




TOP 10
Barriers to Competitiveness

**Tackling the Top 10 Barriers
to Competitiveness 2015**





A message from your President

Canada is struggling to remain competitive. Despite its efforts, our country's level of productivity and, in turn, its level of economic prosperity continues to decline. In its *2014-2015 Global Competitiveness Report*, the World Economic Forum ranked Canada 15th in global economic competitiveness – down one spot from 2013-2014 and 2012-2013 and three from 2011-2012.

As Canada fights to regain its competitiveness, the role of chambers of commerce and boards of trade as advocates for public policies that foster economic growth, increased productivity, job creation and an innovative private sector has never been more important. For this reason, the Canadian Chamber of Commerce continues to focus its policy and advocacy initiatives on restoring Canada's competitiveness. Every year, we identify the Top 10 Barriers to Competitiveness – the key policy and regulatory barriers that are preventing Canadian businesses from achieving their full potential – and urge governments to address these impediments to business success and increase our country's ability to compete globally.

Since launching this initiative in 2012, we have made great progress in furthering our competitiveness agenda, particularly in addressing the barrier our members identified as being the greatest impediment to the success of Canadian business: the growing skills gap. The federal government and several provincial and territorial governments have also named this issue as the country's biggest challenge.

The document that follows sets out our Top 10 list for 2015, which was determined in consultation with our members. I thank our members for their help in identifying the 10 critical policy and regulatory barriers that will be the focus of our advocacy efforts this year. As you will see, the skills issue remains, for the fourth year in a row, a main priority.

The need for action is urgent. The standard of living of every Canadian depends on how well we as a nation respond to the challenge. We must identify and implement real, tangible solutions to break down the barriers to our competitiveness and create more opportunities and greater prosperity for Canadian businesses and families.

I urge all to endorse and actively support this important initiative and I look forward to sharing our successes with you.

Sincerely,

A handwritten signature in black ink that reads 'Perrin Beatty'. The signature is written in a cursive, flowing style.

Perrin Beatty

Table of Contents

In summary	3
Barrier I: Silos in skills development	5
Barrier II: Entrepreneurs lack capital for Canada's fastest-growing companies	7
Barrier III: Lack of clarity regarding duty to consult with Aboriginal peoples	9
Barrier IV: Internal barriers to trade	11
Barrier V: Canada's tax system is too complex and costly	13
Barrier VI: Canadian trade is constrained by infrastructure deficiencies	15
Barrier VII: Canada is uncompetitive in the world's tourism sector	17
Barrier VIII: Innovation rate is not sufficient to help manufacturing rebound	19
Barrier IX: Territorial businesses don't have the tools they need	21
Barrier X: Canada is missing out on foreign trade opportunities	22



Summary

Silos in skills development

Canada is not producing enough graduates with the skills needed for its economy. There are shortages and high demand forecast in a wide range of occupations. As a result of dramatic restrictions, the Temporary Foreign Worker Program no longer presents an effective path to meet short-term labour shortages. In the medium to long term, our education and training systems play a pivotal role in equipping us with people with the right skills. With a demographic reality about to hit our labour market, we need stronger efforts to coordinate between the silos of education and employers. Improving the links between education and employment is not the responsibility of educators and governments alone. Employers are directly implicated. We need to break the silos.

Entrepreneurs lack capital for Canada's fastest-growing companies

One of the most critical determinants of competitiveness is access to capital, especially for start-ups and companies moving from innovation to commercialization. These fast-growing companies often depend upon venture capital (VC) as the lifeblood needed to take a company from idea to market. Canada's VC industry is still small and punching below its weight, particularly when compared to much larger VC industries in the U.S. During the course of 2014, the Canadian Chamber spoke with dozens of entrepreneurs leading fast-growing companies who say one of the biggest hurdles they face is securing capital to take their companies to the next level. In 2015, the Canadian Chamber will advocate a number of initiatives to boost incentives to expand the overall pool of capital and to attract more angel investors and international funds to Canada.

Lack of clarity regarding duty to consult with Aboriginal peoples

Canadian governments have a fiduciary duty to consult and accommodate Aboriginal peoples when proposed developments have the potential to impact their constitutionally protected rights. However, governments are increasingly relying on project developers to assume responsibility for large parts of community consultation and accommodation. This has led to situations where proponents have no clear direction on the extent of the consultation and accommodation required. This year, the Canadian Chamber will explore alternatives to the current scenario for resolution of the development consultation process, which currently seems headed towards lengthy court challenges to produce jurisprudence that guides proponents, opponents and governments.

Internal barriers to trade

The lack of a single domestic market in Canada is a serious and self-imposed weakness in the Canadian economy. Tariff barriers between provinces are banned by the Canadian constitution, yet the national economy is fractured by a host of non-tariff barriers, particularly in procurement, energy, agriculture and transportation, and in the mobility of labour. The federal government must promote more meaningful sanctions against jurisdictions that practice protectionism against other Canadians while supporting those that embrace free internal trade.

Canada's tax system is too costly and complex

Canada over-relies on income and profit taxes rather than on taxes on consumption, which are relatively easy to collect and are least harmful to growth. Canada's tax code is also overly complex and imposes significant compliance costs on businesses and consumers while governments spend billions of dollars each year administering and enforcing convoluted tax laws. Canada must undertake a comprehensive review of its tax system with the aim of reducing its complexity and improving the way it raises tax revenue.

Canadian trade is constrained by infrastructure deficiencies

Public investment in infrastructure has not kept up with Canada's economic needs. Now Canada's investment needs far exceed the availability of public funds. Bringing infrastructure in Canada back to the level needed to support prosperity will require an ongoing commitment by all levels of government, an active engagement with private sector stakeholders and a greater appreciation of the opportunities that exist for Canada to be more competitive through more modern public infrastructure.

Canada is uncompetitive in the world's tourism sector

Canada has slid from the seventh largest tourist destination in the world to the 18th. Today, it is too often a high-cost, high-hassle destination with aging attractions infrastructure and inadequate marketing. Canada's travel and tourism sector is critical to its economy, and the government must both invest in national marketing initiatives and address Canada's inefficient visa system, the very high cost of air travel in Canada and its layers of regulations, fees and taxes.

Innovation rate is not sufficient to help manufacturing rebound

The best way for Canadian companies to compete and win in modern manufacturing is through a strong commitment to innovation. This appears to be a continuing challenge as Canada's innovation rank, a key component of competitiveness, is troublesome. Canada is ranked 22nd by the World Economic Forum for its capacity for innovation. Canadian manufacturers will need to invest more aggressively in disruptive technologies. However, the innovation policy framework that exists in Canada is not sufficient to overcome a number of serious barriers for the manufacturing sector. The Canadian Chamber will explore recommendations to reconcile the disconnect between industry and institutions, find a mechanism to support the commercialization of new technology and look at options to support business in the adoption of new technology.

Territorial businesses don't have the tools they need

The federal government has a critical decision to make regarding Canada's territories if it is to fully leverage their economic potential. That decision is whether or not to provide territorial businesses with the tools necessary to increase their economic footprint. The result would be more financial independence for the territories and a more competitive Canada.

Canada is missing out on foreign trade opportunities

Canada's prosperity depends on access to international customers and participation in global supply chains. Faced with a small domestic market, exporting is often the only way to grow sales and build economies of scale. Moreover, sourcing from and investing abroad allows companies to exploit unique technologies, skill sets and cost advantages. However, Canadian businesses are not globalizing as quickly as their peers. To support the expansion of Canadian companies abroad, the federal government needs to build on recent success and take steps to conclude the next wave of high-quality trade agreements and strengthen Canada's system of trade promotion and economic diplomacy.

I. Silos in skills development and gaps in the workforce

The issue

Canada will find its skills gap growing and its economic growth dampened if it fails to better align its skills development with its immigration policy goals. Currently, the federal government's policies for skills development and for temporary entry into Canada are not integrated and coherent. As a result, Canada risks having insufficient numbers of workers for the jobs available at a time when it struggles to ensure more Canadians are educated and skilled for jobs in the future.

Currently Canada is not producing enough graduates with the skills needed for its economy. Canada has shortages and high demand forecast in a wide range of occupations, from heavy equipment operators to information technology professionals, and its immigration policies are hindering employers' abilities to meet those needs in the short term. As a result of dramatic restrictions, the Temporary Foreign Worker Program no longer presents an effective path to meet short-term labour shortages. Policies regarding intra-company transfers have also been tightened up, affecting the flow of specialized workers to support global mandates in Canada. Impending changes to the permanent residency streams will not allow for employer-sponsored candidates and are untested as a means to fill job vacancies.

In the medium to long term, our education and training systems play a pivotal role in equipping us with people with skills. With a demographic reality about to hit our labour market, we need stronger efforts to coordinate between the silos of education and employers. Employers need to engage more effectively with the education system at all levels to ensure employees have the skills needed.



The barriers

Improving the links between education and employment is not the responsibility of educators and governments alone. Employers are directly implicated: they hire workers to replace retirees and they invest in training to ensure employees have the skills needed. Their role should extend to informing the education and training systems that will produce their future employees.

The challenge for educators is incorporating the business and labour market perspectives with integrity and balance. Recent initiatives in British Columbia and Alberta, for example, suggest there is a way forward to re-orient education to the economic opportunities.

Canada's labour market has been changing over the past decade as employment has shifted away from traditional manufacturing toward natural resources and construction. We are now on the cusp of a major departure of boomers from the labour

force. Meanwhile, there is evidence of overqualified graduates along with under-employment among young people. What is unclear is whether Canada's post-secondary education system is responding to these shifts and recognizing the changing demand for skills and occupations.

Additionally, the government has restricted temporary access of the foreign nationals who until recently, provided a last resort for employers seeking to fill vacancies or a necessary source of specialized knowledge, skill or talent for projects.

The way forward

Addressing silos in skills development

The Canadian Chamber of Commerce will develop a roadmap for better policies, focusing on these key actions:

Promoting the role of better labour market information:

We must recognize that better labour market information is a necessary element of improvements to education, training and labour market outcomes. It matters to the future of young people who may be unemployed or under-employed, to mid-career workers and to employers, who cannot make good decisions without reliable and detailed data. Labour market information that is specific and timely is data that will yield better results.

Engaging employers in education systems:

If our education system is to become more relevant to the opportunities of our economy, employers should be engaged in the design of school curriculum. The structured involvement of employers in the education and training systems would go a long way in improving graduates' success in the employment market.

Focusing on increasing apprenticeship completions:

While we are expanding the numbers of apprentices, less than half of them actually complete their apprenticeships. Without enough new journey persons to take over from retirees, we will be unable to train the next generation of apprentices. We must make it more attractive for employers to allow apprentices the time for formal training. The employers who do train apprentices need to be recognized and supported.

Addressing gaps in the workforce

Canada's future economic growth will be determined by the ability of employers to access and retain workers with the necessary skills to strengthen the workforce. The temporary entry of foreign nationals to fill labour shortages or to support specific short-term projects is a critical measure to support Canada's job and growth objectives.

The Canadian Chamber of Commerce will develop a new approach to filling Canada's short-term labour market shortages with foreign nationals, where Canadians or permanent residents are not available. Addressing short-term employment needs and the temporary entry of specialized talent will bolster Canada's economy and prosperity.

II. Entrepreneurs lack capital for Canada's fastest-growing companies

The issue

One of the most critical determinants of competitiveness is access to capital, especially for start-ups and companies moving from innovation to commercialization. These fast-growing companies often depend upon venture capital (VC) as the lifeblood needed to take a company from idea to market. It may take years to develop and commercialize a new technology or product, and capital is critical to sustaining an innovative company before the revenues start to flow. We have also seen that a vibrant, robust VC industry can have a central role in building business champions, companies such as BlackBerry or OpenText.

Canada's VC industry is still small and punching below its weight, particularly when compared to much larger VC industries in the U.S. During the course of 2014, the Canadian Chamber of Commerce spoke with dozens of entrepreneurs leading fast-growing companies who say one of the biggest hurdles they face is securing capital to take their companies to the next level. Entrepreneurs told us the capital gap is largest when moving from R&D to commercialization.

The barriers

The adjacent chart shows how Canadian jurisdictions are dwarfed by the major U.S. centres, with Ontario attracting just a twentieth of the VC investment of California. Overall, Canadian venture capital funds invested \$2 billion in Canada in 2013, a solid 31% gain over 2012; however, this is still well below a peak of \$4 billion in the late 1990s.



2013 Venture Capital Invested		
State / Province	C\$ Millions	North American Market Share
California	\$15,235.8	47%
Massachusetts	\$3,172.8	9.8%
New York	\$2,969.2	9.2%
Texas	\$1,346.5	4.2%
Washington	\$951.6	2.9%
Maryland	\$680.4	2.1%
Ontario	\$676.4	2.1%
Virginia	\$614.1	1.9%
Québec	\$588.5	1.8%
British Columbia	\$477.8	1.5%
Pennsylvania	\$461.4	1.4%
Illinois	\$452.8	1.4%
Florida	\$437.6	1.4%
Colorado	\$428.7	1.3%
Georgia	\$423.7	1.3%

Source: Thomson Reuters, "Canada's Venture Capital Market in 2013".
Can be viewed at: http://www.cvca.ca/files/Downloads/VC_Data_Deck_2013_English.pdf

While early-stage VC is growing, later-stage start-up financing is actually in decline at the important IPO stage. The past three years have seen a sharp reduction in capital raised by TSX-Venture listed companies and a steep decline in new listings. In fact, the amount of capital raised for TSX-Venture companies tumbled from \$10.1 billion in 2011 to \$6 billion in 2012 and then to \$3.8 billion in 2013. The new listings show a similar decline, falling from 334 in 2011, 240 in 2012 and to just 158 in 2013.

Numerous experts cited the low rates of return for VC funds in Canada as a barrier to attracting more funding. This is not unusual in such a high-risk industry. For example, the pooled average annual internal rate of return (IRR) of U.S. venture capital funds for the 10 years ending December 2000 was a staggering 25.7%, only to be followed by a miserable -0.8% average over the next decade. Yet, if one chose the 10 years ending June 2012, performance perked up to a more respectable 3.5%¹. The high risk and variability of returns is why government incentives are needed.

The entrepreneurs the Canadian Chamber spoke with said they – and others – need more angel investors who have a longer-term mindset and less of a “make it profitable and flip it” mentality.

The way forward

The federal government, via the Business Development Canada (BDC), has done much to support the Canadian venture capital industry. However, the Venture Capital Action Plan is expected to amount to just \$400 million over the next decade², which is small relative to the overall industry. A much larger private sector component is necessary to allow fast-growing entrepreneurial firms to reach their potential.

The Canadian Chamber of Commerce will advocate a number of initiatives to boost incentives to expand the overall pool of capital and to attract more angel investors and international funds to Canada, including:

- Matching funds with a capped return that are provided by the government in order to boost the returns received by private sector VC investors. This improves the return of private sector investments while leveraging up the funding for entrepreneurs.
- Tax incentives and/or matching funds for angel investors’ loan guarantees for follow-on funding. Canadian companies exit much earlier than their U.S. counterparts, cashing out for smaller amounts even before the IPO.
- Changes to guidelines and regulations that would encourage insurance companies and pension funds to invest a small portion of assets in venture capital.
- Government policies aligned to encourage VC and entrepreneurial activity (e.g., public R&D funding that is more conducive to commercialization, with generous IP regulations).

1 “Best Practices in Venture Capital”, IDB Group, <http://lavca.org/wp-content/uploads/2013/12/Best-Practices-in-Creating-a-VC-Ecosystem.pdf>

2 Economic Action Plan <http://actionplan.gc.ca/en/initiative/venture-capital-action-plan-0>

III. Lack of clarity regarding duty to consult with Aboriginal peoples

The issue

Canadian governments have a fiduciary duty to consult and accommodate Aboriginal peoples when proposed developments have the potential to impact their constitutionally protected rights. In fulfilling this duty, governments must balance the business interests of project developers and the constitutional, cultural and economic interests of Aboriginal communities.

However, governments are increasingly relying on project developers to assume responsibility for large parts of community consultation and accommodation. This has led to situations where proponents have no clear direction on the extent of the consultation and accommodation required. Moreover, it is not clear what degree of consensus – short of unanimity – would be required to avoid a lengthy legal challenge by even a small number of opponents.

The barriers

For an investor, the amount and depth of consultation and accommodation and the steps required to obtain the necessary level of Aboriginal community support to build and operate a project in Canada is unclear, as are the probable costs and time frames involved. This increases risk for any project proposed on or within Aboriginal traditional territory, particularly areas where ownership of the land is contested, such as areas that are the subject of unresolved land claims.

Over the next decade, it has been estimated that Canadian businesses plan to invest significant amounts of capital into more than 600 resource



development projects across the country, the majority of which are proposed within or near Aboriginal communities and territories. It is estimated these projects could significantly add to Canada's GDP.

These projects represent an important opportunity for Canada, including Aboriginal Canadians. There are many examples of successful partnerships between resource companies and Aboriginal governments and entities that have provided benefits to all parties when balanced successfully against potentially negative environmental, social and cultural impacts. For Aboriginal communities, these benefits could include revenues and other economic development benefits such as training, employment, increased capacity and business opportunities for Aboriginal entrepreneurs.

Disputes will arise, however, and absent a proactive approach from governments, disagreements will continue to be addressed in a costly, uncertain and adversarial manner through the court system. This state of affairs is negatively affecting investment in Canada's resource and infrastructure sectors.

In British Columbia, the Fraser Institute identifies uncertainty about land claims and the consultation process as the single greatest deterrent to mining investment in the province.

To avoid decades of uncertainty with the huge economic penalties that result, Canadian governments must make it a priority to resolve outstanding land claim and treaty processes. They must be far more proactive in engaging with Aboriginal consultation throughout a project's development and operation. Governments must also be much more willing to enter into 'good faith' negotiations of accommodation, recognizing that project benefits for Aboriginal communities should not come solely from the pockets of project developers, but also through Nation-to-Nation agreements around long-term resource and infrastructure revenues.

The way forward

The Canadian Chamber of Commerce will explore alternatives to the current scenario for resolution of the development consultation process, which currently seems headed towards lengthy court challenges to produce jurisprudence that guides proponents, opponents and governments.

The Canadian Chamber will also:

- Profile successful collaborations between resource developers and Aboriginal communities and draw conclusions about the factors that characterize such success.
- Examine the legal implications of more explicit governmental direction with regard to required consultations by developers. Would more overt government direction have bearing on eventual court rulings?
- Consult Aboriginal communities regarding their experiences and expectations in the consultation process.

IV. Internal barriers to trade

The issue

Minor interprovincial differences in standards, regulations and certification cost the Canadian economy tens of billions of dollars each year. In recent years, provinces have made commitments towards reform but, for the most part, these have not been followed with action. The division of a small national market into a host of even smaller fragments is the most obvious and unnecessary example of self-imposed inefficiency the Canadian Chamber of Commerce has identified.



The barriers

Trade between the provinces is governed by the Agreement on Internal Trade (AIT), which has been in force since 1995. Over the past 20 years, the AIT has evolved significantly, but even with the improvements, the AIT remains flawed. The AIT doesn't cover all regions in Canada; Nunavut is not a signatory to the agreement. Many provinces maintain a long list of exemptions that limit the effectiveness of changes to the labour mobility chapter, very little progress has been made on a chapter covering energy and provinces continue to ignore trade rulings that do not go in their favour.

The governance of the agreement is another major issue. The AIT was designed so that decision-making requires consensus. This framework makes progress very difficult as any party can use the power of veto to prevent developments that do not serve their own interests. Unfortunately, protectionism remains a significant issue amongst the provinces. While protectionist measures can be politically popular, they are very costly in practice. Tariffs, quotas and non-tariff barriers distort the market and limit consumer choice. Many provinces have formed regional trade blocks in response to such issues.

The way forward

Over the past three years, the Canadian Chamber has been calling for reforms to Canada's internal trade regime, and there are positive signs of progress. The 2014 federal budget included a commitment to survey the existing barriers to trade and the Minister of Industry conducted several roundtables throughout the course of 2014 to promote the importance of internal trade. The Council of the Federation recently promised to undertake a comprehensive renewal of the AIT. This renewal would be based on the existing AIT and would keep in mind the need to be consistent with modern international trade agreements. Some of the areas highlighted as priorities include: technical barriers to trade, regulatory cooperation, government procurement, services, goods and investment. And, the premiers launched a steering committee to lead territorial and provincial ministers in this work. Negotiations on a revamped internal trade regime are set to be completed by March of 2016.

With the growing attention to the issue at all levels of government and with a concerted effort by the Canadian business community, a new agreement can be reached.

In 2015, the Canadian Chamber of Commerce will continue to work with relevant stakeholders to push for a new agreement on internal trade. The Canadian Chamber will advocate:

- The negotiation of a new, more comprehensive and binding agreement on internal trade.
- The addition of new chapters to the AIT that cover issues such as energy and technical barriers to trade.
- Improvements to the efficiency, transparency and accessibility of the dispute resolution process.
- Improvements to the governance of the AIT, including strengthening the secretariat and creating a permanent, non-governmental vice chair role.

V. Canada's tax system is too complex and costly

The Issue

Canada's tax system is in urgent need of reform. It has become increasingly complex, multi-layered, and a costly challenge for Canadian businesses of all sizes. The World Economic Forum's Global Competitiveness report cites tax rates and regulations as two of the top five challenges to doing business in Canada.

Our members say that the challenge of tax compliance is significant for businesses of all sizes. This is not just for SMEs who have limited time and resources to devote to book-keeping and the pursuit of tax credits. Many major multinationals also struggle with Canada's lack of a formal system to consolidate the tax reporting of corporate groups or to otherwise transfer corporate profits and losses among related companies.

A streamlined and more efficient tax regime would free up time and capital for Canadian companies so that they can focus on growing their business, investing and creating jobs.

The Barrier

The costs to Canadian business of complying with an increasingly complicated tax system are enormous, both in terms of labour and dollars. From collecting, tracking and organizing the information to complete tax requirements, setting up the accounting systems and working with auditors and paying the fees for accountants and tax preparers. According to a study by the Fraser Institute, the costs of complying with the Canadian tax system are estimated at \$14 to \$18 billion per year.



One important element driving the complexity is that over decades successive governments have added tax credits to favour specific industries, and while many of these are beneficial to business, the large number of credits has proliferated and made the tax system too unwieldy and complicated.

Tax efficiency is not just the alleviation of administrative burdens, according to Canada's Competition Policy Review Panel, "An equally important policy issue is the design of a scheme of taxation and its impact on individual and corporate incentives and behavior".¹

The Way Forward

The Canadian Chamber of Commerce will advocate a streamlined, broad-based tax system with lower rates and fewer tax credits for individuals and corporations alike. Lower tax rates would stimulate economic activity, attract investment to Canada and

¹ Competition Policy Review Panel, "Sharpening Canada's Competitive Edge", Ottawa, Industry Canada, October 2007.

lower tax evasion. This effectively broadens the tax base and can substantially reduce the amount of lost revenue that goes with lowering tax rates.

A multiparty Royal Commission could overhaul Canada's tax system to reduce its complexity by reviewing and clarifying the language used in tax law; recommending changes to existing legislation that is not achieving its purpose or entails costs that outweigh the revenue being raised or protected; and evaluate all tax preferences (credits, deductions, exemptions, rebates) with a view of eliminating those that are not cost effective or are not achieving their intended purpose. The increase in revenue from eliminating credits could then be used to lower rates. The previous Royal Commission on Tax occurred almost fifty years ago, back in 1966. The type of broad-based, fundamental reshaping of Canada's tax code could only occur through a multi-party process, as opposed to piecemeal reform.

Most economists would agree that consumption taxes are generally more efficient than income or corporate taxes. This is because income taxes also affect income earned from investments, and create a "double taxation" on savings (i.e. tax was paid when you earned the money, and then tax is paid again on interest earned from the savings). Shareholders also suffer because business earnings are taxed at the corporate level, and then again when they are received by the investors as income. The Chamber recognizes that to make a significant decrease in overall rates for corporate or personal income taxes would be costly, and could not be done without raising revenue elsewhere, likely through an increase in the HST. The Royal Commission could provide the political cover that the parties need and also educate the public on what is being done, that is to say we are raising the HST by a certain percentage in order to provide a larger decrease in personal income taxes.

Finally, the administrative burden of taxation falls most heavily on smaller firms, those that are most in need of additional cash, so we recommend that the income threshold for the small business tax rate be increased to \$1,000,000 from \$500,000.

VI. Canadian trade is constrained by infrastructure deficiencies

The issue

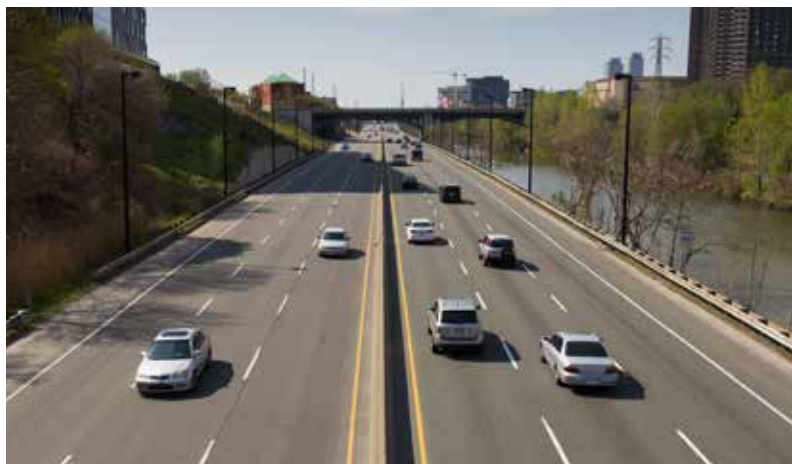
For the past three years, the Canadian Chamber of Commerce has identified the lack of planning and investment in core public infrastructure as one of the key barriers to Canadian competitiveness. Infrastructure is an economic enabler and a cornerstone of a competitive economy. As Canada continues to pursue its ambitious trade agenda, planning and investment in trade-enabling infrastructure becomes all the more critical.

The barriers

In 2013, the Canadian Chamber commissioned a study on the status of Canada's core public infrastructure. The report¹ highlighted the clear ties between infrastructure investment and productivity: a sustained 10% annual increase in infrastructure investment has the potential to reduce the costs of manufacturing by 5%.

Unfortunately, the bulk of Canada's infrastructure stock is well past its service life. Even with the recent upswing of federal funding for infrastructure, Canada's investment needs far outstrip the availability of public funds.

Also concerning is the fact that Canadian communities generally have a very poor understanding of the current state of infrastructure. Very few communities across Canada have the capacity to determine the true state of their existing assets let alone develop long-term strategies for maintenance and renewal.



To address the competitive challenges, a good portion of these strategic investments must focus on areas where we will see the greatest return on our investment.

Canada is a trade-dependent nation in the midst of its most ambitious trade agenda, which involves trade negotiations with major economies like Japan, India, South Korea and the European Union. Partially as a result of these agreements and also of the surge in the global middle class (which is expected to reach almost five billion consumers by 2030), demand for Canadian goods and services is expected to increase. Such an increase will be a tremendous boon for the Canadian economy, but only if we are able to get our goods to market. It is well known that our inability to get our energy exports to tidewater is forcing us to accept lower prices for our landlocked products.

In order to succeed, Canada has to position itself as a reliable, predictable and competitive gateway into and out of North America. A main component of this

¹ The Canadian Chamber of Commerce, *The Foundations of a Competitive Canada: The Need for Strategic Infrastructure Investment*, December 2013.

strategy will be ensuring our infrastructure is able to handle not only existing trade flows but also the expected shifts in our trade patterns.

Fortunately, we have already had some success in this area. As an example, Canada's Pacific Gateway Initiative demonstrates what improvements are possible through the appropriate mix of policy and the integration of various stakeholders in a single strategy.

Significant public assets, including ports and their access roads and commodity handling facilities are nearing their maximum capacities, and Canada still does not have a new gas or oil pipeline to either the west or east coast.

Canada has to create an integrated, strategic approach to trade-enabling infrastructure.

The way forward

To improve Canadian competitiveness, Canada needs a long-term infrastructure investment strategy designed to enable trade, which is both growing and shifting. Such a strategy will focus on public investments that influence or support private investment.

A successful strategy would:

- Recognize the importance of the private sector's involvement in planning and identifying priorities for Canada's trade-enabling infrastructure. At present there are few fora for a longer-term dialogue on potential capacity requirements.
- Focus on areas where there will be the greatest return on economic productivity.
- Foster the appropriate climate to encourage complementary private investment.
- Be predictable and transparent.

VII. Canada is uncompetitive in the world's tourism sector

The issue

A decade ago, Canada was among the top five international tourist destinations and now, it is in 16th place. The effect of this change has been to reduce the contribution of one of Canada's largest economic generators. In 2013, the total contribution of the travel and tourism industry to the Canadian economy was \$84.3 billion, accounting for 4.5% of Canada's total GDP and 600,000 jobs.

Investing in this sector is not only essential for job creation. It also generates \$22.7 billion in tax revenue and plays a pivotal role in driving trade and facilitating export growth. Billions of dollars in revenue that Canadians could be earning are being left on the table.

Canada's tourism competitiveness problems are self-made and can be overcome by better strategies and policies.

The barriers

Inadequate destination promotion

In November 2014, Oxford Economics's *Destination Promotion: An Engine of Economic Development* report stated, "The fundamental motivation driving a visit to a given destination is frequently not the offerings of a single business – instead it is the destination, including a range of attractions and the overall experience of a place. This experience is comprised of a visitor's interaction with, and patronage of, numerous businesses and local experiences: hotel and other accommodations; restaurants; shopping and galleries; conferences; performances and other events; family activities; sports and other recreation; and cultural sites and attractions."



Because a visitor's spending is spread across many industries, no single business in Canada can effectively capture an adequate share of a visitor's spending to rationalize marketing to attract visitors on their own. That is why a federal marketing strategy is needed. A strong national brand is a prerequisite to international tourism marketing as rival nations, such as Australia, Jamaica and Mexico, are demonstrating. Canada's marketing efforts must be substantially increased to capitalize on the Canadian brand and to effectively compete in the global tourism market.

High costs

High costs continue to impede Canadians' ability to travel within their own country. Canada has one of the most expensive air transport markets in the world. User fees and levies on aviation add hundreds of millions to passenger costs, and these non-carrier charges typically account for 40% to 70% of passenger costs. Although most nations support their aviation sector by financing public costs, such

as security, Canada is unique in making air travellers pay the entire cost of public activities and also levies rental charges on Canadian airports.

Investment climate

A steady decline in the number of international visitors undermines investors' confidence among investors, which in turn delays new construction and renovation of the tourism infrastructure. Critical "anchor" facilities, such as convention centres, and major hotel investments have significant spin-off impacts in the communities where they are built.

In light of Canada's relative decline through the 2000s, and especially following the recession of 2008/2009, major hospitality investors announced reductions in their Canadian hospitality/travel investments.

Creating a hospitable environment for investment requires both positive trends in visitor volumes and a host of supporting factors, including regulatory efficiency and a skilled and cost-efficient workforce. Without large, periodic new investments, the Canadian tourism industry will lose ground relative to other nations.

Reinvesting in the visa application process

Upgrading Canada's visa application process to increase its capacity and reduce its complexity and inconvenience for potential visitors would attract growth from countries like Brazil, China, India and Mexico. The visa system generates revenue for the government and those revenues can be enhanced as travel volumes rise.

Visa inefficiency is a serious problem for Canadians at many levels. It diminishes the competitiveness of Canada's general tourism marketing and specifically harms international convention trade and inter-corporate transfers, the latter so essential for a services-based economy such as Canada's.

Visa modernization is a high priority for Canada's Citizenship department, where a host of new technologies and processes are being examined. The constraint is funding.

The way forward

In 2015, the Canadian Chamber of Commerce will:

- Advocate that the federal government invest \$120 million in the Canadian Tourism Commission's marketing budget.
- That the federal government implement measures to alleviate costs borne by airline customers. As the recommendations of the Canadian Transportation Act Review are released, and to the extent that they address these problems, they should enjoy broad support in Parliament and be implemented quickly.
- In cooperation with ally organizations, examine the investment climate for major hospitality and travel facilities, and make conclusions regarding policies at all levels of government, which would stimulate new investments.

VIII. Innovation rate is not sufficient to help manufacturing rebound

The issue

Manufacturing employs millions of Canadians and generates billions in salaries, sales, exports and taxes. In 2013, close to 80,000 manufacturing businesses generated revenues of more than \$590 billion and employed 1.8 million Canadians.¹ In many ways, manufacturing, the largest sector of the Canadian economy, built Canada and it boosts rural and urban economic development from coast to coast to coast.

But, something is happening – or not happening – that is dampening the value and impact of innovation in our manufacturing sector. Canada is now ranked a distant 22nd by the World Economic Forum for its capacity for innovation. Similarly, Canada ranks 27th in company spending on R&D and 22nd in technological readiness.²

Most experts agree that Canadian manufacturers cannot restore their prosperity by competing on price. The best way for Canadian companies to compete and win in modern manufacturing is through a strong commitment to innovation. While some companies are commercializing products that represent breakthrough technologies they have developed themselves, most manufacturers will have to invest in some of the innovative technologies that are just beginning to revolutionize manufacturing globally. Renewed vigour in Canada's manufacturing sector will come as firms here invest more aggressively in these technologies – and in the skilled workforce to use them effectively – than their competitors. The efficiencies gained through the use of disruptive technologies are significant.



The barriers

The majority of Canadian firms are struggling to adopt advanced technologies. For example, just 6% of firms have adopted a strategy to harness the “Internet of things,” allowing them to better monitor their production and distribution processes while only 22% of C-suite executives indicated they are using data analytics as a tool to better understand product cycles and the real value of their own innovations.

The barriers to investment in this sector are significant. In the Canadian Chamber of Commerce's 2014 paper on manufacturing in Canada³, numerous factors are cited to account for the slow adoption of disruptive technologies: investment cost and uncertainty of markets are often cited as the most significant. Canada is a relatively small market with

1 KPMG, *Canadian Manufacturing Outlook 2014: Leveraging Opportunities, Embracing Growth*, 2014.

2 *Ibid.*

3 The Canadian Chamber of Commerce, *Manufacturing Innovation: Driving Canada's Biggest Sector through Disruptive Technologies*, December 2014.

few head offices, meaning investment decisions are made outside its borders, and other jurisdictions are competing for those investments.

Incentives for large scale, innovation investments from global companies (the manufacturing hubs) are not sufficient to overcome the disadvantages of an industrial base that is primarily headquartered outside Canada. This leaves local supply chains (the manufacturing spokes) – the bulk of manufacturing in Canada – with a market disadvantage.

While several provinces have incentive programs to encourage investment in manufacturing, there is no federal government mechanism or program that clearly demonstrates Canada’s commitment to securing and maintaining the high-value jobs the sector provides. Global companies are making investment decisions in jurisdictions where commitment is certain.

The innovation policy framework that exists in Canada is not sufficient to overcome these barriers. Whether the problems stem from cultural factors (aversion to risk), branch plant weakness, inadequate or poorly designed government support programs or other disincentives to investment, the result is a manufacturing sector that is not recovering the ground it lost during the recession.

The way forward

The government of Canada is a world leader when it comes to funding the primary research, science and technology that generates a significant volume of patentable ideas. But, this leadership does not translate into the collaborative efforts and business investments needed to commercialize those ideas. Building on its report⁴ from 2014, the Canadian Chamber of Commerce will explore recommendations to reconcile the disconnect between industry and institutions, find a mechanism to support the commercialization of new technology and look at options to support business in the adoption of new technology.

4 Ibid.

IX. Territorial businesses don't have the tools they need

The issue

Canada needs economic strength in all of its regions to compete. Reducing the dependence of Canada's territories on the federal government for financial transfers and jobs as well as improving the conditions for private sector growth would improve our national competitiveness. With the right tools, businesses in the territories can make economic growth and increased independence from the federal government happen.



The barriers

Recent developments in federal policy-making are taking the territories in the wrong direction. For example, temporary foreign workers are a necessity for businesses operating in Canada's territories, where it can be impossible to find the employees businesses need locally. The recent changes made by the federal government to the Temporary Foreign Worker Program make it more complex and expensive – if not impossible – for territorial businesses to get the workers they need.

Another example is the “cost creep” of doing business in the territories. The federal government has reduced business taxes as well as regulatory red tape through devolution in Yukon and the Northwest Territories. However, a recent analysis by the Northwest Territories Chamber of Commerce highlights that any savings to its businesses are being overtaken by territorial and municipal governments imposing higher taxes and fees on businesses. In addition, the number of territorial government employees is increasing in the Northwest Territories, setting salary and benefit expectations in the workforce that the private sector cannot match. To quote a July 2014 *Northern News* article, “Government grows and businesses close in the NWT.”

The way forward

The tools territorial businesses say are critical to their success and to increasing their economic footprint include:

- Infrastructure funding and investments
- Attracting and retaining talent
- Clarity in regulatory oversight in natural resources
- Constructive relationships with Aboriginal peoples

Providing support to the territories to ensure these factors are improving is an ongoing challenge for the federal government. The Canadian Chamber of Commerce will build upon the work it started in 2012 to identify the key federal policy levers that give businesses the tools to grow by:

- Delving more deeply into those mentioned by business people most often
- Identifying measures the federal government can take to improve the business climate in the territories
- Presenting its findings and recommendations to the federal government

X. Canada is missing out on foreign trade opportunities

The issue

Canada's prosperity depends on access to international customers and participation in global supply chains. Given Canada's small domestic market, exporting is often the only way for companies to grow sales and build economies of scale. Moreover, sourcing from and investing abroad allows them to exploit distinct technologies, skill sets and cost advantages from around the world.

However, Canadian companies are not globalizing as quickly as their peers. According to the World Trade Organization, Canada's exports of goods and services grew by only 43% over the past decade – compared to 137% and 74% in Australia and the U.S. Last year, the Governor of the Bank of Canada noted that over 9,000 companies had stopped exporting since the start of the recession.

Canadian business continues to lag in emerging and frontier markets, where the bulk of long-term growth opportunities lie. The share of exports going to these countries doubled from 2004 to 2009 but has stagnated since. Outside of Latin America, developing countries account for only 1.5% of Canada's foreign investment stock – by far the lowest share among G7 countries. The return of the American economy is a welcome development, but should not distract from the need for Canada to position itself for the future.



The barriers

Many of the biggest hurdles to internationalization come from the policies of foreign governments. Protectionist tariffs and quotas, discriminatory or diverging regulations, subsidies, ownership restrictions, local content requirements and the poor protection of physical and intellectual property all make it difficult for Canadian businesses to compete abroad. Canadian service providers often face entry restrictions and tax disadvantages or find that their credentials and expertise are not recognized.

To reduce these barriers, Canada is pursuing an ambitious agenda of trade and investment agreements with key markets. Major progress was made in 2014 with the conclusion of negotiations with the European Union and South Korea. Canada also ratified an investment treaty with China and

announced talks to explore other arrangements in the future. Ongoing negotiations with Japan, India and the Trans-Pacific Partnership countries hold promise as do multilateral talks on services, environmental goods and information technology.

But these agreements are no panacea. Negotiations are dragging on in some cases. Completed agreements can take years to implement and often do not cover “murkier” forms of protectionism. And there is no guarantee that governments will respect their obligations. Trade disputes are long and arduous and are simply not an option for many smaller companies operating on short timelines.

Agreements also do little to address operational challenges. Companies have to build relationships with new customers and suppliers, access capital, navigate red tape and manage risks – all in a new political, cultural and legal landscape. Broader diplomatic ties between countries matter a lot for business, especially in markets where the state plays a major role in the economy.

In this context, Canada’s foreign service and trade promotion programs are essential. They help companies navigate new markets and represent their interests with local governments. Frequent political engagement through high-profile business and government delegations is also important. In many cases, however, these efforts lack resources and coordination, are poorly communicated to companies or are not adequately tailored to their needs.

The way forward

The federal government needs to build on recent success and take additional steps to conclude the next wave of high-quality trade agreements and strengthen Canada’s system of trade promotion and economic diplomacy.

In 2015, the Canadian Chamber of Commerce will advocate:

- Progress on the bilateral trade agenda, including the ratification of Canada’s agreement with the European Union, the conclusion of negotiations with Japan and India and the launch of exploratory talks with China.
- Canadian leadership to advance regional and global trade talks, including the Trans-Pacific Partnership and plurilateral negotiations on trade in services, environmental goods and information technology.
- Enhanced regulatory cooperation to facilitate the acceptance of Canadian goods and services by major trading partners, including measurable outcomes from the Canada-U.S. Regulatory Cooperation Council.
- The expansion of Canada’s diplomatic presence abroad, including additional resources and enhanced training programs for the Trade Commissioner Service.
- The establishment of a development finance institution to help Canadian business to deploy their technologies, expertise and capital in developing countries.



TOP 10

Barriers to Competitiveness

OTTAWA

420-360 Albert Street
Ottawa, ON
K1R 7X7

) 613.238.4000

☎ 613.238.7643

TORONTO

901-55 University Avenue
Toronto, ON
M5J 2H7

) 416.868.6415

☎ 416.868.0189

MONTREAL

560-999 de Maisonneuve
Boulevard West
Montreal, QC
H3A 3L4

) 514.866.4334

☎ 514.866.7296

CALGARY

PO Box 38057
Calgary, AB
T3K 5G9

) 403.271.0595

☎ 403.226.6930

THE CANADIAN CHAMBER OF COMMERCE

LA CHAMBRE DE COMMERCE DU CANADA



Chamber.ca