

Building a Competitive Advantage in Canada: Everyone's Concern

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CANADIAN BANKERS ASSOCIATION
ASSOCIATION DES BANQUIERS CANADIENS

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Introduction:

Good morning and thank you for the warm introduction. And thank you for the invitation to speak at the Le Cercle de la Finance Internationale de Montréal luncheon.

I am pleased to see so many old and new friends and colleagues in the room, particularly those of you from the banking community.

Even though I've only been at the CBA for 100 days, I recognize that the opportunities and challenges facing businesses, such as banks here in Montreal, are very similar to those facing businesses in cities and communities throughout Quebec and across the rest of Canada. In fact, we're all much more alike than we sometimes realize with respect to the issues we face.

With that in mind, I want to focus on one such issue today – that is, our country's competitiveness and how to drive a Canadian advantage and accordingly, an advantage for Quebec. And, how to ensure that this advantage can be sustained over time in a fiercely competitive global environment.

Driving Competition:

What does it mean to become one of the most competitive jurisdictions and its businesses global champions? And, what will it take to achieve it?

It means creating quality jobs, attracting investment and talent, encouraging innovation, and building a strong tax base that can support the social programs we hold dear.

The success of business, no matter the size and regardless of location, is important to the success of our economy and ultimately the standard of living of every individual across the country.

We all have a role to play in improving Canada's competitiveness.

The Banking Sector: Contributing to the Economy and Prosperity

If we look at the banking sector, I can tell you that we are a major driver of our economy and of local economies in cities and communities across the country.

Let's look at the numbers for a moment.

Banks directly employ a quarter of a million individuals in communities large and small in every province and territory, including 41,000 in Quebec. While the banking industry represents 1.4 per cent of all employees in Canada, our employees generate over 3 per cent of the country's GDP.

Banks have a solid foundation here but they also have a window on the world. Last year, over 40 per cent of Canadian bank earnings were generated outside of Canada. At the same time, over 80 per cent of bank employees were located in Canada and 80 per cent of taxes were paid here.

Banks paid more than \$6.4 billion in taxes combined to all levels of government in 2006. About \$556 million of which was paid in Quebec. This \$6.4 billion is equivalent to the budgets for the federal departments of Agriculture, Foreign Affairs and International Trade combined in 2006, with some money left over. In fact, the banking industry pays more in corporate income taxes than any other industry in the country.

Virtually everyone shares in this success. Bank stocks are an important part of many public and private pension plans. For example, every member of the Canada Pension Plan and Caisse de dépôt et placement du Québec is, whether they know it or not, a shareholder, an owner, of our banks.

The Banks – Competition within the Sector:

There are some who may say, oh, but who are the banks to talk about competitiveness at all? Aren't there really only six banks in Canada?

My response to them is: maybe you haven't been paying attention. There has been a massive change in banking in the past few years with an array of new entrants and brand new financial institutions that we couldn't even have imagined a decade ago.

Today we have over 70 banks in Canada including several virtual banks like ING, and Citizens Bank of Canada. Some of the largest banks in the world are here in Canada such as HSBC. We also have banks that are owned by a grocery store chain, a network of insurance brokers, and a life insurance company.

In short, there is a great deal of competition in the banking industry, and the intensity is only going to increase. Just look at the Quebec market for evidence. Mouvement Desjardins is a formidable competitor and holds a 40 per cent share of deposits.

But can more be done to enhance the environment in which banks and other businesses compete? Can government and business, working together, really drive a Canadian advantage? With all hands on the wheel, I believe the answer is a clear yes.

Government Framework:

Which brings me to my next point – the role governments play in setting the framework for success, for keeping Canada competitive and creating long-term prosperity.

Our tax system, our regulatory system and other key areas such as competition rules, both domestically and internationally, as well as regulations governing the labour market all have an impact on business decisions.

Let's take a minute and look at the federal level where there are several opportunities to look at increasing our competitiveness. This month, Prime Minister Harper will be introducing the government's new priorities in the Speech from the Throne.

Finance Minister Flaherty is also scheduled to provide an economic and fiscal update this fall, and then there is the federal budget in early 2008.

In the meantime, the federal finance and industry ministers together have recently created the Competition Policy Review Panel.

In addition, there are two other panels we are expecting the federal government to announce – the tax fairness and competitiveness panel and the expert panel on a common securities regulator. These three panels give us an opportunity as business, to discuss how we can work cooperatively with the federal government to ensure our place in the global economy.

If we look at our competitiveness from an international perspective, we see many challenges.

We rank 16th in the World Economic Forum's global competitiveness index with the biggest of the G-7 ahead of us. Canada also dropped from 13th position in the year before. The World Economic Forum also ranks Canada poorly in terms of tax rates and regulations.

While there are many aspects to competitiveness that I could discuss, such as trade policies, I would like to take a moment and talk about our country's labour, tax structure and our regulatory policies.

Labour:

Canada is not alone in facing some serious labour force issues in the coming years. We are competing with other countries to attract the best and the brightest. And, our country's success depends on our ability to give new immigrants the opportunity to succeed.

We know that a faster pace of retirement in the baby boomer generation will open management jobs requiring experience and post secondary (and perhaps higher) education.

The pressure to fill these jobs, whether internally or externally, will ensure that the competition for quality employees will continue to be intense.

As our birth-rate continues its steady decline, immigration will continue to be an important component of demographic growth in Canada. Yet Canada - which has traditionally had the largest immigration program in the world - faces growing international competition.

In particular, a number of European countries, as well as Australia and New Zealand are giving us a run for our money. And Australia has mounted a particularly aggressive campaign for skilled immigrants, while Canada's approach has historically been a passive one. How will we compete successfully and attract the talent we are going to need from abroad?

We need innovative thinking and workable strategies to convert these looming challenges into opportunities. Business and government and various departments within government need to co-operate on a range of issues including pensions, skills development and immigration issues. I am glad to note that nine provinces have now abolished mandatory retirement - and Quebec, I believe, was the first province to take that step.

Taxes:

Our competitive advantage also extends to our tax system, one of my favourite topics. Regardless of the industry, regardless of the location in Canada we need to ensure that we have a competitive tax advantage over other countries, which we certainly don't have at the moment.

Indeed, The C.D. Howe Institute's 2007 Tax Competitiveness Report noted that Canada has the eleventh highest effective tax rate on capital among 80 industrialized and leading developing countries.

I can't emphasize enough that our corporate taxation rates should, at a minimum, be competitive with other key jurisdictions, but preferably create an advantage for domestic firms. We all know that global competition reaches into every community across the country. This means that if we are to give our businesses a competitive tax edge, then all levels of government need to participate and contribute to achieving this goal.

Unfortunately, Canada still has a relatively high combined federal-provincial corporate income tax rate at 34.2 per cent. Even though it is scheduled to fall to closer to 30 per cent by 2011, the current average in OECD countries is already lower at 28 per cent.

In the face of such competition, we believe that Canada must continue on the path already started by the federal government of reducing taxes, but these tax cuts must be deeper and happen sooner. At the federal level, the CBA is recommending that the scheduled reductions in the corporate income tax rate should be accelerated and then reduced even further to 16.5 per cent by 2012.

Provincial governments must also take up the cause. Quebec, like every other province, competes domestically and internationally and needs to strive to have a tax regime that will enhance its competitiveness, not detract from it. The Quebec government's decision to eliminate the capital tax is a very positive step in that direction.

And when it comes to personal income tax, we need to be more competitive as well to attract and retain a viable labour force and create incentives to work. A tax system that encourages a strong work ethic through economic rewards will increase our global competitiveness.

While relief for all tax brackets should be addressed in the future, we believe that the short term focus should be on reducing the federal tax burden for the lowest income tax bracket. You might be surprised to know that there are workers in this bracket who face the highest marginal effective tax rate on their income. It's time for governments to leave more money in the taxpayers' pocket.

We at the CBA will continue to make a competitive tax regime a priority. As long as other countries are ahead of Canada on this front we will continue to put forward suggestions about how to create a Canadian advantage.

Regulatory:

One of my other favourite topics getting lots of debate recently is regulatory efficiency and what it means for our competitiveness. This is an issue the banks know all too well. Essentially, banks are affected by everything from bylaws to Basel.

On the domestic side, bank financial groups must comply with some 50 federal, provincial and territorial departments, agencies and authorities. The sector is also affected by another 150 other regulators and agencies. Countless municipal bylaws also touch banks.

On the international side, banks are currently facing an unprecedented number of large complex regulatory compliance projects, for example, to name a few, there are:

- Changes to international accounting standards,
- Adopting updated global capital adequacy standards (Basel II),
- Anti-money laundering/terrorist financing regulations.

And it isn't just banks that are regulated in Canada. Certainly, the burden of regulatory overlap and duplication will continue to be a key challenge for all businesses. From City Hall to the National Assembly and of course on Parliament Hill, a new regulation is born practically every day.

Instead of thinking up new regulations and adding to the burden we need a system that is more flexible and more focused on market-based solutions. What is needed is a regulatory environment that is less prescriptive and intrusive. Our governments should recognize that the best regulator is in fact a competitive marketplace.

We would also like to see clear direction from governments that they will regulate only when necessary and only when analysis has shown that the benefits of the regulation outweigh the cost and that there is a real need for it.

A cooperative working relationship is also needed between business, government and regulators. I know, for example, that the Autorité des marchés financiers is making a strong effort to reach out and consult with business as it carries out its responsibilities.

When talking about regulatory reform, the country's need for a common securities regulator ranks high. Not only are Canadians paying to maintain 13 separate regulatory bodies, the cost to business of complying with 13 sets of rules is substantial.

And this is not just a large business issue. The CBA recently did a study of small- and medium-sized firms raising capital in Canada. Based on the results of our research we found that the current regulatory structure imposes unnecessary costs and inefficiencies on SMEs. More importantly, we determined that a common securities regulator would lower the cost of capital for SMEs, reduce their fees for complying with so much regulation and improve their nation-wide access to investors.

There are provinces, such as Quebec, promoting the passport system of securities regulation. While we recognize that they are taking important steps to make it easier for firms to raise capital, it remains a second-best solution. The passport system still imposes the same infrastructure, costs, and fees of the current multiple regulatory system, and builds in a confusing and overlapping enforcement system. Although there may seem like a lot of disagreement, it is on the issue of enforcement that we have some general consensus. In fact, I have had interesting discussions with Quebec Finance Minister Monique Jérôme-Forget about our shared concern for the need for effective enforcement and how dealing with the issue must be a priority.

When assessing our securities system, we cannot only think domestically. Our current system also impacts our ability to negotiate internationally. While free trade in securities is being discussed will Canada be at the table to negotiate arrangements? We have to be. The question is how can Canada – with 13 security regulators and no single voice speaking on its behalf - negotiate effectively with the US?

In the end, we need to develop the best solution for our country's securities regulatory system. And, I believe the opportunity to do so is before us. The expert panel on securities regulation can be the vehicle to achieve this objective. But, we need all voices at the table and all ideas put forward. I am confident that the best

solution for every region of the country and our collective national interests is possible if we want to make it happen.

And I know there is the will. We all recognize that the current system of securities regulation can be improved. Although we may disagree on what the best model is at the moment, I want to recognize the hard work and tremendous dedication of the provincial leaders on this issue. I know that they are committed to working to improve the current structure.

Conclusion:

My time is running out this afternoon and I should let you get to the office.

There are many elements that make up Canada's competitive advantage. I highlighted just a few areas that we believe should receive the focus of our attention and action.

It would make me very happy if our governments commit to take action in these areas. If they do, then we will without a doubt be the investment location of choice, attract head office jobs and we would ensure that our companies are able to compete with the best in the world.

I remind you, our competitive advantage must include all businesses wherever they are across the country.

When I look around this room I know that our firms and our sector are already making a significant contribution to the economy and to our competitiveness. Can we do more? Of course and we will. I am also confident that if we work with governments at all levels we can make Canada, and all its parts, not just more competitive but the most competitive economy globally.

Thank you.