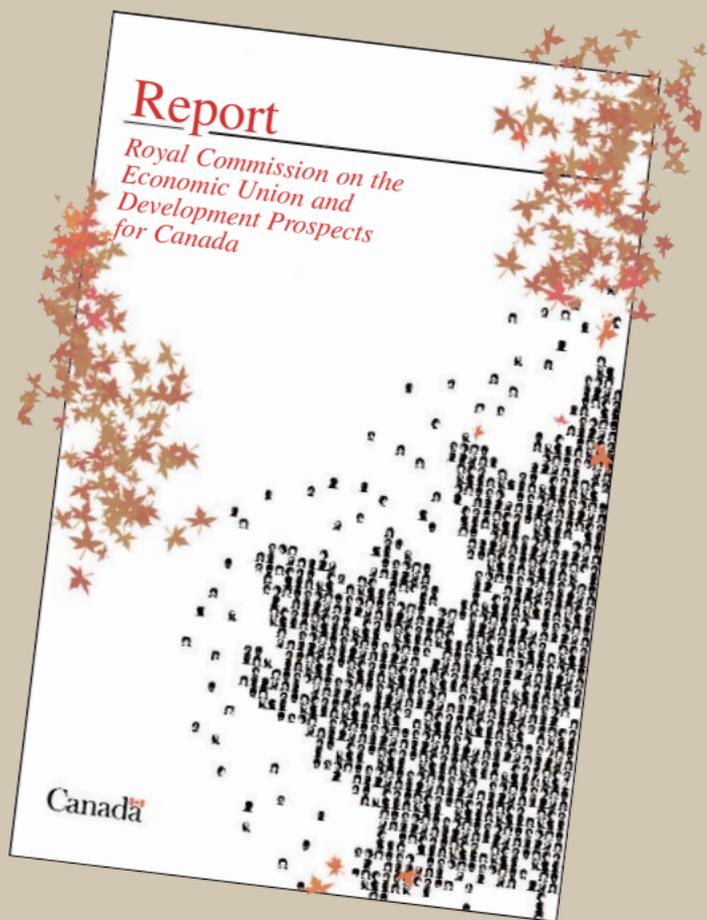


PROSPECTS FOR CANADA

Progress and Challenges 20 Years
after the Macdonald Commission



David E.W. Laidler and
William B.P. Robson,
Editors

C.D. Howe Institute
Institut C.D. Howe



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Policy Study 41

C.D. Howe Institute

C.D. Howe Institute publications are available from:
Renouf Publishing Company Limited, 5369 Canotek Road, Unit 1,
Ottawa, Ontario K1J 9J3
phone: (613) 745-2665; fax: (613) 745-7660;
Internet: www.renoufbooks.com

This book is printed on recycled, acid-free paper.

Library and Archives Canada Cataloguing in Publication

Prospects for Canada: Progress and Challenges 20 Years after the
Macdonald Commission / edited by David E.W. Laidler and William B.P. Robson.

(Policy study ; 41)
ISBN 0-88806-662-7

1. Canada--Economic conditions--1991-. 2. Canada--Economic conditions--
1971-1991. 3. Canada--Economic policy--1991-. 4. Canada--Economic policy--
1971-1991. 5. Canada--Social policy. 6. Canada--Politics and government--1993-.
7. Canada--Politics and government--1984-1993. 8. Royal Commission on the
Economic Union and Development Prospects for Canada. I. Laidler, David, 1938-
II. Robson, William B. P. (William Bertie Provost), 1959- III. C.D. Howe Institute
IV. Series: Policy study (C.D. Howe Institute); 41.

HC115.P756 2005

330.971'064

C2005-905359-3

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Quotation with appropriate credit is permissible.

Cover design by Diane King.

Printed in Canada by Ricoh, 205 Industrial Parkway North, Aurora ON L4G 4C4
September 2005.

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Foreword

Twenty years ago, the report of the Royal Commission on the Economic Union and Development Prospects for Canada, chaired by the Hon. Donald Macdonald, set out recommendations that became a focus for the development of economic and social policy in Canada. One of its most important proposals was for a free trade agreement between Canada and the United States, an idea that the C.D. Howe Institute also considered in its research at that time.

This volume of papers reviews the contribution that the Macdonald Commission's Report made to Canadian public policy, examines the changes since then, and looks at the enduring lessons that policymakers can draw from its conclusions as they confront the complex challenges of today and tomorrow. David Laidler and William Robson, who organized the conference at which the papers published in this volume were initially presented, introduce the package and provide an excellent review of the primary issues.

I want to thank David and Bill for bringing together those papers in a book, as well as Kevin Doyle, who edited it. I also want to thank Wendy Longsworth and Diane King, who prepared it for publication. And certainly not least, I want to thank Donald Macdonald who contributed his thoughts 20 years after his Commission made its seminal contribution to Canadian public policy.

Jack M. Mintz
President and
Chief Executive Officer

Preface

William B.P. Robson

A volume to mark the 20th Anniversary of the publication of the *Report of the Royal Commission on the Economic Union and Development Prospects for Canada* may appear to need little justification. The Macdonald Commission is a pre-eminent landmark in Canadian economic policy. The Commission stands out for the astonishing amount of high quality research it commissioned and published. Its Report stands out for the reasoned tone of its discussion and recommendations. Even if the Report's recommendations had borne no fruit, the Commission's work would still be worth re-reading, discussing, and commemorating.

But, of course, the Macdonald Commission's recommendations did bear fruit. If Canada's economic union and development prospects are different, and in many respects better, than they were when the Commission began its work, some credit must go to the Commission's Report, and to the vigour with which Chairman Don Macdonald traveled the country to tell Canadians about it afterward. So the Report's 20th Anniversary is an apt point from which to look not just backward, but forward as well, and ask what lessons the Commission's work and subsequent experience offer as we confront Canada's economic challenges today.

Some of the Commission's work and recommendations affected policy directly, most notably Canada-U.S. free trade. Others affected policy more indirectly, such as fiscal stabilization. Yet others failed to make a mark, such as the guaranteed annual income. Still, all of them, in their substance, and in their consequences — or lack of them — contain lessons for Canadians today. That fact inspired David Laidler and me to commemorate the Report's

release with a particular type of colloquium. We divided the Commission's work into four main areas: macro stability and economic growth; labour markets and social policy; international trade and federalism, and Canada's economic union. For each of those areas, we invited three experts to comment on, respectively, what the Commission's Report said, what has happened in the 20 years since, and what lessons the Report's recommendations and subsequent experience offer policymakers today.

David Laidler presents the substance of the contributions in the Rapporteur's Summary most ably at the end of this volume and I will not summarize them here. What does merit emphasis at the outset, however, is the overwhelmingly enthusiastic response to our invitations to present papers and to attend the conference. The contributors to this volume are superbly qualified, and the incisive discussion from the floor added in no small measure to the quality of the published papers. I thank the authors, the participants, and my co-editor David Laidler for their willing and able contributions to this project.

Special thanks are due to Don Macdonald himself. It may not be utterly shocking that Don responded positively when we first proposed this conference and volume to him. But his contribution went well beyond approval of the project: He made numerous valuable suggestions about framing the topics, and also contributed an address of his own, the essay that leads off the volume.

Not surprisingly, discussion about lessons for the future in each of the major policy areas often touched on the suitability of a modern-day royal commission to sort out today's challenges. Canada's royal commissions have a mixed record. Some stand out for the quality of their analysis and also for the impact of their recommendations; others fare poorly by either measure. Worse, some that stand out for their quality left little mark on policy, while others that were analytically weak left, or appear likely to leave, a larger policy legacy. Twenty years after the completion of its work, the Macdonald Commission stands out for the quality of its research, the ambition of its recommendations, and the advances in policy it fostered in several vital areas. Canadians seeking the

right balance of established expertise and fresh thinking about today's economic and social challenges should find this volume's perspective on an outstanding Royal Commission informative and inspiring.

The Commission's Work and Report: A Personal Perspective

Donald S. Macdonald

On occasion, a historical event may be captured in a single photograph. One such picture is the photo of Lord Strathcona, sledgehammer in hand and top hat on head, driving in the last spike of the Canadian Pacific Railway in British Columbia. Similarly, photographers captured the final signing of the *Constitution Act, 1982*, on Parliament Hill on a rainy April day.

The Queen is signing the constitutional document under the benevolent eye of Pierre Trudeau and in the background, two young men in morning suits are assisting in the process; they are Michael Pitfield, Clerk of the Privy Council, and Michael Kirby, Deputy Clerk.

They were the most senior public officials supporting the federal government in the constitutional negotiations. The creation of the Royal Commission on the Economic Union and Development Prospects for Canada was one of their next major endeavours.

An issue that influential Canadians and their political leaders had debated widely over the preceding half dozen years leading to the patriation of the British North America Act was how the constitution might be changed to provide for trade within the economic union. Discussion of that question had become stalemated in federal and provincial negotiations and it was put aside while the other changes were discussed and then carried through to adoption.

That question of seeking a better regime to govern internal trade remained on the personal agenda of the Prime Minister, and because of that, Michael Kirby turned up at my house in Toronto

in the early autumn of 1982 to ask me to chair a commission to address the unfinished subject of the economic union.

Let me acknowledge at once that providing a specific and immutable framework for internal trade did not emerge from the Commission's deliberations, while a range of other public policy recommendations, which had not arisen in my recruitment, did.

In the end, the Royal Commission recommended a process rather than a legal amendment to deal with internal barriers to trade.¹ It would be for the First Ministers Conference to establish an entity to set up the institutions, and it would be the political process, not the courts, that would enforce it.

If economic union was the principal motive for the Royal Commission, why then are there three pages of so many other issues in the terms of reference?

Over the weeks that the Royal Commission mandate was being sculpted, I had observed this broadening of the mandate to a much wider set of issues, eventually numbering those three pages of text. What happened? I learned much later that, apart from the economic union, the government's advisers felt that this was an opportunity to have a wider public canvass of a range of policy concerns for which the policymakers had no clear solutions. In effect, it was acknowledged that the government had exhausted its mandate and new policy directions required exploration.

The governing party's program objectives had, for the moment, been attained and there was a lack of direction as to where policymakers should turn their attention next. As a result, the government decided to constitute a commission with broad terms of reference, to be conducted by a group representative not only of the geographical interests of the country, but also different functional interests, including political parties. Its objective was to be an examination of where Canadians were going as a nation, as well the great events that were going to shape the world around them. Ottawa wanted to study a broader group of issues than

1 The monograph of Kenneth Norrie, Richard Simeon and Mark Krasnick, *Federalism and Economic Union in Canada*, Volume 59 of the Commission's research, put the case on internal trade comprehensively.

could effectively be dealt with within the formal structure of the public service, a wider scope of ideas and questions — and, if the recommendations were not acceptable to the government, it could disavow them.

The use of the Royal Commission instrument to develop broad policy responses has now become a pattern in Canada. Rowell-Sirois, Walter Gordon and our Royal Commission, each in its generation provided a perspective on the political economy of Canada, of our place within a changing world, and of policy responses for Canadians to choose.

The first task of the commissioners was to appoint senior staff. Gerry Godsoe became Executive Director; Alan Nymark, Director of Policy; and the Directors of Research were Ivan Bernier, Alan Cairns and David Smith. Several months into the Commission's work, David Smith received an invitation to become Principal of Queens University and stepped down as a Director of Research. Ken Norrie and John Sargent continued their existing occupations and heroically, in the roles of co-Directors of Research, undertook David's task, as well. The research began right away and resulted eventually in over 70 volumes of text dealing with the three major disciplines: economics, politics, and law — and with other subjects, as well.

A major contribution to the Commission's work was the program of public hearings which it held across Canada in the fall of 1983. While the appointment of the Royal Commission had been greeted with scoffing from large swaths of the media, Canadians throughout the country responded with enthusiasm to the opportunity to come and meet and discuss the nation's problems. The membership of the Commission was divided into teams and between us, over a three-month period, we went into all provinces and territories and talked with elected officials, other public leaders, and representatives of different groups — and just plain folks.

On the academic side, there was some skepticism about the value of the public hearing process. However, the commissioners were in no doubt that in the interests of political credibility, to enable the public to be heard, and also for the education of the

commissioners, we should hear the opinions, often differing, of people from all across Canada.

Two of these hearings I still remember well. In Prince George, B.C., Ms. Dino, librarian at the public library, made a plea for government to make it possible for the emerging new means of communications to reach all of the communities throughout Canada, in the same way that the Carnegie endowment in the U.S. had brought learning to previous generations through the public library system. This was in the 1980s, when the Internet was still a mystery. She was a full decade ahead of her time, and was speaking of a technology which the Chairman, at least, did not know anything about; in retrospect it was a remarkably prescient recommendation.

On the other side of the country, in Saint-Georges-de-Beauce, Quebec, we had expected a refreshing presentation from the business community, which is known throughout the province for its enterprise. We were not disappointed. In a classic Quebec small town we heard presentations from local businessmen who were selling products around the world.

At the end of it all, with the hearings' testimony complete and the submissions received, the volumes of research and the conclusions distilled from it, the commissioners then had to sit many long hours agreeing on the text that embodied their conclusions.

Two particular events stand out in my mind because each affected the thinking of the Commission on issues which had not been in the work plan, though they were certainly present in the Commission's conclusions.

On the very first day, the Mining Association of British Columbia offered us an analysis of the competitive position of the base metal mining industries of Canada, indicating that the properties then being developed in British Columbia contained a much lower grade of ore than those that could potentially be exploited by competitors in South America and elsewhere in the developing world. One conclusion drawn by the commissioners from that discussion was that, while resource endowment would continue to be an important base for prosperity, it could not provide the rate of growth that Canadians had come to expect.

The other was at an informal meeting at the Park Public School in Regent Park South in downtown Toronto, from which it became clear that some of the public policies in place, federal, provincial and municipal, to assist the working poor were often competitive and even provided disincentives to those trying to work their way out of their disadvantage. That event was an important stimulus to the work undertaken by Rick Van Loon.

One of the ironies of the Commission's Report is captured in a phrase of Bill Robson, who said that it moved "decisively away from further dirigisme and towards economic liberalism".

The irony is that, looking back to the previous decade, the 1970s, in the two economic portfolios I had held as a minister, I had been responsible for highly dirigiste policies. In Energy, I had been the minister responsible for the National Oil Policy of 1973/1974, the incorporation of PetroCanada, the substantial investment by the federal government in Syncrude to maintain momentum in the oilsands, and Canadian participation in a price control regime for uranium exports.

In Finance, I had become the ultimate, comprehensive dirigiste over the whole economy, as the minister responsible for the wages and prices program.

What changed my viewpoint? My experience in the private sector after my departure from government made it clear that state-controlled programs had failed to achieve the rates of growth to which we all aspire. Did the Report bring about change? I would call as my witness the decade of the 1990s, in which a more open trading environment, and more conventional financial and monetary policies, achieved for Canada a much better economic performance.

Let me express some words of appreciation. I am indebted to Bill Robson and the C.D. Howe Institute, and David Laidler, for providing us this occasion to meet and to reflect on our labours of 20 years ago. Not least, it is a pleasure to gather again with so many of our co-workers from the mid-1980s. We all may have some afterthoughts as to what we recommended, but we can take satisfaction from knowing that our work has been used extensive-

ly by students and makers of public policy in the intervening years.

On a sadder note, as a popular hymn reminds us: "Time, like an ever-rolling stream, bears all its sons away." Alas, there are a number of our colleagues who are no longer with us, but whom we remember with respect. I mention one in particular who made a significant contribution to the Commission's work from the very earliest days until the final paragraph was written and to whom I was and am particularly indebted; he is Gerry Godsoe, who has since died. In his capacity as Executive Director, he took a lead role in creating an organization capable of responding to the heavy demands of an all-consuming order of reference and then, week after week, met the challenges, large and small, arising from the work program. With a high intelligence, he brought a unique capacity for mediation, and an instinct for policy direction that was invaluable.

In concluding, I offer a postscript to the Commission's work and on its recommendations, and I focus in particular on the recommendation that Canada seek a free trade agreement with the United States. While the Mulroney Government reserved its opinions on most of the recommendations, it responded almost immediately with an endorsement of the trade proposal.

Politically, that could not have been an easy choice within Cabinet, because the Conservatives had, for most of the century, been staunch opponents of opening our borders with the U.S. It would not have been a snap decision. The Commission had provided drafts of the near-final text of the Report to the Privy Council Office earlier in the year, pending a final draft in both official languages. Clearly, a decision had been taken by Mr. Mulroney and his colleagues during the months before the final Report became public. In retrospect, I admire their decisiveness and the way they were able to keep their discussion to themselves until the final Report did become public.

After publication of the Report there were declarations of support for the proposals and then, for a period of some months, no further overt acts to carry it forward. The supporters of the concept in the private sector were concerned at the absence of advocacy to

counter the opposition to free trade building up on the public stage.

David Culver of Alcan, and Tom d'Aquino, as I recall it, took the initiative to form a private sector group in support of the concept. As co-Chairmen, Peter Lougheed and I were asked to lead a campaign of positive advocacy in Canada and with appropriate interest groups in the U.S.

It was agreed between us that we would divide the task between the regions, and between groups we each knew best. That turned out to be the short straw for me. While Peter addressed audiences in his own province, and elsewhere in Western Canada that had historically been in favour of free trade, I drew, among others, audiences in the industrial communities of southern Ontario, where there was strong union opposition: Oshawa-Bowmanville, St. Catharines, Burlington, in addition to Metro Toronto.

The debates were often spirited. None was more difficult for me than the Annual Meeting of the Liberal Party in Halifax, ironically the province of W.S. Fielding, the Finance Minister who had prepared the trade agreement in 1911.

A welcome ally to my side of the debate came from academe: Professor John Crispo. I will always be grateful for his robust platform technique which ultimately frightened away the union leaders from contested meetings where initially it was they who had brandished the verbal brass knuckles.

In the end however, it was the electors in the 1988 election who made the choice, and their judgment has been ratified by the results in the 1990s and in this century.

Rapporteur's Commentary

David Laidler

The Macdonald Report marked a major turning point in Canadian economic and social policy and this conference aimed, among other things, at honoring the Commission's achievements 20 years later. Its main focus, however, was on the lessons that we can draw for the future from the Report's prescient conclusions.

In most western countries, post-World War II policy followed the essentially state-directed policy agenda pioneered by the British economists William Henry Beveridge and John Maynard Keynes, as well as the architects of Franklin Delano Roosevelt's New Deal. By the late 1970s, however, that once fast-flowing stream of ideas was rapidly silting up and on its muddy surface inflation and real stagnation were beginning to breed (Macdonald, Chant).¹ In the United States and Britain, particularly, the resulting policy vacuum was being filled by politicians.² In Canada, however, a Royal Commission began the process of examining the country's political economy, and its Report (Royal Commission 1985) advocated a redefinition of the state's role in the economy, rather than a wholesale withdrawal. The Commission encouraged the government to maintain its efforts to provide a generous social safety net, and to promote stability and growth, but by creating a stable economic and institutional framework within which a free-market economy would deliver those benefits.

1 This rapporteur's commentary draws too heavily on the essays printed earlier in this volume to make comprehensive citations stylistically feasible. They are referred to at particularly relevant points simply by the names of their authors.

2 "Ronald Thatcher", as Sylvia Ostry reminded the conference.

The Report's Principal Recommendations and Their Impact

The Macdonald Commission is best remembered for its advocacy of a free trade agreement between the U.S. and Canada. Though the 1989 Canada-United States Free Trade Agreement (FTA), enlarged to embrace Mexico in the 1993 North American Free Trade Agreement (NAFTA), differed somewhat from the original recommendation, it involved a major change in the direction of Canadian policy, with economic results that were only partly as predicted (Winham, Trefler). The Commission had foreseen a significant rationalization and expansion of Canadian manufacturing, accompanied by large productivity gains, as well as the possibility of significant transitional labour market problems, and all of these did transpire. However, an overall productivity improvement reflected the closure of inefficient plants under the pressures of competition and the expansion of efficient survivors, as well as significant gains within the latter group, while in the labour market, some of the resulting damage turned out to be permanent rather than transitory (Trefler).

Senate reform was at the centre of the Commission's plans for strengthening the Canadian federation, but it came to nothing (Cairns). Still, piecemeal adjustments in subsequent years enabled federal institutions to cope with the stresses created by the free-trade-related re-orientation of Canada's economic life from an East-West to a series of North-South axes, in spite of the fact that, in the 1990s, the federation's very unity came under threat from Quebec separatism and the reluctance elsewhere in Canada to accommodate the province's distinctiveness. Canada weathered these stresses, too, however, and perhaps the reduced economic inter-dependence of its regions that free trade created actually made the necessary political accommodations easier to manage (Hale, Norrie).

In areas other than trade policy, the Commission's subsequent influence was both less direct and less immediately visible, sometimes because no attempts were made to implement its recommendations, and sometimes because those recommendations were

somewhat sketchy. However, the Macdonald Report was much more than a one-idea document, and its positions did inform subsequent policy in a number of areas.

The Commission's substantive proposals for macro-economic policy envisaged little more than stabilizing the public debt-to-gross domestic product (GDP) ratio, and using monetary policy to offset any contraction that this process might cause. It did, though, firmly reject some then-popular ideas and cautiously support others that would soon become fashionable (Chant, O'Neill). Specifically, the Report denied that productivity growth was the enemy of job creation, and ruled out wage-and-price controls as a permanent feature of policy. It also recommended that monetary policy should pursue a medium-term nominal target, albeit nominal GDP growth rather than inflation. It also unequivocally supported a flexible exchange rate as essential to Canada's monetary policy independence (O'Neill, Reuber and Robson).

Three features of the early 1980s help explain the Commission's rather relaxed attitude towards macro-economic policy. For one thing, the reduction of inflation from low-double to mid-single digits at the beginning of that decade had been accompanied by the deepest recession since the 1930s, and Canadians were in no mood to accept another slowdown anytime soon. For another, the net debt-to-GDP ratio for the government sector as a whole was about 35 per cent in 1984, about the same level as in 2003 (OECD figures cited by O'Neill). As well, though the ratio was rising fast in 1984 (in contrast to 2003), there still seemed no imminent danger that it would become uncontrollable because the idea that the slow productivity growth of the preceding decade would still be a drag on tax-revenues even as the economic cycle turned upward was still controversial. At the same time, the Commission looked forward to a significant lift to productivity from the implementation of free trade (Chant, Winham).

In the mid-1980s, then, though macro policy was clearly working badly, there seemed to be time to fix it, and the Commission's very modest concrete proposals were at least directionally appropriate. As it turned out, slow productivity growth was much more than a cyclical phenomenon and Canada's fiscal situation would

deteriorate for another decade before the 1995 budget finally put the country's finances on a path consistent with the successful pursuit of the inflation targets that had begun to underpin monetary policy in 1991.

The Macdonald Commission took a bolder approach to the labour market and social policy than to macro-economics (Riddell). Much more striking in 1985 than now was the Commission's acceptance of the idea that unemployment tends to fluctuate around a long-run level — a non-accelerating inflation rate of unemployment (NAIRU) — that is not susceptible to monetary and fiscal policy, but can be affected by micro measures (Chant). Proposals to introduce the experience rating of employers into the unemployment insurance system and to remove regional differences in the program's generosity, among other modifications, were explicitly aimed at reducing the NAIRU, and accurately so in the light of much subsequent research. Political obstacles rather than economic doubts have, however, prevented meaningful reform to this day (Kesselman).

The Commission was also bold in arguing that the simplest cure for poverty is to provide income to those who lack it. This notion underlies Canada's present approach to the specific problem of child poverty, though the Commission's more sweeping proposal for a comprehensive guaranteed minimum income program went nowhere. That the guaranteed-income proposal failed did not reflect another trumping of good economics by politics; rather it was a result of a deepening economic understanding of the limits of such programs and also of the complex nature of poverty itself (Kesselman, Richards). The Commission knew that general income support at any useful level is expensive and that its provision through a pure version of a negative income tax would require rather high marginal tax rates on better-off Canadians. It also understood that any claw-back of benefits at a rate above that embedded in the income tax system itself would imply high effective marginal tax rates for those whose incomes fell in the relevant range. Economists nowadays are even more keenly aware of the inefficiencies in resource allocations associated with high marginal tax rates, and universal programs generally have lost much of

their appeal, with even current child support policies sometimes looked at askance (Kesselman).

We have also begun to understand that poverty is often not so much a first cause as an effect of other socio-economic problems that general income support sometimes does little to ease, and that marginal dollars might be more effective in reducing poverty when directed to specific programs. This seems to be particularly the case with child poverty because the social problems associated with it often affect the educational achievements of children, their subsequent labour market experience, and the eventual social and economic well-being of their own children (Kesselman, Richards).

The Commission advocated special transitional relief for workers displaced by the introduction of free trade with the U.S. This proposal, too, never got off the ground and, in fact, when considered in the light of actual post-FTA experience, the Commission may have been addressing the wrong problem in any case. Many low productivity workers, whose poor education made it hard for them to move into other jobs, suffered long-term rather than temporary losses (Trefler). In an economy as open to foreign competition as Canada's has become, such difficulties are permanent features of the labour market and their remedy seems to lie in ensuring that higher minimum levels of education are attained than in the past. Viewed in this light, the currently high drop-out rates of high school students, particularly those of young men, do not augur well for the future.

Looking Ahead

Twenty years after the Macdonald Commission reported, Canada still has much policy work to do.

Poverty is a case in point. Since 1985, Canada has lessened the prevalence of welfare traps — those quirks in the profile of effective marginal tax rates that provide incentives for people to stay out of the labour force altogether. However, they have often been replaced by success traps — which remove incentives for low-productivity workers to take the risks implicit in acquiring extra education and training in order to raise their incomes from employment (Kesselman). Not only that, in relying as heavily as

we now do on income support to families to fight poverty among children, we may be missing opportunities to improve their educational attainments and their long-run income prospects, as well as those of future generations (Richards).

In this context, social and labour market policies come into contact with a central piece of unfinished macro-economic business, the pursuit of higher productivity growth. Many commentators have stressed the importance of human capital in this area, though the focus has been almost exclusively on post-secondary education and the knowledge economy. Too often they have overlooked the importance of improvements in primary and secondary education that would not only contribute to the growth of Canada's stock of human capital, but also contribute to the amelioration of poverty. The connections among these policy goals are underappreciated.

As well, what is now called Employment Insurance (EI) still needs reform. Many might argue that this cause is almost lost and not worth the expenditure of scarce political energy. Perhaps, but public awareness and disquiet about the extent to which, under current arrangements, the revenue raised from employment insurance payments exceeds the payment of benefits might just generate enough political energy to support action and to create an occasion to re-base the current EI scheme on insurance principles. It is, therefore, worth keeping our understanding of these issues alive and up-to-date and being ready to exploit the opportunity should it arise. This is not the only area where such an attitude might pay dividends. Canada's current two-percent inflation target is hard to defend as an ideal long-run anchor for monetary policy; it endures, in part, because many think the efforts involved in moving closer to price stability outweigh the benefits of doing so (Reuber and Robson). Here too, however, an unexpected opportunity to make an improvement could conceivably arise.³

More generally, reform of Canada's overall fiscal system has considerable potential to improve the economy's performance (Reuber and Robson). An increase in the tax system's efficiency,

3 As former Bank of Canada Governor John Crow reminded the conference.

especially in the corporate area, would help productivity, an important consideration now that the gains from free trade have largely been captured.⁴ Furthermore, the creation of a well-designed medium-term federal budgetary framework might complement inflation targeting in creating the reliable macro-economic stability that is so conducive to good business decisions.

Currently, the unpredictability of federal outlays under shared-cost programs continuously threatens medium-term fiscal stability, while also exacerbating the apparently perpetual political tensions to which Canada's political union is subject (Reuber and Robson, Hale, Norrie). Senate reform, the Macdonald Commission's principal remedy for relieving such political stresses, proved elusive and, though a good deal of piecemeal progress has been made since the 1980s in maintaining and even improving Canada's economic union, successive federal governments have not identified a policy goal that can form the centrepiece of a nation-building political agenda. Recently, solving the problem of health care for a generation has been assigned this role, though there should be concern about this casting (Norrie).

Political support for the current system is certainly strong and national in scope, but health care remains under provincial jurisdiction and is funded on a shared-cost basis. The federal government's efforts to use its spending power to influence provincial policies in this area, with a view to setting national standards, seem bound to create fiscal uncertainty and to exacerbate federal-provincial tensions, as well. Perhaps it would be better to concentrate nation-building efforts in areas where federal jurisdiction is clear and not subject to provincial challenges: foreign affairs in general, say, and defense and trade policy in particular.

Policy towards the U.S. is now very much on Canada's agenda. Perhaps the emergence of such economic giants as India, China and Brazil is indeed opening up new opportunities for trade diver-

4 In this context, though, it is worth noting explicitly that such measures as EI reform, designed to improve the employment prospects of low productivity workers would actually hold down measured productivity, but should not be avoided for that reason.

sification (Winham). In fact, though, the Canadian economy is now more dependent on trade with the U.S., and in some areas much more deeply integrated into the U.S. economy, than it was 20 years ago, and any discussion of trade policy must have this reality as its starting point (Winham, Hart).

Indeed, Canada-U.S. trade poses many challenges. Disputes with the U.S. persist, notably over softwood lumber, while cross-border road and bridge links, particularly those that are so vital to the smooth functioning of the automotive industry, are already badly stretched by the sheer weight of traffic and are in constant danger of becoming chronically congested as a result of post-September 11, 2001, security measures. At the same time, the conventional gains from free trade within North America now seem to have been largely exhausted (Winham, Hart). In Canada, they are, in fact, being eroded as the U.S. expands a network of bilateral free-trade agreements that exposes Canadian exports to increased competition from third parties, while simultaneously enhancing the relative attractiveness of the U.S. as a location for North American production.⁵

The status quo in Canada's trade relations with the U.S. is, at best, unstable and perhaps unsustainable, particularly at a time when strong differences of opinion about the invasion and occupation of Iraq and continental missile defense have strained political relations. These matters require attention, and the phrase Tinker or Transform neatly summarizes Canada's dilemma (Hart). Should the aim be piecemeal improvements to the status quo where possible, and its ad hoc management where they are not, or should the big idea of much deeper North American economic integration be pursued? There can be little doubt about the purely economic attractions of the latter option. The gains to be had from regulatory integration between the two countries, from the creation of a customs union and a common security perimeter that would permit the opening up of the U.S.-Canada border to the free

5 As Ronald Wonnacott ruefully remarked to the conference, for Canada, at least one fate would be worse than to assume the status of a spoke in an emerging U.S.-centred hub and spoke trading system: namely, to be excluded from the system altogether.

movement of goods, services and people, would surely generate noticeable material benefits and because of the differences in size between the two countries it is hard to see how the advances would not be particularly significant for Canada (Hart).

There are, however, serious political issues at stake. Perhaps many Canadians might accept common regulatory standards for automobile safety, or perhaps for food and drug safety, even if, as would be likely, the bigger country ended up having the predominant say in both their configuration and enforcement. But, suppose a customs union agreement were to involve something as apparently simple as Canada adopting U.S. policy towards trade in sugar? What would that do to the country's ability to act independently in the Caribbean and elsewhere in other matters? And what might a common security perimeter and a more open border than now exists imply for Canadians' ability to exercise their own judgment in the areas of immigration and refugee policy?

A badly conceived and executed version of the big idea could create a degree of dependence in matters of trade and investment large enough to put significant limits on the effective powers of Canadian governments to formulate independent policies in areas where the electorate's ability to enforce accountability upon them is currently taken for granted. This very consideration led the Macdonald Commission to recommend that Canada seek a free trade agreement rather than any deeper relationship with the U.S., and it remains critically relevant to our choices today.⁶ It is highly unlikely that deeper economic integration of Canada into the U.S. would lead to it becoming a 51st state.⁷ Should that happen,

6 Specifically, the Commission noted that Canada had in the past exercised policy independence towards China and Cuba (Volume I, p. 306.) and, prophetically, expressed concern that even the degree of economic integration implicit in a free-trade agreement could lead to pressures on the Canadian government to support future U.S. military interventions in Latin America and elsewhere that might prove politically divisive at home (p. 361).

7 As Winham ironically suggested during the course of a discussion with Hart about how far it was desirable to push North American integration.

though, former Canadians would at least be able to participate fully and equally in U.S. democratic processes, as they would not were Canada to stumble into the status of a dependent territory, subservient in foreign policy, but with some scope for self-government in matters that are judged by the U.S. authorities to be of purely domestic Canadian interest.⁸

This is not the place to debate specific versions of the big idea for Canada's place in North America. These need dispassionate analysis to reveal their advantages and potential flaws, in which it is important to avoid at least two pitfalls. First, we should recognize the claim that much deeper economic integration in North America is already inevitable, with only some details remaining to be discussed, as a rhetorical device intended to pre-empt careful criticism of this option. Second, we should recall that Allan Gotlieb's (2004) suggestion that Canada reject romanticism in favour of realism in foreign policy was not intended as a call to put the pursuit of material gain above adherence to political ideals. Rather it was a reminder that, in general, to ignore political and economic constraints in the pursuit of ideals can be dangerous and that such a pursuit can sometimes come at a significant material cost that might not — or might, depending on specifics — be worth incurring, but should always be taken explicitly into account when formulating policy.

Conclusion

Though policy in any democracy necessarily proceeds in piecemeal fashion, concentrated in particular areas, rather than according to a single overarching plan, it is sometimes worthwhile to step back from the details and look at how they interact. And it is also valuable to bring the best available academic analysis to bear on

8 To judge by the alacrity with which representatives of the U.S. government, apparently with support from Canadian opponents of the measure, noted the likely side-effects of the decriminalization of the possession of small amounts of marijuana on the smooth flow of traffic across the border, the range of such matters might prove to be remarkably restricted.

these matters. The Macdonald Report showed the value of doing these things and so, we hope, in its smaller way, will the proceedings of this conference.

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