, at a time when they will also be facing extensive skills shortages. Those skills shortages are already acting as significant constraints on business and economic growth in western Canada; and,
5. Competitive returns on investment that can be earned in jurisdictions around the world. Tax structures are very important in this respect. In spite of commitments to tax reduction on the part of both federal and provincial governments in this country, the marginal effective tax rate paid by Canadian business on their investments is among the highest in the world.

Canadian manufacturers and exporters are taking steps to respond to the short-term challenges of dollar appreciation, rapidly rising business costs, and increasing low-cost competition from other countries. They are cutting operating costs, reassessing product lines, downsizing production, improving operating efficiencies, reducing inventories and overheads, consolidating production, taking advantage of new market opportunities, and outsourcing both production and services.

Manufacturers themselves are taking the lead in changing their operations, competing for market share, and growing their business. But, they require a world-class business environment in order to be world-class competitors. In turn, they depend on governments to take a strategic approach to policy-making, to put in place a world-class tax and regulatory structure, and to make strategic investments in supporting public infrastructure.¹

In reviewing Canada's competition and investment policies, the panel's recommendations can help shape this world-class business environment.

Given the scope of the mandate assigned to the Review Panel and the number of policy questions that it has been asked to examine, CME wishes to focus its policy recommendations in two specific areas:

1. Improving Canada's ability to attract and retain foreign investment, particularly in its manufacturing sector;
2. Improving Canadian firms' ability to invest in global markets.

Improving Canada's Attractiveness As An Investment Location

Is the modernization of Canada's competition and investment laws sufficient for successfully attracting foreign direct investment in Canada? What other priorities and policy issues should governments address?

As Canada's manufacturers and exporters respond to the challenges of dollar appreciation, rapidly rising business costs, and increasing competition for investment, market share, knowledge, technology and skilled workers, these are in our view two of the key questions posed in the Review Panel's consultation document.

For businesses, attracting investment depends on two elements. First, it depends on businesses' ability to adapt to the changing business environment faster than their competitors. To do so, companies must innovate and become more specialized, customized, efficient, and fast. They need to invest in new technologies, new products and services, new markets, as well as in upgrading the knowledge, skills, and expertise of their workforce. Secondly, attracting investment depends on governments' ability to provide businesses with a predictable and internationally competitive tax and regulatory environment, reliable and cost-competitive infrastructure, secure and efficient access to domestic and international markets, and a highly productive and cost-efficient services sector. It is clear that simply modernizing Canada's competition and investment laws will not be sufficient to successfully attract foreign investment.

More specifically, from a public policy standpoint, improving Canada's attractiveness as an investment location depends on our ability to:

¹ For more information on the future of manufacturing in Canada, please read *The Future of Manufacturing in Canada: Executive Overview* published by Canadian Manufacturers & Exporters as a result of its Manufacturing 20/20 initiative, one of the largest privately-run business consultations in Canadian history. The document is available online at: <http://www.cme-mec.ca/pdf/Exec%20Overview.pdf>.

1. Build the most attractive tax environment in the world for business investment in productive assets, innovation, and skills development. Policy reforms required to do this include:
 - Extension of the two-year write-off for investments in manufacturing and processing machinery and equipment for at least another five years;
 - Improvements in the Scientific Research and Experimental Development tax credit system to make the credits refundable and reduce administrative uncertainties;
 - Extension of tax loss carry-back provisions from three to seven years;
 - Introduction of an Employers' Training Tax Credit, creditable against Employment Insurance premiums;
 - Immediate elimination of provincial capital taxes;
 - Transformation of provincial sales taxes into a value-added tax structure; and,
 - The reduction of Canada's combined federal and provincial corporate tax rate to 22% by 2012.
2. Coordinate efforts in support of encouraging business investment in new production facilities, technologies, and innovation initiatives. Federal as well as provincial investments are necessary if Canada is to compete with other industrial economies in securing business investment, product mandates, and industrial innovation activity.
3. Harmonize and coordinate regulations to eliminate unnecessary differences, streamline regulatory requirements, and reduce compliance costs. Government should take every opportunity to create a competitive regulatory environment in Canada by simplifying regulations, building enabling regulatory frameworks for new technologies, reducing the cost of regulatory compliance, eliminating duplication and inconsistencies in regulatory requirements, and eliminating regulatory restrictions on trade and labour mobility across Canada. Clear timetables for regulatory reviews should be established in order to provide greater certainty for investment. Furthermore, we recommend the establishment of a Canadian Competitiveness Commission, based on the Australian model, which would assess federal and provincial regulatory initiatives with respect to their impacts on economic competitiveness.
4. Expedite and coordinate investments in border, security, and transportation infrastructure based on a national logistics strategy aimed at ensuring the efficient flow of goods between Canada and our largest trading partner, the United States, while making Canada the preferred logistics hub for trade between North America and the rest of the world.
5. Respond to the skills shortages that Canadian businesses are facing by jointly encouraging closer collaboration between industry and our universities and colleges with respect to both research and education, speeding up entry procedures for temporary foreign skilled workers, and helping Canadian workers enter productive employment in labour markets across the country.
6. Ensure that federal and provincial investments in innovation, education, workforce development, and public infrastructure generate the greatest possible economic benefits for Canadians. Government procurement should aim to leverage business opportunities and encourage innovation on the part of Canadian industry. Canadian governments would simply be following the lead of every other industrialized country in this regard.
7. Make the investments and expedite the regulatory processes required to ensure that Canadian industry has access to reliable and cost competitive energy supplies now and in the future.

These measures will significantly enhance the business environment for manufacturers, as well as for other business sectors, across Canada. They will encourage the growth of value-adding businesses and enable companies to make the changes they require to compete and win in global markets with our currency trading at or above par with the US dollar. All Canadians will benefit because their prosperity and employment opportunities depend on both the competitiveness and growth prospects of Canada's manufacturing and exporting sectors.

Improving Canada's Regulatory Environment

Of all of the factors influencing investment decisions, the need to improve Canada's regulatory environment is one that should be addressed by the review panel in its recommendations to government.

Inefficient regulations negatively affect Canada's performance at attracting foreign investment for a number of reasons²:

- They raise unit costs and reduce profitability. Since Canada is a small and fragmented market, complex and inefficient regulations reduce returns on investment obtained by companies. This is an issue especially for pharmaceutical products, medical devices, chemical products, consumer and food products, animal and crop health products.
- They slow decision-making and investment processes, (for example large-scale mining or pipeline projects, entry of new pharmaceuticals into the market, local zoning regulations, licensing, and approval of foreign investments in some sectors).
- They act as a barrier to entry by regulating which firms can enter markets.
- They can drive up the cost or the complexity of the process of entering a market such that only large firms have sufficient resources to enter.
- They limit the availability of key resources used in the production process (for example regulations concerning the immigration of skilled workers and the constraints of the domestic certification process for professions such as engineers, nurses and doctors; movement of people and goods between provinces, imports of poultry or dairy products)

According to CME's 2007-2008 latest Management issues survey conducted with 1,014 business leaders across Canada, businesses' top five recommendations to government to improve regulatory management systems are: simplifying compliance requirements; reducing the paper burden and reporting requirements; ensuring uniform interpretation of regulatory requirements; reducing duplication of requirements across jurisdictions; and, achieve greater harmonization of compliance requirements in Canada with those in the US.

Implementing these five recommendations and minimizing the negative impact of regulations on investment attraction requires that government decision-making and regulatory processes be modernized and streamlined. Governments and regulatory bodies must work closely with business to design and implement the most practical and effective means of achieving desired outcomes at the lowest possible compliance costs. Unnecessary red-tape and time delays have to be eliminated, as do overlap, duplication, and inconsistencies across jurisdictions. There must also be greater harmonization of regulatory compliance requirements across provinces, and between Canada and our major trading partners, especially the United States. Canada needs to be recognized as the world's leader in "smart" regulation.

² Source: *Developing a Framework for Assessing Innovation, Productivity, and Business Impacts of Regulation*, a joint collaboration between Industry Canada and the Policy Research Initiative, prepared by Roy Atkinson, September 2006.

The Government of Canada's Policy Research Initiative, as part of its *North American Linkages* project, has performed extensive research on this issue and provides several recommendations for improvement.³

Creating a National Competition Commission

Minimizing the negative impact of regulations on investment attraction requires that existing regulations and regulatory processes be streamlined, and that new regulations be assessed in terms of their impact on Canada's competitiveness.

Just as manufacturers need to continuously improve their productivity to remain competitive, improving Canada's regulatory framework will require continuous improvement.

The creation of an agency within the government responsible for coordinating regulations to eliminate unnecessary regulatory differences, streamlining existing regulatory requirements and reducing compliance costs is needed to ensure the realization of these objectives.

Australia effectively dealt with this issue by creating an Australian Productivity Commission ten years ago. The commission's role includes conducting public inquiries on key policy and regulatory issues, supporting the government's performance monitoring, encouraging the appropriate use of regulation and the reduction of unnecessary regulation, and reviewing regulations to ensure they do not impose unnecessary costs on business and society. The commission also reports annually on the government's compliance with regulation impact statement requirements.

Creating a National Competition Commission based on the Australian Productivity Commission's model could also address the need identified by the review panel to continuously review Canada's competition, investment and productivity performance in order to ensure our economy's sustained competitiveness.⁴

Promoting Canadian Direct Investment Abroad

The barriers that Canadian firms face when seeking to make investments and acquisitions abroad is another key issue the review panel wishes to examine. In *Sharpening Canada's Competitive Edge*, it rightly asks the questions of how the government should adapt its policies to promote increased Canadian direct investment and acquisitions abroad, and what measures have been adopted by other countries that are relevant to Canada.

Investing abroad to take advantage of global sourcing opportunities and to expand export business is a condition for success for an increasing share of manufacturers and exporters as they compete in world markets.

³ For more information, we recommend consulting the following Working Papers issued by the government's Policy Research Initiative: *Developing a Framework for Assessing Innovation, Productivity, and Business Impacts of Regulation* by Roy Atkinson; *Regulation, Growth and Prosperity: An Alternative Approach to Assessing the Implications of Regulations for Innovation, Productivity, and the Business Environment in Canada* by Bryne Purchase; and *Successes and Failure of Regulatory Co-operation in the European Union: Lessons for Canada - US Regulatory Co-operation* by Joelle Anne Schmitz. These documents are all available on the Policy Research Initiative's website at www.policyresearch.gc.ca/.

⁴ More information about the Australian Productivity Commission is available online at <http://www.pc.gov.au>. We particularly recommend reading the following paper intended for a foreign audience: *Structural Reform Australian-Style: Lessons for Others?* by Gary Banks, available online at <http://www.pc.gov.au/speeches/cs20050601/cs20050601.pdf>.

One of the barriers to making investments abroad is the absence of a Canadian Development Finance Institution (CDFI). The creation of a CDFI in Canada, something that exists in every other G8 country, would help promote private investment in foreign markets by providing risk capital for project development.

To win business in developing economies, the rules of the game have evolved considerably. A decade ago, firms normally accessed these markets by establishing crucial export footholds. Once trade relationships were firmly established, exporters could consider enlarging their market presence via partnerships, joint ventures, and direct investment.

Today, the process has reversed. More often than not, up-front partnering and project investments are key ingredients in creating trade opportunities. With host-country governments favouring public-private partnerships and turnkey projects solutions, successful firms are those that can quickly muster the resources and risk capital needed to develop nascent opportunities into export contracts.

While Canadian firms may be sought after for their world-class technical skills, many of these same firms, especially SMEs, lack the staying power and resources (particularly financial and risk management capacity) to compete effectively. This is particularly true for projects in developing and transition economies, where gestation periods are measured in years, and development costs in the millions of dollars.

When Canadian firms look homeward for assistance and expertise, they perceive a striking gap in our country's institutional support during the crucial project development stage, when risks are peaking, capital requirements are accelerating, and export contracts not yet in sight.

At the project *feasibility* stage, Canadian firms highly value the institutional support of programs such as the Canadian International Development Agency's (CIDA) industrial cooperation program in helping define project parameters, foster in-country partnerships, and undertake viability studies. Unfortunately, this program provides neither direct advisory support nor project risk capital. As a result, Canadian firms tend to win feasibility study mandates, while losing out on more lucrative downstream project opportunities.

Likewise, the Canadian Commercial Corporation (CCC) and Export Development Canada (EDC) provide pivotal support to Canadian firms at the project *procurement* stage, by way of bid submission and contract negotiation (in the case of CCC), export financing and insurance (in the case of EDC). However, as evidenced by the failure of many Canadian-sponsored projects, these institutions lack the mandate, resources, and services to adequately help firms develop projects into viable candidates for export support.

These early-stage project challenges are not unique to Canadian firms. However, Canada is unique among major industrialized countries (including all other G8 nations) in failing to deliver effective, targeted institutional support for home-country firms. Other countries have development finance institutions (DFIs), which channel billions of dollars worth of project support and expertise to hundreds of projects each year in developing and transition economies. Canada does not operate a DFI, and provides no such support.

DFIs promote economic progress in developing and transition economies by catalyzing participation in commercially-viable projects. DFIs work closely with domestic and international financiers to stimulate investment and encourage private enterprise. Moreover, they fill gaps in private-sector support, without subsidies, by virtue of their market expertise, investor relationships, government status, and "patient" capital. While laudable for their host-country development policy impact, DFI activities are largely driven by home-country trade, industry, and employment opportunities.

Typical services provided by DFIs include:

- introductions to potential partners;
- advisory services for financial structuring;
- minority and temporary share capital holdings;
- medium-term project development debt;
- investments in and/or management of private equity funds;
- structuring and syndicating financings;
- technical assistance and consultancy services; and,
- accessing international investor networks.

Most countries operate both DFIs and export credit agencies (ECAs), viewing them as essential and complementary institutions in marshalling end-to-end project support. Each has a crucial yet distinct role to play: DFIs during the earlier stages to facilitate partnering, financial structuring, technical assistance, and untied development capital; ECAs at the later stages to clinch export contracts and mitigate defined project risks.

By providing crucial development-stage project support in developing and transition economies, a CDFI would:

1. Help firms bridge the divide between the feasibility and procurement stages.
2. Achieve Canada's dual public-policy goals of supporting sustainable socio-economic development while facilitating partnering and commercial opportunities for home-country firms.
3. Level the international playing field for Canadian firms (especially SMEs), by ensuring these firms have the same arsenal of project development support enjoyed by foreign competitors.⁵

⁵ For more information on the creation of a Canadian Development Finance Institution, please consult: *The Case for a Canadian Development Finance Institution* by the Asia Pacific Foundation of Canada, published in Canada Asia Commentary, Number 18, February 2001 and available online at: <http://www.asiapacific.ca/analysis/pubs/pdfs/cac18.pdf>, and *Étude sur la pertinence d'un outil de financement des investissements directs des entreprises québécoises à l'étranger* by the Montreal World Trade Centre published in September 2005 and available online at: http://www.ccmq.ca/documents/etudes/2005_2006/05_09_20_Etude_FIDE_fr.pdf.