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## Searching for stable ground: securing the future of Canada's auto industry

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Canada's auto industry has survived unprecedented upheaval since the global financial crisis and resulting recession of 2008-09. On one hand, the industry has demonstrated impressive resilience: output and exports have reattained levels similar to those that prevailed in the years before the crisis (with total assembly output stabilizing at just under 2.5 million vehicles per year, and parts shipments rebounding to above \$25 billion per year). Modest but continuing job-creation in both assembly and parts is another encouraging sign. Canadian plants continue to achieve superior recognition for their quality, productivity, and consumer appeal.

The Canadian auto industry is certainly smaller and leaner. And auto manufacturing communities have endured painful dislocation. But the industry is still here, and continues to make an enormous and strategic contribution to national output, exports, productivity, and incomes.

On the other hand, the industry's long-term future in Canada is far from secure. Our plants face an intense global competition for new investment and product allocations, which they need in order to remain highly utilized and profitable. Globalization and free trade agreements have undermined the demand for Canadian-made products, and made it easier for auto companies to exploit low-cost, often repressed workers in other countries. Employers then take advantage of unemployment and insecurity here in Canada to further drive down compensation and working conditions here at home.

### **Still Critical:**

Auto assembly and parts manufacturing, despite the troubles of the last decade, still make a disproportionate contribution to key Canadian economic metrics:

- Total Direct Employment: 120,000.
- Total Employment (counting "spin-off" jobs): over 400,000.
- Total Shipments: \$56 billion (assembly); \$27 billion (parts).
- Total GDP: \$17 billion value-added.
- Exports: \$66 billion (second-most important export industry).
- Productivity: \$210,000 per worker per year (assembly).
- Average Annual Incomes: \$72,000 (assembly), \$55,000 (parts).

All data 2014. Source: Unifor Research from Statistics Canada, Industry Canada Strategis, includes auto assembly and parts. Spin-off jobs generated at 10:1 ratio from major OEM plants (Center for Automotive Research, *Contribution of the Automotive Industry to the Economies of all Fifty States and the United States*, 2010).

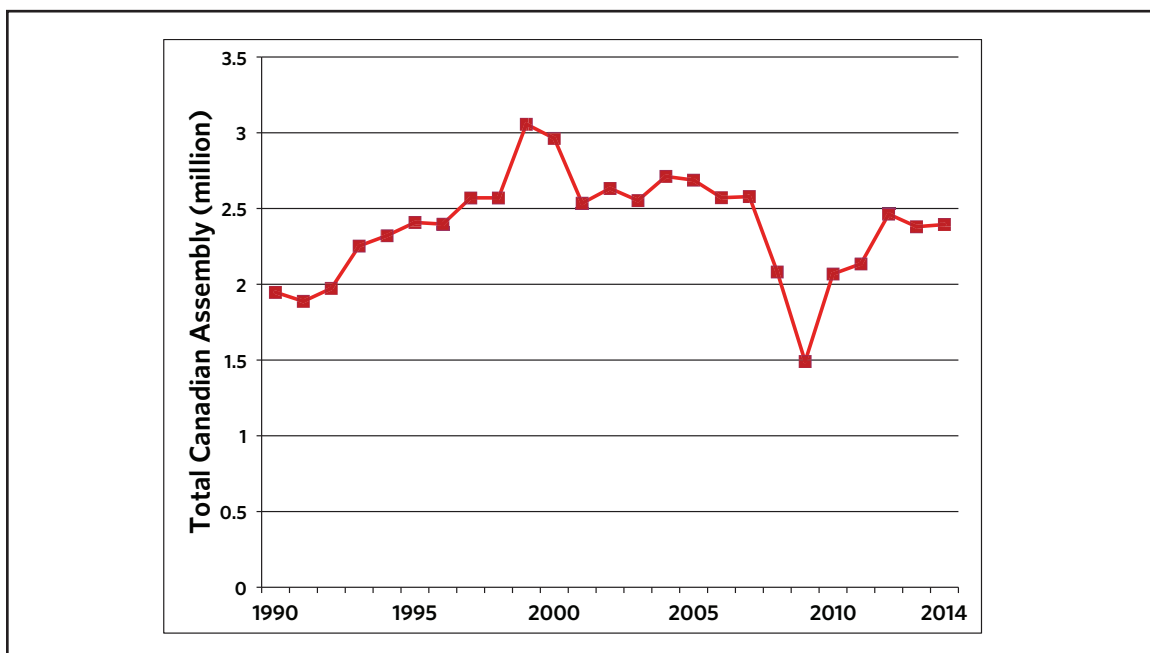
Meanwhile, our own governments have been tentative and uncertain in response to these challenges. To be fair, they have made important efforts to support Canadian investments – but in an ad-hoc and inconsistent manner, with no clear strategic vision to guide them. It is obvious that Canada lacks an effective, focused, consistent National Auto Strategy. But that’s exactly what we need if we are to retain the industry we have left – let alone successfully grow it in future years.

This bulletin will review the recent performance of Canada’s auto industry, highlighting both the challenges it continues to face, and its enduring strengths. It will describe the important spin-off benefits (employment, trade, and fiscal effects) which the industry continues to generate for Canada’s entire economy. And it will reinforce that Canadian governments must move energetically to reinforce the industry with a strong National Auto Strategy, if we want to continue to harvest those benefits in the years ahead.

## Output

Figure 1 shows annual assembly output from Canada’s auto industry. The industry peaked at a record of over 3 million vehicles in 1999: driven by smart trade policy (namely, the Canada-U.S. Auto Pact), a competitive currency, the savings from public health care, and outstanding productivity growth and quality performance. Ironically, that was the same year the World Trade Organization first ruled that the Auto Pact violated the “laws” of global free trade (and two years later Canada’s government bowed to the WTO’s wishes and dismantled the Pact altogether). Meanwhile, Mexico’s industry was taking off in the wake of the 1994 NAFTA deal, and the surge of offshore imports to North America was gathering momentum.

Figure 1: Canadian Assembly Output



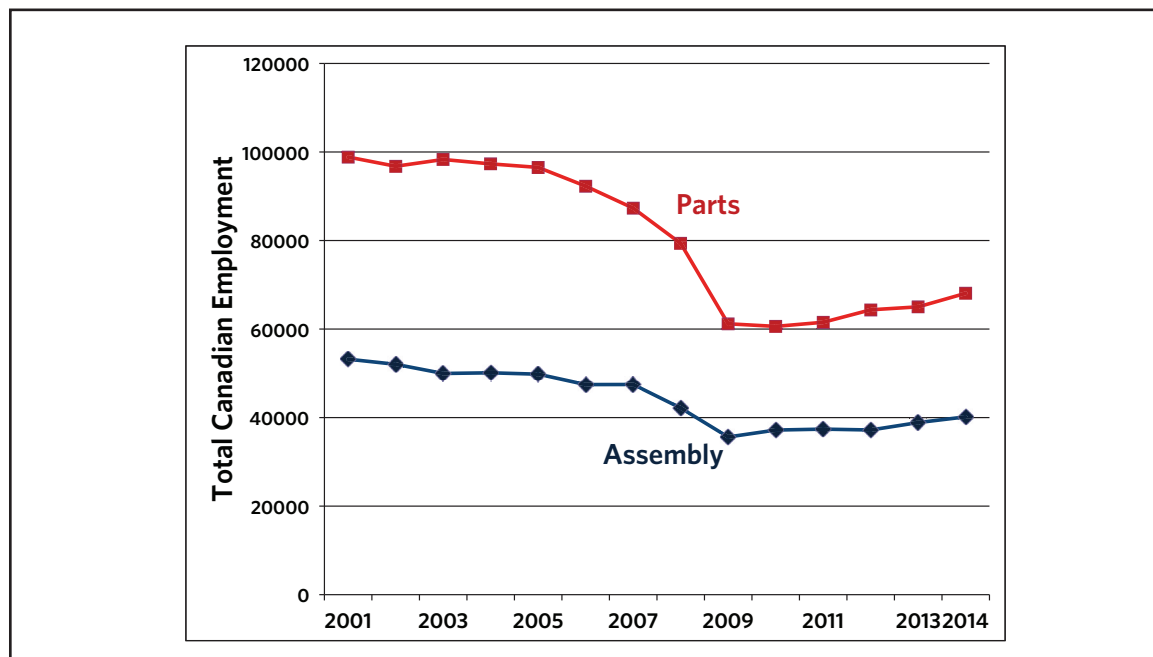
So Canada’s output slipped over the coming years, and Canada fell from the 4<sup>th</sup> largest auto producer in 1999 (a remarkable achievement for a small country) right out of the top ten by 2008. That’s when things got much worse: with a global financial crisis unleashed as a result of failed financial speculation and weak government regulation. The auto industry was hit hard, and output fell dramatically (to the lowest level since 1982). We avoided total collapse, however, thanks to the sacrifices of Canadian auto workers, strong government interventions in Canada and the U.S. to save GM and Chrysler, and a surprisingly quick rebound in continental sales. Output rebounded 65% over the next three years, and has since stabilized at just under 2.5 million units per year (see Figure 1).

## Employment

Like output, employment hit a low point in the 2008-09 downturn, when sales contracted badly in the face of weak demand, corporate restructuring, and plant closures. Since then, however, about 12,000 auto jobs have been created in Canada: half in assembly and half in parts. By 2014 over 120,000 Canadians were employed in automotive manufacturing: close to 70,000 in parts and components production, 40,000 in vehicle assembly, and another 12,000 in the manufacture of bus and truck bodies and trailers (see Figure 2). The industry has regained about one fifth of the jobs it lost in the years culminating in the 2008-09 recession. That’s not enough – but at least employment is heading in the right direction.

Incomes in the auto industry are superior to other occupations – although real wages have been clawed back significantly during the last tough years. Average annual incomes in auto assembly

**Figure 2: Canadian Auto Manufacturing Employment**



in 2014 were \$72,000 (about 50 percent higher than the Canadian average). Incomes in parts production (averaging \$55,000 in 2014) are about 15 percent higher than average. Outstanding productivity (the average auto assembly worker produces an incredible \$210,000 of GDP per year – making it one of the most productive industries in Canada’s entire economy) provides a real economic foundation for that prosperity. In sum, the auto industry is a crucial source of well-paying, high-productivity jobs, all the more important given the preponderance of low-wage, part-time, precarious jobs in recent years.



## International Trade

The global auto industry incorporates very strong international trade links. Indeed, trade is essential to successful auto production: strong specialization and economies of scale in auto assembly mean that no single economy could ever single-handedly produce all of the different vehicles demanded by its consumers. Ever since the Canada-U.S. Auto Pact of 1965, Canada’s auto industry has been fully integrated on a continental basis: most of our output is sold into the U.S. market, while most of our purchases come from the U.S. and other countries. This pattern of specialization and trade can be highly beneficial – but only if trade is two-way, broadly balanced, and mutually beneficial.

Until the late 1990s, Canada’s strong position in continental investment and production generated healthy automotive trade surpluses. The Canadian content requirements of the Auto Pact, the strong productivity and quality record of Canada’s relatively modern auto plants, and the advantages of a competitive currency and our public medicare system allowed Canada to win a share of auto production that exceeded our share of total auto sales. But our trade success was never “one-way”: our surplus was modest as a share of total two-way trade with the U.S., we shouldered a large ongoing trade deficit in auto parts, and we also experienced a chronic outflow of profits and other investment income (because our assembly industry was 100% foreign-owned). So while Canada benefited from this trade, so did the U.S.

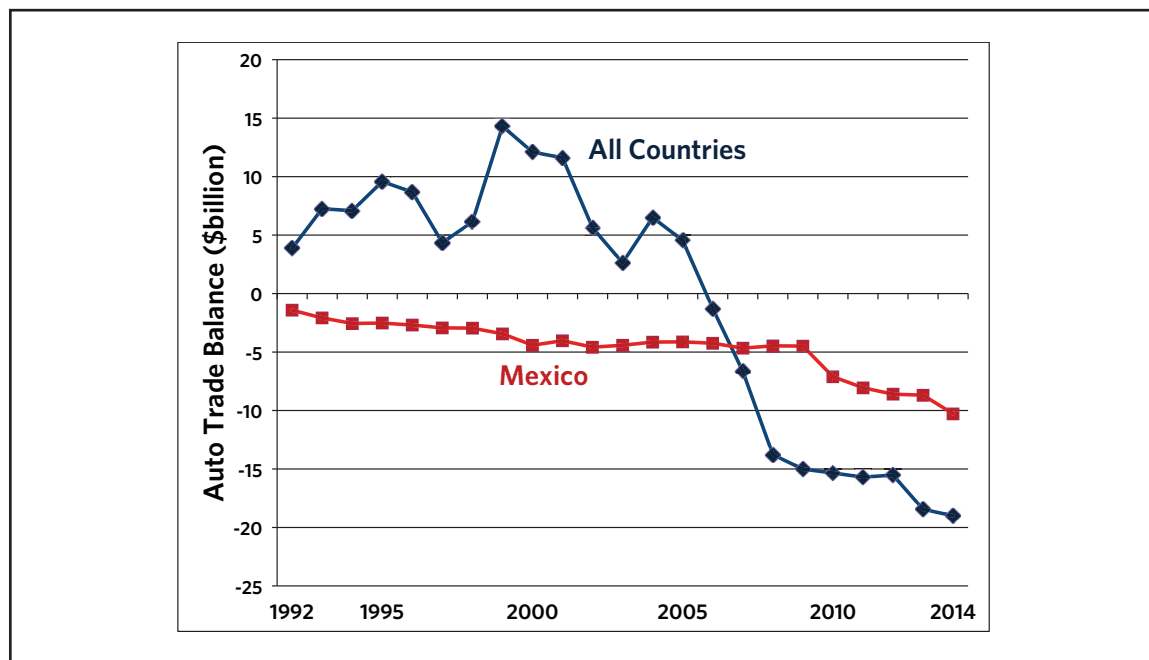
That trade success began to crumble after the turn of the century, for several reasons. The WTO banned the Auto Pact (and hence the requirement that participating manufacturers maintain a proportionate share of production in Canada was abolished). The Canadian

dollar took off to the stratosphere beginning in 2002 – due to soaring oil prices and unchecked financial speculation. The surge of imports to North America (from Japan, Korea, and Europe) also accelerated, undercutting demand for Canadian-made products both at home and in the U.S. And Mexico’s auto industry reached critical mass and began to suck in a huge share of total North American auto investment. Within a decade after signing NAFTA, Mexico suddenly became the favoured jurisdiction for new plants: based on super-low labour costs, suppression of normal union activity and political dissent, and a rapidly developing supply base.

The resulting flood of imports from Mexico, Asia, and Europe ate away at Canada’s trade performance. Our once-mighty automotive trade surplus became a net deficit by 2006 (see Figure 3), and this deficit swelled further in subsequent years. By 2014 the deficit reached a record \$19 billion. This marks an incredible \$35 billion deterioration in net trade performance in just 15 years (compared to the peak surplus of almost \$15 billion enjoyed in 1999). Over the half the auto trade deficit is now with Mexico.

Despite the erosion of our overall auto trade balances, the industry is still a crucial element of Canada’s participation in world trade. Automotive products are still Canada’s second-largest export (second only to petroleum). Given the recent decline in oil prices, it is possible that automotive products will regain its first-place position as Canada’s top export in the years ahead.

**Figure 3: Canada’s International Automotive Trade Balance**

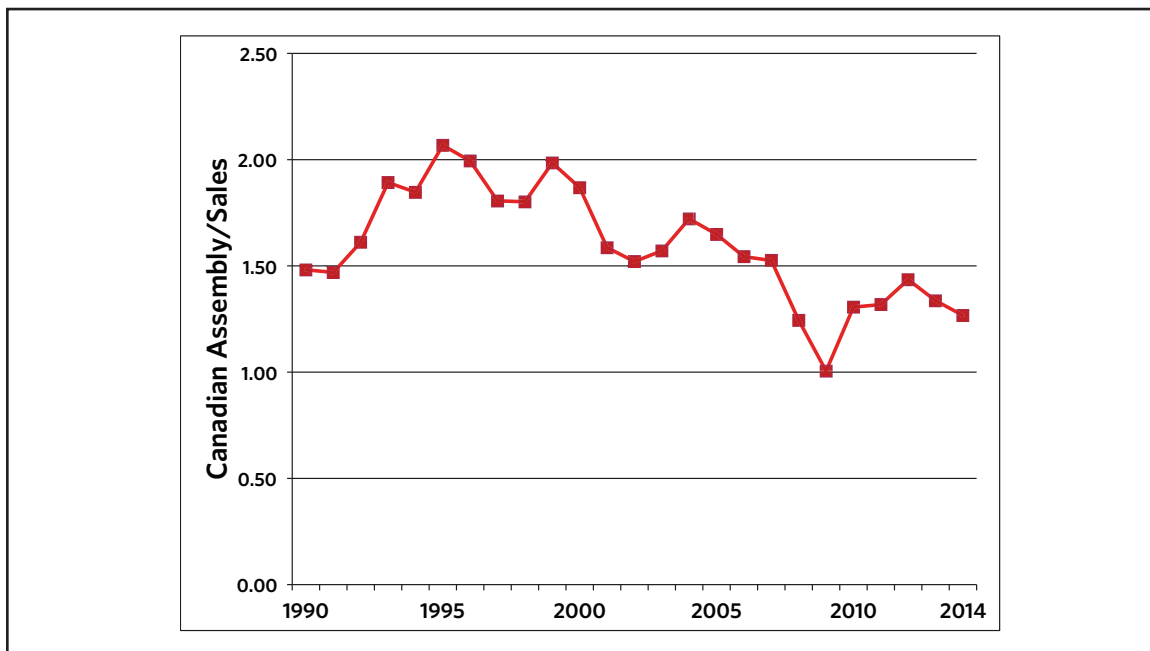




## Key Ratios

Several other key measures further attest to the relative erosion of Canada’s automotive position within the globalizing world industry. One important measure is the ratio of auto production in Canada, to the level of auto sales. As we have seen, output in Canada stabilized at under 2.5 million units per year (after the 2008-09 crisis). But Canada’s own auto sales remained relatively vibrant throughout this period – and more recently have been setting annual sales records, year after year. The combination of stagnant production with growing sales implies that our industry is not keeping up with the domestic market. This is evidenced by the declining ratio of assembly to sales in Canada (see Figure 4): this ratio declined from over 2 during the peak years of the late 1990s, to 1.25 in 2014 (this ratio even plunged briefly to 1-to-1 in the crisis year of 2009).

**Figure 4: Production-to-Sales Ratio**



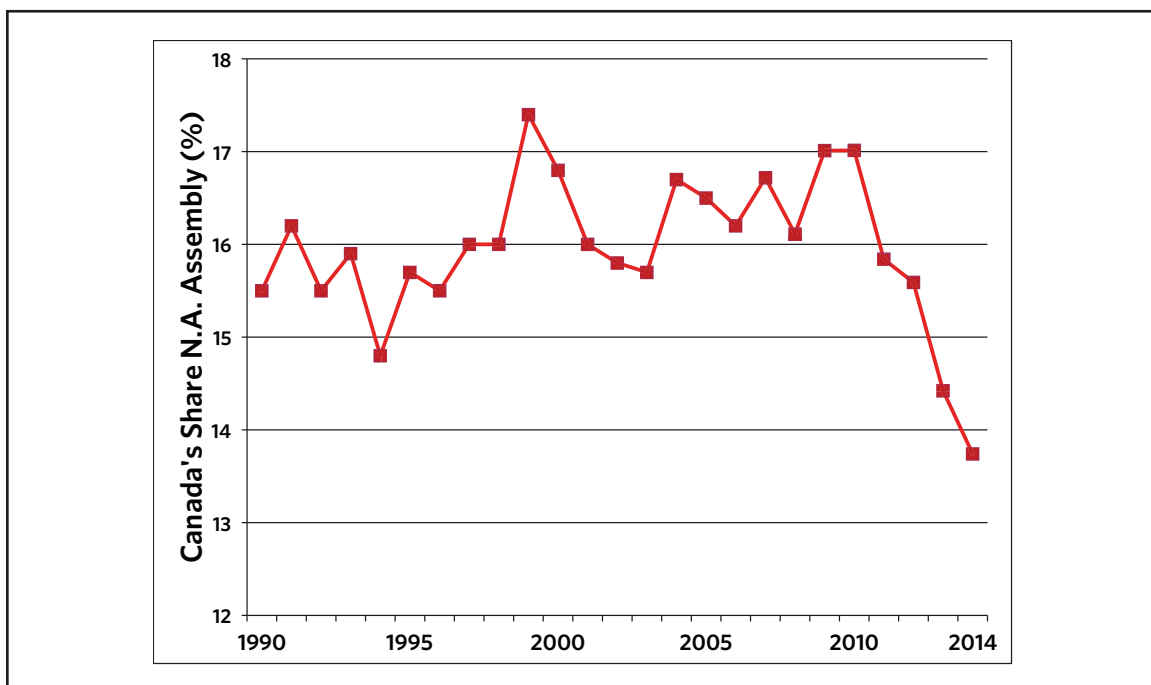
Some might conclude that since this ratio is still above 1 (for now, anyway), Canada has “nothing to complain about”: we still produce more than we consume. But this conclusion is misleading. First off, don’t forget that Canada produces far fewer auto parts than we consume (\$21 billion less in 2014) – and most of the value-added in a new car comes from its parts, not from its assembly. So on an overall basis, Canada already produces less automotive *content* than we consume, even though we assemble more vehicles than we buy. (This explains why we have an automotive trade deficit, despite producing more vehicles than we sell here; the deficit in auto parts is much larger than our surplus in finished vehicles.) Moreover, the declining trend in the production-to-sales

ratio is a clear warning sign that Canada could quickly lose its place in the global industry if we don't turn things around.

A similarly worrisome sign is the erosion of Canada's share of total production within the integrated continental marketplace. Traditionally Canada represented at least 15% of all North American assembly. This ratio even grew somewhat in the initial years after NAFTA. Overall industry conditions during that time were being undermined by the growth of imports from offshore. But within North America, at least, Canada was able to hold its own, for a while. Ironically, even in the crisis-ridden years of 2009 and 2010, Canada's continental share reached 17% – a near-record high. This was partly due to the effective "Canadian manufacturing footprint" measures implemented by our governments at that time, as a condition of their participation in the binational effort to rescue GM and Chrysler from collapse.

Since 2011, however, Canada's share of total continental production has declined dramatically – and it shows no sign of pulling out of that nose dive (see Figure 5). It's not that Canadian output has fallen: as noted, assembly has stabilized (at close to 2.5 million vehicles per year) since the financial crisis. But as continental sales recover (U.S. sales in particular have rebounded faster than analysts expected, driven by strong job-creation and growing consumer confidence), Canada's producers have not been sharing in the new opportunities.

**Figure 5: Canada's Share of North American Assembly**





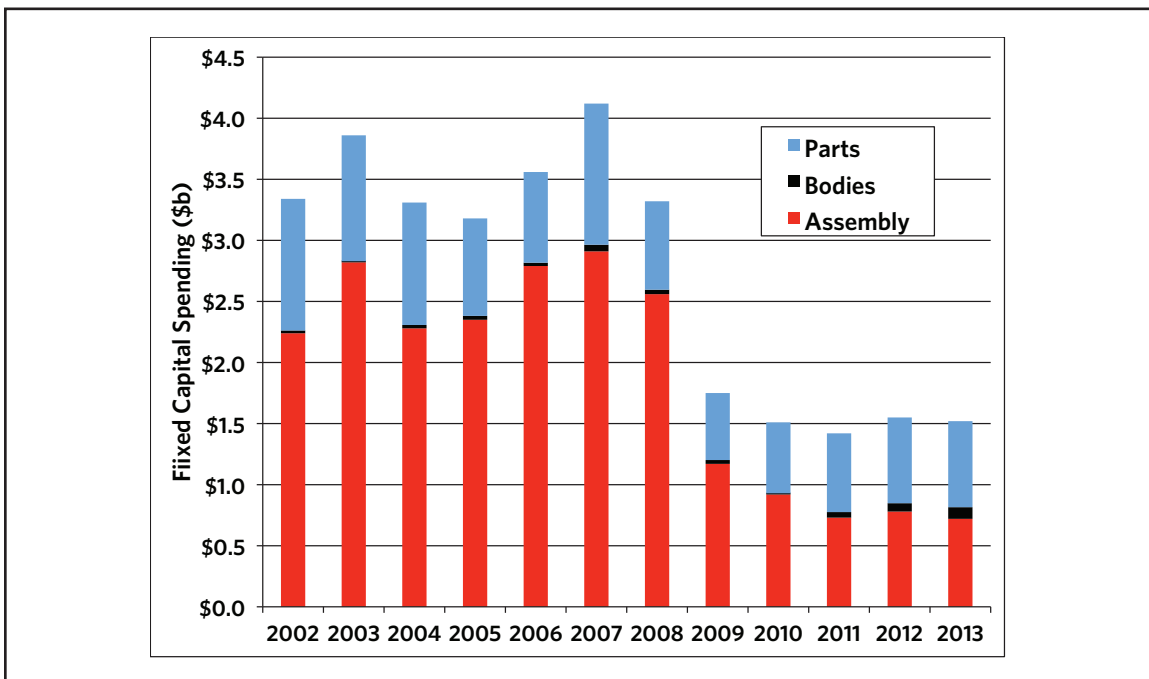
Instead, the overwhelming share of new growth has been captured by Mexico. Since 2009 that country has “landed” eight new assembly plants, as automakers of all kinds rush to take advantage of low labour costs, a developing transportation infrastructure, and an expanding supply base. Mexico now accounts for one in five of all vehicles assembled in North America. The U.S. accounts for two-thirds of continental production (a share that has been stable since the financial crisis). And Canada is down to producing less than one vehicle in seven.

## Investment

One especially worrying indicator of Canada’s automotive position has been the decline of new investment spending in Canadian plants. Whether it is investing in new tooling in an existing facility (perhaps in conjunction with a new product allocation), or building a brand new greenfield plant, continuing capital spending is essential to maintain the vitality and viability of our industry. Strong capital spending in previous years (especially the booming 1980s and 1990s) laid the groundwork for quality, productivity, exports, and job-creation. But now, in the context of global pressure and the race to Mexico, investment spending in Canadian facilities has suffered.

Prior to the financial crisis of 2008-09, capital spending in Canadian assembly and parts sectors averaged over \$3 billion per year (Figure 6). New investment declined sharply during the crisis, to less than half that traditional level; this was not surprising, given miserable market conditions and the financial crunch faced by many auto producers. But even in the years since the recovery began, investment has not yet regained its former levels.

**Figure 6: New Capital Spending in Canadian Auto Plants**



Some important new investment commitments to Canadian plants have been made in the past year, and those commitments (once operationalized) will lead to an improvement in the data illustrated in Figure 6. These include major capital spending in Chrysler's assembly plant in Windsor, Ford's Oakville operation, GM's plant in Ingersoll, and re-tooling and expansion at Toyota and Honda. In every case, government played a crucial role in cementing new capital spending: including investment supports, restructuring assistance (tied to Canadian content), and infrastructure improvements. But several other auto facilities in Canada are in a desperate struggle to confirm future investment and product allocations. Taking active measures to enhance Canada's share of automotive investment spending, and ensure a long-run future for our existing plants (perhaps, one day, even winning new ones) must be the number one priority for a National Auto Strategy.

## Trade with Mexico is Not “Free”

The stunning take-off of Mexico's auto industry occurred in the wake of the North American Free Trade Agreement (NAFTA), signed in 1994. That deal gave Mexican plants full, unconditional access to the U.S. and Canadian markets – with no requirement for reciprocal trade. Of course, no industry can pack up and move to another country overnight: especially an industry with large fixed capital requirements, like auto. But over time, industries can migrate as surely as birds: old plants are worn down and not replaced, and new ones are built elsewhere. Initially, Mexico's expansion was limited by a lack of reliable transportation infrastructure and regional auto parts capacity. But that changed over time, as more parts plants joined the migration south, and transportation links became more developed.

The “giant sucking sound” which NAFTA critics warned of in 1994 has proven absolutely true: global companies treat Mexico primarily as a source of cheap labour. Export-oriented production in Mexico does not translate into a mutual and beneficial two-way trade flow. Our jobs are lost as more plants move south. And the continental race-to-the-bottom unleashed by this distorted version of “trade” undermines wages and working conditions across the continent.

In Canada's case, Mexico's rapid automotive expansion translates inevitably into a huge and growing bilateral auto trade deficit. Mexico is producing more vehicles and selling into Canada without limit. Investment in Canadian facilities is undermined accordingly – not surprisingly, given the lure of rock-bottom production costs down there. Yet Mexicans cannot afford to buy the vehicles (or much of anything else) that we produce. The result is a one-way street that is rapidly becoming a superhighway.

Since NAFTA was signed, Canada's automotive imports (vehicles and parts) from Mexico have grown five-fold, reaching \$11 billion in 2014. Our exports to Mexico last year were

## Winning Streak:

Since the global financial crisis and world recession of 2008-09, eight new vehicle assembly plants have been constructed or announced in Mexico:

- General Motors San Luis Potosi.
- Honda Celaya.
- Audi San Jose Chiapa.
- BMW San Luis Potosi.
- Nissan Aguascalientes.
- Mazda Salamanca.
- Mercedes Benz Aguascalientes.
- Toyota Guanajuato.

These new plants could push Mexico's assembly output from over 3 million units per year today, to over 5 million units within 5 years. And Canada's already huge auto trade deficit with Mexico could double.

*Source: Unifor Research from media reports.*

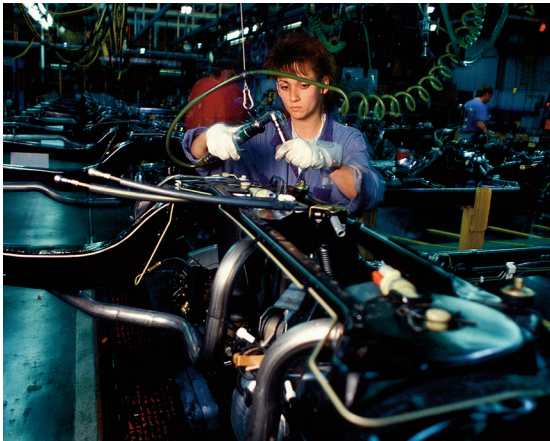
only \$800 million – actually lower than a decade ago. (So much for Canada benefiting from Mexico's growth.) Surging imports and insignificant exports can mean only one thing: an enormous and growing automotive trade deficit that exceeded \$10 billion in 2014 (see Figure 3). That is the largest bilateral trade deficit that Canada has ever experienced (much bigger even than huge auto deficits experienced in various years with Japan).

The most galling and offensive aspect of Mexico's automotive take-off is that average Mexicans are not even benefiting from this southward continental migration. Real industrial wages in Mexico are no higher (after inflation) than they were when NAFTA was signed – despite the incredible expansion of output, quality, and productivity since then. Mass displacement of agricultural populations (another legacy of NAFTA) has pushed millions of desperate Mexicans off the land and into urban labour markets. Most insidiously, there is a demonstrated and sustained pattern of democratic and labour suppression in Mexico that prevents Mexicans from winning a fairer share of the growing pie they produce. A few Mexicans have benefited enormously (telecommunications magnate Carlos Slim, for example, is the richest person in the world, with a personal fortune of \$80 billion). But most still live in poverty, and it is a deliberate goal of government policy to keep wages low. Mexico has by far the worst inequality of any country in the Organization for Economic Cooperation and Development. Industrial wages in China are now higher than in Mexico.

The frightening and violent reality of Mexico's political and labour relations climate has become increasingly obvious in recent years. One shocking example was the massacre of

43 student protestors in Iguala in 2014 – a crime against humanity committed with the complicity of local police and government officials, and which the government (and the media) only began to investigate seriously following unprecedented nation-wide protests. Canadian government officials have made no comment on this outrage (even as they wax eloquent about human rights and religious freedom in the Middle East). Media pundits blame the whole problem on “drugs.” But there are deeper, systemic problems of corruption, rule of law, and police violence that suppress the normal economic and social processes expected in a free society. Violence, extortion, hijackings, and kidnappings are even a worry for top managers of the global companies who have established facilities in Mexico (forcing them to spend significantly on security and related costs). But this does not stop them from rushing to take advantage of Mexico’s desperate, low-cost, repressed labour force.

This situation can hardly be described as “free trade” in any legitimate sense of that concept. Mexican workers are hardly free: they have no power to demand and win a decent share of the wealth they produce. Mexicans working in an auto factory are no doubt grateful for the job they have been able to find – but that is only relative to the deprivation and violence that surrounds them. And conditions, compensation, and legal rights in Mexican auto plants can only be described as outrageous by Canadian standards. Worst of all, they are not getting better.



NAFTA defenders smugly claim that those who opposed continental free trade had their “heads in the sand,” and that subsequent events have proven free trade was the right idea all along. This claim is nothing more than the propaganda of those with power.

Canada’s trade relations with Mexico are one-sided and indisputably damaging to our economy and labour market. (Remember, our enormous automotive trade deficit is joined by an even larger deficit in other

manufactured goods, producing an overall bilateral imbalance that exceeded \$23 billion in 2014.) It is time to have an honest discussion in Canada about the long-run loss of investment and employment that NAFTA continues to facilitate – and to investigate the reasons behind both the unsustainable imbalance in our bilateral trade with Mexico, and the continued languishing of economic and political conditions there. For this reason, Unifor is asking the House of Commons International Trade Committee to conduct an official inquiry into the causes and consequences of Canada’s trade imbalance with Mexico. Remedies to the situation can then be informed by a better understanding of the nature of the problem.

## Tracking the Spin-Off Effects

The positive employment, fiscal, and trade spin-off effects from auto production are well-appreciated by economists, industry, and government alike. There are several key reasons why the auto industry plays a uniquely important and strategic role in the national economy:

- The industry is very technology-intensive, and uses a high amount of capital equipment in production.
- Thanks to capital tooling and highly-skilled workers, productivity is very high.
- Thanks to high productivity (and to the efforts of unions), incomes are also relatively high.
- Most of the industry's output is exported, and hence it contributes to national trade performance.
- The industry supports an extremely complex supply chain, which leads to additional jobs in many different industries.

Because of these features, each job in a major auto facility ultimately supports a much larger complement of employment and income throughout the national economy. These positive spin-off effects can be grouped into two broad categories:

- “Upstream” effects: Jobs and income generated in auto parts production and all the other specialized supply and service industries which provide inputs to auto production (including metal, plastic, electric and electronic, utilities, business and marketing services, transportation, and more).
- “Downstream” effects: Jobs and income generated in the domestic industries which depend on the incomes and spending power of those employed in auto production and the supply chain (including home-building, local consumer goods and retail, entertainment and hospitality industries, and even public services such as education and health care... which after all are financed in part from the taxes paid by auto workers).

Past research has indicated that each job in a major auto facility (assembly or powertrain) supports a total of ten positions elsewhere in the national economy, thanks to both upstream and downstream spin-off effects.<sup>1</sup>

To enhance our understanding of the importance of these linkages in the Canadian context, Unifor recently commissioned an independent research study from the Centre for Spatial Economics (C4SE, an economic consulting firm based in Ontario). The study considered the potential loss of employment, incomes, and tax revenues resulting from a worst-case scenario: the total closure of one of Canada's major automotive assembly facilities (the GM

1 For example, see Kim Hill, Debra Menk, and Adam Cooper, Contribution of the Automotive Industry to the Economies of all Fifty States and the United States (Ann Arbor, MI: Center for Automotive Research, 2010), 64 pp.

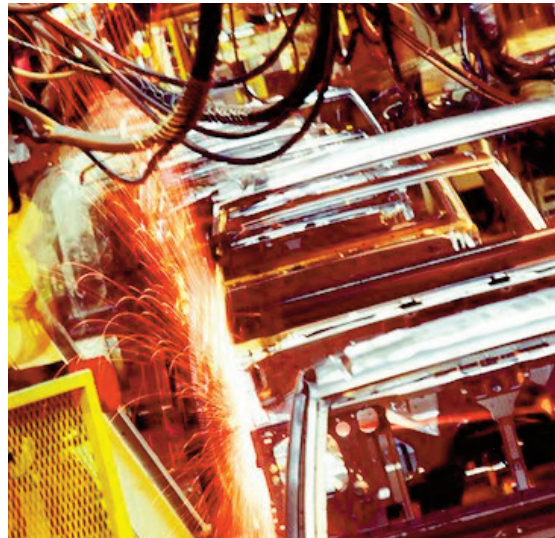


complex in Oshawa). This facility (like many others in Canada) is currently fighting to win future capital investment and product mandates.

The C4SE report (available on the Unifor website, [www.unifor.org](http://www.unifor.org)) provided concrete, surprising evidence of the enormous impact that even a single automotive complex can have on the evolution of the entire national economy:

- Within two years of the closure of the complex (eliminating 4100 direct and salaried positions), a total of 33,000 jobs were lost in the broader economy (due to spin-off contractions in the supply-chain and in downstream consumer spending).
- National GDP contracts by over \$5 billion per year.
- Wages decline across the entire labour market, shocked by the loss of so many highly-productive well-paying jobs: on average, workers in Ontario each lose over \$300 in annual labour income.
- Other long-run labour market effects include a significant out-migration from Ontario.

Perhaps most tellingly, the federal and provincial governments are among the stakeholders most harmed by the loss of this major automotive manufacturing complex. Their combined loss of revenues (income taxes, sales taxes, and corporate taxes, all resulting from the contraction in broader GDP) exceeds \$1 billion per year in the period immediately following closure. Even many years after closure, the two levels of government still forego hundreds of millions of dollars in revenue each year.



Ottawa's losses exceed the revenues lost by the provincial government (reflecting the federal government's larger tax take in the whole economy).

This finding gives the two governments ample fiscal reason to act quickly to protect Canada's auto manufacturing footprint. And it disproves the claim that government participation in new auto investments represents some kind of "hand-out" or "corporate welfare": to the contrary, if government does not act to stabilize and grow Canada's industry, then government budget balances (and all Canadian taxpayers) will suffer enormous revenue losses. Supporting the auto industry truly constitutes a fiscal "investment" by government – and one with a very quick and beneficial pay-back.



## Getting Back on the Road:

Canada's auto industry can survive, and thrive, even in a hyper-competitive global environment. But to do so, it must be supported by a focused, consistent, and effective National Auto Strategy. So far, despite years of talking, and many ad-hoc interventions, the federal and Ontario governments have failed to implement such a Strategy. Many policy tools must be invoked, to create the winning conditions for a successful and stable industry – including fiscal, trade, technology, procurement, skills, and infrastructure measures. (The former CAW outlined a detailed proposal for such a strategy in its 2012 document, *Rethinking Canada's Auto Industry*.) To get the ball rolling, here are eight immediate and pragmatic measures that would better align and focus Canada's auto policy, and win a fair share of the auto investments we desperately need. They are described further in the following pages::

1. Better integrate the federal and provincial investment attraction efforts, and develop a “one-stop” system to win new investment in Canadian assembly and parts plants.
2. Ensure Canada's investment incentives are competitive and efficient, with flexible rules and procedures, and sensible fiscal and tax features (for example, removing the current federal tax which is charged on up-front incentives).
3. Ask the House of Commons International Trade Committee to commission an independent study of the \$10 billion trade deficit in automotive products with Mexico, its causes and consequences, and potential strategies for reducing it.
4. Increase fiscal support for Canadian research and development in new automotive products and technologies, in conjunction with industry and universities, with provisions to ensure that Canadian production benefits from the resulting research.
5. Currency imbalances can dramatically affect trade flows and investment decisions. Canada's interest rate and banking policies should take into account the importance of stabilizing the Canadian dollar at or near its fair value. And future trade agreements must contain measures which offset currency manipulation and distortions by other countries.
6. Ensure that Export Development Canada's top priority is attracting and supporting investments in Canadian-based factories (not foreign factories).
7. Ensure that Ontario's new carbon pricing system is applied in a manner that enhances the business case for new investment in Ontario automotive plants.
8. Commit to engaging all stakeholders (through the Canadian Automotive Partnership Council and other bodies) to finally develop and implement a focused, consistent, and effective National Auto Strategy.

## Taking the Next Steps

It would be easy to be pessimistic about the future of Canada's auto industry, given the daunting global trends which confront this vital sector. But that would be a mistake. There are plenty of other countries where a combination of active policy support, collaboration among key stakeholders, and a commitment to top-notch quality and innovation have combined to support continued industrial success – even in a relatively high-cost environment. For example, countries such as Germany, Japan, and Korea continue to implement a broad mix of policies (from active trade supports to technology incentives to strategic subsidies to outright public ownership) to ensure continued investment, employment, and net exports from their auto producers. Even the U.S., despite its supposed commitment to “free enterprise,” has wielded strong government measures (including huge capital subsidies, “Buy America” procurement policy, and moral suasion) to stabilize its share of investment and employment.



Canada's governments (both federal and Ontario) have taken some important steps in recent years to defend Canada's industry in the face of the 2008-09 downturn, and other continuing challenges. Most notable, of course, was the dramatic and successful joint effort (in conjunction with the U.S. government) to save GM and Chrysler from collapse in 2009; that restructuring stabilized the Canadian footprint of both companies, and helped win crucial new investments in some of their Canadian

plants. But now the governments are ending their direct involvement with the two companies (selling off their shares, and allowing the Canadian footprint commitments to lapse). For other auto producers, and in the parts sector, government policy interventions have also been important (helping win key new investments), but have been similarly inconsistent and ad-hoc. Crucial potential investments (like an important recent proposal to build high-tech small engines in Ford's Windsor complex) have slipped through our fingers, in part due to Canada's inconsistent and uncertain auto policy framework.

The need for a clear, consistent, and powerful National Auto Strategy in Canada has long been acknowledged by automotive stakeholders – including through industry bodies like the Canadian Automotive Partnership Council (CAPC), which Unifor participates in. Despite their occasional interventions, despite the existence of pre-approved budget programs

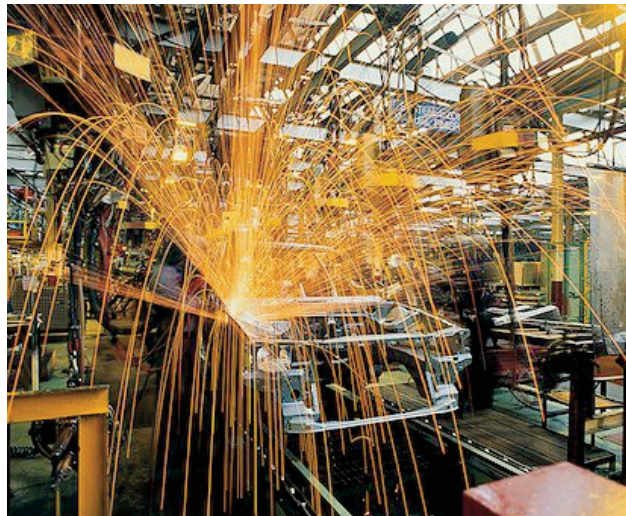
(such as the federal Automotive Innovation Fund), and despite the rhetoric of campaigning politicians, Canada still does not have such a Strategy.

The industry has demonstrated its resilience by surviving the turmoil of global crisis and corporate restructuring. And it continues to generate huge economic and fiscal spin-off benefits that demonstrably improve the well-being of all Canadians (not just those who work directly in the industry). Now is the moment for government to support the long-run stabilization, and eventual growth, of our industry. They must work with industry stakeholders (through CAPC, and through other forums), to define and implement policies that truly allow Canadian operations to not just survive – but to thrive. We propose several immediate, concrete steps (summarized in the box, on p.15) that could be taken to kick-start a National Auto Strategy.

- 1. Better integrate the federal and provincial investment attraction efforts.** At present there is little coordination between federal and Ontario governments in pursuing potential investments for Canada, and supporting those investments with fiscal incentives and development approvals. More coordination and cooperation between the two governments would go a long way toward presenting a consistent, more appealing Canadian case to global automakers. The Canadian Automotive Partnership Council has proposed a joint federal-provincial bureau to coordinate the investment attraction effort – but the idea has been turned down by the federal government.
- 2. Ensure Canada's investment incentives are competitive and efficient.** Previous investment incentives have been provided on an ad-hoc basis. Some investments are supported, some are not, and the level of support is never clear to automakers ahead of time. Some rules associated with investment incentives make them of little practical value. In some cases, the government actually takes back some of the support as soon as it is given: for example, the federal government treats investment supports as a form of taxable income, so the automakers must return some of the money immediately to Ottawa. Innovative ownership structures could be pursued (where governments take an equity position in new projects, perhaps through build-and-lease arrangements) to maximize the appeal of a Canadian location, while protecting the public interest. Incentives can be tied to specific commitments regarding proportional production shares and other flexible rules. A good example of this approach is the “Canadian footprint” commitments negotiated with both GM and Chrysler in the 2009 restructuring deals, which were a powerful factor behind the continued strong Canadian presence of both companies – but which unfortunately expire at the end of 2016.
- 3. Study the automotive trade deficit with Mexico.** The evidence is overwhelming that automotive trade and investment relations with Mexico are unbalanced and highly damaging to Canadians. No matter how often politicians repeat their mantra that “free

trade is perfect,” the inconvenient facts (a \$10 billion auto trade deficit, corresponding to the loss of at least 15,000 good auto jobs) cannot be denied. NAFTA is not set in stone. As a simple first step, we ask the House of Commons International Trade Committee to commission an independent study of the imbalance in automotive trade with Mexico, its causes and consequences, and potential strategies for reducing it. The study should also consider the economic implications of free trade with a jurisdiction in which the normal processes of dissent, collective bargaining, and public opinion do not exert their expected influence (and hence wages and other prices do not respond normally to economic growth and productivity). This problem is reflected most worryingly in the continued suppression of human and labour rights in Mexico, and the resulting stagnation of wage levels despite soaring exports and productivity.

- 4. Increase fiscal support for Canadian research and development, tied to Canadian production.** Recent changes to Canada’s long-standing R&D tax credit system will have a range of impacts (some positive some negative) on R&D in the auto industry. More research is no panacea for Canada’s automotive challenges – especially since global companies can still take advanced technologies, but put them to work in low-cost foreign jurisdictions. And the number of new engineers who could be hired in Canada through expanded R&D efforts can never offset the mass disappearance of production jobs. However, assisting Canadian-based companies to upgrade their technical and engineering capacities, and develop and produce new products, can generate some economic benefits here at home. We support measures to support greater R&D and innovation by both assembly and parts companies, but those measures should include provisions to ensure that resulting research and innovation translates into increased production and employment in Canada.



- 5. Make sure currency imbalances do not negatively impact Canadian jobs and production.** Currency misalignments can dramatically affect trade flows and investment decisions. Many other countries actively manage their exchange rates (explicitly, or indirectly through alternative policies such as “quantitative easing”) to support domestic production and boost net exports. Canada has traditionally left these decisions up to “market forces” (which actually means leaving them up to unregulated financial

speculators betting on the connection between our currency and oil prices). The long run-up in the Canadian dollar (which began in 2002, and only subsided recently) imposed dramatic costs on Canadian auto producers (especially in the parts sector). Here at home, our interest rate and banking policies should take into account the importance of stabilizing the Canadian dollar at or near its fair value. Economists believe, on the basis of relative prices, that the loonie's fair value is around 80-81 cents U.S. At that level, our producers have a fair shot at winning new business (since our relative international costs reflect our true costs). Our policy-makers must ensure that future oil price surges do not flow through into another overvaluation episode (which would undo much of the progress our industry has made since 2009). Globally, too, we cannot ignore the impacts of currency misalignments. Future trade agreements must contain measures to curtail and punish deliberate efforts by other countries to manipulate and distort their currencies in order to artificially generate and maintain trade surpluses.

- 6. Put Export Development Canada's focus where it should be: on supporting Canadian production.** Canadians were shocked recently to learn that EDC, a federal export credit agency, had loaned \$525 million to Volkswagen in support of its major new auto investments in Mexico and Tennessee. Why would a Canadian public bank offer its support to a company which sells \$4 billion per year worth of vehicles in Canada – yet which has no direct manufacturing presence here at all? EDC's stated rationale (the loan would allow them to demand that VW at least talk to Canadian parts suppliers about new contracts) is utterly unconvincing. The federal government should review EDC's lending practices, and direct the agency to use its resources to attract and support investments in Canadian-based factories (not foreign factories) as its top priority.
- 7. Ensure Ontario's new carbon pricing system is applied in a manner that enhances new investment.** Ontario has moved pro-actively to reduce the environmental side-effects of electricity generation, by phasing out coal-fired plants (the most polluting source of electricity) and encouraging more renewable energy sources. These efforts have been important for the environment, but have also had implications for electricity prices. Special policies for major industrial users have helped mitigate the impact on manufacturers; those policies must continue. Now Ontario is moving to a cap-and-trade carbon pricing system. This system must be implemented in a manner that does not hurt the business case for new investments in Ontario, that prevents companies from avoiding climate rules by outsourcing production to foreign jurisdictions, and that rewards the industry for measures it has taken to reduce emissions. Done right, Ontario's energy and climate policies could give our industry an edge as the global auto industry moves to a cleaner future.



**8. Engage all stakeholders to finally develop a focused, consistent, and effective National Auto Strategy.** In the self-help movement, it is often said that admitting you have a problem, is the first step toward a solution. Canada’s policy-makers have yet to even acknowledge the absence of a focused and consistent National Auto Strategy. Despite many ad-hoc (and often important) interventions over the years, there is no clear policy framework which announces to global automakers that Canada is here for the long-term. In contrast, some recent federal actions (such as the premature sale of public shares in GM and Chrysler, and the new free trade agreement with Korea which offers no prospect of increased automotive exports for Canada) could even be interpreted as a signal that Canada is “giving up” on auto. After years of stop-and-go actions, it is time for the federal and provincial governments, in conjunction with all automotive stakeholders (including automakers Unifor, parts companies, municipalities, universities and colleges, and more), to finally put together a consistent, effective national plan. Merely acknowledging that we need one, and getting serious about its development and implementation, would be an important signal that Canada means business.

## A Time for Action

Canada has a long and rich automotive history. Only recently we ranked as the fourth largest producer in the world, and punched far above our weight in international auto trade. Unfortunately, that legacy has been undermined by global pressures and policy neglect. Yet despite its recent tribulations, Canada’s auto sector remains vibrant and resilient, and is still crucially important to our national economy.

Signs of potential prosperity abound: growing auto sales, renewed investment in some facilities, gradual job gains, and a lower dollar. To make the most of these opportunities, it is essential that the federal and provincial governments cooperate to develop a truly consistent and effective National Auto Strategy. With a federal election this autumn, and Ontario a key electoral battleground, this is a crucial moment for autoworkers, and everyone with a stake in this industry, to make our voices heard.

Talk to your local political candidates. Enlist the support of local businesses and chambers of commerce. Discuss the issue at your local union or community meeting. Write a letter to your local paper.

Make sure your voice is part of our call to sustain and grow this vital part of Canada’s economy.

