

A Federal Economic Agenda for Ontario

Discussion Paper

Mowat Centre

ONTARIO'S VOICE ON PUBLIC POLICY

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Introduction

What is the Federal Economic Agenda Project?

The Mowat Centre, the Institute for Competitiveness and Prosperity, and the Northern Policy Institute are collaborating with a broad range of Ontario's key economic stakeholders to develop a Federal Economic Agenda for Ontario leading up to the next federal election, expected in October 2015.

Through this consensus-based initiative, our goal is to define clearly the challenges and opportunities facing Ontario, develop a common vision and agenda on key economic issues, inform public dialogue, outline policy options that could be pursued by the federal government, and inform platform development by political parties in the lead up to the federal election.

We believe that an economically vibrant Ontario is in the interest of every Canadian. Ontario is home to over 38% of the Canadian population and its share of national GDP, 37%, is nearly twice the size of Quebec's and more than double Alberta's. As the country's largest exporter of goods and services and with 50% of the Canadian knowledge-sector workforce, Ontario's success will be crucial to the country's prosperity in the decades ahead.

The challenges, opportunities and options facing Ontario should be important to federal parties during the next year. The Ontario economy is facing global forces that are producing a once-in-a-century transformation in the provincial economy. These forces include globalization, digitization, urbanization, climate change, a sustained commodity boom, and a decline of traditional employer-employee relationships. The approaches that worked for Ontario's industrial age may no longer fit the 21st century.

This discussion paper is intended to serve as a basis for conversations with a broad range of Ontarians who are interested in the province's economic

future. As a starting point, we would propose five objectives that a federal policy agenda should support:

- » increased labour force participation;
- » increased productivity;
- » improved economic opportunity for all and reduced poverty;
- » increased exports; and
- » an improved federal fiscal framework that supports Ontario.

This discussion paper focuses on seven issues that require attention from the federal government if we are to see measureable progress in achieving the five goals we have identified:

- » Infrastructure
- » Workforce development
- » Immigration
- » Trade and investment
- » Innovation
- » Federal transfers
- » Targeted strategies for sectors and regions

In all these areas, cross-cutting themes emerge, such as greater Aboriginal participation in the labour market and economic opportunity for young people.

Please read this short paper and provide your advice on the issues it raises. Based on the advice we receive and additional research we are conducting, our intention is to release *A Federal Economic Agenda for Ontario* in the spring of 2015 to help shape the policy debate in advance of the federal election.

Why does Ontario need a Federal Economic Agenda?

Ontario has historically been a desirable place to live, work and prosper. Our competitive business environment, safe communities, stable government, diverse population, access to natural resources, and high quality education and social programs have attracted people and investment from around the world throughout our history. A prosperous Ontario has historically been the foundation of a strong Canadian economy.

Despite all of these assets, Ontario is facing a clutch moment. The economy is growing at a slower pace than it once did, and is expected to continue to do so well into the future.¹ Lagging innovation and productivity, weak job growth (particularly for youth and immigrants), an ageing population and large public debt loads are amongst the many challenging issues facing governments and policy-makers.

A clear understanding of these challenges, along with realistic policy options to respond, is necessary. In October 2015 voters from across the country will cast their ballots in the federal election. There is currently no federal agenda uniquely designed to respond to the forces, challenges and opportunities facing Ontario or a strategy designed to strengthen the Ontario and, by extension, the Canadian economy.

While the provincial and local governments, the private and not-for-profit sectors, labour and others all have a significant role to play in addressing the challenges outlined in this discussion paper, our project is focused on the federal role. Some issues cannot be left to any actor than the federal government. For example, the structure of fiscal federalism continues to shift resources away from rather than towards Ontario at a time when Ontario's fiscal capacity and GDP are below the national average. The fact that the suite of federal fiscal transfers leaves Ontario worse off rather than better off is something that the federal government alone can change.

1 Government of Ontario. Ministry of Finance. 2014. Ontario's Long Term Report on the Economy. <http://www.fin.gov.on.ca/en/economy/ltr/>

Drivers of change and impacts on Ontario's economy

The last decade has seen enormous change in the structure of the global, Canadian and Ontario economies. It is likely that the next decade will continue to demonstrate structural and disruptive change. Globalized trade and increased competition, the rise of the Canadian dollar, the financial crisis and subsequent recession, the rise of emerging markets and a new middle class, and the sustained commodity boom have each, in their own way, been experienced by Ontario.

The consequences of these larger global forces are well-known to Ontarians:

- » growing income inequality, wage stagnation, and an increase in precarious employment, which now accounts for almost a quarter of all employment in Ontario;²
- » low productivity growth, with both Ontario and Canada experiencing over the past 30 years a sustained plateau in productivity growth compared to our peers³;
- » high levels of public debt; and
- » the striking decline of the manufacturing sector, which has shrunk by 30% and 300,000 jobs over the past decade.

While governments cannot control the forces that are shaping economies globally, they can react to them. They should use the wide variety of policy tools at their disposal to anticipate and respond to these disruptive forces to support communities in their efforts to emerge stronger from this period of transition.

The forces have been experienced differently in different parts of the province, with mid-sized communities with a heavy reliance on manufacturing being particularly hard-hit. But no part of the province has been immune to the forces or the

2 Law Commission of Ontario 2012. *Vulnerable Workers and Precarious Work. Final Report.*

3 Government of Ontario. Ministry of Finance. 2014. Ontario's Long Term Report on the Economy. <http://www.fin.gov.on.ca/en/economy/ltr/>

problems that have been caused. In many parts of the province there is widespread anxiety about the future. Nearly 60% of Ontarians expect that the next generation will be worse off 25 years from now than people today.⁴ Despite this loss of confidence, there are also enormous opportunities that can be seized during this period of global and national economic re-structuring. An engaged federal government is necessary for communities across the province to build the foundation for the next era of Ontario's prosperity.

Opportunities for Future Prosperity

Ontario has many strengths, and with the right efforts by governments and other actors, is well-positioned for future prosperity. A diverse, well-educated population; a competitive tax environment; vibrant safe cities; a dynamic global city-region; a healthy ecosystem with access to water, natural resources and arable land; and a diversified economy with globally competitive firms and clusters will continue to support economic growth, job creation and attract foreign direct investment. This discussion paper is intended to support a conversation that will lead to a credible actionable federal agenda to support the next wave of Ontario prosperity.

The federal government controls many of the levers required to unleash Ontario's full economic potential. This paper suggests some of the possible ways those levers could be deployed. Upon completion of this project, our hope is that all Ontarians will have an evidence-based resource to use to raise important issues with federal political parties during the next federal election. Our goal is that all federal parties clearly articulate how they will work with the Ontario government, stakeholders and specific communities and sectors to ensure that Ontario has a strong economic future in the coming decade.

⁴ http://www.ekospolitics.com/wp-content/uploads/full_report_october_17_2013.pdf

Infrastructure

In Ontario, transit and core infrastructure are in need of repair and are necessary to ensure future economic growth. An ageing capital stock built mostly in the 1950s and 60s, years of underinvestment and the downloading of a large portion of public infrastructure maintenance to municipalities has resulted in significant gaps in Ontario's infrastructure investment and stock, with this amount for Ontario municipalities pegged at \$60 billion.

- » Current levels of total public investment in infrastructure (by federal, provincial and local governments) fall shy of optimal levels by two percentage points of GDP.⁵
- » Municipal governments are responsible for the majority of infrastructure in Ontario but lack fiscal capacity to finance needed infrastructure projects. Additionally, under the present funding arrangements, provincial and municipal governments bear the brunt of the financial risk for infrastructure investments—taking on 88% of infrastructure risk, while the federal government covers only the remaining 12%.
- » New infrastructure delivery and funding models, such as P3s, infrastructure banks (“IBanks”), Asset recycling programs, Green Bonds and Community Benefit Agreements are providing governments’ with innovative opportunities to capitalize on new infrastructure investment opportunities.

5 Smetanin, P., Stiff, D., and Kobak, P. 2014. Ontario Infrastructure Investment: Federal and Provincial Risks & Rewards. The Canadian Centre for Economic Analysis.

Policy Challenges

- » GTA's ageing transportation infrastructure contributes to traffic gridlock and shipment delays that amount to an annual loss of \$2 billion for the region. Numerous studies have also demonstrated the linkages between infrastructure investment and manufacturing sector productivity.⁶
- » Much of the infrastructure built in Canada during the previous century was not designed for emerging policy challenges, such as increasingly common extreme weather events and the risks posed by climate change; increased density of urban areas, an aging population; and the integration of digital and mobile technologies into transportation and energy systems.
- » Current funding models and approaches do not provide sufficient stable revenue to ensure adequate investments for either building or maintaining critical infrastructure.

Opportunities

- » As outlined in the 2014 Ontario Budget, Ontario plans to invest \$130 billion in infrastructure construction over the next 10 years. The federal government has committed to a 10-year Building Canada Plan, of which Ontario will receive \$2.72 billion, and just over \$3.874 billion in federal gas tax funding for Ontario municipalities from 2014 to 2019.
- » The need for infrastructure funding has come into governments’ focus: an Infrastructure Summit, hosted by the Premier of Ontario, where Premiers, Ministers and stakeholders met to discuss infrastructure needs and opportunities, took place in August 2014.

6 TD Bank Financial Group. 2004. In: The Foundations of a Competitive Canada: The Need for Strategic Infrastructure Investment. Canadian Chamber of Commerce. 2013. http://www.chamber.ca/media/blog/131218-The-Foundations-of-a-Competitive-Canada/131218_The_Foundations_of_a_Competitive_Canada.pdf

Discussion Questions

- » Which intergovernmental infrastructure arrangements and partnerships can establish clear shared priorities and have appropriate policy, funding, and delivery roles for federal, provincial and local governments?
- » How can governments ensure that infrastructure investment links to broader public policy goals (i.e. the development of healthy communities, diversifying trade, and enhancing productivity) and align with economic development strategies?
- » How can governments support and capitalize on different models and financing mechanisms to deliver infrastructure more efficiently and effectively?
- » Which new nation-building and province-building infrastructure investments should be considered?
- » What criteria should the federal government use to determine which infrastructure to fund to achieve the outcomes we are trying to achieve?
- » Should the federal government play a more active role in ensuring that infrastructure is built in Ontario? What should that new role be?

Further Reading

Cautillo, C., N. Zon and M. Mendelsohn. *Rebuilding Canada: A New Framework for Renewing Canada's Infrastructure*. Mowat Centre publication no.92.

Fenn, Michael. *Recycling Ontario's Assets: A New Framework for Managing Public Finances*. Available at: <http://mowatcentre.ca/wp-content/uploads/publications/85-recycling-ontarios-assets.pdf>

Smetanin, P., Stiff, D., and Kobak, P. 2014. *Ontario Infrastructure Investment: Federal and Provincial Risks & Rewards*. The Canadian Centre for Economic Analysis. 2014.

Workforce Development

Ensuring that Ontario educates, attracts and retains the best workers is essential to the province's prosperity. In the short-term, Ontario continues to experience higher unemployment rates relative to the national average, especially among youth, recent immigrants and Aboriginal populations. Many workers are having trouble finding full-time work in their field, while some sectors are concerned about skill shortages. In the longer term, there are concerns about slow labour force growth, with fewer Ontarians amongst the working age population.

- » Ontario represents 39% of the Canadian population, yet almost 42% of unemployed Canadians reside in the province. Youth unemployment in Ontario, at 16.1%, is also higher than the Canadian average of 13.7%.
- » Ontario's current share of Labour Market Development Agreement funding does not reflect the province's share of population, unemployment or EI contributions.
- » Federal-provincial engagement on labour market investments and programs has been characterized by a high degree of tension. The proposed Canada Job Grant (CJG) is meant to expand labour market training to workers not eligible through EI, but the program does not offer new funding, creating an additional fiscal burden on the province while jeopardizing existing well-functioning programs.
- » The Temporary Foreign Workers (TFW) program has been popular with employers and has been used to fill short-term labour shortages. However, concerns about program misuse have led to increasing worry about displaced Canadian workers, lower employer investments in training for Canadians, and a downward pressure on wages.

Policy Challenges

- » Most workers in Ontario in need of training, including the long-term unemployed and those currently employed in low-skilled jobs, are not eligible for federal training programs.
- » More workers in Ontario today are faced with precarious employment situations. Between 2001 and 2012, routine-service jobs (e.g., retail, clerical posts, food service) that are precarious rose by 33%, nearly twice the overall growth rate of routine-service jobs. Nearly half the Toronto CMA workforce is employed in routine-service jobs.⁷
- » Fewer Ontarians are expected to be of working age, with the ratio of those in the labour force to those outside ("the dependency ratio") continuing to decline.⁸ Ontario will rely on immigration for almost all of its labour force growth in coming decades.⁹
- » A lack of accurate labour market information, particularly at the local level, inhibits the ability of governments to accurately combat skill shortages and mismatches. The federal government has recently taken commendable steps to improve labour market data, but more work remains to be done.

Opportunities

- » The new Canada Job Funds agreements could potentially grant provinces greater flexibility in funding labour-market development.
- » By 2026, the on reserve First Nation population is expected to increase by 64%, to 667,900.¹⁰ Serious

7 Institute for Competitiveness and Prosperity. 2013. Untapped Potential: Creating a better future for service workers. Working Paper 17. http://www.competeprosper.ca/uploads/WP17_FINAL_V2.pdf

8 Government of Canada. 2013. Update of Economic and Fiscal Projections. <http://www.fin.gc.ca/efp-pef/2013/pdf/efp-pef-13-eng.pdf>

9 Government of Ontario. 2014. Ontario's long-term Report on the Economy; Chapter Chapter 1. <http://www.fin.gov.on.ca/en/economy/ltr/2014/ch1.html>

10 Bennet, Paul W. and Anuik, Jonathan. 2014. Picking up the Pieces: A community-school-based approach to first Nations Education Renewal. Northern Policy Institute

discussions on how to address historical failures, under funding and community engagement to enhance education and labour force participation of our aboriginal population are starting to occur..

- » New projects and emerging sectors, such as the development of the Ring of Fire, create an opportunity for integrated labour force planning in smaller communities and improved training for Aboriginal populations.

Discussion Questions

- » Are there labour market training approaches that can ensure that more Ontarians benefit from economic growth?
- » What are the key changes that must be made to EI?
- » How can other parts of the system (e.g. LMAs, CJG, TFW) be leveraged to improve outcomes for those experiencing under/unemployment?
- » What employer-based approaches—i.e. “demand approaches”—can be used to improving the training regime?
- » Are there policy or fiscal tools to encourage more Ontarians to stay in the labour force longer?
- » What changes to Statistics Canada and the collection and distribution of labour market data should be considered?

Further Reading

TD Economics. 2013. *Jobs in Canada: Where, What and For Whom?* Available at: <http://www.td.com/document/PDF/economics/special/JobsinCanada.pdf>

Mendelson, Michael and Zon, Noah. 2013. *The Training Wheels Are Off: A Closer Look at the Canada Job Grant.*

Immigration

Ontario will rely almost entirely on immigrants for future labour force growth. However, immigration to Ontario has declined in the last decade by roughly 30%, due to the increased attractiveness of other Canadian provinces, competition from other countries, and policy changes introduced by the federal government. Once here, newcomers experience higher un- and under-employment and skilled professionals continue to face obstacles working in their field.

- » The Federal Skilled Worker program, the main source of immigrants to Ontario and Canada, has been reduced by over a third since 2001.
- » The federal funding formula for immigrant settlement services, which is supposed to be structured on an equal-per-client basis, allots less to Ontario than some other provinces. This is particularly significant as many immigrants are ineligible for job training and employment programs funded through EI.

Policy Challenges

- » Over the last decade, overall immigration to Ontario has fallen by 30%, while the share of economic class immigrants has fallen even further, by nearly 50%. As the balance of immigration shifts towards the Temporary Foreign Worker program and non-economic admissions classes, Ontario loses the opportunity to benefit from immigrants' long-term success and commitment to Canada.
- » Compared to previous generations, immigrants to Ontario are seeing lower wages and higher unemployment.¹¹ Newcomers seeking employment in regulated professions face significant accreditation challenges. In the Toronto region alone, delays associated with credential recognition have estimated costs between \$1.5 - \$2.5 billion to the local economy.¹²

11 Statistics Canada. 2013. Analysis of the Canadian Immigrant labour market, 2008 to 2011. <http://www.statcan.gc.ca/pub/71-606-x/2012006/part-partie1-eng.htm>

12 Toronto Region Board of Trade. 2013 Federal Pre-Budget Submission. <http://www.bot.com/advocacy/Documents/BudgetSubmissions/Federal/2013FederalPre-BudgetSubmission.pdf>

Opportunities

- » Ontario is poised to pass a new immigration act that would enable the province to work more closely with the federal government on recruitment, selection and admission of skilled immigrants to Ontario.
- » There is growing awareness that immigrants are not performing as well economically as previous generations and a growing focus on how the economy can be more inclusive.
- » Federal and provincial governments are piloting a new Express Entry system (formerly the Expression of Interest model) that would allow employers greater involvement in the immigrant selection process based on needed skills.

Discussion Questions

- » How can the current system of federal immigration supports and programs (e.g. settlement services, labour market opinion process) better serve the needs of newcomers and employers?
- » How should Ontario work with the federal government on the new Express Entry model?

Further Reading

Expert Roundtable on Immigration. 2012. *Expanding Our Routes to Success: The Final Report by Ontario's Expert Roundtable on Immigration*. Available at: http://www.citizenship.gov.on.ca/english/keyinitiatives/imm_str/roundtable/roundtable.pdf Conference Board of Canada. 2014. Do Recent Immigrants Advance Canada's Export Agenda?

Bitran, M., and S. Tan. 2013. *Diaspora Nation: An Inquiry into the Economic Importance of Diaspora Networks in Canada*. Mowat Centre Publication no.72. Available at: http://mowatcentre.ca/wp-content/uploads/publications/72_diaspora_nation.pdf

Trade and Investment

While international trade and investment present key opportunities for Canadian business growth, export and outward investment have nearly flat-lined in recent years as a result of low productivity growth, increased global competition, persistently high exchange rates, and skill shortages. These factors help to explain Ontario's reduced export competitiveness, especially among SMEs, few of which engage in any export activity.

- » In recent years, persistently-high exchange rate drastically reduced the competitiveness of Canadian firms, particularly those in the manufacturing sector in Ontario. Many businesses have had to close or are still coping with the after-effects of the high dollar.
- » Since 2000, Canada's share of the global export market has declined from 4.5 per cent to 2.5 per cent.¹³ Exports remain 6.5 per cent below their pre-recession peak, with little sign of recovery.¹⁴
- » The Canada-U.S. border remains sticky and an obstacle to the manufacturing sector and exports.

Policy Challenges

- » Though more companies are steadily diversifying to key emerging markets, nearly 80% of Ontario's exports still make their way to the U.S.¹⁵ Even amongst Ontario's exports to the U.S., there is a heavy concentration in a small number of states, like Michigan.¹⁶
- » Manufacturing exports to the U.S. have declined by 12% in the last decade.¹⁷

13 Bank of Canada. 2013. Global Growth and the Prospects for Canada's Exports. <http://www.bankofcanada.ca/2013/10/global-growth-and-prospects-canada-exports/>

14 Ibid.

15 Trading Economics. 2014. Canada Exports. <http://www.tradingeconomics.com/canada/exports>

16 Government of Canada. 2014. Canada and the United States. State Trade Fact Sheets

http://can-am.gc.ca/business-affaires/fact_sheets-fiches_documentaires/index.aspx?lang=eng

17 From 2003-2013 in constant current dollars. Industry Canada Trade Data Online. <https://www.ic.gc.ca/app/scr/tdst/tdo/crtr.html>

Opportunities

- » Ontario's numerous immigrant communities present a huge opportunity to make inroads into growing global markets. Over a fifth of Canada's population, and 28.5% of Ontario's total population, is foreign-born, and much of our immigration growth stems from countries with burgeoning economies.¹⁸
- » Canada is concluding a major free-trade agreement with the EU (CETA) and is entering into negotiations with Asia Pacific Nations through the Trans-Pacific Partnership (TPP). These agreements will have enormous impact on Canadian firms' export potential, but negotiators must ensure the benefits of new trade policies are shared as widely as possible.
- » Ontario is the third most attractive North American jurisdiction for foreign direct investment (FDI).¹⁹ This success could continue to be leveraged to produce even greater R & D, high value exports and productivity gains.
- » In May 2014, the federal government announced plans to embed over 25 trade commissioners in business organizations across the country. The strategy could help better coordinate existing trade programs and supports with current business efforts.
- » Existing Canada-U.S. processes like Beyond the Border and the Regulatory Cooperation Council are well-regarded and could be strengthened.

18 Government of Canada. 2011. The 2011 National Household Survey.

<http://www.fin.gov.on.ca/en/economy/demographics/census/nhshi11-1.html>

19 Government of Ontario. Ontario Budget 2014. Chapter 1—Section C. <http://www.fin.gov.on.ca/en/budget/ontariobudgets/2014/ch1c.html>

Discussion questions

- » What role should the federal government play in promoting and diversifying Ontario's exports?
- » How do we continue to build on our strengths in attracting investment and expanding firms globally?
- » Are there policy tools available to the federal government that could support the growth of Small and Medium Firms, which make up the vast majority of enterprises in Ontario, without creating perverse incentives to "stay small"? Can the work of Export Development Canada be improved?
- » Are there other key challenges and opportunities related to trade and investment?

Further Reading

Institute for Competitiveness and Prosperity. 2010. Trade, innovation, and prosperity. Working Paper 14. http://www.competeprosper.ca/uploads/ICAP_WP14_FINAL.pdf

Innovation

Innovation in all its forms will be crucial to increased prosperity and economic growth in Ontario. . However, since the mid-80s, productivity growth in Ontario, and Canada, has consistently lagged and in the past decade has plateaued.²⁰ Also, Ontario's record in business innovation has been weak, despite a high capacity for innovation given its well-educated workforce, competitive business tax environment and generous R&D tax credits.

- » Private sector spending on R&D in Ontario remains low despite generous federal and provincial government support for R&D; as a percentage of GDP, U.S. firms invest nearly twice as much in R&D as Ontario firms and Ontario business investment in R&D is just 75% of the OECD average.
- » Ontario continues to maintain and foster a globally competitive tax system; recent tax reforms supporting investment, exports and growth are saving Ontario firms more than \$8 billion annually.²¹
- » Larger, global firms are more likely to invest in research, ICT and machinery and equipment, which contribute to higher levels of innovation and productivity.

Policy Challenges

- » Ontario faces declining productivity growth and a widening productivity gap with other advanced economies. Particularly, Ontario's productivity gap with key US competitors increased to \$13 GDP/hour in 2012, more than doubling from \$6 GDP/hour in 2010.²²
- » Ontario experiences low levels of commercialization.

- » There is a lack of alignment between federal and provincial programs designed to support innovation.
- » Ontario firms are more likely to be SMEs—which usually invest less in R & D than larger firms—than those of our peers.

Opportunities

- » Ontario's 2014 Budget outlines a number of measures that could enhance its innovative capacity—including a \$2.5 billion Jobs and Prosperity Fund to improve Ontario's ability to attract significant business investments—but these tools must be properly designed if they are to be effective at driving innovation.
- » The federal 2014 budget introduced a \$1.5 billion Canada First Research Excellence Fund which over the next decade will help Canadian post-secondary institutions excel globally in research areas that create long-term economic advantages for Canada. Further, \$46 million per year of new federal funding was allocated for advanced research and scientific discoveries and an additional \$500 million over two years to the Automotive Innovation Fund, to support new strategic R&D projects and long-term investments in the Canadian automotive sector.
- » Many emerging global challenges, such as resource stress and climate change will require clean technology solutions where Ontario has expertise and resources.

²⁰ Government of Ontario. 2014. Ontario's long-term Report on the Economy 2014; Chapter 5. <http://www.fin.gov.on.ca/en/economy/ltr/2014/ch5.html>

²¹ Jobs and Prosperity Council. 2012. Advantage Ontario. <http://docs.files.ontario.ca/documents/340/jpc-advantageontarioenglish.pdf>

²² Ontario Chamber of Commerce. 2014. Emerging Stronger 2014. http://www.occ.ca/Publications/EmergingStronger2014_web.pdf

Discussion Questions

- » How can the federal government better align its policies and supports for business innovation in order to avoid unnecessary overlap with provincial programs?
- » How can the federal government better incent firms to invest in R&D and better benefit from these tax credits?
- » Are there policy tools available to the federal government that could support the growth of firms?
- » What approaches should be taken to encourage more scientific research and technology investments?

Further Reading

Ontario Chamber of Commerce, The Mowat Centre and Leger Marketing. *Emerging Stronger 2014*. http://www.occ.ca/Publications/EmergingStronger2014_web.pdf

Task Force on Competitiveness, Productivity and Economic Progress. 2013. Course correction: Charting a new road map for Ontario. Twelfth Annual Report. http://www.competeprosper.ca/work/annual_reports/annual_report_course_correction

Johal, Sunil, Mendelsohn, Matthew and Zon, Noah. 2013. *Let's Talk: Coordinating Economic Development Spending in Canada*. Available at: http://mowatcentre.ca/wpcontent/uploads/publications/77_lets_talk.pdf

Don Drummond. *Confessions of a Serial Productivity Researcher*. Centre for the Study of Living Standards. *International Productivity Monitor* (22), p. 3-10, Nov. 2011. <http://www.csls.ca/ipm/22/IPM-22-Drummond.pdf>

Federal Transfers

Long-standing allocation formulae in transfers, along with changes to the Equalization program in recent years, deprive Ontario of funding during a time of relative economic decline. The current system does not reflect the current economic reality and has resulted in Ontario spending less per capita on just about every public service compared to other provinces.

- » Ontario is the only province to be a net contributor to the federation—the gap between what Ontarians pay in through taxes and what they receive in return through federal transfers and spending amounts to a gap of \$9B-\$12B (in 2009-10)—while having below average fiscal capacity and per capita GDP since 2009.²³
- » In recent years, changes to the Equalization formulae have resulted in significant claw-backs to Ontario's payments, despite a reduction in the province's fiscal capacity.
- » Ontario and the federal government have signed tax collection agreements, creating a more unified system of personal, corporate and value-added tax collection, but removing some of the policy tools that Ontario once possessed. The result has been a loss of revenue for Ontario.

Policy Challenges

- » Ontario has below average fiscal capacity and GDP yet continues to redistribute funds elsewhere in Canada in general and through the Equalization program specifically.
- » Federal spending and program decisions in a number of areas key to the province's future prosperity—such as Employment Insurance, labour market training, housing and infrastructure—presume Ontario needs less federal spending than other provinces.
- » There are many misperceptions about fiscal federalism.

Opportunities

- » There is growing awareness of these issues in Ontario within the policy and business communities. The Ontario government is highlighting these issues in a very public way, creating a window of opportunity for change.
- » With the federal government returning to surplus, there will be pressures from provinces on what the federal government should do with its fiscal capacity.
- » The Council of the Federation is undertaking work on Canada's fiscal arrangements with the goal of seeing how much common ground exists among provinces and territories.

²³ Thomas Granofsky and Noah Zon. *Cheques and Balances: The Finances of the Canadian Federation*. Mowat Centre. Research Note #87. Available at: <http://mowatcentre.ca/cheques-and-balances/>

Discussion questions

- » How should the federal government reform the equalization program so that it is fair and principled?
- » How could other transfers – including infrastructure, housing, and job training– be structured on a more principled basis?

Further Reading

Matthew Mendelsohn. 2012. Back to Basics: The Future of the Fiscal Arrangements. <http://mowatcentre.ca/back-to-basics-future-fiscal-arrangements/>

Thomas Granofsky and Noah Zon. Cheques and Balances: The Finances of the Canadian Federation. *Mowat Centre*. Research Note #87. Available at: <http://mowatcentre.ca/cheques-and-balances/>

Targeted Strategies for Sectors and Regions

The province is home to numerous high-performing clusters such as those in the life sciences, clean-tech, and the agri-food sectors, which fuel prosperity, innovation and job creation across Ontario and Canada. Equally, the not-for-profit sector is an important and growing space for innovation - one in need of firmer financial footing as it continues to take on a greater role in public service delivery. Regions such as the Ring of Fire hold enormous potential, but require equally sizeable investments and community development if they are to yield equitable and on-going benefits.

- » The current system of federal R&D support is weighed heavily toward indirect programs (i.e. tax credits), meaning that Canadian firms in dynamic industry clusters have less access to direct innovation supports that offer higher returns on investment.
- » Place-based and sectoral economic development strategies have become increasingly successful in communities like Waterloo, Guelph and Stratford.
- » Medium-sized communities are developing unique advantages in the value chain in relation to and in partnership with Toronto.
- » Federal business development supports exclude non-profits, despite the fact that non-profits are increasingly professionalizing and adapting business-derived best practices to meet funding and program requirements. Current CRA rules also limit the revenue-generating capacity of non-profits.

Policy Challenges

- » Uneven economic growth across the province means many communities have experienced flat or negative growth over the past decade.
- » Regions and clusters are not consistently able to mobilize the resources necessary to achieve success in an increasingly competitive global market.
- » Medium-sized cities often compete with each other for investment, creating a “race to the bottom.”
- » Regional and cluster-based approaches can lead to siloed implementation, making horizontal alignment more difficult. Funding approaches that emphasize collaboration are necessary.

Opportunities

- » Ontario’s 2014 budget introduced new funding for innovative research in sectors such as life science, manufacturing and infrastructure, through the Jobs & Prosperity Fund.
- » In 2013, the federal government renewed FedDev Ontario until 2019.
- » Many mid-size Ontario cities are engaged in active discussion of their economic development strategies.
- » Expected infrastructure investments could support greater integration of economies in Southern Ontario.

Discussion questions

- » What approaches can be deployed to improve the economic performance of particular communities and regions?
- » Should the federal government be changing its approach to cluster development?
- » Are there policy tools available to encourage greater economic integration across communities in Ontario so that smaller communities can benefit from the growth experienced elsewhere in the province?

Further Reading

Jobs and Prosperity Council. 2012. Advantage Ontario. <http://docs.files.ontario.ca/documents/340/jpc-advantageontarioenglish.pdf>

Ontario Chamber of Commerce, the Mowat Centre and Leger Marketing. *Emerging Stronger 2014*. http://www.occ.ca/Publications/EmergingStronger2014_web.pdf

Conclusion

The issues and challenges outlined above are highly complex and require considerable effort by all levels of government to address. And while stakeholder input and participation is critical to devising appropriate policy responses, government leadership is also essential to achieving systemic and sustainable solutions.

We look forward to discussing and reviewing your feedback as we move forward with this initiative. Thank you for your time and we hope you stay engaged with this project as it continues through the Spring and Summer of 2015.

To share any comments or feedback, or to arrange a presentation and a facilitated discussion based on the report, please contact director@mowatcentre.ca.

