

Building Competitiveness in Atlantic Canada



***Strategic directions for improved productivity and prosperity -
for ourselves and future generations***

What is competitiveness? How do we define it? Can we compete effectively? Can we increase the return to our shareholders and our workers? How does one country or region move ahead while others slip back? These are all questions central to our understanding of Atlantic Canada's place in the world.

Earlier this year, APEC launched its Forum on Competitiveness, a unique five-year research and policy reform initiative designed to set a clear path for improved growth and prosperity in Atlantic Canada.

Naturally, as we've moved into a global economy, our ability to comprehend the determinants of competitiveness has taken on increasing importance. To that point, we focused on global business as the theme of APEC's Outlook 2007 conference.

The following text is taken from a speech delivered to conference delegates by Elizabeth Beale, President & CEO of APEC. It sets the context by discussing issues related to competitiveness in the region and highlights key policy considerations.

Competitiveness Defined

There are many ways to depict the competitiveness framework. One simple definition is: the factors, policies and institutions that determine the level of productivity and, thus, the prosperity that flows back to individuals.

However the one that I like to use is taken from the work of business professor and analyst Michael H. Best. It is a useful model because it emphasizes the interconnectedness of firms, workers and the business environment. It also suggests that competitiveness is a dynamic process –

a virtuous circle of business and socio-economic processes that encourage firms to innovate and drive prosperity to new levels.

In this, two themes emerge. One is technology. Competitiveness is, more than ever, determined by technological advancement. In fact, productivity improvements over the past 15 years have been driven by explosive growth in information and communication technologies. These ICT technologies have vaulted us into a rapidly evolving global economy. This fact underscores the other theme, which is that competitiveness is much more closely integrated with global economic conditions than ever before.

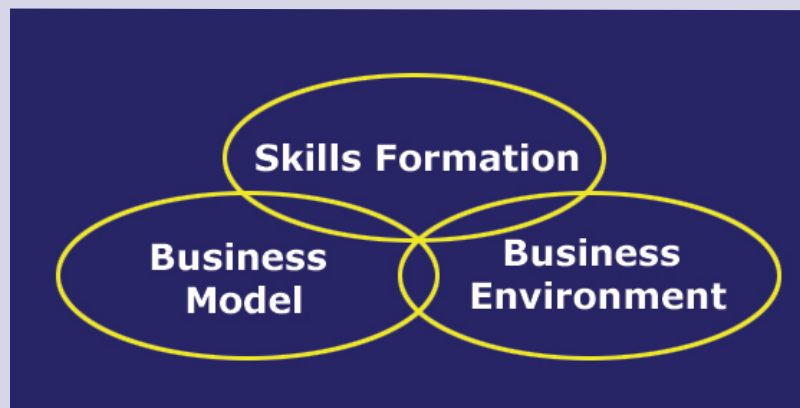
In terms of the business model, competitiveness focuses on entrepreneurial firms and their capacity to develop a unique capability to gain competitive advantage. But in an environment of rapid technological change, it's not just individual firms that play a vital role. It is also the



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Competitiveness

Factors, policies and institutions that determine the level of productivity and thus prosperity to individuals



A "virtuous circle" of business and socio-economic processes that encourage firms to innovate, driving prosperity to new levels.

Source: Michael H. Best, *The New Competitive Advantage*, 2001

“Competitiveness is, more than ever, determined by technological advancement.”

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open system, network or cluster of enterprises in which they operate. In a competitive environment, firms are encouraged to focus on their core capabilities and use the network for sharing ideas and complementary capabilities.

This establishes a continuing dynamic of product-led competition, with technological diversification reinforcing the drive to develop unique products and applications. Interestingly, the description applies not only to the tech sector, but to many established industries as well. Compare the success of the Asian auto industry with that of its North American counterpart, and you get the point.

Within this context, a truly competitive business environment will be one that provides efficient and open markets (with respect to trade, investment, regulation, tax, labour mobility); advanced technological capabilities (including high-quality research institutions); top notch transportation and communications infrastructure; sophisticated financial markets; and stable but flexible and responsive public institutions and governments.

Clearly, skills formation to support competitiveness requires an open educational system focused on improving outcomes. This means a system that reduces barriers to entry, avoids rigid structures and/or programs, and ensures accountability in terms of what is produced and spent. A key priority must be to support world-class attainment, particularly in scientific and technical fields, as these are many of the skills necessary to lead. Indeed, many countries have targeted enrolment in these fields as a catalyst for economic growth.

At the same time, effective innovation rests with firms. So, skills development must be fully integrated with firm capabilities. This speaks to the need for continuous on-the-job training.

What, then, are the benefits of improved competitiveness? They include: improved ability to trade in global markets; greater responsiveness

to changes in global opportunities; faster medium- and long-term growth; and higher overall per capita incomes. The evidence is everywhere and for all to see.

Models of Competitiveness

Many countries and regions have improved their competitiveness, and substantially transformed their economies in the process.

There is, for example, Ireland, which benefits from a responsive government, flexible institutions, an attractive corporate tax regime, an open policy towards foreign direct investment, and a highly educated and available labour force. Ireland for many years has been a growth leader in Europe.

There is the U.S. Southeast Research Triangle, which, from a small base of three universities and related research institutions in the centre of North Carolina, launched a coordinated effort to become a high-tech centre in biotechnology, microelectronics, and information technology. It has attracted many leading firms, and its success has been significant enough to take the state from a position in the mid-1950s, when it had the second lowest per capita income of any state, to close to the national average today.

And there are established countries like Switzerland, Sweden and Finland, which all took top marks in this year's Global Competitiveness Index due to their innovation capacity, sophisticated infrastructure, and strong record of fiscal management.

Atlantic Canada's Performance

What does Atlantic Canada's recent economic performance reveal about its competitiveness? The good news is that there has been a clear improvement in economic performance in terms of real GDP per person. This can be attributed to the growth of new industries, particularly oil and gas, and services; better labour market performance; and the fact that we are going global.

Dynamic and entrepreneurial firms in this region as well as established firms are all reaching out to global markets. Energy products are our largest source

of international export growth. As a result, overall export growth has exceeded national standards. Moreover, as the U.S. economy slows, we are finding expanding markets for resource and other products in Asia.

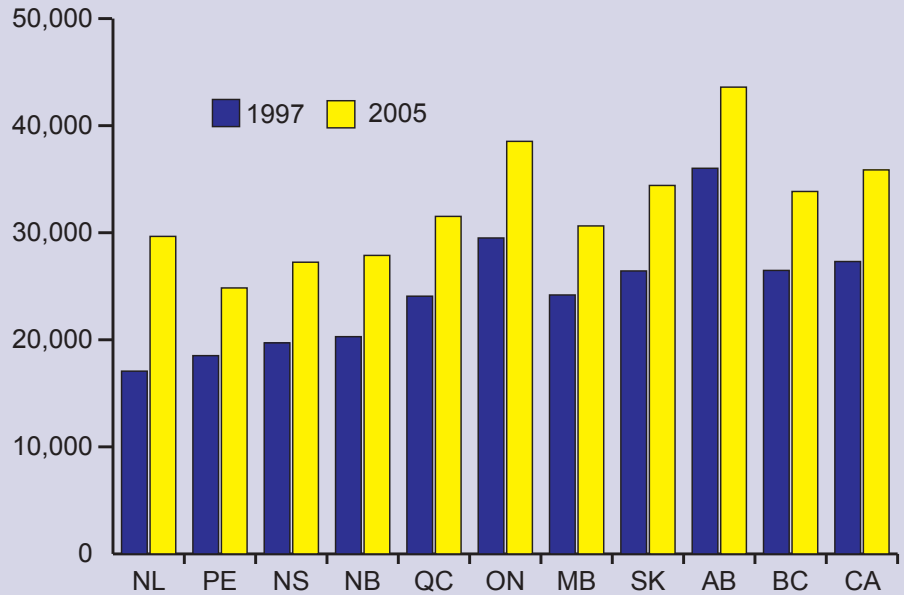
The bad news is that Atlantic Canada's overall growth has not kept pace with the nation. In the 1980s, we matched national performance in economic growth. In successive five-year periods, however, we have slipped. Newfoundland and Labrador has vaulted to the top in terms of output growth but its prospects hinge on the promising, but volatile oil industry. The three Maritime provinces have fallen well back compared to the other provinces. Since 2000, the annual growth rate of the three Maritime provinces has averaged about 2.1%, compared with 2.6% in Canada as a whole.

In employment, net growth has come almost entirely in the service sector. However, many of the faster growing service industries, including business services, which includes call centres, offer relatively low average wages. And call centre employment growth has levelled off in the past couple of years. Employment in the higher wage industries such as the professional, scientific and technical fields has grown at a faster pace than in the country as whole. However, the share of employment in these fields in Atlantic Canada is still relatively small.

Employment growth across Atlantic Canada has been very muted, largely as a result of what is happening in the resource industries and related manufacturing. The region has seen a larger drop in manufacturing jobs (down about 12,000 jobs since 2004) than the country as a whole. And this followed a steady drop in resource industry employment since the early 1990's, notably in Newfoundland and Labrador as a result of the closure of the groundfishery. Big offshore oil projects have contributed significantly to output growth in that province but have done little to arrest the losses in employment from other sectors, and the ensuing outmigration of population.

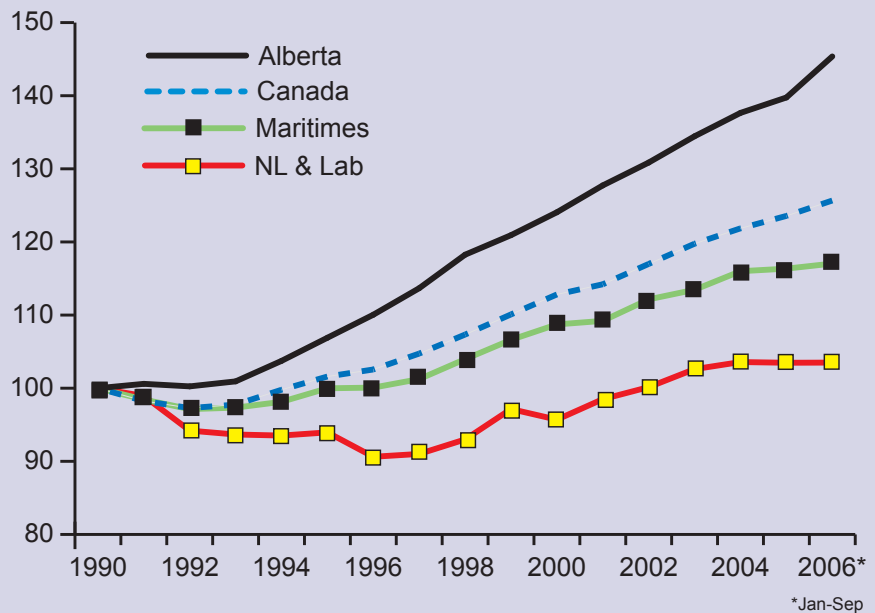
With employment growth concentrated in lower paying industries, a persistent wage gap exists between Atlantic Canada and the country in general. Average

Real GDP per Person, Chained 1997 Dollars



Source: Statistics Canada/APEC

Index of Employment (1990=100)

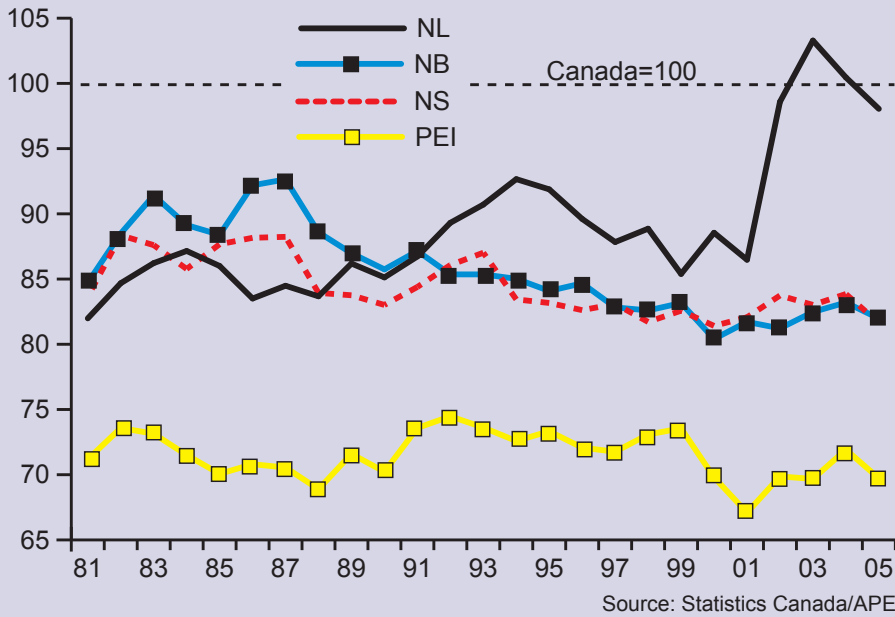


Source: Statistics Canada/APEC

weekly wages in 2005 were almost 20 per cent higher in Alberta than in Nova Scotia.

This points to a central challenge. With the exception of Newfoundland and Labrador, Atlantic Canada's productivity performance has persistently lagged behind the national average since the late 1980s – all of which makes it appropriate to ask whether the region has become stuck in a low-productivity trap.

Real GDP per Hour Worked, (Canada=100)



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A Perspective from Foreign Firms

One of our areas of enquiry under the APEC Forum on Competitiveness has been to ask business how they rank the competitiveness of Atlantic Canada. In a new study of foreign direct investment, foreign firms were asked to compare the business climate in this region with jurisdictions in which they have similar operations. It's worth emphasizing that between 50 and 75 per cent foreign firms rated Atlantic Canada as average on any one factor. This should be reassuring, in that the region is not widely out of line with competing jurisdictions. And on some factors, such as unit labour costs, there was a clear advantage for Atlantic Canada.

But on many other factors, the region was scored at a disadvantage. A significant number of respondents rated Atlantic Canada as worse or much worse on such factors as transportation systems, energy costs, tax rates and the regulatory environment.

This points to the importance of targeted strategies to address deficiencies in our business environment. But these alone are not going to vault us out of the low productivity trap.

Policy Considerations

In reality, we need a bolder vision of competitiveness; one that embraces technology and innovation, world-class educational attainment and strong and flexible institutions. It seems clear that for mature economies, competitiveness should never be a race to the bottom. We can never win against a never ending flow of new low wage competitors.

Governments are increasingly aware of the need for sophisticated strategies to address the competitiveness challenge. But they face competing interests, and as a result their strategies often remain diffuse rather than narrowly targeted and tied specific deliverables.

Here are some suggestions to target as part of building a competitiveness strategy for Atlantic Canada:

Fiscal Framework: A Tougher Stand in Favour of the Equalization program.

The responsibility for economic development is increasingly shifting away from the federal government, towards provincial governments. But in order to provide the essential services and new investments necessary to support a growing economy, each of our Atlantic provinces needs adequate resources, and that goes beyond what is available from their own source revenues. Thus federal provincial transfers, particularly the Equalization program, are essential to support the capacity of poorer provinces to provide a competitive environment in terms of provincial services. Yet the Equalization program is under attack from many sides, and in this region, we have been much too apologetic, and reluctant to come to its defense. We need to change that, to put up a strong fight for this program as an essential tool to support the economic development of all regions across Canada, reminding all Canadians of the constitutionally enshrined principal that “provincial governments have revenues to provide reasonably comparable levels of public services at reasonably comparable levels of taxation”.

Business Environment:

Creating a More Open Economy

Atlantic Canada needs to build a business environment that emphasizes more open markets – focusing on reducing barriers to trade and improving the effectiveness of our regulatory environment. Inefficient regulation imposes unnecessary costs, slowing or restricting investment and creating uncertainty. However, improving regulatory effectiveness must also take into account the need to meet the appropriate standards with respect to the mitigation of public risk and protection.

A new initiative in western Canada points to a path which the Atlantic provinces might pursue in terms of reducing interprovincial barriers to trade. An agreement between B.C. and Alberta on trade, investment and labour mobility is designed to create an open market in those two provinces, and provide a better platform for movement of goods and services between the Pacific coast and the oil patch. It ensures that both professionals and tradesworkers are treated in British Columbia as they are in Alberta – and vice versa – as long as they're occupationally accredited in either of the two provinces and able to show up for work on time. Finally, it harmonizes investment regimes and regulations, government procurement policies, agricultural output and pricing, transportation infrastructure and related development, and financial services. Soon, its signatories say, the agreement may encompass various segments of the public sector, including municipalities, school boards, publicly funded academic institutions, health and social services, and provincial Crown corporations.

Strategic Investment in Innovation

Substantial public investment has been made over the past ten years in research, particularly at our universities. Yet the tangible results of much of this investment have yet to be realized, perhaps reflecting the long term nature involved in developing many of these new technologies. Now, there are signs that the initial enthusiasm in support of increased

national investment in research is on the wane, with some of the regional initiatives being subject to the greatest level of scrutiny.

For Atlantic Canada, this poses a challenge: this could cut the ground out from under some of our important initiatives before they have really had a chance to show any success. However at the same time, this exposes the need for us to focus on creating more targeted initiatives, ones that will reward success in commercial applications or build key research clusters rather than trying to support a myriad of small initiatives across the region.

Building Productivity:

Investing in a Skilled Labour Force

Improving productivity is one of our greatest challenges for this region. Yet provincial policies to encourage employment - labour subsidies to firms relocating to the province - are too often directed at firms who are low on the innovation scale and have little commitment to investing in the skills of their workers, thus exacerbating low productivity levels. To the extent that incentives remain part of the provincial arsenal for economic development, it is important to shift these in favour of encouraging investment in new technologies, rewarding firms and workers for productivity improvements, rather than simply subsidizing job creation.

One practical suggestion on the skills side is a human resource tax credit to encourage hiring new graduates, or encourage firms to invest in on-the-job-training. Innovative firms require highly qualified workers who are continually developing and acquiring new skills. Supporting this process contributes directly to improved productivity.

Conclusion

These are all big questions. And we will have to come up with answers that make sense in a regional perspective. But this is, after all, Atlantic Canada's competitiveness challenge. And the objective is clear: To boost productivity and prosperity in this part of the world for ourselves and future generations.

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