CANADIAN MANUFACTURERS & EXPORTERS

MANUFACTURIERS & EXPORTATEURS DU CANADA

WRITTEN SUBMISSION FOR THE PRE-BUDGET CONSULTATIONS IN ADVANCE OF THE 2022 BUDGET

BY: CANADIAN MANUFACTURERS & EXPORTERS (CME)

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RECOMMENDATIONS

1. **Recommendation 1**: That the government de-risk and encourage manufacturers to digitize, automate, and adopt advanced technologies. Specifically: (i) Introduce a 10 per cent refundable investment tax credit; (ii) Expand and make permanent the Strategic Innovation Fund (SIF) and commit at least $2.5 billion in annual funding; (iii) Relaunch investment support grant programs like the CME SMART Program for small and medium manufacturers.

- **Recommendation 2:** That the government support R&D spending and scale-up of companies by improving and enhancing the SR&ED program. Specifically: (i) Expand the range of SR&ED-eligible activities; (ii) Introduce a refundable component to the SR&ED credit for all claimants; (iii) Return the SR&ED tax credit rate to 20 per cent; (iv) Support scale-up by reducing the SR&ED grind down for growing companies.
- **Recommendation 3:** That the government implement a patent box regime to reward commercialization and production of goods and advanced technologies in Canada.
- **Recommendation 4:** That the government support manufacturers in their efforts to address current and anticipated labour and skills shortages. Specifically: (i) Renew and expand funding for CME's Women in Manufacturing initiative; (ii) Introduce a 50 per cent worker training tax credit; (iii) Increase the size of the Canada Jobs grant to $1 billion annually, make it permanent, and expand it to include on-the-job training.
- **Recommendation 5:** That the government help the manufacturing sector adapt to and advance Canada's climate change goals. Specifically: (i) Provide direct investment supports for emitters of all sizes to help them adopt emissions-reduction technologies; (ii) Provide financial support for the creation, commercialization, and manufacture of low- and no-carbon products in Canada through tax incentives and government procurement; (iii) Create an SME net-zero transition strategy.
- **Recommendation 6:** That the government work to increase Canadian value-added exports. Specifically: (i) Fund the creation of an Exporter Concierge Service that enables trade associations to connect their members to government export agencies and services; (ii) Create a "Trade Barrier Hotline" for exporters to call and report trade barriers and to offer exporters assistance in overcoming trade barriers; (iii) Invest in infrastructure that facilitates trade and industrial development.

INTRODUCTION

By any measure, manufacturing is critical to Canada. The country's 90,000 manufacturers directly generate over 10 per cent of the country's GDP and nearly two-thirds of its merchandise exports. Including direct and indirect impacts, the sector's footprint amounts to nearly 30 per cent of Canada's economic activity. The sector directly employs 1.7 million Canadians and supports their families and communities through stable, highly skilled, high wage jobs, and supports over 3 million more Canadian jobs through its massive integrated supply chain.

The sector's critical importance has been amplified during the COVID-19 pandemic. At the onset of the crisis, many manufacturers ramped up or shifted production to make more food, PPE, and other health care products that have helped in the fight against COVID-19. And, because the industry was deemed an essential service and allowed to continue operating, it helped to stabilize the economy during the various waves of the pandemic.

As the pandemic recedes, climate change and the transition to a low-carbon economy is moving to the top of the policy agenda. Canadian manufacturers are committed to creating a clean and healthy environment for all, and many of Canada's top industrial companies have pledged to reach net zero emissions by 2050. However, this transition will be incredibly difficult and prohibitively expensive. It will only succeed with the right levels of investment and support from the government.

Along with the need to reduce its carbon footprint, the manufacturing sector faces several challenges that threaten its outlook, including supply chain disruptions, labour and skills shortages, and a prolonged investment slump. Indeed, spending on machinery, equipment and intellectual property products in Canadian manufacturing has fallen by almost 7 per cent since 2005, leading to a decline in the global competitiveness of the sector and of the overall Canadian economy. Unfortunately, sluggish manufacturing output and export growth has been the inevitable consequence of this investment slump.

A strong and resilient manufacturing sector must be a central pillar of Canada's economic growth plan. With the pandemic exposing the fragility of supply chains, the potential for reshoring manufacturing in Canada has become a real possibility. This, along with the enormous potential of Canadian firms to tap into the rapidly growing clean technology sector, suggest that there is no better time to push for a revival of Canadian manufacturing. To seize this opportunity, and to build a more competitive, greener, innovative, inclusive, and resilient economy, the federal government must work with our sector to implement this submission's recommendations.

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RECOMMENDATIONS

Recommendation 1: De-risk and encourage manufacturers to digitize, automate, and adopt advanced technologies

Canada lags other industrialized countries when it comes to business investment, digitization, and the adoption of advanced manufacturing technologies. Between 2015 and 2019, manufacturing investment in 31 OECD countries together totalled $1.77 trillion per year in PPP terms. With average annual investment of $21.6 billion, Canada accounted for just 1.2 per cent of this amount. By comparison, the US and Mexico's share of OECD manufacturing investment was 28.1 per cent and 12.3 per cent, respectively. CME's goal is to increase Canada's share of OECD manufacturing investment to 2 per cent, equal to $35.4 billion in PPP terms and CDN$43.0 billion. Industry is willing to lead this effort, but it requires a strong partner in government and bold policies. Therefore, CME recommends that the government:

1. Introduce a 10 per cent refundable investment tax credit on the purchase of new machinery, equipment and technologies, including software. This could be achieved by extending the Atlantic Investment Tax Credit so that it applies across the country.
2. Expand and make permanent the Strategic Innovation Fund (SIF) and commit at least $2.5 billion per year in funding to support large capital projects in manufacturing.
3. Relaunch investment support grant programs for smaller firms, modelled after the successful CME SMART programs that operated after the previous recession.

Recommendation 2: Support R&D spending and scale-up of companies by improving and enhancing the SR&ED program

Along with technology adoption, Canada is also a weak performer on R&D spending. In fact, Canada's business expenditures on R&D (BERD) as a share of GDP are well below the OECD average and have continued to fall since its peak in 2001. Reversing this trend would see Canada's spending levels move closer to peer countries internationally, thus encouraging new discoveries and innovation. This could be best accomplished by enhancing the Scientific Research and Experimental Development Tax Credit Program (SR&ED), the main mechanism through which the federal government supports business R&D. CME asks the government to:

1. Expand the range of SR&ED-eligible activities.
2. Introduce a refundable component to the SR&ED credit for all claimants.
3. Return the SR&ED tax credit rate to 20 per cent.
4. Support scale-up by reducing the SR&ED grind down for growing companies (the refundable tax credit expenditure limit is grinded down if taxable capital employed in Canada in the previous tax year exceeds $10 million and is eliminated at $50 million).

Recommendation 3: Implement a patent box regime to encourage domestic innovation, commercialization and production

Canada also struggles with commercializing ideas and bringing products to markets. Too many of our ideas end up generating wealth for others. One tool available to the government to help Canada overcome its commercialization gap would be to adopt a patent box regime. Patent boxes allow corporate profits related to the sale of patented products or the use of intellectual property to manufacture products to be taxed at significantly lower rates than those applied to ordinary business income. Such a regime provides firms with a strong incentive to undertake innovation, commercialization and production activities locally. Accordingly, it is CME's position that the government should:

1. Implement a patent box regime to reward commercialization and production of goods and advanced technologies in Canada, thus eliminating a key competitive disadvantage between us and a growing number of our international peers that have implemented this tool.

Recommendation 4: Provide employer incentives to upskill, hire, and retain workers to help address labour and skills shortages in manufacturing

Manufacturers often cite labour and skills shortages as one of their most pressing challenges. Unfortunately, these challenges are going to intensify in the coming years as the large baby boom cohort continues to exit the workforce. Among the policies that are available to replenish the workforce, two of the most effective involve reskilling and upskilling the existing workforce and increasing the labour market participation of underrepresented groups (women, Indigenous peoples, people with disabilities, and visible minorities).

Among our many efforts to address these critical labour issues, CME launched the *We Can Do It* campaign in 2018, aimed at increasing the number of women in manufacturing by 100,000 in five years. Attracting more women into manufacturing professions would not only help companies grow and replace their aging workforce, but it would also provide women with careers that are full time, highly skilled, and high paying.

At the same time, manufacturers are eager to upgrade the skills of their workers. However, companies tend to underinvest in training and development due to concerns over turnover and poaching. Given the wider societal benefits of upskilling the workforce, it makes sense for governments to provide financial assistance to firms to increase their training activities. Thus, CME recommends that the government:

1. Renew and expand funding for CME's Women in Manufacturing initiative to increase their participation in the sector and help manufacturers grow.
2. Introduce a 50 per cent worker training tax credit that helps offset company costs.
3. Increase the size of the Canada Jobs grant to $1 billion annually, make it permanent, and expand it to include on-the-job training.

Recommendation 5: Help the manufacturing sector adapt to and advance Canada's climate change strategy

CME recognizes and believes that all Canadians, including the manufacturing sector, have a responsibility to help address climate change. As such, we support the shift to a low carbon economy. However, the scale and magnitude of the government's climate change plan necessitates proportional countermeasures to help ease the transition for Canadian businesses, especially those in energy-intensive, trade-exposed industries (EITEs). It is particularly important that these incentives support all the many things that manufacturers do to improve their environmental performance, both big and small, because it is going to take a collective effort to win the fight against climate change. Therefore, we recommend that the government:

1. Provide direct investment supports for emitters of all sizes to help them adopt emissions-reduction technologies, ensuring that support approaches are technology-agnostic.
2. Provide financial support for the creation, commercialization, and manufacture of low- and no-carbon products in Canada through tax incentives and government procurement.
3. Create an effective and targeted SME net-zero transition strategy, with a specific focus on education and global supply chain competitiveness.

Recommendation 6: Provide more support to help Canadian businesses increase their value-added exports

Canada is a trading nation. This is evidenced by the fact that exports account for over 30 per cent of the country's GDP. The manufacturing sector is a key reason why Canada has earned this reputation: it is responsible for roughly two-thirds of the country's outbound goods. However, Canada's export performance in recent years leaves much to be desired. Over the past 20 years, Canada has posted the slowest growth in exports of manufactured goods among the G7 countries (valued in US dollars). Clearly, more needs to be done to help Canadian companies, especially SMEs, to go global. Therefore, CME asks the government to:

1. Fund the creation of an Exporter Concierge Service that enables trade associations to develop programs that link their members to government export agencies and services.
2. Create a "Trade Barrier Hotline" for exporters to call and report trade barriers and to offer exporters assistance in overcoming trade barriers.
3. Invest in infrastructure that facilitates trade and industrial development, thus creating jobs, stimulating the economy, generating demand for domestic manufactured goods, and paving the way for higher value-added exports.