

INTERNAL MOBILITY AND THE WELL BEING OF CANADIANS

(Transcribed presentation as edited by author)

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I THINK MARC'S PRESENTATION is a hard act to follow. I actually agreed with a lot of what he said in terms of how we should balance the issues. I disagree with him on whether the *Agreement on Internal Trade* is the right balancing tool or the wrong one for enhancing Canada's economic prospects, while at the same time preserving very high standards in a lot of areas of public interest and public concern. I personally think the *AIT* is the right tool – we can get into that debate a bit later – but I think Marc's presentation was very balanced.

I was very pleased to hear Marc talk about provincial rights, flexibility, the nature of federalism, which I would contrast with the imposition of national standards in areas of provincial jurisdiction. And I was very pleased to hear about the progress we have made over the past 134 years of, as he calls it, 'nation-building', although as an economist I might think more in terms of building a sizeable internal market with a common currency and so on. As a result, we Canadians are able to trade so much more easily with each other than we are with the United States, even with the Canada-U.S. Free Trade Agreement, and that's as it should be.

Somewhat in contrast, Marc also talked about 134 years of inertia. And indeed, regarding the topic of this conference, I agree that there has been inertia in getting rid of a patchwork of provincial regulations. Not getting rid of the regulations, mind you, but getting rid of a sometime incoherent patchwork where labour mobility, transportation and other areas relevant to Canadians' economic relations with each other are concerned. (Note: in this text, by "provinces," I include the territories).

I don't think anybody disputes the fact that internal trade barriers are not the greatest problem – sorry if I offend the organisers of the conference – facing the country today. Whether obstacles to trade are currently costing us half a percent or two percent of GDP, we clearly have other problems that are even bigger. And furthermore we don't want whatever we do to remove those barriers to hinder our efforts at solving other problems, perhaps more pressing, in other areas of public policy. And so there I completely agree with Marc. I think we need to get the proper sense of perspective.

I. THE IMPORTANCE OF OPEN INTERNAL TRADE FOR GROWTH

BUT I THINK THAT ADOPTING A PROPER PERSPECTIVE also requires us to think a little bit about why we are trying to remove obstacles to trade and mobility in the first place. The studies that were quoted and often rightly critiqued by the previous speaker tended to focus on the issue of the enhancement of our economy's efficiency. The question these studies were trying to answer can be summed up as follow. How much more money would Canadians make on average if we allowed Canadian resources, capital and labour force to be employed in serving a single Canadian market, instead of a market fragmented into a number of provincial and territorial jurisdictions?

It does turn out that these calculations show that, while removing some barriers to procurement, agricultural trade and so on, would indeed leave most Canadians somewhat better off, the number is not very high – in most cases less than one percent of GDP. But that is just what we would gain by using existing resources more efficiently – a one-off gain. There are other issues with building a more open internal market that speak to the building of a more dynamic economy – one that is better at fostering future growth opportunities.

And here I would like to point out that large multinational corporations often can get around a lot of the barriers and in fact they do so on a regular basis in dealing, not just within the country, but especially in dealing between Canada and other countries. They have the size and the resources to overcome the barriers. This is often not the case for small or medium-sized businesses, which have been less dynamic here than in the United States, where these businesses tend to grow more easily into larger concerns than in Canada. And in terms of factors influencing the growth of small and medium size businesses, the existence of internal barriers constitutes a big difference between the Canadian and US markets.

If small Canadian firms want to grow, they have to turn first to the Canadian market, and indeed that's what surveys show they tend to do. This is probably because there are so many obstacles that remain in accessing the geographically close US market. These obstacles include procurement preferences, threats of anti-dumping duties, having to prove the origin of your product in order to qualify for duty-free status, restricted mobility of personnel, and regulatory barriers. But these remaining difficulties in accessing the US market only accentuate the need to strengthen access by Canadians to the domestic market.

II. LET'S NOT COPY FOREIGN BARRIERS WITHIN CANADA

YOU KNOW IT'S QUITE INTERESTING THAT AS CANADIANS we complain when the US Department of Agriculture imposes what does seem to me to be some excessive restrictions on Canadian potatoes, due to a (non health-threatening) problem with a tiny fraction of the PEI crop. But at the same time many people seem quite flustered by the *AIT* dispute settlement process that has come out against restrictions on PEI imports of milk products from Nova Scotia – which were clearly imposed without any legitimate reason, as an *AIT* panel found after a thorough investigation.

In the latter case, the *AIT* dispute settlement panel in effect asked PEI to give a reason, like a health protection reason, for stopping the imports from coming in. Something that you could justify under the *AIT* because the *AIT* is very clear about the right of provinces to stop trade, if need be, in order to retain the ability to enforce their standards of all kinds where provincial governments have legitimate public concerns. But PEI could not do so, leading to conclusions that they were simply trying to protect their own industry at the expense of their neighbour's. Well, it seems to me that complaining on the one hand about being denied access to the US market on spurious ground while also complaining about an agreement we have that removes those similar barriers in Canada, is not necessarily very logical.

Another relevant comparison, between our stance on external trade and that on internal trade involves, and now I am moving away from the small business angle, the bidding wars between Bombardier of Canada and Embraer of Brazil, who are using their respective governments as proxies in these wars. And when you think about both the Canadian and Brazilian governments financially helping these companies fight for contracts, every commentator I know has said that such behaviour is a negative-sum game. But it is one that the parties feel they have no choice but to engage in, for fear that the outcome would be even worse if they let the competitor run away with contracts. I am not saying that each party individually is wrong to play this game, because you could certainly argue that this is one of those cases where we need a mutual agreement, rather than unilateral disarmament, before stopping. So I do not want to pronounce on this particular case.

But contrast the response to this international case – a general agreement (except of course from U.S. and other plane purchasers) that these government-supported bidding wars are ridiculous – with lukewarm national support for the *AIT*. The *AIT* has sought to reduce similar bidding wars between provinces by including a modest subsidy code among

Canadians. Why is that not a good thing, an important achievement in ensuring that public funds in Canada are not used to undermine a sister province's economic activity? So I see some contradictions there in terms of barriers that we are complaining about at the national level and our lack of support for the *AIT*, which seeks to remove similar barriers at home.

So, there are all kinds of barriers that our businesses face in accessing the international market. The way to grow, the way to start growing, is by accessing the Canadian market, and this is one reason why we have more internal trade within Canada, relative to our population and vast distances, than with the United States. And so if there is an agreement such as the *AIT* that removes some barriers, even at the margins, provided that it doesn't create a huge bureaucracy to administer the *agreement*, I think that is a good thing.

III. INTERNAL MOBILITY REDUCES RISK

NOW ECONOMISTS TEND TO THINK IN TERMS OF ECONOMIC EFFICIENCY and economic growth – usually measured in monetary terms using Gross Domestic Product – when they think of open markets. But there has recently been a lot of public discussion, and quite rightly so, about GDP not necessarily being a good measure of welfare. And that's true. You don't want welfare to be judged only in terms of purchasing power and material accumulation. One other basis on which you want to judge your welfare is how secure your position is. How much risk you are facing in terms of your job, your markets, your incomes? And here I think that strengthening the internal market really reduces risks for Canadians. If things do not go very well in your province of origin, are your qualifications going to be accepted in another province? If you are a firm operating in one province and there is an economic downturn in that province, are you able to compensate by having access to, for example, procurement opportunities in another province? I think that having access to opportunities across the country is a very important way by which Canadians help share economic risks and rewards – i.e. diminish the risk that each region would face as a stand-alone economic unit.

There is in this respect a very interesting paper by Michael Goldberg and Maurice Levi, which was published a few years ago in *Canadian Public Policy*.¹ It was written in the context of our constitutional debates, but I think that it is very relevant to the discussion about internal trade.

¹ Michael A. Goldberg and Maurice D. Levi (1994). "Growing Together or Growing Apart: The Risks and Returns of Alternative Constitutions of Canada" in *Canadian Public Policy – Analyse de Politiques*, XX:4:341-352.

This paper makes the case that Canada constitutes an efficient portfolio, in the sense that given the "return" earned by our economy (GDP), the risk we face in terms of variability of GDP is about as low as it can get. That is, relative to the current configuration between provinces and territories, we couldn't lower the volatility of GDP even if we could somehow make specific provinces more or less important than they currently are in the Canadian portfolio, or even cast one or more province aside. This desirable result stems from the differences in economic strengths between the regions of Canada.

Conversely, given the low "risk" attendant to the Canadian portfolio (due to low covariance between the GDP of the various provinces), the returns (GDP growth) are, under the current political arrangements, about as high as you could hope for. That is, you couldn't somehow change the weights of the country's constituent parts and get higher GDP growth for Canada overall, without paying some price in terms of economic instability.

Goldberg and Levi's approach looks not just at the contribution of the economic union to the average standard of living, but also argues that Canada, as a good portfolio should, minimizes the variability in outcomes for its citizens. They explain that both interregional transfers and open internal trade are two mechanisms through which this result is concretely felt. Their result underscores that we are a less risky proposition as a single market than if we were separate economic units.

For example, when oil prices go up, an event which is not under Canada's control, we all know that oil producing regions in the country benefit, while oil-consuming regions are going to suffer somewhat as a result. But if you couldn't easily move human resources or bid for contracts from one part of the country to another, these shifts would be at the same time less beneficial for the oil-producing region and costlier for the oil-consuming region. Furthermore, the outcome would be riskier for both regions. If we didn't have labour mobility or an open procurement process, something which the *AIT* is trying to strengthen, there would still be winners and losers each time oil prices go up or down. But everyone would end up with a costlier and riskier economic proposition, because the country as a whole would not be able to make the best out of shifting economic circumstances.

Note that it is not the movement of people or trade between provinces itself that constitutes the ongoing benefit in this context, but the ability to do so, which makes your situation more secure. This is not something that is captured in GDP.

IV. REGIONAL DEVELOPMENT AND THE AGREEMENT ON INTERNAL TRADE

WHILE IT IS IMPORTANT TO ALLOW ALL CANADIANS to partake in economic growth that takes place in one region or another, something which is helped by open internal trade and easier mobility, it is also important to ensure that each region attains its economic potential. Paying individuals to stay in one place, when their services are needed and would be rewarded in another region, does not constitute sound economic policy. But mobility is not an end in itself, only a way for businesses and individuals to tap economic opportunities that may not exist in their own region. In this context, stimulating regional development may make sense if it means that individuals from a region find more permanent and rewarding employment opportunities closer to home.

This being said, you want to make sure that you do in fact build a more dynamic regional economy under the regional development rubric, since this is the only economically valid goal for such programs. I am taking for granted that economic development programs imply that some preference – such as procurement or employment preferences – will be granted to individuals or firms from a region. This does seem to fly in the face of open, non-discriminatory trade principles, however. So what does the *AIT* say about such discriminatory trade restrictions taken in the name of regional development?

The *AIT* say, roughly speaking, that regional development is a valid reason to allow special treatment for individuals or firms from a disadvantaged region, provided that you report to your partners in confederation on the results of your policy. That is, if you stop other Canadians from bidding or being employed on a project because they are not from the region designated as disadvantaged, you should explain why and how this helps in fact develop your region. The idea is that what you are doing is not simply to favour established firms in your area, for example. I think this obligation to justify your discriminatory policies is a fair price to pay, I would say a reconciliation, between the objectives of regional development on the one hand and the objectives of making sure that all Canadians have access to opportunities in every region when they present themselves.

In summary, we should not think of trade within Canada, and of the *AIT* more specifically, only in terms of an increase in economic efficiency. We should think of it in terms of the dynamism of the small-medium business sector, that is, future growth for the country, and we should also think of it in terms of helping to reduce economic risks for everyone. Short of joining up with the United States, which would entail the huge

cost of abandoning the institutions we have built in this country over far longer than the 134 years since Confederation, building on the advantages of the Canadian economic portfolio is a smart strategy on all grounds.

V. WHERE DO WE GO FROM HERE

I HAVE INDICATED ALONG THE WAY WHY I THINK THE *AIT* is the right tool for the job, as far as drawing out the advantages of the internal market is concerned, while preserving the benefits of a decentralized federation. But a better job can and should be done, by building around this instrument. For a start, we should focus on completing the *AIT* itself. There are a lot of promises in that agreement, many of which are falling behind schedule. This is the case for the important labour mobility provisions, the promised reporting on regional development programs, and many others. As I have explained the importance of these provisions, I am naturally all in favour of completing those under the terms of the *Agreement*.

I think we should also address, as the Europeans did some fifteen years ago now, the question of whether we should continue to progress by consensus, or whether we should actually have a weighted majority system regarding internal trade matters. This would ensure that a single province could not stop progress on a particular issue under already agreed upon terms of the *Agreement*. I think the EU got the formula right, by saying in effect, "look, we want to agree, we want unanimity on the principle of what we are trying to achieve, but the nitty-gritty of specific technical measures can be adopted by qualified majority voting". Otherwise, the problem is that some participant can always hold out for more advantages on a question of detail, rather than on a question of principle. And I think that we could usefully adopt that model. That is to say, once you agree on the principles and the end game, any one province or territory could not block implementation at the technical level, as long as the vast majority of others agree on how the unanimously agreed objective is to be implemented.

I reiterate that there is nothing in the *AIT* that commands that we all have to have the same standards, if there are truly large differences in needs between provinces with respect to certain standards. But I think we could usefully attempt to devise a common national template for standards in a lot of areas (as the EU countries did as a base for mutually recognizing each other's standards). Markedly higher standards than the national norm could then be allowed, according to specific provincial circumstances, where there is an objective need for them, or simply where a provincial electorate wishes explicitly to adopt a much higher standard.

But small and often unnecessarily costly differences would tend to disappear. Again, such a process could be built around the *AIT* as currently formulated.

So, I would sum up this last part of the discussion by saying that the *AIT* is a very flexible instrument around which more could be done to strengthen Canada's economic portfolio. But perhaps it is too flexible in that its implementation is lagging behind the promises it contains, and not flexible enough in terms of decision-making process, requiring as it does consensus on every minute decision.

Thank you for your attention.