Session 8

The Private Sector Response to Economic Challenges Facing Canadians

R. Martin Thank you. I'm Roger Martin from the Rotman School of Management. And I will try and be brief and stick to my 10 minutes.

The first thing I'd say is congratulations to you Randall and your co-author. I think it's a well framed and valuable argument you make in your paper. Perhaps I come to the paper with a biased point of view. I don't carry around a rabbit's foot for good luck, but I always make sure to keep a first edition copy of The Road to Serfdom within arm's length of me in my office. So you've found a receptive audience in me. Though I would argue that the authors implicitly found that the normative output of the Austrian school probably doesn't match its descriptive elegance. It contains a whole lot of "don't dos" to which I subscribe: don't subsidize small businesses, pick winners, etc.

But it doesn't provide as much provide as much help as I wish it did to the question of what do you do, especially if you're in Canada and you are obviously and clearly dropping back in the global competitiveness race. And that answer is not a trivial answer. I don't think Randall said it's a trivial answer, and I think the authors make some very helpful points in the article on that question. Helpful point one is the importance of innovation and in particular the importance of distinctiveness. All the research work I've done and my colleagues have done would confirm the notion that distinctiveness is absolutely critical to firms moving ahead, economies moving ahead and to prosperity. We know this from work that my colleague Mike Porter has done on the competitive advantage of nations where the model of prosperity is built on the constant upgrading of capabilities of firms that otherwise have the same endowment of resources, same labour costs, etc. The pressures to upgrade and create a distinctive product or process are what move them ahead. We know this from the most recent work that he and I have done on firm level strategy that stresses the value of creating distinctive activity systems as Southwest Airlines or Progressive Insurance have done.

The one place where I would actually beg to differ considerably is the "winner take all" notion. That has not really proven to be the case and all the Santa Fe folks I think are a little bit too captured by the notion of increasing returns. Our research finds that the push for distinctiveness tends to create more ways to satisfy the various segments of the market. Markets are rarely homogenous; they're not monolithic. Coming up with a distinctive edge often captures, if you will, *all* of only a *piece* of the market. You have many firms that can prosper simultaneously in that world. To give a somewhat trite example, Pepsi is the "winner takes all" for those who are part of the *Pepsi generation* and Coke is the "winner takes all" for those who believe *Coke and a smile* is an attractive slogan. So they're both making lots of money and they're both showing distinctiveness in their markets. If you want to make the increasing returns argument, not in terms of market segmentation, but in terms of product segmentation you could say that IBM was the winner take all in the computer business. They benefited from increasing returns, got gigantic scale and, IBM is now worth $180 billion. But it turns out that they turned their back on 2 tiny little pieces of that market, one called PC operating systems and the other called computer logic chips. And we now have a $500 billion company called Microsoft, which hasn't taken all either because Intel, the logic chip company is worth another $250 billion. So I see innovation as actually not having the harsh result of driving other firms out of the business, but rather of pushing firms into different parts of the market, whether by product, whether by customer, geography or, etc. And so for me innovation and distinctiveness are unalloyed goods rather than problems that get created.

The second thing I found very helpful in the paper is discussion about competition among governments. I think this is a great concept and we should focus on it more. I would argue that this is a field that has not gotten nearly enough work: the emerging competition for governments. They will compete for the products and services they offer. James Buchanan, who I love dearly, is absolutely right on that point and I would argue that with only 3 exceptions that I can think of, the governments of Canada have not been distinctive or unique. They were distinctive and unique with the National Policy designed to protect our economy. This was distinctiveness of the sort we don't want to have; that is, an utter disaster for us that we'll live with for another century. The second one was the National Energy Policy, which encouraged Canadians to buy into the energy sector at its highest real cost per BTU in the history of human endeavor. The third though was a very distinctive move that we should be proud of I think. That is the indexation of tax brackets in the early 1970's that caused us to have a better economic performance than the United States during the 1970's, until we reversed course and de-indexed in the 1980's. So I believe that thinking about how governments can be actually more distinctive and not patting ourselves on the back for matching other governments will be a key part of getting competitive advantage for Canada.

The third contribution that I saw in the paper is bringing public choice theory to bear. Probably after von Hayek and Stigler, my favourite economist is James Buchanan for actually a different thing than what Randall showed. Buchanan provides us with a fabulous yardstick for every time we want to do something from a public policy standpoint. He notes that we find it quite easy to declare private market failures. For example, we say there isn't enough low cost housing – a private market failure. Then we create a public market solution that we do not subject at all to the same analysis to which we subjected to private market when we declared it to be a failure. And this is what causes us to come up with incredibly stupid public choice ideas like rent control that have nothing but a pernicious affect on markets, being for example highly correlated with homelessness. So if we keep Buchanan's yardstick in mind – that is: use a public choice mechanism to solve a private choice failure only if you subject that public choice mechanism to the same standard to which you submitted the private choice- I think we'd have lots fewer misguided policies as we pursue competitiveness policies. In a world of increasing global competitiveness where our government policy has to compete with those of others, we'll need to have yardsticks like that to help us make better choices.

The fourth thing that I thought was a contribution was highlighting the importance of corporate culture using the Milgram experiment as your illustration. That is an area of fruitful work actually and, and there is a lot of good work going on in this area. Two professors who I work with, Chris Argyris and Mike Jenson, a Chicago trained Austrian school finance theorist, are working together to understand what it is about managers that causes them to consistently avoid short-tem pain, even though their actions produce greater long-term pain than they avoided in the short-term. We are trying to understand what it is about the way that they work and the kind of environment in which they work that causes that to be the case. There is good work underway there and it will help us understand why Canadian companies find being innovative in the short-term to be painful, and even though it's obvious they need to be innovative, they avoid such innovation only to suffer greater pain long-term. It seems illogical, but there is a set of mechanisms that cause that to be the case.

So I would say those are four things that I found to be very helpful in moving the ball forward on Canadian competitiveness. I think the challenge for Canada is that we do have a managerial problem and it's a managerial problem both at the firm level and the government level. Neither level has a history or practice in seeking distinctiveness. And seeking distinctiveness is something that takes practice. I think managers in our corporations have not sought distinctiveness enough because we have a huge per capita natural resources endowment, great proximity to a the great US market and have had protection of the Canadian economy for so very long. Those historical factors are borne out in some of the initial data that's coming out in the work that my colleague Mike Porter is doing with the World Competitiveness Forum. The initial data shows Canadian managers pursuing competitive advantage based on low cost labour and/or low cost raw materials to a much greater extent than on the basis of unique products and processes. In fact we ranked 21st in the world in his survey on that dimension behind such superpowers as Iceland and New Zealand. Until we get that turned around, we're not going to have the kind of innovation that we need.

So I think in summary, I think the paper makes an excellent advance in the competitiveness debate. It digs around in the right area. There remains a lot of work to be done and I'm glad to be a part of the work ahead.

APPLAUSE