Industry Canada / Industrie Canada

Canada in North America
Economic Opportunities & Challenges

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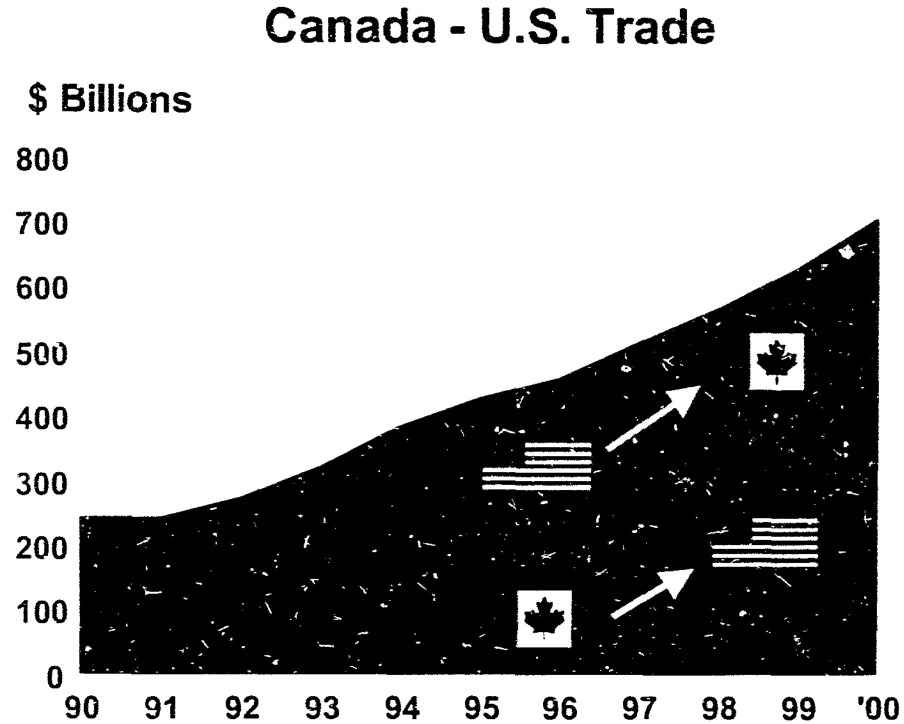
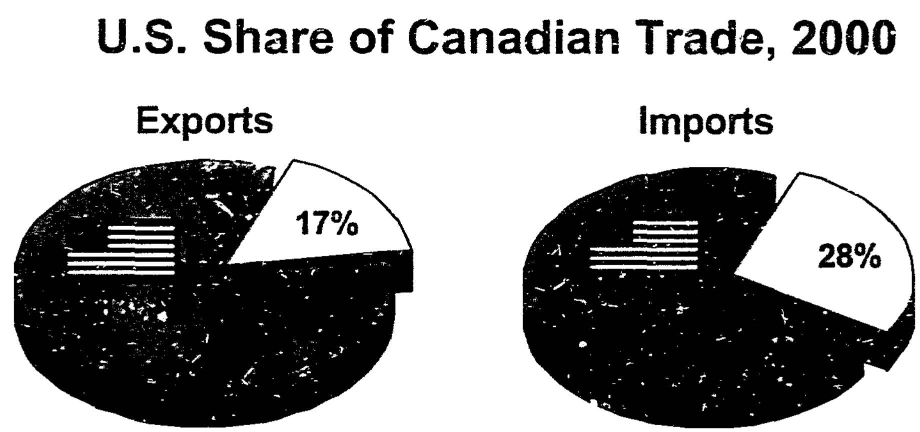
Trade with the U.S. is vitally important to the Canadian economy

- International trade represents nearly 90% of Canadian GDP, the highest among the G7.
- The U.S. accounts for 83% of Canadian exports of goods and services and 72% of imports.
  - Canada-U.S. trade now stands at $700 billion per year — $1.3 million dollars every minute!





Source: Statistics Canada

Trade linkages with the U.S. increased for all Canadian provinces in the 1990s

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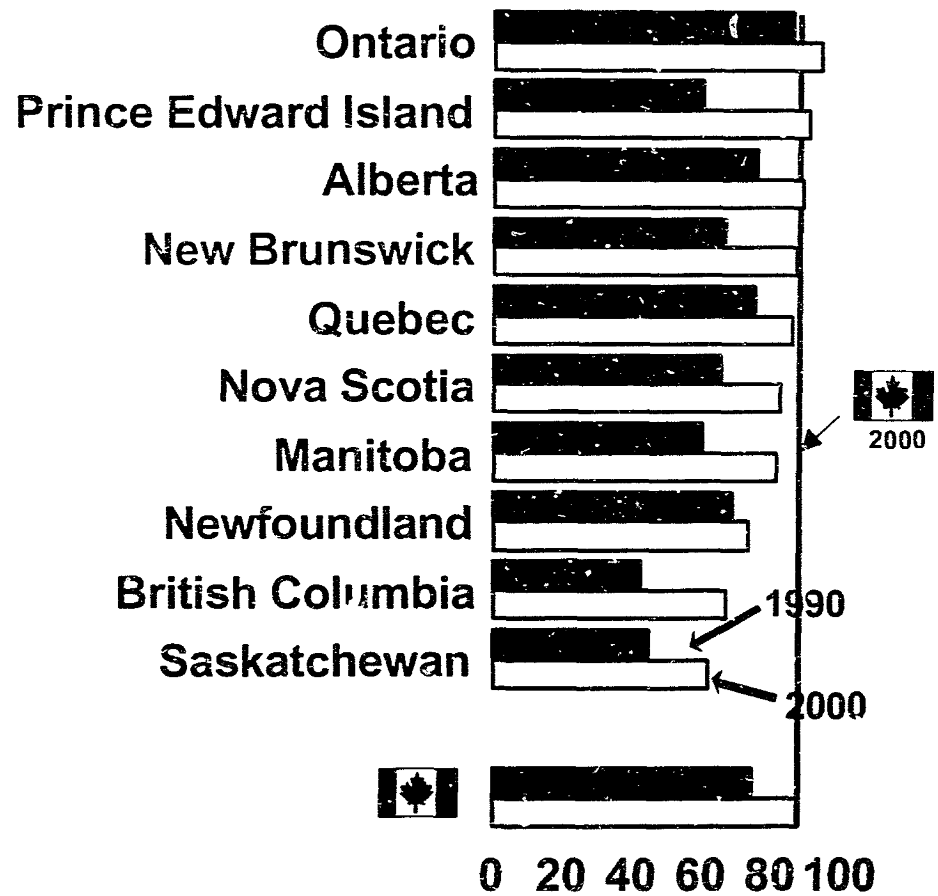
Share of Exports* going to the U.S. by Province

- Over 87% of Canadian merchandise exports now go to the U.S.
- The share of exports going to the U.S. has increased in every province.
  - 62% of Saskatchewan's exports go to the U.S., the lowest share in Canada.
  - Ontario is the highest at 93%.



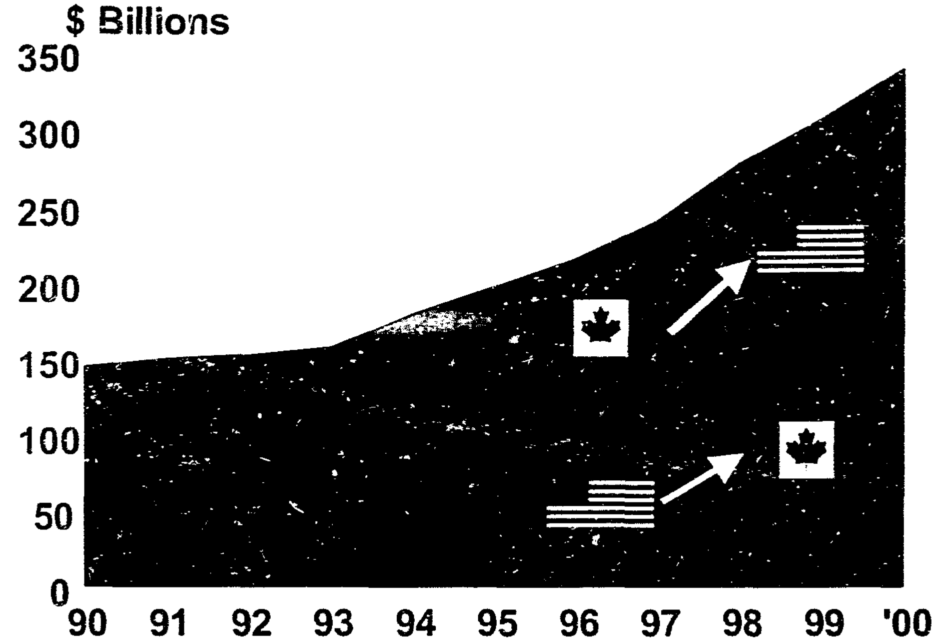
* Merchandise exports

Source: Industry Canada compilations based on Statistics Canada data

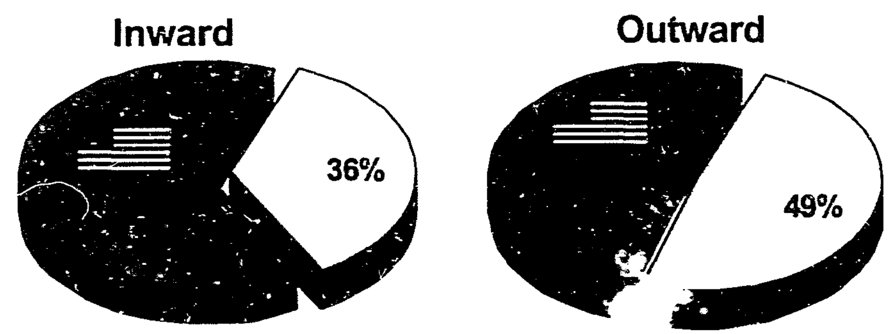
Investment linkages are also strong and growing

- Direct investment between Canada the U.S. totalled \$340 billion in 2000, up from \$144 billion in 1990 — an increase of 136%.
- The U.S. now accounts for 64% of FDI stock in Canada and 51% of Canadian investment abroad.

Canada - U.S. Foreign Direct Investment*



U.S. Share of Canadian FDI*, 2000

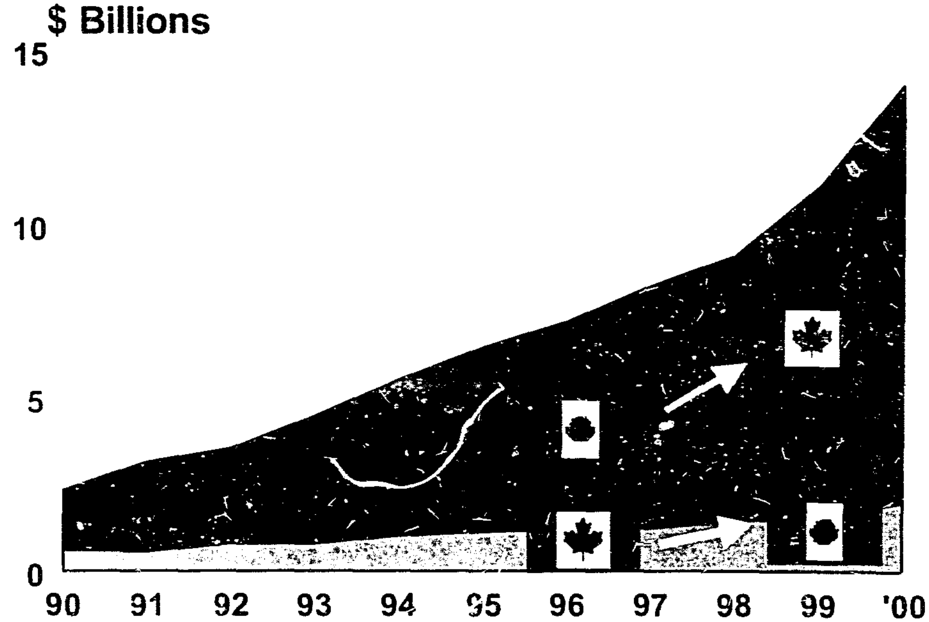


* Stocks
Source: Statistics Canada

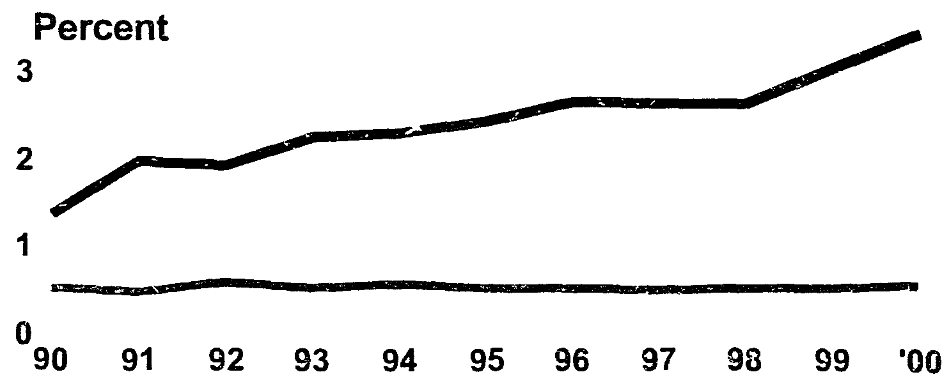
Canada's trade links with Mexico are small but increasing

- **Canada-Mexico trade reached $14 billion in 2000, a 500% increase over 1990 levels!**
- **Mexico now accounts for 3.4% of imports and 0.5% of exports.**
- **Mexico is also an important player in the U.S. market.**
  - **Mexico's share of U.S. imports has nearly doubled in the 1990s, while Canada's share has remained relatively unchanged.**

Canada-Mexico Trade*



Mexico Share of Canadian Trade*

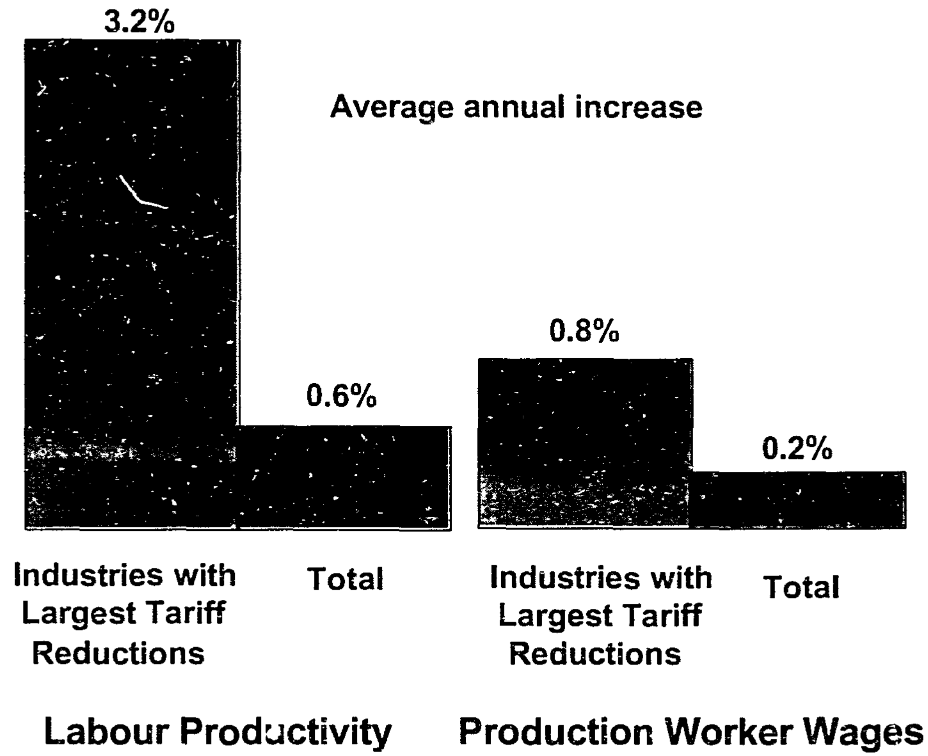


* Merchandise trade
Source: Industry Canada compilations based on Statistics Canada data.

ome more productive

- Freer trade stimulates productivity through a number of channels:
  - increased competition
  - transfer of new knowledge and technologies
  - scale and scope economies
  - increased specialization
- Industries that had the largest reductions in tariffs under FTA/NAFTA, such as furniture, clothing and textiles, have achieved the largest gains in productivity and wages.

Impact of FTA on Canadian Manufacturing

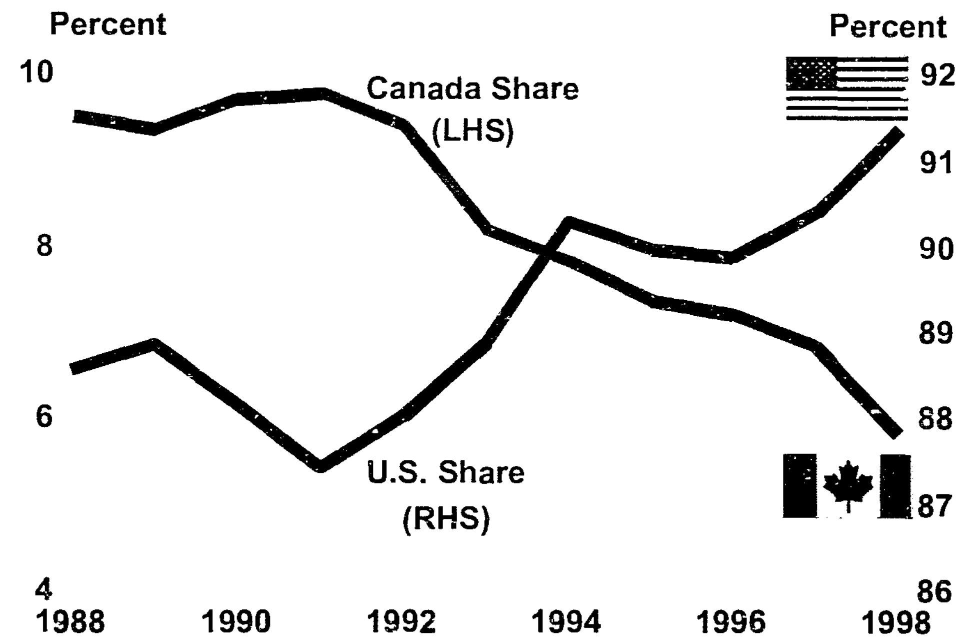


Source: "The Long and Short of the Canada-U.S. Free Trade Agreement" by Daniel Trefler

...has declined...

- **Canada's share of North American inbound FDI has dropped from 10% in 1991 to 6% in 1998.**
  - **Over the same period, the U.S. share has increased by about the same amount, increasing from 87% to 91%.**
- **In 2000, Canadian inward FDI stock increased by a record $45 billion.**
  - **The U.S. however, is likely to have experienced a similar, if not larger, increase.**

North American Inbound FDI



* Excludes intra North American FDI.

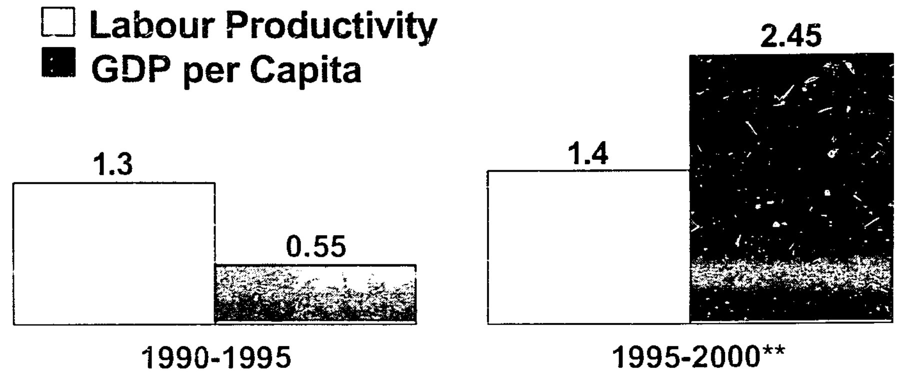
Source: Industry Canada compilations based on data from Statistics Canada, BEA, OECD and U.N, World Investment Report.

widened

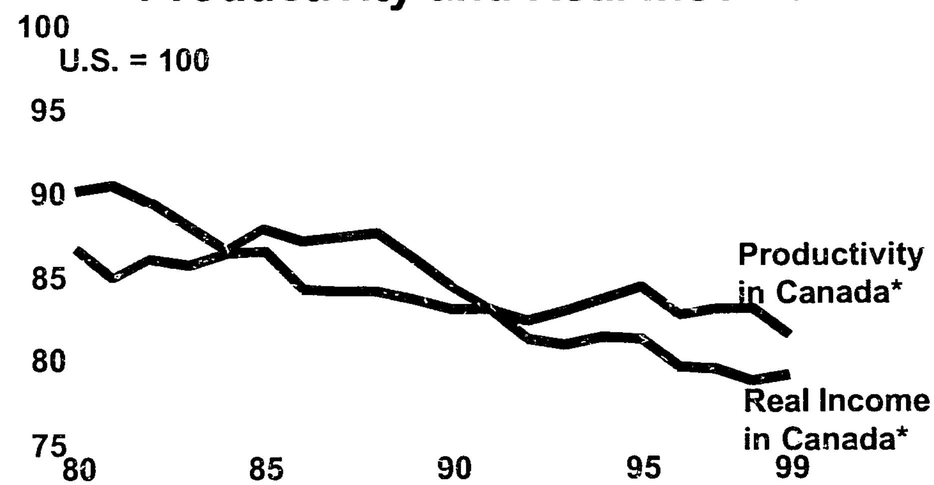
- Labour productivity and GDP per capita both grew at a faster pace in the second half of the 1990s.
- However, Canada's performance lagged behind the U.S., resulting in the widening of the productivity and real income gaps.
  - The productivity gap is responsible for about 85% of the real income gap between Canada and the U.S.

Growth in Labour Productivity and Real Income*

Percent per year



Trends in Canada-U.S. Productivity and Real Income



* Real GDP per hour for business sector and GDP per person, Canadian values converted to U.S. using 1996 PPPs

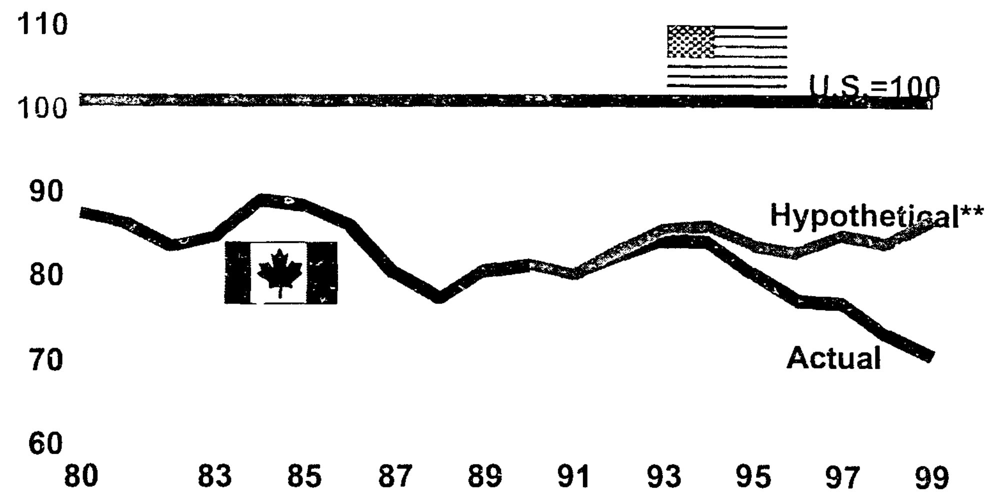
** First three quarters of 2000, population estimated using past population growth

Source: Statistics Canada and U.S. BEA

ivity gap

- If labour productivity of ICT manufacturing in Canada had grown at the U.S. rate in the 1990s, the productivity gap would have stayed roughly the same.
- The productivity challenge for Canada is not just about the "new economy". Why hasn't the gap narrowed?

Productivity Levels*: Manufacturing

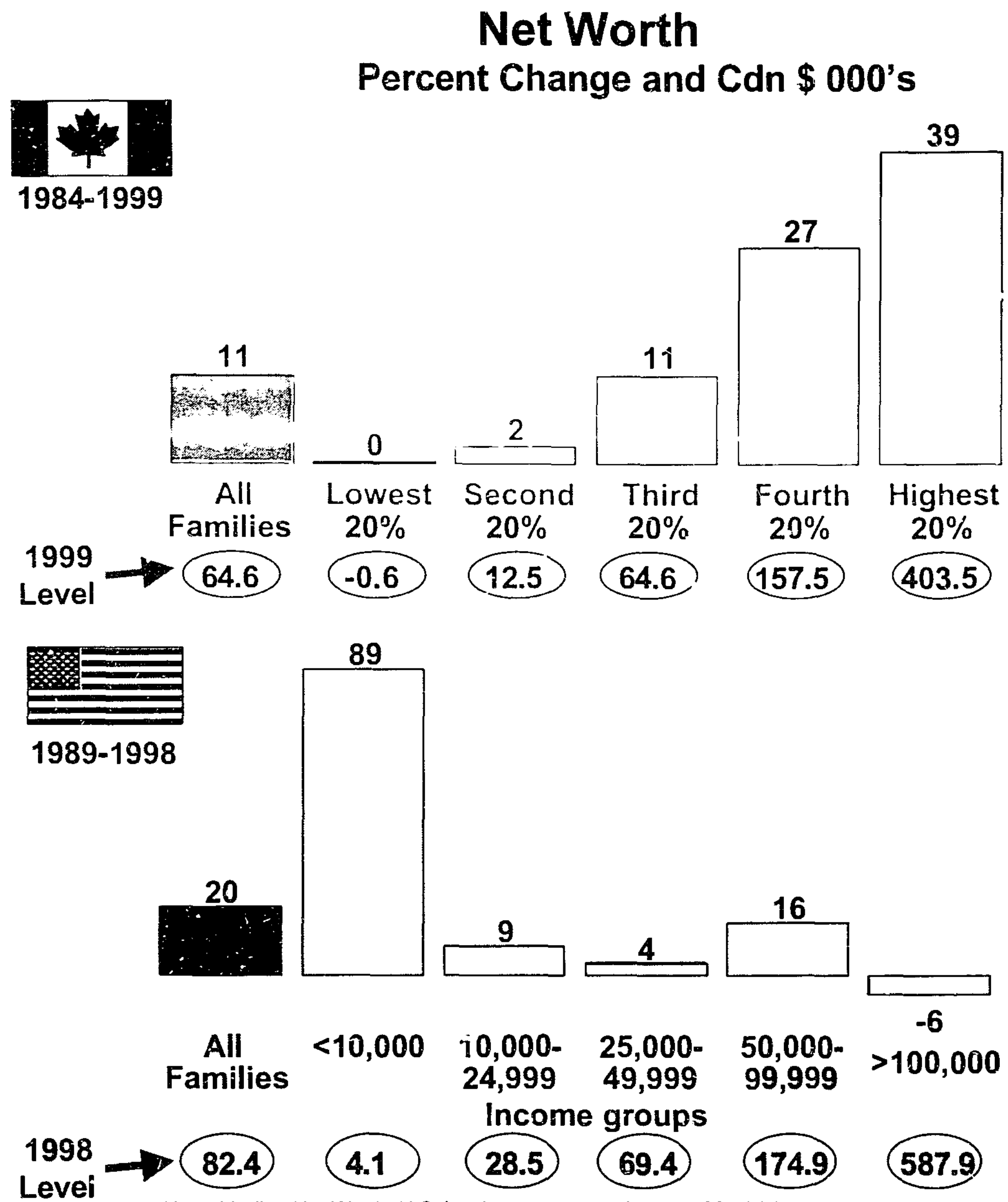


*GDP per hour
** Assume that labour productivity in Canada's ICT manufacturing (excluding instruments) grew at the same rate in the U.S. during the 1990-99 period.

Source: Statistics Canada, U.S. Bureau of Labour Statistics

...the poor in...

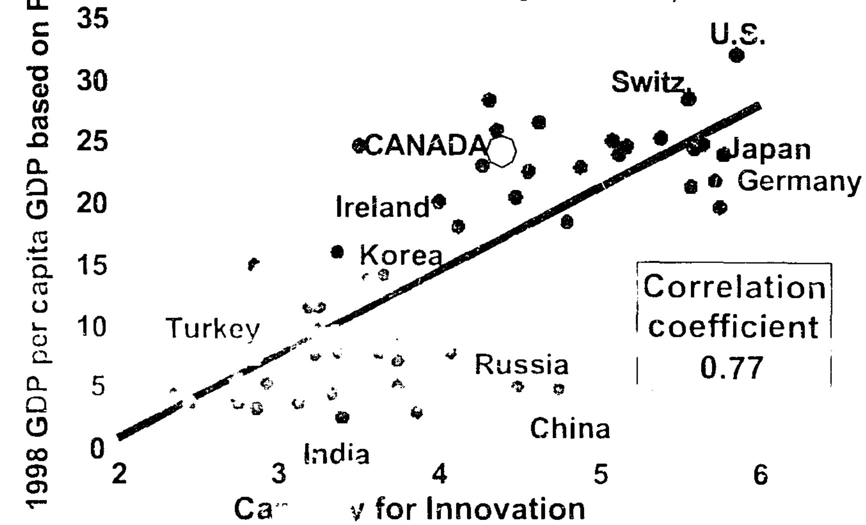
- **Median net worth of all families in the U.S. increased on average 20%, over the 1989-98 period, compared to only 11% in Canada during the 1984-99 period.**
    - **The poorest families in the U.S. have seen the largest growth in net worth. In Canada, the wealthiest families saw the greatest improvement.**



Note: Median Net Worth, U.S. levels are converted using 1999 PPPs
Source: Statistics Canada, 2001 and U.S. Federal Reserve Board, 2000

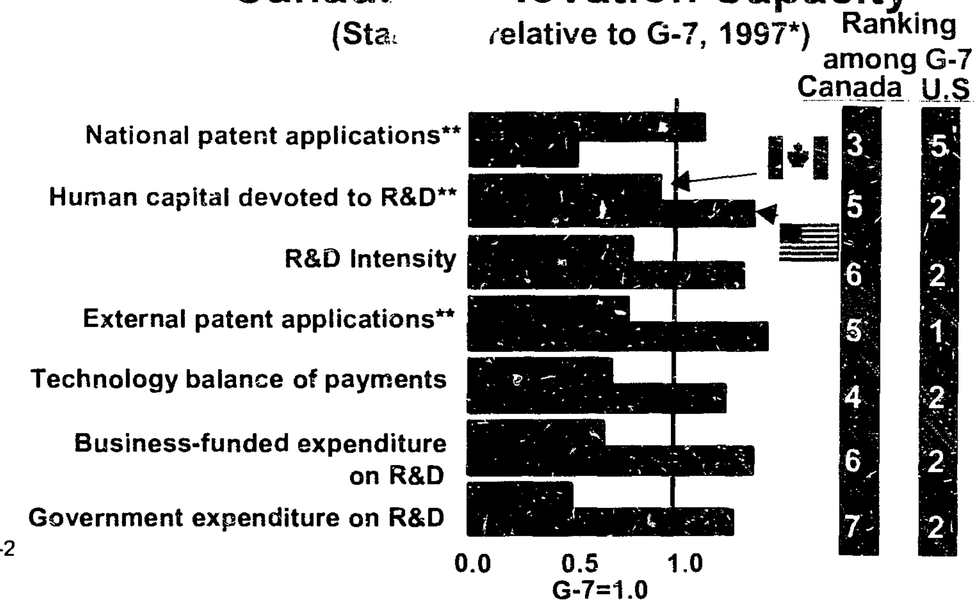
- **There still exists a significant innovation gap between Canada and our main competitor, the U.S.**
- Although innovation indicators have been improving faster in Canada than most other G-7 countries, our ranking remains near the bottom.
- **We need to become more innovative faster – our competitors are not standing still!**

Relationship between Capacity for Innovation and GDP per Capita



Canad... ...ovation Capacity

(Sta... ...relative to G-7, 1997*)



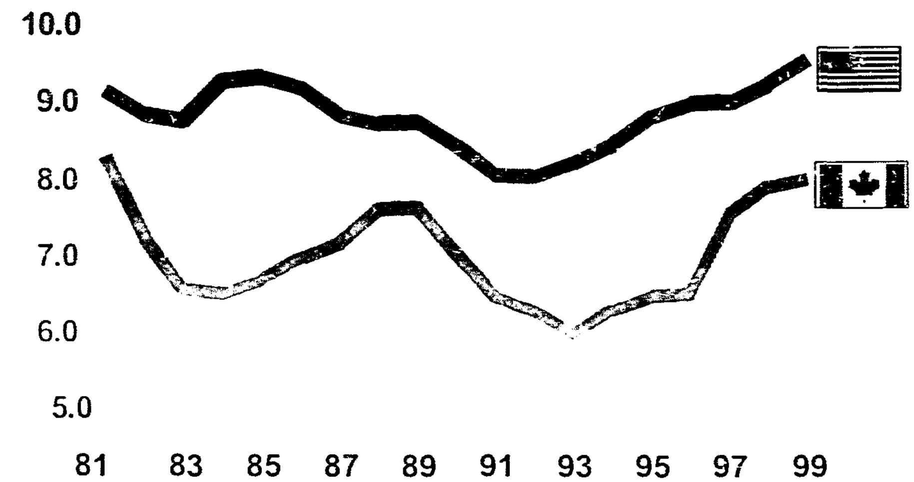
* Or latest year available
** Adjusted by labour force
Source: OECD, Main Science and Technology Indicators 1999-2

- **Investment in all forms of Machinery and Equipment is significantly lower in Canada than it is in the U.S.**

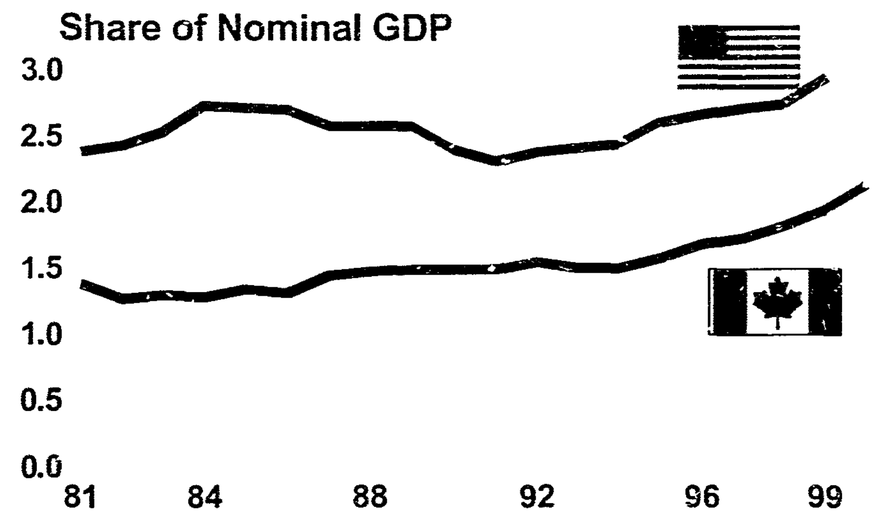
- ICT investment as a share of GDP in Canada was two thirds **that in the U.S. in 1999 (1.9% in Canada** v.s. **2.9% in the U.S.).**

    - **ICT investment in Canada accounted for 23.8% of total machinery and equipment investment in 1999 -- lower than the 30.3% share in the U.S.**

Investment in Machinery & Equipment



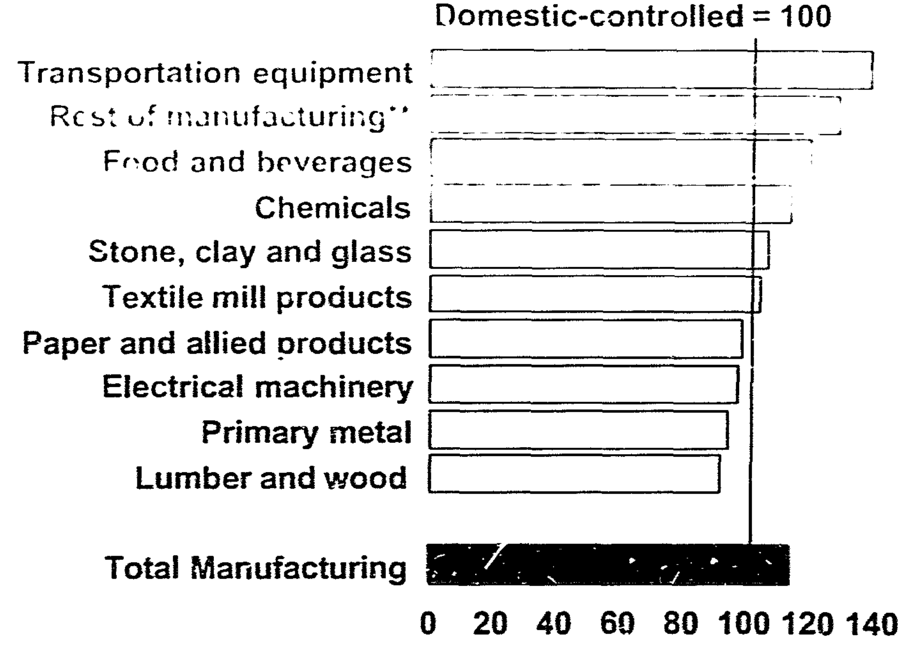
Investment ICTs



* Computer, office, and communication equipment
Source: Statistics Canada and U.S. Bureau of Economic Analysis

- **Foreign direct investment makes an important contribution to Canada's productivity performance.**
  - Foreign-controlled manufacturing firms are on average about 13% more productive than Canadian firms.

Productivity* of Foreign-controlled Firms – by sector, 1993-95

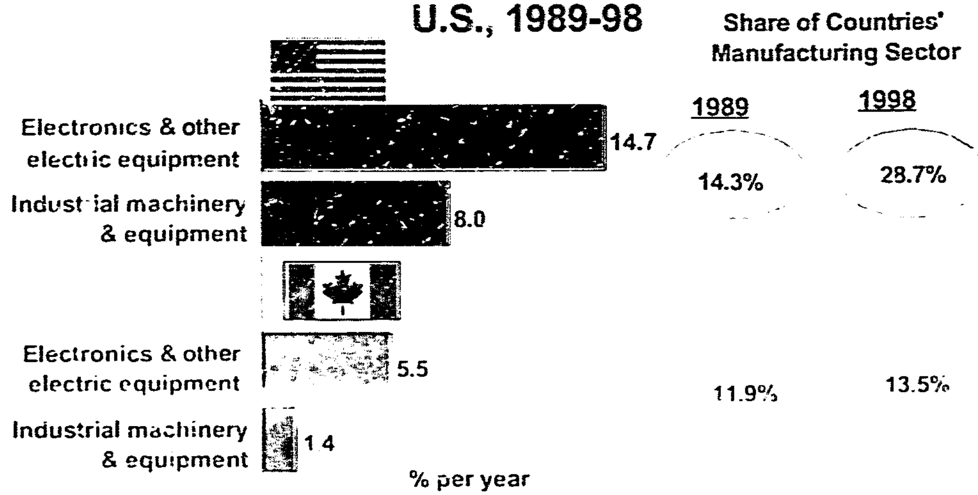


*Labour productivity
**Includes Tobacco; Furniture & fixtures; Printing & publishing; Leather industries; and Other manufacturing
Source: Tang, J. and P.S. Rao "Are Canadian-controlled Firms Falling Behind Foreign-controlled Firms in the Canadian Manufacturing Sector?", 1998

- **The U.S. economy appears to shift resources more quickly towards high growth, high productivity industries.**
- For example, U.S. productivity has been driven by two sectors (electronics & electric equipment, and industrial machinery). These two "gazelle sectors" outpaced their Canadian counterparts by a factor of three.
- **In Canada, the two industries with fastest productivity growth (rubber and refined petroleum & coal products) are mature, slow-growing industries.**

The U.S. Benchmark

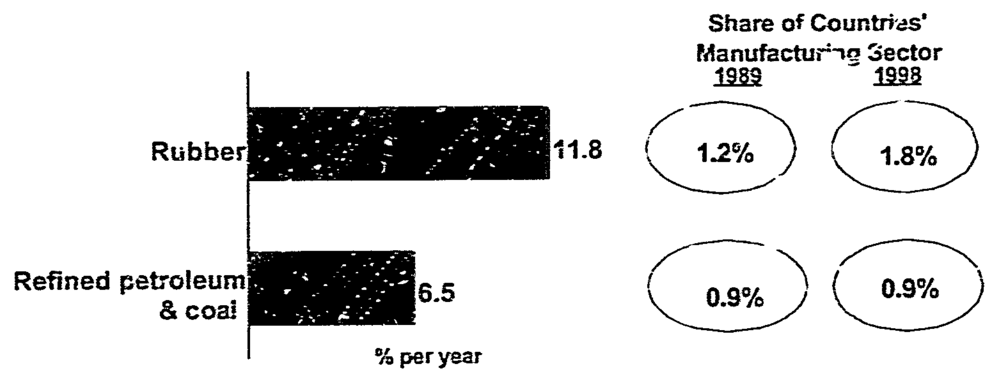
Two fastest productivity growth sectors in the U.S., 1989-98



Source: Centre for the Study of Living Standards, Statistics Canada and Bureau of Economic Analysis

The Canadian Benchmark

Two Fastest Productivity Growth Sectors in Canada, 1989-98



Source: Centre for the Study of Living Standards, Statistics Canada, and Bureau of Economic Analysis

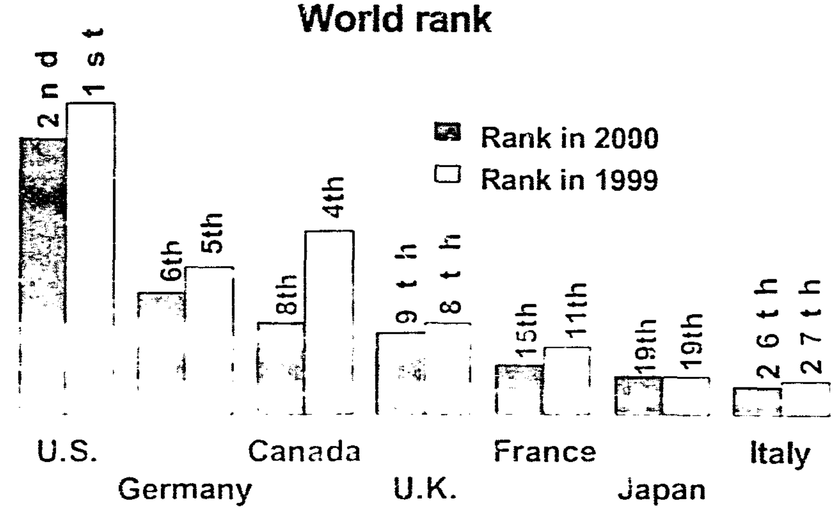
- **In 2000, Canada's business environment was ranked eighth in the world by the World Economic Forum (WEF), down from fourth position in 1999. Among G-7 countries, Canada ranked third after the U.S. and Germany in 2000.**

- **The WEF ranks Canadian companies considerably lower in taking advantage of this business environment in their corporate strategies.**

> **"Rather than pursue competitive advantage through unique products and processes, Canadian firms, to too great an extent, pursue advantage through cheap raw materials or low-cost labour."**
>
> **Roger Martin, Dean**
> **Rotman School of Management**
> **University of Toronto**
> **September 1999**

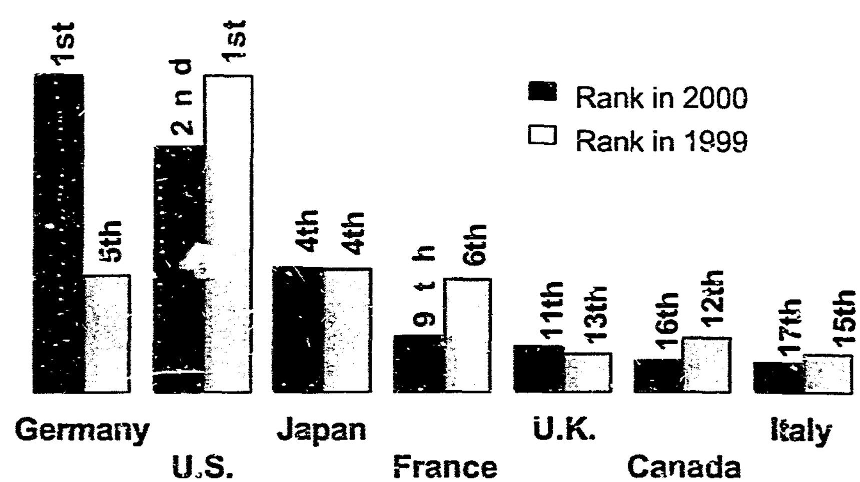
Microeconomic Business Environment

World rank



Company Operations and Strategy

World rank



Source: Global Competitiveness Report 2000, World Economic Forum

- The gap in Canada-U.S. living standards is large and widening.
- Productivity explains 85% of the income gap.
- The challenge to close the productivity gap is daunting and requires:
  - closing the innovation gap;
  - closing the investment gap;
  - attracting & retaining FDI;
  - ensuring a flexible and dynamic industrial structure, and
  - develop corporate strategies geared towards improving productivity.
- The ultimate benefit of higher productivity is higher standard of living and broader range of private and social choices.