



Federal Election Economic Policy Primer



British Columbians and the rest of the country go to the polls on October 19. In voting, they will help to set the course for the nation's economy in 2016 and over the rest of the decade. In this pre-election briefing document, we outline some of the BC business community's priority issues, both for the election itself and for the agenda of the federal government that Canadians will choose on October 19. Note that our principal focus is on economic policy matters, broadly defined.

Economic Setting and Near-Term Outlook

Canada's economy lost momentum over the first half of 2015, largely due to the impact of sharply lower oil prices together with widespread weakness in the markets for many other traded commodities that form a large part of Canada's export basket. More recent data signal a modest pick-up in economic activity over the summer and into the early fall. However, for 2015 as a whole, real GDP growth for Canada is unlikely to top 1%, down significantly from an average of 2.2% over 2013-14.

At this point, there is little the federal government can do to address the soft economy of 2015. Most forecasters see the

economy gaining strength through 2016, in response to continued growth in the United States, some improvement in economic conditions in the EU, and a stabilization of oil and other commodity markets. Even so, real GDP growth is only expected to reach 1.7-2.2% next year.¹

It follows that the federal government elected later this month will assume office against the backdrop of an economy that is growing at a relatively muted pace; that has been hit hard by the downturn in global commodity markets – a development which has led to a sizable decline in Canada's terms of trade; and that has become overly reliant on residential investment and rising household debt levels to sustain activity.

The next federal government needs to frame and implement an economic policy agenda that will allow Canadian enterprises and workers to compete and succeed on the global stage. In our view, that agenda should focus on fostering greater innovation and productivity, strengthening the foundations of an increasingly knowledge-driven economy, and connecting Canada to growing external markets. With this in mind, below we identify six broad policy areas that we judge to be important to Canada's future economic success along with some specific suggestions for action in each area.

¹ September 2015 Canadian economic forecasts from RBC Economics, TD Economics, and BMO Capital Markets Economics; and the IMF's October 2015 forecast update.

Priority Policy Areas

The Business Council has identified the following high-level economic policy priorities which we believe the next federal government will need to tackle over the next few years.

Stable and Competitive Taxes



Canada currently benefits from comparatively low business income tax rates and reasonably competitive federal income taxes for most individuals and families. On the whole, these are positive features of the Canadian tax system.

In the business community, there is a strong preference for a broadly stable tax regime. There is concern that significantly higher income tax rates on enterprises, entrepreneurs and families may dampen future investment, job creation and new business formation.

Our specific recommendations to the next federal government on taxation are noted below:

- Consider new tax measures specifically targeted at boosting investment in machinery, equipment, software and advanced process technologies that are critical to increasing productivity in the business sector.
- As fiscal circumstances permit, expand the Working Income Tax Benefit, which strengthens work incentives and increases the after-tax returns from

working for individuals with low- to modest-paying jobs.

- Implement stepped-up tax enforcement focused on businesses and the self-employed, in order to improve the actual and perceived fairness of the income tax system. Increase the resources available to the Canada Revenue Agency for tax compliance, and accelerate efforts to combat tax evasion linked to the underground economy.
- If the government requires new revenue sources going forward, it should look first to the Goods and Services tax, which was reduced on two separate occasions a few years ago. Research by Finance Canada and academic experts confirms that the economic cost of consumption taxes such as the GST is lower than the cost associated with most other forms of taxation.² A broadly based consumption tax also has the advantage of reflecting the faster growth of service industries relative to goods-producing industries in the economy – and the larger role that services are playing within overall household consumption.

Credible and Realistic Budgets

In general, aiming for balanced government budgets makes sense – not least, because doing so helps to contain the constant pressure for higher spending. That said, it also makes sense to calibrate federal fiscal policy – i.e., whether to run surpluses or deficits – with an eye to the state of the economy and the expected near-term outlook. During periods of macro-economic

² B. Dahlby and E. Ferede, “What Does it Cost Society to Raise a Dollar of Tax Revenue? The Marginal Cost of Public Funds,” *C.D. Howe Institute Commentary*, March 16, 2011;

M. Baylor and L. Beausejour, “Taxation and Economic Efficiency: Results from a Canadian CGE Model,” *Finance Canada Working Paper 2004-10*, 2004.



weakness, countercyclical fiscal policy can help to offset any fall-off in private sector spending, thus mitigating the severity of a downturn. This insight was borne out, in both Canada and the United States, during the 2008-09 recession.

However, looking ahead, Canadian policy-makers need to be realistic about the economy's growth path. Canada's potential economic growth rate – defined as the growth of output, or real GDP, that is consistent with maintaining low and stable inflation – is lower than it was one or two decades ago, and is certainly no higher than 2%. It would be unwise to base fiscal planning on the assumption that the economy can (and will) expand faster than potential over the medium term. At the same time, government fiscal policy needs to take account of the impact of Canada's aging population and workforce – demographic trends that promise both to weigh on future economic growth and to magnify the fiscal pressures facing the public sector. Among other things, these considerations argue for keeping a close watch on the federal debt/GDP ratio, which currently stands at 31%.

Our specific recommendations to the next federal government on budget policy are noted below:

- Provided the economy is growing at or near potential, keep the federal budget balanced or in a small surplus position.
- Target the debt/GDP ratio, rather than the annual operating budget, as the most important fiscal variable to monitor and

to manage, and work to lower the ratio over time.

- In light of the growing fiscal burden that will materialize post-2020 due to an aging and more slowly growing Canadian population and workforce, the next federal government should commit to reduce the debt/GDP ratio to 25% by the end of the decade.

Getting Canadian Products and Services to Market



As a mid-sized economy with a diverse set of export industries – including several based on the country's extensive storehouse of natural resources – Canada needs access to foreign markets for our traded goods and services. And we must have the infrastructure in place not only to efficiently move Canadian goods to external markets, but also to enable imports of the commodities, intermediate goods and consumer products that Canadian households and businesses rely on. Unfortunately, Canada's performance as a trading nation has been mediocre at best over the past decade, with feeble gains in merchandise exports and a worrisome erosion of our market share in the United States. A paucity of new trade agreements and inadequate domestic infrastructure to facilitate trade and support the development of global-scale Canadian enterprises are among the factors that have hindered the country's international competitiveness.

Our specific recommendations to the next federal government to help get Canadian

products and services to market are noted below:

- Implement the Canada-EU Comprehensive Economic and Trade Agreement (CETA), which promises to strengthen trade, investment and other commercial ties with the vast EU market consisting of 500 million consumers and hundreds of thousands of sophisticated businesses.
- Complete the final technical and legal work on the Trans-Pacific Partnership (TPP) agreement, and ensure that Canada is part of the evolving trade and investment architecture in this important and economically dynamic region. We are confident the TPP will be beneficial to BC businesses, workers and consumers by expanding export markets, encouraging investment and giving British Columbians better access to competitively priced imports from TPP partner jurisdictions. Moreover, we believe it would be disastrous for Canada to be left out of a new trade and investment arrangement involving countries that collectively represent 40% of the global economy.
- Continue to invest in transportation infrastructure to enhance Canada's ability to participate in international trade, global supply chains and the expanding world tourism marketplace.
- Develop the infrastructure needed to allow Canadian energy and other resource industries to sell into offshore markets as a means to maximize the value of the country's resource wealth and support job creation and income growth at home. Make sure that domestic regulatory processes affecting pipelines and other infrastructure

development are aligned with this overarching national objective.

- Press ahead with the Beyond the Border Action Plan developed with the United States, with a view to establishing a joint Canada-US "perimeter" approach to security.
- Revisit current federal government policies that have raised the cost of air travel within (and from) Canada as a result of excessive fees, taxes and airport rents.

Building a More Innovative and Productive Economy



In an era of continuous and often disruptive technological change, many BC businesses are struggling to adapt and stay ahead of the curve. Others are working hard to develop leading-edge technology-based products and services for which global demand is growing briskly. For firms in every sector of the economy, innovation is becoming an imperative. Successful innovation, in turn, can pave the way to higher productivity at the enterprise level, and also for the economy as a whole.

Federal government support for innovation has been heavily oriented toward post-secondary and health-related research, along with the recently modified Scientific Research and Experimental Development (SRED) tax credit which is available to companies that invest in certain types of commercial and pre-commercial research and development.

The Conference Board reports that Canada ranks 12th among 16 peer nations in overall innovation performance. That is not good enough for a country that aspires to be a leading 21st century economy. As the Conference Board recently observed, “[C]ountries that are more innovative are passing Canada on measures such as income per capita, productivity and the quality of social programs.”³

Our specific recommendations to the next federal government to spur the development of a more innovative and productive economy are noted below:

- Consider new incentives to speed the movement of commercially-promising ideas and products to market by encouraging their adoption, commercialization and use. One option might be to establish an “innovation box” regime that lowers the tax burden on revenues earned from Canadian-developed patents and other technologies.⁴
- Streamline and improve application and approval processes for accessing federal direct funding programs for the ICT, life sciences, other high technology and advanced manufacturing sectors.
- Increase the financial and human resources allocated to the Industrial Research Assistance Program (IRAP), which is generally acknowledged to be the most successful and cost-effective of the federal government’s industrial support programs.
- Put a high priority on the further development of digital infrastructure

through direct funding as well as by exploring mechanisms that incent increased private sector capital to build out this key enabling sector.

- Use federal government procurement to provide better market access for innovative products and technologies developed by Canadian firms.

Advancing Talent and Skills



A strong education system and a high quality workforce are among the most essential ingredients for a prosperous and competitive Canada. The federal government has an important role in meeting the nation’s human capital needs through its management of the immigration and Employment Insurance systems, its financial contributions toward education at the university and college levels, and its oversight of the broad Canadian labour market. Effective human resource planning is not a simple matter in a country as large and as heterogeneous as Canada. That the provinces have the primary responsibility for education as well as for employment standards, occupational licensing and many other aspects of labour market policy complicates the picture and calls for close intergovernmental collaboration in areas such as immigration, foreign credential recognition, and labour mobility.

Immigration policy will be central to workforce development in the coming decades. In BC, for example, immigrants are

³ Conference Board of Canada, “How Canada Performs: Innovation,” www.conferenceboard.ca/hcp/details/innovation.aspx.

⁴ Nick Pantaleo, Finn Poschmann and Scott Wilkie, “Improving the Tax Treatment of Intellectual Property Income in Canada,” C.D. Howe Institute, April 2013.

projected to account for more than two-thirds of the net growth in the working-age population through 2031. Given the patterns of seasonal work in some parts of the country, the impact that large-scale resource and infrastructure projects can have on the demand for skilled labour, and the small size of local labour pools in many rural and remote regions, Canada can benefit by allowing employers to access temporary foreign workers as well as by maintaining regular streams of permanent immigrants.

Our specific recommendations to the next federal government with respect to talent and skills development are noted below:

- Canada needs better and more timely labour market information, as the federal government itself recognized in the most recent budget. Past federal-provincial discussions, through the Forum of Labour Market Ministers, have failed to produce substantive results in this area. Accordingly, the federal government should take the lead to establish and operationalize an improved and regularly updated system of high quality labour market information.⁵
- The BC business community generally supports the changes that have been made to federal policies affecting permanent immigration over the past few years – including the shift to the Express Entry system and the creation of the Canadian Experience Class. Looking ahead, the federal government should continue to modify immigration policy and immigrant selection criteria to ensure appropriate alignment with the

country's labour market and economic needs over the medium- and longer-term.

- There is a legitimate place for a temporary foreign worker (TFW) program as part of the federal government's immigration policy toolkit. The main focus should be on: i) defined categories of TFWs (e.g., seasonal agricultural workers and live-in caregivers), ii) foreign workers who have particular skills needed to develop large projects and/or fill jobs in remote/rural areas, and iii) well-paid workers who possess specialized academic, professional or technical expertise that employers in Canada require to succeed and to grow.
- As an alternative to a revamped TFW program, the federal government could consider the idea of a new "introductory visa" program that would allow employers to access TFWs – with the proviso that those holding such visas would have the opportunity to achieve permanent residency status over time, based on rules to be determined and administered by Citizenship and Immigration Canada.
- Post-2020, the federal government should consider options for further changes to pension, EI and tax policy designed to encourage a greater number of older workers to stay in the labour force.

⁵ Don Drummond, "Wanted: Good Canadian Labour Market Information," Institute for Research on Public Policy, *IRPP Insight*, June 2014.

First Nations Engagement and Economic Development



British Columbia is home to almost one-third of all First Nations groups in Canada; it is also the province where the role of First Nations in economic development arguably has increased most significantly. The Business Council strongly supports continued efforts to achieve reconciliation between First Nations and the Crown through various types of government-to-government agreements as well as via greater participation by aboriginal communities in all aspects of the province's economic and social development. The business community in BC has an important part to play in advancing this work.

Progress in this complex legal and policy domain depends on a collaborative approach and a common understanding between the federal and BC governments. It also requires that the national government show leadership and commit the resources necessary to build and sustain constructive relationships with First Nations. While the BC government has primary jurisdiction over land and resources in the province, the federal government is an essential partner and player on most matters touching the interests of First Nations. In our judgement, in recent years the necessary level of federal government engagement has not always been evident when it comes to First Nations in British Columbia.

⁶ Forging Partnerships, Building Relationships: Aboriginal Canadians and Energy Development, Report of the Special Federal Representative on West Coast Energy Infrastructure, 2013.

Our specific recommendations to the next federal government in this area are noted below:

- Continue to implement the recommendations outlined in the report of the Special Federal Representative on West Coast Energy Infrastructure in his 2013 report (the "Eyford Report"⁶). The Business Council supports all 29 recommendations contained in Mr. Eyford's report.
- Act on the recommendations developed by Mr. Eyford in his subsequent report to the Minister of Aboriginal Affairs and Northern Development Canada on renewing the comprehensive land claims policy.⁷
- Increased support for First Nations youth to improve educational outcomes and attainment.
- Allocate additional federal funding to support and encourage enhanced First Nations' participation in economic development in British Columbia.

Conclusion

The Business Council of BC appreciates the opportunity to share our perspectives on the economic policy challenges facing the country and the actions that the next federal government needs to take in order to make Canada one of the best jurisdictions in the world in which to invest and do business.

We look forward to the working with the federal government that Canadians elect to office on October 19.

⁷ A New Direction: Advancing Aboriginal and Treaty Rights, Report to the Minister of Aboriginal Affairs and Northern Development Canada, 2015.