

WORKING PAPER

EVALUATION
OF THE
INDUSTRIAL INCENTIVE GRANTS PROGRAM

PREPARED BY
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"THE VIEWS EXPRESSED
IN THIS REPORT
ARE NOT NECESSARILY
THOSE OF DREE"

"LES OPINIONS EXPRIMEES
DANS CE RAPPORT
NE SONT PAS NECESSAIREMENT
CELLES DU MERN"

Preface

This paper sets out an effectiveness evaluation of the industrial incentives program carried out by the Program Evaluation Branch (Finance and Evaluation Division). The evaluation is based on a number of separate studies carried out over the last six months.

The paper is divided into two sections: one an overall assessment covering a summarized version of the major questions pursued and the findings; and the second section, Evaluation Report, which sets out in more detail the scope and conclusions of the evaluation. It should also be noted it has not been possible to incorporate into this document all the detailed supporting studies which are of course available for individual review as necessary.

January, 1973

Section I

Over-all Assessment

The central question that has been pursued in our investigation is the ability of incentive grants to shift investment from non-designated regions to designated regions by offsetting differential rates of return among regions as a result of different operating and selling costs. That is not to deny the arguments advanced for speeding up investments in time, increasing scale, increasing viability, etc. However, the incentives program cannot rely on these effects for long: ultimately, for regional disparities to be alleviated, investment must be shifted in a geographic sense by overcoming locational cost differentials.

It has been embodied in the goals of the department that supported investment should be deployed to the maximum extent possible in a growth centre context. In that event, the benefits of agglomeration in conjunction with programs of infrastructure and social adjustment will be captured. In the context of the growth centre philosophy then, we have looked for relatively large amounts of activity (larger at least than their current share of manufacturing employment) in the industrial growth centres and some relationship between incentives activity and infrastructure activity.

In addition to the questions that flow directly from the central theme of shifting investment geographically in a growth centre context, several subsidiary lines of investigation have been pursued in this paper:

- has the effective impact of a grant varied appropriately from area to area according to different needs?
- is the grant rate structure embodied in the legislation biased against certain industries or regions?
- has support gone to operations with a natural preference for non-designated regions versus industries that probably would have located in the designated regions regardless?
- how successful have incentive grants been in attracting high growth - high technology - high skill industries?
- are incentives grants contributing to "turning over" regions by supporting industries that do not merely replicate the existing industrial base?
- what proportion of all eligible investment and job-creation in designated regions is the incentives program supporting?
- is the tax treatment and method of payment of grants conducive to attracting and keeping firms in designated regions?

As noted, the central question considered is the ability of incentive grants to shift investment from non-designated regions to designated regions by offsetting differential rates of return among regions as a result of different operating and selling costs. In the context of what the legislation can do (as distinct from what we did under the legislation), we examined the potential impact of an incentives grant as a continuing subsidy to compensate for higher costs in designated regions. The average maximum impact of the grant is roughly four cents on a dollar of sales (after the fact that much of the grant returns to the federal treasury through income taxes is considered). This would be effective in inducing locational shifts only in a minority of instances and most likely in regions close to the Canadian industrial heartland where development need is least.

An analysis of the grant rate structure provided for in the legislation reveals a basic anomaly. The grant system is more capable at the maximum rates in terms of cost-offsetting ability for capital-intensive projects than for labour-intensive projects. This is inconsistent with what we interpret as priorities in the department's goal structure: quantity of jobs over quality of jobs, and recognition that the greatest development need is in the Atlantic provinces. This anomaly underlies the ineffectiveness of the special development incentives program in the Atlantic so far: capital-based constraints in the grant rate structure (specifically, one-half of capital employed) in the Atlantic where labour-intensive activities predominate made the raising of the employment related grant ceiling of very little significance.

Over and above the question of the magnitude of the grant is the question of the method of payment provided for in the legislation. The current system involves some of the worst of both worlds. On one hand, the grant is received by the firm after it has the greatest need for it, i.e., during the construction phase. In this circumstance the firm usually requires some sort of interim financing that cancels out part of the grant benefit if a risk rate of interest is demanded by the banks. On the other hand, the current system of paying the full grant over a relatively short period of time may reduce the incentive for companies to remain in the designated region over the longer term. The grant can offset cost disadvantages but it does not remove them: a firm which would face a continuing operating loss situation after a grant is received may terminate operations so that the incentive has induced only short-run benefits.

Much of the above discussion would be discounted in the event of an effectively implemented growth centre approach. In the last situation, for example, the firm would not terminate operations if the benefits of agglomeration made the designated location as profitable as a non-designated location after some point in time. It would be expecting much of companies supported so far to have gambled on our success in this sense. Moreover, we have not found evidence of a conscious effort in a growth centre context. The infrastructure and incentives programs have been implemented without any direct relationship to each other. Moreover, within the incentives program, no systematic pattern of diversion of investment to the growth centres is evident (e.g. through more generous use of discretion available.) As a result,

the growth centres have not received a larger share of activity than one would expect simply on the basis of their pre-existing share of the designated regions manufacturing employment.

In a broader regional context, an examination was made of the grant rate from province to province. The grant rate can be expressed in many ways of course. If the grant is expressed as a proportion of capital costs, the Atlantic provinces appear to be favoured. But projects there are relatively more labour-intensive so that the grant expressed on a per job basis is less favourable. On the other hand, the more relevant measure in a locational shift sense is the grant's ability to compensate for cost differences. In these terms, the grants from province to province revealed a certain sameness which is inconsistent with differing needs in terms of isolation from central markets.

The evaluator is still left with a formidable amount of program activity to explain after all of the preceding limitations are considered. Studies by the Program Evaluation Branch suggest that the preponderance of grants represent activity that would have taken place anyway since most grants have gone to activities that already have a strong preference for the designated region because of factors such as local market orientation or dependence on the availability of a key resource. In the Atlantic provinces particularly, grant activity is concentrated in those sectors that were already dominant in the industrial base. Moreover, a broad success has not been obtained in attracting high skill and growth industries (although there are some important individual exceptions.) It was also found that most of the eligible investment spending in the designated regions is supported by an incentive grant.

On the basis of all the evidence available, we conclude that incrementality under the program in a locational sense cannot exceed the range of 25-33%. If this level of incrementality were maintained with the current rate of annual job support under the program, about three-quarters of activity that would have occurred without the program would be supported. ?

At the present time, we are at an annual rate of job support in the designated regions of about 18,000 (excluding Region C).¹ This may decrease in the short-run until an extension of the program is announced but our judgement is that it would rise again unless we become more efficient: i.e., support a lower proportion of activity that would have occurred in the natural course of events without grants. An 18,000 job support rate per year with the upper range of incrementality - namely 33% - would, however, still imply a significant degree of target achievement despite the high degree of inefficiency. These parameters would suggest that one-half of the targets in the RDIA Targets Task Force would be achieved. Hopefully, over time, changes in the legislation and in administration of the legislation can be made that allow achieving a higher degree of incrementality and efficiency which should result in fuller target achievement at perhaps a significantly lower level of program activity per year.

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It should be noted that the actual current rate of job support may be different than the published figures that go to Parliament. On the basis of evidence regarding the ADIA program, intentions and achievements were close, but the evidence on the RDIA program so far is inconclusive.

Section II

Evaluation Report

Introduction

The Program Evaluation Branch presented an evaluation strategy for the incentives program in mid 1972. The strategy emphasized that evaluation should be undertaken from several angles as there is no single indicator that determines program effectiveness. Over the last six months, several of the studies indicated in the strategy document have been carried out and there now exists some considerable basis for synthesizing these efforts and making a broad evaluative statement.

The primary concern has been with effectiveness as distinct from efficiency. The two of course are not separable. However, the main objective of the work to date has been to measure program impact, while the question of the cost of this impact has received little attention. The latter would involve examining some administrative aspects of incentives activity that we do not see as being central to our mandate.

To say that evaluation efforts have been focused on determining impact does in itself not go far enough to capture the essence of effectiveness evaluation: the measured impact must be related to a goal structure. As is well known, this department has not as yet been specific in articulating a goal structure. In the evaluation strategy a more specific goal structure was outlined which attempted to make the oft-stated general goals regarding unemployment, participation in the labour force and average income levels more operational from an evaluation point of view. This goal structure was largely qualitative and indicated directions rather than distances. Since the preparation of the evaluation strategy, a considerable amount of work has gone into quantitative targets - in terms of job creation particularly - under the RDIA Targets Task Force chaired by the Director of Program Evaluation. The Task Force has not yet submitted its final report but preliminary results are used in this paper.

This report then begins with a statement on RDIA targets. The subsequent sections discuss several evaluative aspects of the program: the impact of RDIA in overcoming cost differentials among regions; the impact of the program on broad macro-indicators; locational options and incrementality; quantity versus quality of jobs supported; the impact of incentives on the existing industrial structure of regions; incentives in the context of growth centres; the adequacy of the legislation in terms of maxima, method and timing of payments, tax treatment of grants; and discretion.

1. The Goals of the Incentives Program

(a) The Qualitative Goals

The publicly stated goals of the department are deceptively simple: to reduce unemployment rates, increase participation rates and raise average income levels in designated regions relative to nondesignated regions. That tripartite statement does not leave the evaluator much to go on. In essence however, these general goals are apparently to be achieved by increasing job opportunities.

The goals regarding per capita income, unemployment rates and participation rates might have been achieved in the natural course of events without new policy. However, the long-run evidence is that any progress along these lines would have been of small magnitude and not likely to materialize in a reasonable period of time. The rationale for the formation of DREE was the acceleration of this process by the creation of new job opportunities. The realization of this basic strategy lay in a number of interrelated programs, among which the provision of incentive grants for industrial development was most important.

Incentive grants are provided in regions and special areas designated for that purpose under the Regional Development Incentives Act and the Department of Regional Economic Expansion Act. These grants are available generally for secondary manufacturing industries, i.e., manufacturing industries other than initial processing, because these industries not only produce job opportunities themselves but as well induce job creation in other sectors of economic activity such as the service sector. The basic purpose of the grants is to shift investment in either a geographic sense or in a timing sense. In other words, the grant is to induce investment in a designated region or special area which would not have taken place there at all or not at that time. Both types of shifts are in keeping with the legislation, but it seems clear that in the long-run, location shifts will be more significant in achieving the development goals of the department. Consequently, while a broad range of manufacturing industries are eligible for incentive grants, the implementation of the legislation is based upon the use of discretion which allows offers of grants to be made to induce investments which would not have taken place without the grant.

In order to induce locational shifts, the grant must overcome differences in operating costs between designated and non-designated regions, or between different locations within the designated regions. Again, it is clear that the prime need is for shifting the location of investment from non-designated regions, although intra-designated region shifts can be appropriate if the additional job creation and investment

were to be concentrated in industrial growth poles. The net effect of these results should be an acceleration of increases in manufacturing investment in the designated regions - and particularly the growth centres - at a rate faster than the national rate, leading to an increase in the share of national investment accruing to these regions.

The job creation objective of the incentive grants program is basically three-headed: to create more jobs, to create "better" jobs and to save existing jobs. That is the reason for the provision of grants to expansions and modernizations of existing facilities as well as to new plants. Volume expansions and modernizations save and improve existing jobs by making existing operations more competitive through scale economies or improved techniques of production, thus providing a hedge against bankruptcies and phase-outs. The objective of creating more job opportunities is particularly served by the provision of incentive grants to new plants and new product expansions.

The job opportunities of real interest are the additional and continuing ones: those relating to incremental investment projects. Most obviously, such jobs will not be created if we support projects that merely displace workers employed elsewhere in the designated regions. This possibility will be less likely if projects are supported that have a heavy export orientation or that displace imports. The job creation objective will also be more apt to be achieved if incentive grants are provided to projects with growth potential and/or labour intensive in their operations. The "better jobs" target will be reinforced through support of high skill and high technology industries. ?

It was never believed that the direct impact of incentives supported projects would in itself be sufficient to solve the regional disparities problem. Rather, this over-all result was dependent on the manner in which the activities of the assisted projects were transmitted to other manufacturing industries and to other sectors of the regional economies: i.e., to the construction industry, to suppliers of raw materials and intermediate manufacturers and to the tertiary sectors (government, insurance, personal services, etc.). This transmittal process must take place in sufficient magnitude and in the appropriate direction so that the broad objective of reducing regional disparities can be achieved.

(b) The Quantitative Goals

The preceding section provided a description of program effectiveness in terms of direction. But this qualitative expression of development needs does not say how large the task is, and how much regions vary in development need. Also it says nothing about how many new additional continuing jobs are likely necessary to meet these broad regional development needs. Such a quantification will be attempted in this section.

(i) Overall Departmental Target:

The degree of disparity among regions in terms of participation rates, unemployment rates and income levels has been well documented and it is not our intention here to undertake an exhaustive statistical analysis. Rather, in the following table one can see how much earned income a "have-not" province in 1971 falls short of the level that would have prevailed had the participation rate, unemployment rate and earned income per worker in that province been the same as for the country as a whole.

TABLE 1

Earned Income Short-Fall in 1971
by Province

	<u>"Target"</u> <u>Earned Income</u> (\$000)	<u>Actual</u> <u>Earned Income</u> (\$000)	^{gap} <u>Short-Fall</u> (\$000)	<u>Short-Fall</u> <u>as % of Actual</u>
Newfoundland	1,362,592	845,691	516,901	61.1
Prince Edward Is.	294,196	180,992	113,204	62.5
Nova Scotia	2,070,985	1,631,350	439,635	26.9
New Brunswick	1,710,982	1,231,265	479,717	39.0
Quebec	16,885,302	14,621,568	2,263,734	15.5
Manitoba	2,667,119	2,565,466	101,653	4.0
Saskatchewan	2,523,892	2,041,254	482,638	23.6

It is evident that the difference between "what is" and "what ought to be" is greatest for Newfoundland and Prince Edward Island. These two provinces would need an earned income level almost two-thirds above their actual level in 1971 to give them Canadian standards in terms of participation rate, unemployment rate and earned income per worker. New Brunswick, Nova Scotia and Saskatchewan display a development gap of from two-fifths to a quarter. While Quebec's income gap is relatively small in absolute terms it accounts for more than half of the total need for all the provinces analyzed.

(ii) R.D.I.A. Targets

The broad target then is to alleviate these disparities in some time frame. However, while it may be appropriate to express broad departmental targets in terms of income, it is more appropriate in the context of the incentives program to express targets in terms of new continuing jobs, for such jobs are the medium through which broad targets are to be achieved in conjunction with adjustment and infrastructure programs. The department has not, as yet, developed a set of regional or provincial job creation targets for the incentives program related to broad development needs. It has however established a Task Force¹ for this purpose.

¹This Task Force was set up under the chairmanship of the director of the Program Evaluation Branch and submitted a preliminary report on October 13, 1972.

The data in Table 2 indicate targets for RDIA supported jobs with various assumptions concerning efficiency rates.¹ It is indicated that the need for net new continuing jobs under RDIA in the "have not" provinces (excluding Region C) is about 8,200 annually to 1991.² Somewhat more than this will require incentives assistance because some supported jobs will be "lost" through bankruptcies, capital substitution, etc. This requirement boosts the target level to slightly over 11,000 annually. It should be borne in mind that these are annual averages over the entire target period. The suggestion is not being made that of 11,000 jobs supported in an individual year, almost 3,000 will be lost during that year. A job depletion rate of 4% was used: in the early years, relatively few jobs will be lost, but as the stock of RDIA supported jobs builds up over time, a job depletion rate of 4% per year means a large amount will be lost in the later years. The 11,000 annual average support figure assumes that no jobs will be supported that would occur anyway in the regular historical process of job creation. If efficiency were 50%, i.e., half of the historical job creation was supported, then the required job support level, while still meeting targets for new incremental activity, would be 19,000 per year. If there was complete inefficiency as defined in Table 2, i.e., all historical job creation was supported, the implied rate of RDIA job support is 27,000 per year.

These targets naturally invite comparison with activity to date under the program. This type of exercise is fraught with dangers in that incentives activity so far has involved a break-in period for the program and projections over a long-run period are tenuous. If the 1971-72 average rate of activity of about 17,400 jobs³ is assumed to be sustained over the long-run, a variety of incrementality - efficiency - effectiveness combinations can be postulated. If all jobs supported were incremental,

¹The complete technical methodology underlying these targets will not be discussed here, but some of the assumptions underlying them cannot go unstated. Firstly, the Task Force assumed that the incentives program and other departmental programs will influence the provincial distribution of population and employment but not the total national levels. It is assumed then that the development job will be accomplished by a switching process within Canada between the "have" and the "have not" provinces. Secondly, the Task Force postulated its targets on the assumption that Canada will successfully implement a national industrial strategy directed towards manufacturing which will terminate the secular decline in manufacturing's share of the total employed labour force. A third assumption underlying the estimates in Table 2 is a "death rate" for jobs of 4% annually through bankruptcies, other terminations, the substitution of capital for labour, etc. Any net gain in the job level is the result of gross job creation through new activities and expansion of old activities more than compensating for these job losses.

²In order to put this figure in some perspective, it is interesting to note that in the 1961-70 period, the average annual net increase in manufacturing employment in these regions was only about 4,300.

³It should be noted that these jobs are estimated as at the time of offer. There is no good basis yet for making a judgement on the reliability of these estimates. Under the ADIA program, realizations and expectations were close, although with an employment-related grant system such as RDIA, there may be a basis for expecting some underachievement.

TABLE 2

RDIA Job Support Targets under Various Efficiency^{a)} Assumptions
Yearly Average, 1972-91

	Net Job Support Requirement	Gross Job Support Requirement with Efficiency Assumptions of				
		100%	75%	50%	25%	0%
Newfoundland	725	1,001	1,177	1,352	1,528	1,704
P.E.I.	115	160	194	229	263	297
Nova Scotia	970	1,334	1,803	2,273	2,742	3,211
New Brunswick	745	1,024	1,432	1,840	2,248	2,657
Atlantic Quebec ^{b)}	2,555 4,105	3,519 5,446	4,606 7,433	5,694 9,421	6,781 11,408	7,869 13,396
Manitoba	810	1,102	1,868	2,634	3,400	4,166
Saskatchewan	725	1,025	1,204	1,383	1,562	1,741
Total	8,195	11,092	15,111	19,132	23,151	27,172

a) efficiency is defined as the proportion of gross historical job creation (that would have materialized anyway) that is not covered by RDIA

b) excluding Region C

we would be creating jobs at a rate of 1 1/2 times the target rate indicated by the Task Force report. At the other extreme, if no jobs supported were incremental, the activity of the program would represent virtual complete coverage of the historical job creation that would have been occurring anyway. If one-half of jobs supported were incremental, about 45% of historical job creation that would have occurred anyway would be covered, but this would still mean that about three-quarters of targets are being achieved. These observations are quite hypothetical, but what is firmly illustrated is that a high level of support such as prevailed over 1971 and 1972 can mean both a high degree of effectiveness in terms of target achievement and a high degree of inefficiency: i.e., a large proportion of grants merely subsidizing the activity that would have occurred anyway rather than inducing new activity.

In addition to the problems of projecting program activity, the sensitivity of the target exercise to different assumptions about the job depletion rate should be understood. The RDIA Targets Task Force has worked with a 2% rate and a 4% rate.¹ The 4% rate has been judged the more realistic for the purposes of this document. However, it may be noted that the targets indicated in Table 2 are a fifth to a third higher (depending on the province) than they would be under a 2% assumption.

¹ See Appendix B to the Task Force Interim Report: "The Effects of Varying the Job Depletion Rates and Efficiency Levels."

2. The Impact-Effectiveness of an Incentives Grant

In order for a grant to be effective in inducing an investment to shift its location from a non-designated to a designated region, it must be sufficient to compensate over the long-run for higher operating and selling costs that affect its return on investment adversely. Indeed, that will merely equate opportunity among regions and a higher grant rate would be required to guarantee a shift in location. Further the grant may have to more than compensate for incentives available outside DREE in non-designated regions. The important question then is how great these cost differentials are, and to what extent the existing incentive grants can compensate for these differentials.

(a) The Need: Cost Differentials among Regions

The first systematic work along these lines, of which we are aware, was undertaken by Wonnacott and Wonnacott ("Free Trade Between the United States and Canada: The Potential Economic Effects", Harvard University Press, 1967.) They estimated the percentage that total costs (labour, transportation, resource and capital) in selected areas are lower or higher than in Ontario. The results for the Maritimes, Quebec and the Prairies are presented in Table 3. The Quebec figures would be dominated by the Montreal area and should not be interpreted as typical of the original designated regions in that province. In the other areas, cost differentials are often substantial and almost uniformly so from industry to industry in the Maritimes.

TABLE 3

Estimated Cost Differentials in 1958 - Manufacturing Industries -
Ontario Versus Maritimes, Quebec and Prairies

<u>Industry Group</u>	<u>Percentage that Total Costs are Lower (-) or Higher (+) than in Ontario</u>		
	<u>Maritimes</u>	<u>Quebec</u>	<u>Prairies</u>
Food	5.77	0.12	6.44
Tobacco	9.99	-0.14	1.55
Textiles	4.27	-0.36	7.14
Apparel	6.85	-1.16	-0.31
Wood Products	20.18	-2.45	23.45
Paper	12.88	-0.05	10.27
Printing	-2.62	0.77	-1.24
Electrical Equipment	0.45	-0.94	-0.12
Chemicals	9.46	-0.39	7.37
Petroleum Pr.	52.49	1.16	37.97
Rubber & Plastics	-0.04	-4.15	-1.09
Leather goods	5.27	-3.15	6.98
Non-Metallic Mineral pr.	58.25	2.58	42.21
Metallic products	15.91	-1.45	11.14
Transportation Equip.	1.65	-1.61	1.40
Miscellaneous	-1.33	-2.46	0.84

More recent work has been undertaken by Professor Roy George in terms of a comparison between Nova Scotia and the Quebec-Ontario industrial heartland ("A Leader and a Laggard", University of Toronto Press, 1970). His broad conclusion was that higher costs in Nova Scotia were equivalent to about 5 cents on a dollar of sales.¹ Our own work² is consistent with this conclusion. In addition, our work suggests that Nova Scotia is by no means in the worst position: cost differentials in the more peripheral regions - particularly in Newfoundland - are in the range of 10-15 cents on the dollar on average. There is a band effect then: cost differentials in relation to an Ontario location are highest in Newfoundland and fall as you move west into the industrial heartland and then rise again in the Prairies.

(b) The Instrument: The Cost-Offsetting Impact of a Grant

It is evident that most industry groups experience higher costs of production in the peripheral regions than in the industrial heartland. This should not be interpreted to mean that all industries with higher operating costs in the designated regions should be the recipient of a "cost-offsetting" incentive grant. Generally speaking, grants should be considered primarily for projects which have a realistic option to locate outside the designated regions, and which cannot pass the higher locational costs on to the consumer.

In this section the discussion will centre on how much the incentive grant can offset higher costs of production for an investment in a designated region where it would not have located without the grant. It is important to note that the grant does not "ipso facto" reduce operating costs of the supported project. A grant is nothing more than an injection of outside money into the cash flow of the firm. The intention of the department is to see this grant used as a fund to offset higher operating costs on a continuing basis. However, there is no assurance that the firm in question will use it for that purpose. Similarly there is no assurance, let alone an obligation, that the firm will incorporate the grant in the operational cost structure of the supported project to reflect the cost-reducing and profit-enhancing impact. In fact beyond the control period there is nothing that ties the grant to the continued operation of the supported project. This discussion assumes that there is indeed a cost-offsetting impact and will attempt to measure its size. The following table indicates what the cost offsetting impact of a maximum combined grant under RDIA would be on the average Canadian corporation by industry group (based on average 1965-1969 financial data).³

¹It should be noted that Professor George attributed the entire differential to inferior entrepreneurial skill. He concluded that there was a considerable wage advantage in Nova Scotia in that wages were lower than in Quebec - Ontario but workers were equally efficient. If managerial skills could be shifted to Nova Scotia as well as capital, the cost differential would disappear. The question still remains though - why hasn't Nova Scotia been able to attract and retain managers. Presumably non-monetary factors would discount the equal monetary returns that George's analysis implies.

²Program Evaluation Study: The Impact-Effectiveness of Grants under RDIA and Special Areas Legislation, October 19, 1972.

³These are preliminary results of a study undertaken by Professor Carlton Dudley of the Centre for Regional Studies at the University of Ottawa with the financial assistance of this Department. Note that this refers to a maximum combined grant for regular development incentives only.

On average therefore the maximum combined grant could reduce operating costs by 4 percent. It should be noted too that the impact would be smaller for primary grants: it was estimated that for all manufacturing the maximum primary regular development incentive (excluding a special development incentive) would have an impact of only 1 1/2 cents on a dollar of sales.

It is clear therefore that even at a maximum level the combined regular development incentive is over the long run not able to offset the additional operating expenses of a location in a designated region.¹

TABLE 4

Cost Offsetting Impact of Maximum Combined RDIA Grant
by Industry Group
(Based on 1965-69 Average Canadian financial data)
(cents on a dollar of sales)

<u>Industry</u>	<u>Grant Impact</u>	<u>Industry</u>	<u>Grant Impact</u>
Food	1.98	Printing & Allied Industries	4.94
Beverages	7.23	Primary Metals	7.47
Tobacco	1.53	Metal Fabricating	3.70
Rubber	2.86	Machinery	2.67
Leather	1.29	Transport Equipment	2.84
Textile Mills	2.77	Electrical Equipment	2.87
Knitting Mills	0.68	Non-Metallic mineral	
Clothing	1.05	products	4.22
Wood	2.18	Petroleum & Coal Products	2.25
Furniture	1.73	Chemicals	3.67
Paper & Allied		Miscellaneous	4.02
Industries	4.48	All Manufacturing	3.88

¹Several objections to the preceding approach might be lodged. Firstly, it can be claimed that grants are not only intended to cover locational cost differentials, but to speed up investment, increase scale, improve viability, etc. That is acknowledged, but the department's public stand is that the main goal of the incentives program (except possibly in Montreal) is to shift investment in a locational sense. In our view, that is the only way regional disparities can be overcome so that the incentives program must be evaluated in that context. Secondly, it can be claimed that an RDIA grant alone doesn't have to overcome the entire cost differential (the Michelin case of course comes to mind). The analysis presented would accommodate this view if two conditions were met: the impact of additional forms of assistance was about twice the impact of the development incentive grant, and the availability of other forms of assistance was inversely related to the fiscal strength of provinces. Only infrequently will both these conditions hold. Thirdly, it might be claimed that regional differentiation is now operative in our grant rate structure - particularly with the availability of special development incentives in the Atlantic provinces. That view will be discussed in a later section. Finally, and most fundamentally, it may be claimed that firms supported with an incentive grant will not have to be subsidized at current cost differentials over the long-run because the benefits of infrastructure and "agglomeration" will reduce and perhaps remove cost differentials before many years. We will discuss this question in a separate section except to say here that it would be asking much of companies supported so far to gamble in this fashion on DREE success.

This is particularly evident for the Atlantic Region and the Prairies, and is probably applicable also to Eastern Quebec. Of course the grant may be sufficient to offset the additional operating costs in the short-run; but this would mean that the resulting job creation is far from permanent or continuing.

The cost-offsetting impact of combined offers made and accepted thus far has been even less than that indicated above, because grants have on average been only two-thirds of maximum. Thus on average the cost-offsetting impact has been 2 1/2 cents on a dollar of sales, very much out of line with estimates of cost differentials. This analysis suggests therefore that the investment projects supported with an incentive to date in most instances do not represent long-run locational shifts due to the grant. They may be short-run locational shifts. Or again they may be projects that can pass higher operational costs on to the consumer and would have occurred without assistance.

4. ^{to quote} The Adequacy of the Legislative Instrument

In this section, certain broad aspects of the incentives legislation itself are discussed: specifically, effective maxima under the Act (with particular reference to special development incentives), the method and timing of payments and the tax treatment of grants.

(a) The Effective Maximum Grant

One charge levelled against the previous Area Development Incentives Act was that its assistance favoured capital-intensive operations. Since a more equal treatment of labour and capital intensive operations was desirable the current incentives program recognizes not only capital invested but as well job creation in its grant rate. In a nominal sense then the department awards a percentage of eligible capital costs and in some cases a grant per direct job created. The ability to award the nominal maximum (e.g., 25% of capital costs and \$5,000 per job) is subject to two further limitations: i.e., half of capital employed (including working capital as well as fixed capital assets) and \$30,000 per job. The question of which maximum tends to be the effective limit of the grant is an important evaluative one. If the "capital to be employed" maximum is the effective maximum when the emphasis is to attract labour-intensive operations, then there is a suggestion of an inconsistency between goals and instrument.

*Loi Art 5
page 5*

This question is also important in determining the impact of special development incentives which were introduced in December 1970. Region C was made eligible for these special development incentives, while the Atlantic Region was eligible for special development incentives in addition to regular development incentives. Other designated regions continued to be eligible for the regular development incentives only. Therefore the department presented a three-tier nominal rate structure which would recognize differences in regional development gaps. However, the addition of the special development incentives for the Atlantic Region was not accompanied by an increase in the "half of capital employed" and "\$30,000 per job" ceilings. The implications of this will be discussed.

An examination of the effective maximum on all combined grants to mid-1972 (excluding Region C) indicates that the \$30,000 ceiling is effective in only a few isolated and extremely capital-intensive projects such as Proctor and Gamble. The bulk of cases are divided 60% - 40% as between "half of capital employed" and the nominal "% of capital costs-grant per job" ceiling respectively. The greater incidence of the "half of capital employed" ceiling was particularly evident in the Atlantic provinces: here three-quarters of the cases faced this effective ceiling.

The lifting of the 25% - \$5,000 ceiling in the Atlantic provinces to 35% - \$7,000 was stated at the time as being a means of maintaining the attractiveness of the Atlantic provinces vis-à-vis the new Montreal region. Why this should have been necessary when the primary intent of the Region C designation was to speed up projects that would have occurred there anyway is not clear. Nevertheless, this could not have been effective in that - as indicated above - most firms in the Atlantic face the "capital employed" restriction so that a lifting of the ceiling respecting percentage of capital and grant per job would be meaningless in most cases. Specifically, 100 cases of combined grants¹ made after January 1, 1970 up to mid-1972 were examined. Of these, 82 faced the "half of capital employed" restriction. Of these, 51 could not have received 25% - \$5,000 let alone 35% - \$7,000. Further, there wasn't a single instance of a combined grant given that could not have been given before the ceiling was raised. For example, a grant of 30% plus \$2,000 might have been given whereas 20% plus \$4,000 could have been given; both resulting in the same dollar grant. Further, it is worth noting that a significant portion of special development activity involves giving a new plant or new product expansion a primary grant only: e.g., 30% of capital costs. This creates the impression of a special incentive and also saves the department the problem of auditing jobs.

The over-all conclusion suggested then is that even though RDIA - in contrast to ADIA - introduced an employment-related grant, the over-all posture of the grant rate structure at the maxima is still biased in favour of capital-intensive activities. Clearly, half of capital employed means much more to capital-intensive activities than to labour-intensive activities. On a regional basis, this is most restrictive for the Atlantic provinces, where activities are relatively more labour-intensive. Increasing the employment related combined incentive grant would generally be ineffective as long as the "half of capital to be employed" maximum was not raised. Consequently, the special development incentive failed to effectively extend the range of incentives assistance in the Atlantic Region. *Conclusion*

¹ In this paper, a combined grant is defined as a grant based both on capital costs and jobs, and a primary grant is one based only on capital costs. This is slightly at variance with the terminology of the legislation. In the legislation, for example, a grant of 25% of capital costs might be literally a combination of a primary grant of 20% plus a secondary grant of 5%, or a combination of a regular primary grant of 20% and a special development primary grant of 5%. Because of the inherent confusion in the legislation, we adopted the simpler version of a combined grant. *def*

(b) The Tax Treatment of RDIA Grants

Although RDIA is not legally tied to any specific expenditure (i.e., once received, the company can literally do with it as it wishes) the inference has been made that it is intended to offset the initial costs of capital. This impression is conveyed in departmental publicity material and has been taken to heart by taxation authorities. The acquisition cost of capital is then considered to be net of the grant, and hence that part of plant and equipment covered by the grant is excluded from normal depreciation for tax purposes. This greatly reduces the value of the grant in terms of cost reduction or profit reinforcement. Preliminary findings by Professor Dudley of the Centre for Regional Studies at the University of Ottawa suggest that as a result of this tax treatment the grant is on average worth only half of its nominal value. In other words, previously it was indicated that the maximum combined grant could compensate for a cost differential of 4 percent. With more favourable tax treatment this impact would increase to 8 percent; a level which would greatly increase the potential for long-run effectiveness of the grant, particularly in the Atlantic Region and the Prairies.

(c) The Method and Timing of Grant Payments

Under the current system, recipient companies receive no money until commercial production, at which time up to 80% is received. The remainder of the grant is paid out no later than 42 months after commercial production. The current system has some serious shortcomings. First, the grant is not paid when it is often needed most - i.e., during the construction phase. This usually means that interim financing is required at a risk rate of interest which involves higher costs to the company and which may partly defeat the cost-offsetting purpose of the grant. Secondly, it can be argued that the department pays the first money too late but the last money too soon. The explanation for this statement lies in the nature of the grant. As stated before, the Department sees the grant as a fund to compensate for higher operating & distribution costs. However, in bookkeeping terms it does not actually reduce costs but it increases the firm's (project's) income position. Moreover that income position improves only during the year when the firm receives the incentive payment. In all other years the firm will continue to incur the additional costs of the designated region location. Since there is nothing that ties the grant to the assisted project on a continuous basis, the sooner the grant is paid the sooner the firm would begin to consider a move to the least cost location had the grant not been available. So even in those instances where the grant is successful in inducing additional new job creation, the method and timing of grant payments does not assure that these jobs will be continuing in nature.

Condition

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The preceding discussion, admittedly based on judgement rather than extensive research, suggests that the department ^{prolonger} the control period by (1) providing greater and cheaper access to financing during the construction phase through a more vigorous use of loans and loan guarantees (2) by stretching grant payment over a longer period of time, or (3) by

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obtaining a permanent claim on the assets of the project by way of a non participating equity position (non-voting and non-dividend) or long-term debt (non-interest bearing and non-repayable). These measures, it is suggested, would provide some assurance that in the case of support to incremental investment the jobs will be continuing.

5. Locational Options in the Context of Incrementality

The existence of a locational option cannot be taken as prima facie evidence of incrementality. The actual location decision for an investor is made - possibly from among several options - on the basis of a complex of monetary and non-monetary factors. Further, it should be emphasized that the concept of incrementality that we have been concerned with in this paper is in an "investment" sense rather than an "investor" sense. The grant may induce an individual investor to locate in a designated location, but if it is a case of "if not him, then somebody else" (e.g., for a local market industry where imports are not a factor) then the investor may be incremental but not the investment. It is a long jump then from the existence of a locational option to the judgement that the investment is incremental to the designated region. //

Our first approach to this question was to ask a consultant¹ to make a judgement by three-digit manufacturing industries about varying degrees of preference² for a location other than the designated region: this exercise was carried out for the Atlantic, Quebec (excluding Region C) and the Prairies separately. The categories were as follows:

hypotheses:

- (1) having a strong economic motive for locating in the region;
- (2) having a low preference for locating outside the region;
- (3) having a medium preference for locating outside the region;
- (4) having a strong preference for locating outside the region;
- (5) most unlikely to locate in the region.

In terms of incrementality, the following interpretations are realistic in terms of the categories. By definition, category five would be incremental. On the other hand, category one doesn't involve locational options and so ipso facto doesn't involve incrementality. The middle categories all have some degree of locational options and incrementality, but category two would have more of the former than the latter, with incrementality increasing through the third and fourth categories.

Table 5 indicates the distribution among the categories of incentives activity in terms of expected jobs to October 31, 1972. This exercise then establishes only the outer bounds of incrementality possibilities. At least 4% of activity is incremental, but at the same time about one-third is definitely not.

¹"Identification of Industry Locational Choice at the Three-Digit Standard Industrial Classification Level", Kates, Peat, Marwick & Co. study for Program Evaluation Branch, October 30, 1972

²Based on such criteria as existing capacity in the industry, market patterns, availability and costs of labour, availability and costs of materials, etc.

TABLE 5

Distribution of Expected Jobs by Region
in Terms of Increasing Categories of Incrementality
(based on Activity to October 31, 1972)

	Atlantic	Quebec (ex. Region C)	Prairies	All Regions
Category 1	40.7	30.5	26.9	32.5
Category 2	3.9	11.1	16.2	10.2
Category 3	26.8	24.1	23.0	24.6
Category 4	22.2	31.9	28.3	28.5
Category 5	6.4	2.4	5.7	4.2
Total	100.0	100.0	100.0	100.0

It is equally important in an incrementality context to examine the grant rate from category to category. This examination revealed that there was no discernible pattern in the rate of award of a grant (standardized for different capital/labour proportions) from one category to another: i.e., the award did not rise with increasing need on the basis of preference for locating elsewhere. In the Atlantic, category 2 received the highest awards; in the Prairies, category 1 received the highest awards; and in Quebec, the grant rate was virtually uniform from category to category. This alignment of actual grant rates in view of differing need is disturbing. It is inexplicable, in the context of locational shifts, why industries in the first categories got as high or even higher grants than those in the last categories. At the same time, one must ask why firms in the last categories accepted such grants. In terms of analysis in other parts of this paper, these categories seem like good candidates for viability problems or for a short-run strategy on the firm's part to remain in the designated region only until the benefits of the grant can be fully capitalized on.

A second approach to the question of locational options and incrementality involved an examination of 52 applications for grants in the Atlantic provinces which were coded in the incentives data-system as being foreign controlled.¹ This category of cases was examined with a particular view to determining the ability of an RDIA grant to attract this relatively footloose type of investment and the factors that entered into the grant calculation. The results of this study have not been prepared systematically yet, but the following impressions emerge.

Where a grant was given, an alternative location was mentioned three-quarters of the time. However, seldom was systematic data submitted by the applicant regarding cost differentials. In addition, when it was submitted, it was accepted at face value without an apparent attempt to validate it. An analysis was usually done on the pre-grant and post-grant

¹The sample consisted of all cases with capital costs greater than half a million dollars and a random selection of smaller cases.

rate of return at the designated location. But the relevant calculation was seldom done: the pre-grant rate of return in the designated region compared with the non-designated region and the ability of the grant to close the gap. Rather the grant was usually calculated on the basis of a "financing short-fall" technique which bears no particular relationship to locational cost differentials. //

6. Quantity vs. Quality of Jobs

The broad departmental job creation goals as indicated in the early portions of this paper contain both quantity and quality aspects. If "more of the same" is supported under incentives legislation, much may be done in the way of increasing the employment rate and participation rate, but little for increasing the average level of income. On the other hand, ^{$\frac{E}{E + \text{Churnage}}$} if incentives activity is concentrated on capital intensive industries employing highly skilled labour - but not much of it - we may have more impact on average incomes than on the rate of employment and participation in the labour force. The performance of the incentives program in relation to the "quantity-quality" dimension has been examined¹ with the overall conclusion being that there is no pervasive pattern in the administration of incentives towards "desirable" industries in these terms (based on offers accepted excluding Region C to September 30, 1972).

Two observations stand out from the mixture of results presented in table 6. -) There was a heavy concentration of incentives activity in the top group of industries in terms of skill level and technology level (as measured by value added per employee.) This is particularly true when activity is measured in terms of capital costs. -) Secondly, an examination of the distribution of incentives activity in terms of growth industries reveals that activity did not concentrate in the top group of industries in these terms but at the same time there was little support given to the slowest growing industries. On the whole though, incentives support went to above-average industries in growth terms: activity was particularly concentrated in the second top 25% group of industries as measured by 1961-69 growth in employment.

The relative concentration of incentives activity in areas which have exhibited an above-average growth rate and technical level is indeed a positive indication of program effectiveness. On the other hand, the evidence should not be interpreted in a conclusive manner. The results with respect to skill-technology are generated largely through the influence of a few large grants to capital-intensive projects in the primary metals and pulp and paper groups. The results with respect to growth industries must be qualified as well for by definition these industries would in the normal historical process participate relatively heavily in new activity in the designated regions. The real question is whether the program is adding to normal activity and bringing about a change in the industrial structure of designated regions. This question will be examined in the next section. ?

¹Program Evaluation Branch study: "The Degree of Support under RDIA and Special Areas Legislation to High Growth/Labour Intensive and High Skill/High Technology Industries".

TABLE 6

Incentives Activity in Terms of Quantity-Quality Aspects
(to September 30, 1972)
(based on data at the three-digit SIC level)

	<u>In Terms of Expected Jobs</u> %	<u>In Terms of Capital Costs</u> %	<u>In Terms of Incentive Grants Acceptances</u> %
<u>Growth</u> ¹⁾			
- top 25%	27	14	18
- second 25%	40	60	55
- third 25%	16	21	21
- fourth 25%	17	5	6
<u>Labour Intensity</u> ²⁾			
- top 25%	33	13	24
- second 25%	28	17	34
- third 25%	16	42	23
- fourth 25%	23	28	19
<u>Skill Level</u> ³⁾			
- top 25%	19	55	39
- second 25%	15	10	13
- third 25%	41	25	33
- fourth 25%	25	10	15
<u>Technology (1)</u> ⁴⁾			
- top 25%	17	52	39
- second 25%	13	14	15
- third 25%	38	22	28
- fourth 25%	32	12	18
<u>Technology (2)</u> ⁵⁾			
- top 25%	32	21	25
- second 25%	38	19	26
- third 25%	15	21	20
- fourth	15	39	29

1) % change in employment from 1961 to 1969

2) average ratio of wages and salaries to value added in 1961 and 1969

3) average wages and salaries per employee in 1961 and 1969

4) average value of value added per employee in 1961 and 1969

5) % change in value added per employee from 1961 to 1969

7. RDIA Activity in Relation to the Existing Industrial Base

Broad regional industrial development in the long run cannot be achieved solely by doing more of the same. In fact it requires the introduction at an accelerated pace of new industrial activities that shift the industrial structure away from the traditional industries which are largely local market and resource oriented. If an examination of incentives activity to date reveals a different industrial structure than existed before the introduction of the program then this is evidence that the program is indeed introducing new activities. Table 7 examines the industrial distribution of expected jobs under incentives relative to the distribution of manufacturing employment in 1970.

In the Atlantic Region the distribution of expected jobs is broadly similar to the 1970 distribution of regional manufacturing employment, and is concentrated on what may be called the traditional activities of fish processing, sawmills and shipbuilding. There are, however, examples of significant additions of new manufacturing activities in the region.

In Quebec incentives activity in knitting mills and transportation equipment appears to be well placed. Both industries have been fast-growing employers of labour during the past decade, and thus have become relatively more prominent on the industrial scene in Quebec. Moreover, the weight of these industries in total Quebec incentives activity far outweighs their industrial importance. On the other hand, the incentives assistance committed to textiles and clothing is not equally commendable. These two traditional sources of employment in Quebec have become less important, and growth as employers has been minimal or lacking. Of course, some degree of assistance is warranted as a defensive measure to slow down the adjustment process. The wood products group is another area where incentives activity is open to question; an industry which increased its employment by 17 percent from 1961-1970 has received assistance for 4,800 new jobs. This would represent an increase in capacity of 25 percent over 1970. It is difficult to believe that this can be absorbed without internal adjustment problems. Overall, 54 percent of all expected jobs from offers accepted in Quebec were in industries that, in terms of employment, grew at an above-average rate. These industries accounted in 1970 for 45 percent of Quebec manufacturing employment. In general, therefore, there is some evidence of a reinforcement of structural change in Quebec manufacturing through the industrial incentives program.

In Manitoba, the foods and beverages industry accounts for almost one-quarter of the manufacturing labour force but only one-twelfth of expected incentive jobs. The second largest employer - the clothing industry - accounts for 13% of the labour force and 16% of expected jobs. The reorientation under the incentives program was largely toward rubber and plastics, and transportation equipment.

TABLE 7

Expected Jobs from Incentives Accepted
and Manufacturing Employment
(Incentives Activity to September 30, 1972)

	Atlantic		Quebec		Manitoba		Saskatchewan	
	1970 Base(%)	Expected Jobs(%)	1970 Base(%)	Expected Jobs(%)	1970 Base(%)	Expected Jobs(%)	1970 Base(%)	Expected Jobs(%)
Food & Beverage	37.5	32.8	11.9	7.1	22.6	8.0	39.6	24.8
Tobacco Products	X	0.2	1.2	-	-	-	-	-
Rubber & Plastic	0.2	11.9	2.4	3.9	0.7	5.2	0.7	26.6
Leather	0.4	0.2	2.7	1.8	1.4	-	-	0.7
Textiles	2.0	3.1	7.2	8.3	1.4	2.6	0.8	-
Knitting Mills	X	2.0	2.8	8.0	0.6	0.6	-	-
Clothing	X	1.5	12.2	10.0	13.1	15.6	X	15.6
Wood	8.2	11.9	3.8	10.9	2.5	4.7	6.4	6.2
Furniture & Fix.	X	4.0	3.3	3.9	3.8	3.9	0.4	-
Paper & Allied	X	0.2	8.5	3.2	3.8	2.1	X	0.4
Printing & Pub.	X	1.0	4.3	1.9	8.4	4.2	10.6	1.6
Primary Metal	X	1.0	5.1	5.0	5.2	1.8	X	23.0
Metal Fab.	X	3.2	7.0	5.6	5.6	5.3	7.1	15.6
Machinery	1.1	1.9	2.9	2.6	2.6	5.8	4.4	3.6
Transportation Eq.	9.3	8.3	6.6	11.9	11.9	27.8	2.4	6.1
Electrical Prop.	X	9.7	6.6	6.8	3.6	6.6	X	-
Non-Metallic Min.	X	1.1	2.5	3.1	2.6	1.9	4.4	-
Petroleum & Coal	X	0.1	0.6	0.1	X	-	4.8	-
Chem. & Chemical Prod.	X	0.5	5.4	2.4	2.1	0.6	1.4	-
Miscellaneous Mfg.	1.2	5.3	3.0	3.7	X	3.2	1.9	-
Confidential Ind.	(40.1)	(24.1)	-	-	(3.2)	(3.2)	(15.0)	(39.0)
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

X - Confidential

Half of Saskatchewan's manufacturing employment in 1970 was in the foods and beverages group and in printing and publishing. The first has declined as an employer and the latter's growth has been average over the last decade. One quarter of expected jobs from accepted offers of incentive grants in Saskatchewan are in foods and beverages. Assistance to printers and publishers has been insignificant. In addition to foods and beverages, expected jobs were also concentrated in clothing, primary metal and metal fabricating.

Conclusion
The overall impression for all regions is that while much of the incentives support has been allocated to traditional industries, there is evidence of structural change by way of support to new additional activities. The Atlantic Region is the area of particular concern in this context where almost half of incentives activity is in the traditional food and wood sectors.

8. Incentives Activity in a Growth Centre Context

The promotion of industrial growth centres constituted a special spatial element of the industrial incentives program. Through the interaction of the department's infrastructure and incentives programs, it was envisaged that a process of agglomeration could be generated that would concentrate manufacturing activity in the industrial growth centres and exert favourable linkage effects to the hinterland area and thus lift the entire region from the centre. In this section the discussion will centre on the extent to which the incentives program has concentrated activity in special areas and growth centres; whether this concentration is likely to lead to their greater importance as manufacturing centres; and whether there is evidence of a conscious pursuit of a growth pole policy under the incentives program.

Evidence clearly indicates that special areas as a whole or industrial growth poles have not played the hoped-for role¹ in incentives program activity to date. Less than one-quarter of the number of offers accepted have been in a special area. Activity in terms of jobs, value of offers and capital costs is indicated in table 8. As for the industrial growth centres of St. John's, Halifax-Dartmouth, Moncton, Saint John, Three Rivers and Quebec City, an even smaller concentration of incentives activity emerges. These six growth centres have accounted for little more than 20 percent of incentives activity in the Atlantic Region and Quebec (ex. Region C).

Furthermore, while in relation to two growth centres, Moncton and Three Rivers, there is the prospect that incentives activity may lead to an increasing concentration of manufacturing activity, there is little evidence which points to a conscious pursuit of a growth centre strategy in the administration of the incentives program. This suggests also that the intended coordination between the infrastructure activities in the growth centres and the incentives program has also not been fully achieved. //

¹The early 1969 thinking (see for example February 10, 1969, memorandum to Cabinet) was that most employment related grants would be in the industrial growth centres.

TABLE 8

Net Offers Accepted in Special Areas¹⁾
as a percentage of all offers accepted
in the province
(inception to September 30, 1972)

	<u>No. of Cases</u>	<u>Eligible Capital Costs</u>	<u>Expected Jobs</u>	<u>Value of Offers Accepted</u>
Newfoundland	57.1	59.4	52.0	64.6
Nova Scotia	24.1	9.0	31.0	16.4
New Brunswick	34.4	35.7	36.2	33.1
Quebec	20.8	49.2	28.0	35.8
Ontario	30.8	12.5	32.7	22.3
Saskatchewan	66.7	80.1	42.6	77.3
Alberta	20.9	74.8	43.8	70.5
Canada	22.8	38.2	28.9	32.8

¹⁾ Activity in all special areas except Ste. Scholastique is expressed as a proportion of all provincial activity excluding Region C.

TABLE 9

Net Offers Accepted in Industrial Growth Centres
to September 30, 1972

	<u>No. of Cases</u>	<u>Eligible Capital Costs (\$'000)</u>	<u>Expected Jobs</u>	<u>Offers (\$'000)</u>
St. John's	18	5,692	513	2,770
Halifax-				
Dartmouth	25	13,636	1,396	4,474
Moncton	23	8,113	610	3,391
Saint John	21	15,378	1,208	5,463
Quebec City	50	20,684	2,569	5,217
Three Rivers	44	90,352	2,614	14,494
Total	181	153,855	8,910	35,809

In the following paragraphs, a brief evaluation is made of RDIA activity in individual growth centres.

Halifax-Dartmouth

In terms of most indicators, Halifax-Dartmouth has participated in the incentives program only to the extent that could be expected from its share of provincial manufacturing employment. There is no particular concentration in this growth centre. Indeed, it has received a relatively low proportion of the value of grants, not only because of smaller projects than in the rest of the province but because of a lower rate of award (in terms of grant per job, grant as a percentage of capital costs or grant as a percentage of the maximum grant possible). There is no evidence then that activity was consciously diverted to the growth centre through preferential grants.

Moncton

Moncton has participated in the incentives program to a greater extent than its share of the total provincial employment base would suggest. To September 30, 1972, for example, it had 12% of expected jobs in the province although it had only 8% of provincial employment in 1969. It is not clear whether RDIA is leading growth or growth is leading RDIA: total employment in Moncton over the last decade has grown at twice the over-all provincial rate. As with Halifax-Dartmouth, projects outside the growth centre have received higher rates of support than inside.

Saint John

Almost one-quarter of the provincial manufacturing base is in Saint John. This proportion also applies with respect to Saint John's share of incentives activity. Projects in the Special Area do seem to have obtained some edge in terms of grant size. The question is begged as to whether particular projects that went outside the area could have been induced to establish in the area with the use of some of the extra discretion available to the department - particularly with respect to a few metal-working projects that located outside, but within 30 miles, of Saint John.

Three Rivers

Three Rivers accounts for some 10% of the Quebec manufacturing labour force outside Region C. In terms of expected jobs, an equivalent percentage of RDIA activity went to the special area. However, the level of activity has accelerated through time. Although the evidence is mixed, the balance of results suggests that projects in the Three Rivers Special Area have received a premium in grant rates. Over-all then, there is the prospect that RDIA will help this area to make up ground lost in the last few years when total employment has declined.

Quebec City

Quebec City accounts for some 12 percent of provincial manufacturing employment outside Region C while expected jobs under RDIA so far represents about 10 percent. As a result then, RDIA is not contributing to a concentration of manufacturing in this Special Area. A contributing factor behind this result is a lower rate of award inside the Special Area than outside it. Infrastructure activity has been very vigorous in this Special Area and is likely a substantial contributing factor in the relatively rapid rate of growth in total employment in this area in recent years (i.e., 13% growth from 1968 to 1971 compared with 1% growth in the province as a whole and a decline of 1% in Three Rivers). The concern that must be expressed here, however, is that these gains may be transitory in that the greater proportion of job-creation under the infrastructure program does not last beyond the construction phase.

9. The Impact of Incentives Activity on Broad Economic Indicators

In this section, regional trends in the broadest impact indicators - unemployment rate, participation rate and average incomes are discussed. In addition, an analysis is made relating incentives activity in terms of jobs and capital costs to the total eligible¹ job creation and capital spending in regions - specifically, how much of the total pie are we covering? The latter aspects are treated in greater detail than the former aspects. Both approaches are fraught with conceptual and measurement difficulties but these are more prohibitive in the former. It is unrealistic to expect to disentangle the separate influence of the incentives program on the broad macro-indicators, (i.e., unemployment, participation and average income), for the incentives program is only one of several inter-acting departmental programs. In addition, of course, a large proportion of incentives-supported

TABLE 10

Unemployment Rates by Region
1961-72

	Atlantic	Quebec	Prairies	Canada
1961	11.2	9.2	4.6	7.1
1962	10.7	7.5	3.9	5.9
1963	9.5	7.5	3.7	5.5
1964	7.8	6.4	3.1	4.7
1965	7.4	5.4	2.5	3.9
1966	6.4	4.7	2.1	3.6
1967	6.6	5.3	2.3	4.1
1968	7.3	6.5	3.0	4.8
1969	7.5	6.9	2.9	4.7
1970	7.6	7.9	4.4	5.9
1971	8.6	8.2	4.5	6.4
1972 ³⁾	9.3	8.2	4.4	6.3

(3) based on January to November data.

¹ / the context of 'eligibility' in this section refers to job creation and investment in manufacturing activities which under the RDIA Regulations are eligible for consideration for an incentive grant.

projects will not reach commercial production for some time, so that much of the impact (including indirect multiplier effects) will not have been felt by the regional economies. Finally, the broad indicators move through time on the basis of secular, cyclical and "irregular" factors. The investigator has the difficult job of abstracting from cyclical and trend elements to detect a disturbance in the irregular element that can be attributed to policy.

The overall evidence regarding program effectiveness from a detailed examination² of regional trends in key macro-variables is ambiguous, and is therefore not fully developed here. However, as illustration of the problems with this approach, Table 10 indicates the trend by region in unemployment rates from 1961 to 1972. The Atlantic Region's position relative to Canada is particularly noted. Over the entire period, there has been a converging trend in unemployment rates in the Atlantic and Canada with the sharp drop in the differential occurring in 1970 - the first full year of departmental activity. On the other hand, in 1971 and 1972 the differential widened. This might be taken as evidence of program ineffectiveness: but it has been a cyclical characteristic that when the national unemployment rate is on an upward trend, the differential between Canada and the Atlantic widens: perhaps the incentives program reduced the degree to which the differential would have widened without program activity.

A more fertile approach than the above is an analysis of the more direct relationship between supported job creation and investment in place and the total level of eligible job creation and investment activity in the designated regions. The objective of the industrial incentives grants program is to effect a redistribution of Canadian manufacturing activity towards the slow-growth regions. The past trends in this direction had been inadequate and the industrial development grant program was established to provide an incentive for new manufacturing investment to locate in these slow-growth regions that would not have located there otherwise. Consequently, the aim of the incentives program was to improve upon the long-run trend in the share of Canadian manufacturing investment accruing to the slow-growth regions. In relation to incentives-supported activity estimated to be in place thus far, the following analysis will seek to determine whether such a relative improvement has occurred, and what the implications are for incrementality and program effectiveness.

(a) Quebec

- 11 In 1970, while the absolute level of eligible manufacturing investment in Quebec advanced marginally, the share of the Canadian total dropped sharply. The absolute level dropped by about \$50 million in 1971, but this rate of decline was about the same as for the nation as a whole, so that Quebec's relative position changed little. In 1972 manufacturing investment in Quebec apparently expanded rapidly. Eligible manufacturing investment rose by some \$90 million and its relative position improved by 3 percentage points.

¹ Program Evaluation Branch Study "The Impact of DREE Programs - An Assessment of Key Indicators of Socio-Economic Gaps", October 16, 1972.

TABLE 11

Capital Expenditures in Manufacturing
and RDIA Activity
Quebec (including Region C)
(millions of dollars)

	Capital Expenditures on Manufacturing		Quebec's Share of Canadian "Eligible" Manufacturing	Estimated RDIA Supported Investment in Place	Supported Cap. Exp. as Percentage of Supportable Capital Expenditures
	Total	"Eligible"			
1968	600.4	424.9	23.9	-	
1969	617.9	469.9	22.4	.5	0.1%
1970	623.6	472.0	19.5	43.6	9.2%
1971	538.3	426.0	19.3	156.8	36.8%
1972	665.8	517.0	22.2	332.2	64.2%

Notes: The major exclusions from eligibility for RDIA incentive grants are petroleum refining and pulp and newsprint activities. Due to statistical limitations the entire paper and allied industries and petroleum and coal products group had to be excluded. On the other hand capital expenditures on projects ineligible because of size restrictions are not excluded. Further, there are some incomparabilities between the concept of eligible capital costs under RDIA and the Statistics Canada survey of investment. The former allows used machinery, for example, while in the latter, machinery is counted only when the first user puts it in place. At the same time, a fleet of trucks would be included in the survey of investment expenditures but not as eligible capital costs for calculating an RDIA grant.

Table 11 shows the estimates for the value of incentives-supported investment put in place. It is evident that the proportion of Quebec's investment that received incentives grant support has grown sharply, so that the program in 1972 accounted for about two-thirds of total eligible capital spending in manufacturing.

The relative improvement in Quebec's position in overall Canadian eligible manufacturing investment since 1970 suggests that the incentives program has thus far been effective. In fact it is likely that the incentives program prevented further deterioration in 1971 and 1972 and brought forward a levelling out and improvement by several years. Consequently, a relative improvement of 3 to 5 percentage points can be attributed to program effectiveness.¹ In other words, \$70 to \$110 million of the RDIA supported investment in place can be said to have been effective in the sense that it represented activity which would not have occurred without incentives support.

¹ It may be claimed that this understates RDIA effectiveness because the historical share includes the cumulative incremental impact of previous regional development programs - particularly ADIA. This is granted but the degree of understatement is considered small in light of consensus judgements about the slight incremental impact of these prior programs. Indeed that was the rationale for the formation of DREE and the phase-out of ADIA.

Conclusion
2)

It is self-evident that program effectiveness was accompanied by considerable inefficiency or support of investment that would have taken place anyway. To suppose that all supported investment would not have taken place without incentive support is to say that eligible manufacturing investment in Quebec would have been only \$270 million in 1971 and \$180 million in 1972; clearly an unacceptable hypothesis. It would seem therefore that of the \$533 million of supported investment estimated to be in place, some \$423 million to \$463 million would have taken place anyway.

The expansion in program activity in Quebec is due much more to greater coverage of the eligible base than to incremental activity. This in turn suggests that, in large part, RDIA activity is not an independent phenomenon, but one dependent on and a reflection of the 'normal' level of investment activity in Quebec. One could say that as long as current designated regions are maintained, and applications meet the same success, the current level of RDIA activity will be maintained. There is no reason to believe otherwise.

TABLE 12

Manufacturing Employment and
R.D.I.A. Job Creation
Quebec (including Region C)

	Manuf. Employment in Large Est. R.D.I.A. Eligible Industries	Estimated Gross Job Creation	Estimate of R.D.I.A. Assisted Jobs in Place	Jobs in Place as Percent of Estimated Gross Job Creation	Expected Jobs from Total Net Offers Accepted (Per date of Acceptance)
1968	424,589	23,500			
1969	431,891		216	.9%	1,320
1970	424,589		1,006	4.3%	6,061
1971	428,000		6,488	27.6%	17,784
1972	428,856 (Est.)	23,500	7,610	32.4%	25,296

Notes: The employment data indicated is for large establishments only: i.e., with an employment greater than 20. The complete Census of Manufactures figure is available only to 1970 when the level in Quebec was 467,047 compared to 424,589 in the large establishment survey. The gross job creation figure is based on an average 5% job depletion rate on the Census of Manufactures base. This is somewhat higher than the rate used in the section on targets at the beginning of this paper as the 1968-72 period was a downturn one cyclically when presumably the job loss rate would be relatively high. Eligible industries exclude pulp and paper and petroleum and refining. Due to statistical limitations the entire paper and allied industries and petroleum and coal products group had to be excluded. Expected jobs are those reported at time of offer of incentive: 1972 represents nine months activity expressed at an annual rate.

3) Similarly there is as yet no reason to believe that the RDIA job support rate will not be around the 1971-72 average of 21,500, (assuming the continued designation of Region C) and that these assisted jobs, when in place, will not represent 66 percent or more of total provincial job creation in eligible manufacturing. Thus far assisted jobs in place are estimated at 15,320. However, it is already evident that these assisted jobs are not being reflected in a similar net increase in manufacturing employment; some 4,300 since 1970. Moreover, the rate of growth in RDIA job creation is considerably greater than for manufacturing employment as a whole. This suggests that, in terms of jobs also, program growth is a reflection not only of new additional activity but as well of greater coverage of normal activity. Is it a mere coincidence that the number of expected jobs from offers accepted in 1971 and 1972 - an average of 21,500 is very close to the average annual level of gross provincial job creation in manufacturing of 23,500? It appears probable then that the level of assisted job creation is in total largely a reflection of normal on-going economic activity. This appraisal of program effectiveness and efficiency applies to Quebec inclusive region C and Quebec excluding Montreal (see Table 13).

TABLE 13

Manufacturing Employment and
R.D.I.A. Job Creation
Quebec (Ex. Montreal)

	Manuf. Employment in Large Est. R.D.I.A. Eligible Industries	Estimated Gross Job Creation	Estimate of R.D.I.A. Assisted Jobs in Place	Jobs in Place as Percent of Estimated Gross Job Creation	Expected Jobs from Total Net Offers Accepted (Per date of Acceptance)
1968	162,905	9,350			
1969	171,116		216	2.3%	1,320
1970	169,953		1,006	10.8%	6,061
1971	171,634		4,306	46.0%	7,870
1972	167,172 (Est.)	9,350	4,620	49.4%	9,344

Note: (See Table 12)

(b) Atlantic Region

The Atlantic Region has since 1969 increased its share of Canadian capital expenditures in manufacturing. Excluding the major industries not eligible for R.D.I.A. support, the region probably had some 9.4% of 1972 Canadian investment in eligible manufacturing activities. This compared with 5.4 percent in 1969 and 4.8 percent in 1970. Much of this relative improvement in share is accounted for by investment receiving A.D.I.A. support. Nevertheless in terms of investment that could have received R.D.I.A. support the Atlantic Region improved its share.

TABLE 14

Capital Expenditures on Manufacturing
and R.D.I.A. Activity
Atlantic Region
(millions of dollars)

	Capital Expenditures on Manufacturing			Atlantic Region Share of Can. Eligible Capital Expenditures on Manufacturing	Estimate of R.D.I.A. Supported Investment in Place	Supported Cap. Exp. as Percentage of Supportable Cap. Expenditures
	Total	Eligible for RDIA ¹⁾	Eligible and not Supported under ADIA ²⁾			
1968	172.8	140.0	-	7.9%		
1969	232.0	113.0	-	5.4%	1.5	1.3
1970	358.6	117.0	87.0	4.8%	26.0	29.9
1971	412.0	182.0	118.0	8.3%	55.0	46.6
1972	377.5	218.0	138.0	9.4%	77.0	55.8

Notes: 1) See note to Table 11

2) This also excludes a substantial amount of manufacturing investment eligible under R.D.I.A. but that had already received support under A.D.I.A.

TABLE 15

Manufacturing Employment and
R.D.I.A. Job Creation
Atlantic Region

	Manuf. Employment in Large Est. R.D.I.A. Eligible Industries	Estimated Gross Job Creation	Estimate of R.D.I.A. Assisted Jobs in Place	Jobs in Place as Percent of Estimated Gross Job Creation	Expected Jobs from Total Net Offers Accepted (Per Date of Acceptance)
1968	59,078	4,000			
1969	59,744				859
1970	58,935		831	20.8%	2,823
1971	61,400		1,850	46.2%	4,852
1972	59,251(Est.)	4,000	2,393	59.8%	6,477

Notes: See notes on Table 12

2) It is also evident that the incentives program is covering a high proportion of the investment eligible for support - estimated at 56% in 1972. The growth in investment put into place clearly has not been reflected in a corresponding absolute increase in total eligible manufacturing investment. Much of the activity in any given year would have occurred in that year without incentives assistance. For a program which according to its enabling legislation was limited to providing assistance to additional investment only, the proportion of total eligible investment supported is obviously too high. If one were to assume that the entire increase in eligible supportable manufacturing investment since 1969 - \$51 million - was new additional activity attributable to the incentives program, then incremental activity would represent some 32% of the \$158 million of supported investment thus far estimated to have been put into place.

The preceding analysis suggests that the incentives program has indeed been effective in bringing about new activity in the region and achieving its goal of increasing the region's share of manufacturing investment. On the other hand, there is also evidence that there has been support of much activity that would have taken place anyway. In other words, to a large extent program activity is effect rather than cause. The evidence is similar when one considers the level of manufacturing employment in the region.

(c) Manitoba and Saskatchewan

In the following table it can be seen that Manitoba and Saskatchewan are getting a declining share of Canadian capital spending eligible for incentives grants. In fact the level of 2.8 percent in 1972 is the lowest of the past decade. Therefore, on the basis of the standard established at the beginning of this section, the incentives program has not been effective in these provinces, since the relative position as a location for investment has not improved.

The lack of effectiveness in this sense does not deny that to some degree incentives activity represents new activity which would not have occurred without incentives support and which in part prevented a further deterioration in the relative position of this region. On the other hand, to assume that all of the supported investment was incremental would suggest that eligible investment in 1970, 1971 and 1972 would have been \$59 million, \$40 million and \$33 million respectively. While some incrementality can be conceded, one is faced by the inevitability of considerable support of 'normal' investment. To do otherwise is to take the position that the industrial incentives program prevented a crisis in investor confidence for these two provinces.

TABLE 16

Capital Expenditures in Manufacturing and
R.D.I.A. Activity
Manitoba and Saskatchewan
(millions of dollars)

	Capital Expenditures on Manufacturing	Manitoba and Saskatchewan's Share of Can. Eligible Cap. Expenditures on Manufacturing	Estimate of R.D.I.A. Supported Investment in Place	Supported Cap. Exp. as Percentage of Eligible Cap. Expenditures
	<u>Total</u>	<u>Eligible for R.D.I.A.</u>		
1968	116.3	102.0	5.7	
1969	98.4	77.0	3.7	
1970	125.8	75.0	3.1	15.8
1971	84.1	73.0	3.3	33.3
1972	74.8	66.0	2.8	32.5

Notes: The major exclusion from eligibility for R.D.I.A. incentives grants are petroleum refining and pulp and newsprint activities. Due to statistical limitations, the entire paper and allied industries and petroleum and coal products group had to be excluded. On the other hand, projects ineligible because of size restrictions are not excluded nor are capital expenditures in those parts of Saskatchewan and Manitoba not designated under the R.D.I.A. or the Department of Regional Expansion Act. On balance, therefore, probably less investment was eligible for incentives support than indicated above.

TABLE 17

Manufacturing Employment and
Incentives Job Creation
Manitoba and Saskatchewan

	Manuf. Employment in Large Est. R.D.I.A. Eligible Industries	Estimated Gross Job Creation	Estimate of R.D.I.A. Assisted Jobs in Place	Jobs in Place as Percent of Estimated Gross Job Creation	Expected Jobs from Total Net Offers Accepted (Per Date of Acceptance)
1968	55,021	3,200			
1969	56,242		32	1.0	203
1970	55,741		451	13.9	2,050
1971	57,000		1,188	37.1	3,316
1972	54,153 (Est.)	3,200	1,800	56.2	2,809

Notes: See note on Table 12

The preceding conclusions are reinforced by an assessment of changes in manufacturing employment in Manitoba and Saskatchewan. The department has assisted some 3,500 jobs in place; yet there is no evidence of a net increase in manufacturing employment, rather if anything a decline. It would seem that in 1972 assisted jobs put into place represented nearly 60 percent of the average annual gross job creation; a proportion which suggests that, besides the possibility of some net new continuing job creation there is also support of jobs, like investment, which would have come about without incentive grants.

(d) Summary

An attempt has been made to assess the effectiveness of the program and the degree of incremental activity realized by the program in the Atlantic Region, in Quebec and in Manitoba and Saskatchewan. In summary it was shown that these designated regions accounted in 1968 for 37.5 percent of Canada's capital expenditures eligible for incentives support under the current legislation. This proportion (see table 19) dropped to 27.4% in 1970. This downward trend was reversed in 1971 and further relative improvement to a level of 34.4 percent is anticipated in 1972.

TABLE 18

Capital Expenditures on Manufacturing and
R.D.I.A. Activity: The Atlantic Region
Quebec (including RegionC), and Manitoba and Saskatchewan
(millions of dollars)

	<u>Capital Expenditures on Manufacturing</u>		<u>Eligible Cap. Exp. as Percentage of Total Can. Elig. Cap. Exp.</u>	<u>Estimate of R.D.I.A. Supported Investment in Place</u>	<u>Supported Cap. Exp. as Percentage of Eligible Cap. Expenditures</u>
	<u>Total</u>	<u>Eligible</u>			
1968	889.5	666.9	37.5		
1969	948.3	659.9	31.5	2.0	0.3%
1970	1108.0	634.0	27.4	85.4	13.5%
1971	1034.4	617.0	30.9	245.1	39.7%
1972	1078.1	721.0	34.4	441.7	61.3%

Notes: See note on Table 16

In terms of measuring program effectiveness and incrementality one could take one of the two following positions;

(1) the relative position would have stabilized without R.D.I.A. at 27.4%, the 1970 level; i.e., the relative improvement of 7 percentage points since 1970 is attributable to the R.D.I.A. program.

(2) the relative position would have continued to decline without R.D.I.A. though at a reducing rate; i.e. the relative position in 1972 would have declined to for instance 23.5% and would have levelled out at that point in time, i.e. a relative improvement of 11 percentage points is attributable to the incentives program.

In the first case \$165 million of assisted investment put into place was incremental or new additional activity, while in the second case this level of incrementality would increase to \$255 million. In terms of \$773 million of supported investment estimated to have been put into place, this implies a degree of incrementality of at least 21 percent and as much as 33 percent. It is evident that activity under the program has grown more rapidly than total eligible capital spending, and that while the growth in part represents additional or incremental activity, a large part of it would have occurred in the region, at that time, without incentives support.

10. The Use of Discretion and the Incentives Program

The availability of discretion under the Regional Development Incentives Act was provided so that to the maximum extent possible only projects would be assisted which would not go ahead without such assistance, and so that the amount of assistance would be sufficient to realize the intended investment. Discretion was to be used to minimize assistance to investment projects which would have gone ahead anyway; and to introduce a differentiation in assistance between regions and between industries. Such differentiation was to bring about regional equality of opportunity of economic development.

In the previous section it was concluded that the program has, thus far, supported much investment and job creation that represents on-going normal activity. Discretion has been too little used in refusing assistance, as evidenced by the high proportion of eligible investment supported and by the fact that only 5 out of 100 applications for incentives assistance are rejected because the project would have gone ahead anyway.

Furthermore, in those cases where incentive grants were offered there is little evidence of differentiation in assistance which corresponded to differences in locational costs (see Table 19). The Atlantic provinces clearly received generous grants when related to capital costs. However, there is no corresponding generosity in terms of grant per job, because the capital requirements per job are much less. Analysis of the grant impact on the cost structure of the average project supported moreover leaves the overall impression of a uniformity among regions rather than differentiation. This impression has been confirmed in a more detailed examination by this branch.¹

¹Program Evaluation Study, "The Impact-Effectiveness of Grants under RDIA and Special Areas Legislation", October 19, 1972.

TABLE 19

Value of Incentive Grants:
Combined Grant Cases
Outside Region C
to June 30, 1972

	Value of Grant			Approved Capital Costs Per Authorized Job
	Per Authorized Job	As a Percentage of Eligible Capital Costs	As a Percentage of Maximum Possible Grant	
Newfoundland	\$4,189	47	63	\$8,879
P.E.I.	3,279	40	59	8,169
Nova Scotia	3,210	41	51	7,738
New Brunswick	6,270	49	82	12,878
Quebec	4,671	25	65	18,818
Ontario	6,084	20	59	30,365
Manitoba	3,127	34	53	9,084
Saskatchewan	4,334	32	63	13,535
Alberta	13,128	16	82	81,661
British Columbia	2,745	31	51	8,725

It is evident as well from the table that a considerable degree of discretion remained for the department to award grants that more realistically differentiated among regions on the basis of the relative difficulty of attracting new investment. The over-all conclusion suggested is that discretion was not utilized to deploy investment spatially - either in terms of broad regions or, as we have seen earlier, in terms of the industrial growth centres.

The question is then why have the discretionary powers of the present legislation not achieved their objectives? The present Act and its Regulations assumes that, in the case of new plants having a locational choice between the non-designated and designated regions, there is technical capacity within the department to determine locational cost differences as a basis for calculating the level of incentive grants. This capacity is not present. In those cases where locational cost differences were a consideration, it was not the department who determined these differences, but the applicant. The locational cost data then can merely be part of the company's bargaining stance - indeed companies have accepted grants that fall short of covering the costgaps that they submitted.

If the technical capacity to determine locational cost differences is lacking, then discrimination between new plants with a locational disadvantage and those without a disadvantage is not possible. That does not mean that those without a disadvantage should not be assisted. These new

facilities as well as new facilities without a locational choice may be pulled ahead in time, or may be larger, or more technically advanced as a result of an incentive. But is a gain in time, in size or in technology of the same value as a locational gain? Generally speaking not, but how much less and how much less in the Atlantic than in Quebec or in the West.

The same situation applies to new product expansions. Generally speaking, there is not a locational choice, let alone a locational cost disadvantage. Nevertheless, new product expansions are important in terms of regional industrial development; though generally less important than new facilities which represent truly new activities. Again, however, there are no standards which dictate the relative importance of new product expansions, and hence differential treatment has been on an ad hoc basis.

The discretion available also allowed differentiation among industries. But what criteria does one use to determine industrial priorities among twenty major industry groups or 139 sub-groups. Should the criterion be growth, technology, value added per man, earnings per production worker, backward and forward linkages? This would vary from region to region (or province to province). Moreover, what incentive value does one put on the industry differences whatever criterion is used?

The implementation of the incentives program also contained a particular spatial approach within the designated regions, namely a concentration of new investment in growth poles. This would require knowledge of locational cost differences between a location in a growth pole and a location elsewhere in the region of which it is a part. Without this

TABLE 20

"ADIA" Costs of RDIA Program: By Province
(Based on activity to November 30, 1972
excluding modernization)^{a)}
(millions of dol-ars)

	<u>All Offers Accepted</u>	<u>Discretionary Rejections</u>	<u>Total</u>	<u>Comparable Actual RDIA Offers</u>
Newfoundland	5.9	1.8	7.7	9.6
P.E.I.	2.0	0.6	2.6	2.6
Nova Scotia	33.9	3.6	37.5	39.2
New Brunswick	15.7	5.9	21.6	26.4
Quebec ^{b)}	86.9	54.3	141.2	98.6
Ontario	23.7	10.5	34.2	23.5
Manitoba	16.5	6.7	23.2	16.8
Saskatchewan	7.6	4.4	12.0	7.2
Alberta	14.6	7.3	21.9	23.0
British Columbia	4.3	3.3	7.6	3.7
Total	211.1	98.4	309.5	250.6

a) modernizations were not eligible under the A.D.I.A.

b) excluding Region C

knowledge, one would not know what premium would be necessary to draw the investment into the growth centre.

There have been, in conclusion, no criteria for the use of discretion that matches assistance with need. Clearly the incentives officer was asked to make a difficult judgement without area-industry strategies and guidelines having been worked out as a framework within which to guide the administration of grants. The discretion that has been used has most frequently been based on "financing short-fall", i.e., the amount of the incentive has been calculated from the amount by which cash flow fell short of cash requirements. However, financing shortfall bears no relation to the various criteria discussed above.

Since discretion has not eliminated substantial support to non-incremental investment and job creation, the usefulness of discretion in its present form and scope becomes questionable. In this context it would be of interest to see what the current incentives program would have cost under the A.D.I.A. which was relatively non-discretionary as to eligibility for assistance and rates of assistance.

It can be seen in Table 20 that for combined offers accepted under the current incentives program the "A.D.I.A." cost would have been \$40 million less. However, applications rejected under the current legislation for truly discretionary reasons would have received assistance under A.D.I.A. in the amount of \$98 million. Thus the comparison is between an "A.D.I.A." cost of \$310 million and a current program cost of \$250 million. Moreover the federal treasury may get up to half of the value of the grants under the R.D.I.A. back through income taxes, because of the differential tax treatment of grants under the current program.

Conclusion
Despite all the limitations cited for the current program, the conclusion still remains that the present program has been more effective and cheaper than the previous program. This can be attributed to the industry and area designations as well as to the judgement of incentives officers in the face of great constraints. Clearly, however, discretion in the present form has not reaped the hoped-for benefits. It is a two-edged sword: the incentives officer is not in a position to make categorical judgements from case to case on how much to give (including nothing); on the other hand, the applying company is never quite sure how much it can expect to receive.

