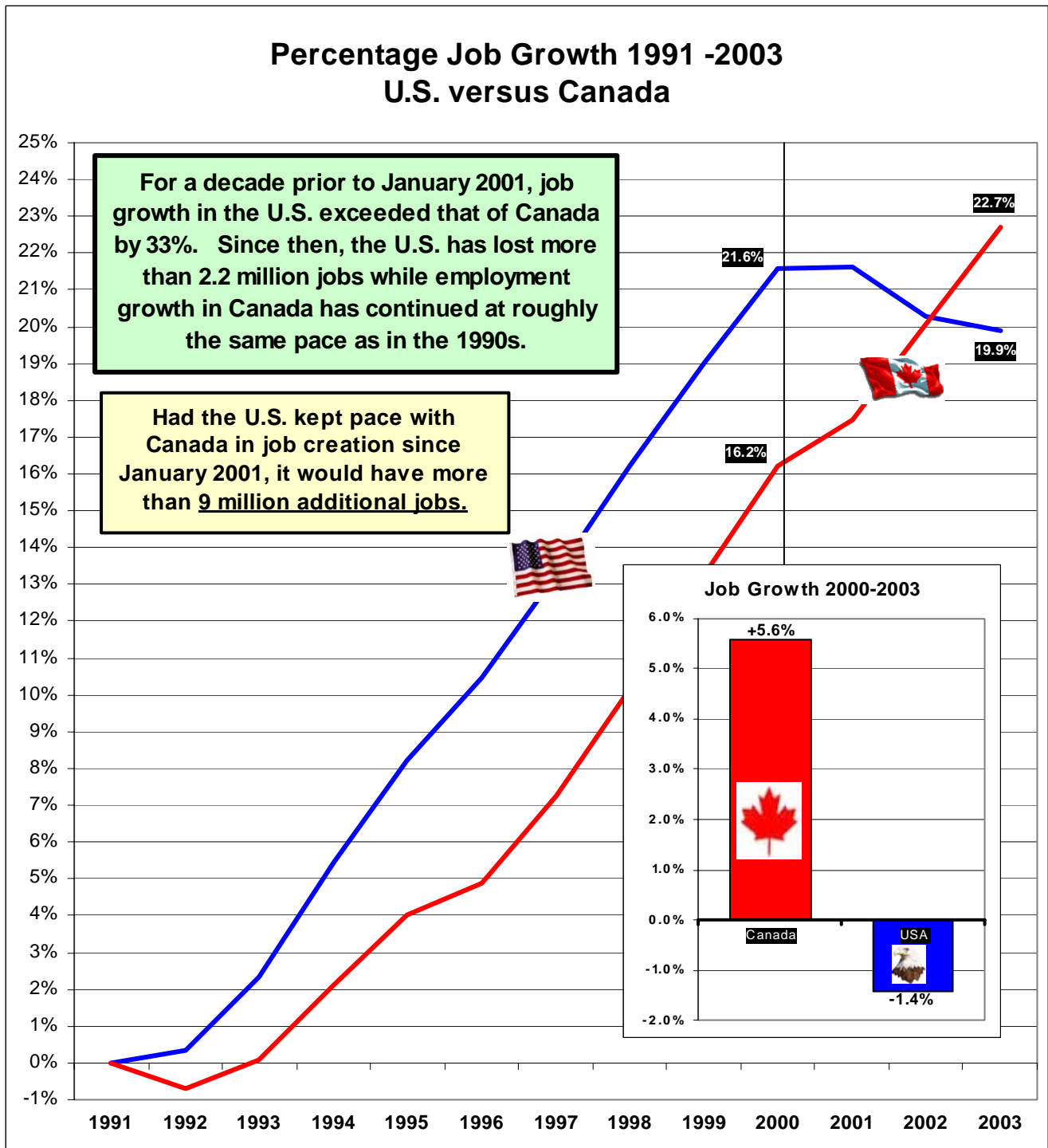


Canada Moves North of U.S. in Job Creation



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During the ten years from January 1991 to December 2000, the United States and Canada experienced very similar rates of economic growth. Canada's growth was weaker toward the beginning of the period and stronger toward the end. Overall, the Canadian economy expanded by slightly more than 36% during the period, and the U.S. economy expanded by slightly less than 35%.

During 1990s Job Creation in U.S. was More Rapid than in Canada

But with respect to job creation, the United States had a significantly better record. During that 10 year period, employment in the United States (*Nonfarm Payroll*) grew from 108.4 million to 131.8 million or by nearly 22%. The number of jobs in Canada grew from 12.8 million to 14.9 million or by a little more than 16%.

As a result, the rate of new job creation was on average about **one third higher** over the course of the decade **in the U.S.** than in Canada. That trend ended abruptly in 2001.

U.S. Job Growth Ended In April of 2001

Although the U.S. economy created new jobs during the first three months of 2001, it began losing jobs in April and lost them at an average rate of

135,000 a month through August of 2001. During the six months following September 11th, the rate of job loss accelerated to about 185,000 jobs a month.

But the most perplexing part of the U.S. job picture is the fact that there was no rebound. Job losses continued through the end of 2002 and into 2003. While there was ample reason to expect a deterioration in the job picture in the months that immediately followed the 9/11 attack there was also every reason to expect a significant rebound after the economic dislocations had worked through the



"Job creation is the number one priority out of Washington, D.C."

President Bush, August 13, 2002

system and reconstruction and new security efforts began to provide new employment opportunities. That has not happened. The March 2004 employment report showed that nationwide our economy had added fewer than 100,000 jobs since March 2002 six full months after 9/11. Furthermore, average hours worked had actually declined over the course of those two years and if one looked at only jobs in the private there were fewer in March 2004 than there had been two years earlier.

Understanding the March 2004 Employment Numbers

There may be some who will argue that concern over U.S. employment levels is misplaced based on the most recent survey data which showed the U.S. economy added 308,000 jobs in March and that gains in January and February were somewhat better than expected.

This argument ignores the magnitude of the jobs lost over the course of the past three years and the unprecedented failure of the U.S. economy to bounce back from those losses even in the face of massive levels of fiscal and monetary stimulus.

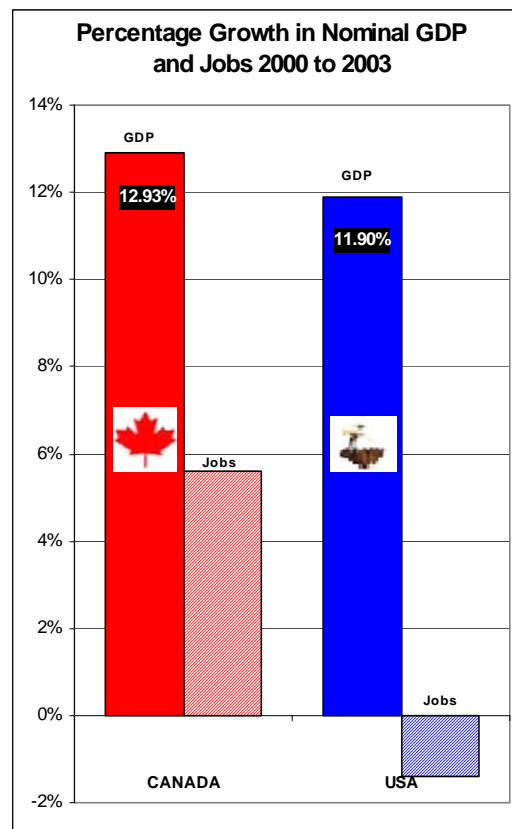
It is also important to note that the March increase is quite modest by historical standards, particularly when compared to previous periods following substantial job loss. The 0.24 percent increase in total employment represented by the 308,000 March figure was matched on seven occasions in the 1990s and surpassed on 27. If we consider the

first quarter as a whole, it would represent the fifth worst quarter out of the 32 quarters between the beginning of 1993 and the end of 2000.

Canada Continues to Convert Economic Growth Into Job Opportunities

The challenges faced by Canada in the wake of the September 11th attacks were enormous. More than 40% of Canada's GDP is derived from exports and 88% of them go to the United States. Any period of economic weakness in the United States has always placed severe downward pressure on the Canadian economy.

Further, concerns about Canadian immigration policies, the ability of Canadian courts to indict and prosecute suspected terrorist cells and concerns about the use of Canadian Airlines to



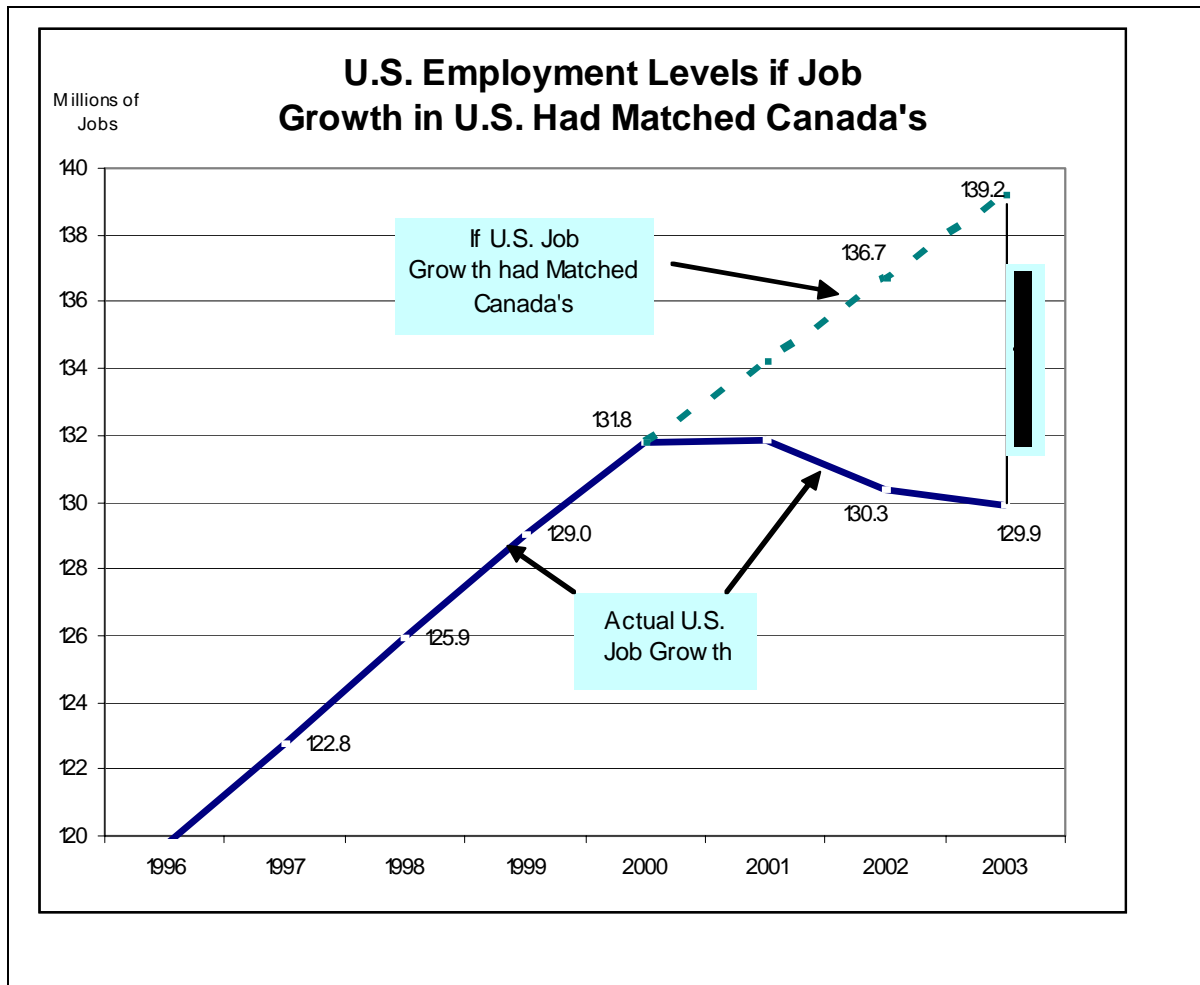
launch attacks against the U.S. prompted homeland security efforts and expenditures that paralleled those in the United States.

Most importantly, Canada needed to respond to demands for far more strenuous monitoring of the U.S.-Canadian border in ways that not only satisfied security concerns, but which also insured the continuous and timely flow of commerce between U.S. and Canadian manufacturing, wholesaling and retailing enterprises. Such disruptions were potentially damaging to both economies, but the threat to Canada was far greater given Canada dependence on U.S. exports.

Within three months of the September 11th attacks, Canadian exports to the United States had dropped by 20% below prior year levels. Exports to the United States remained at 10% below 2000 levels for all of 2002 and were 5% below 2000 levels in 2003.

None the less, Canada was able to maintain a reasonable level of growth during 2001, 2002 and 2003—a level slightly above her neighbor to the South. Between 2000 and 2003 Canada experienced nominal GDP growth of almost 13% while the U.S. experienced growth of almost 12%.

The record of the two economies with respect to job creation, however, was



totally divergent. Canada's total employment level expanded from 14.9 million to 15.75 million, an increase of 5.6%. During that same period employment in the United States declined from 131.8 million to 129.9 million. (If monthly data is used to measure U.S. job loss rather than the annual data used in this comparison, the drop in U.S. employment would appear even greater because the U.S. economy continued to add jobs through all of 2000 and through the end of the first quarter of 2001. The number of Americans employed in March 2001 was 722,000 greater than the average level of employment for the year 2000.)

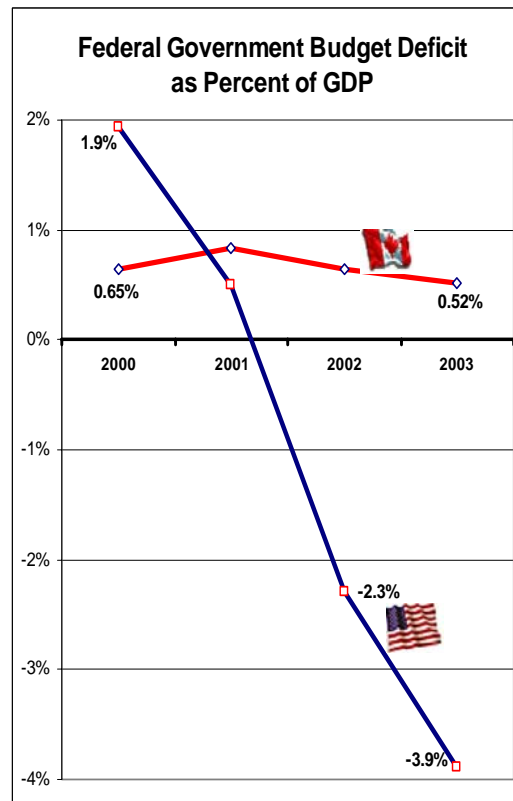
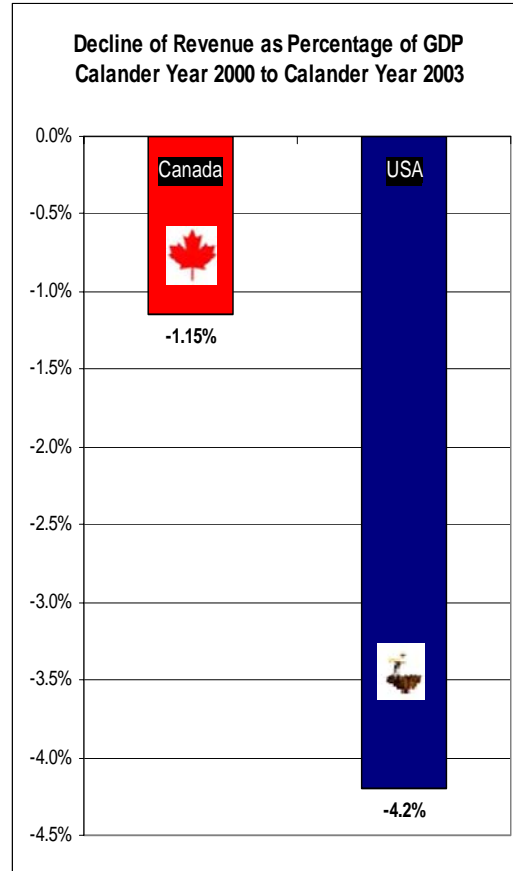
U.S. Could Have Had 9.3 Million Additional Jobs if Pace of Job Growth had Matched Canada's

To provide some understanding of exactly how divergent the job creation trends were in the two economies one could ask, how many jobs would the United States now have if it had kept pace with Canada in job creation? A 5.6% increase in 131.8 million (the 2000 level) would yield 139.2 million jobs or about 9.3 million more jobs than the U.S. had in 2003.

Looking for Clues to Explain Canada's Dramatically Better Record for Job Growth

There are a variety of possible explanations for why Canada produced jobs at a dramatically more rapid pace than the United States between 2000 and 2003.

One policy option for job creation that has received a great deal of attention in the United States is the use of tax cuts and fiscal stimulus. Did Canada institute tax cuts and were they larger and more powerful than the tax cuts



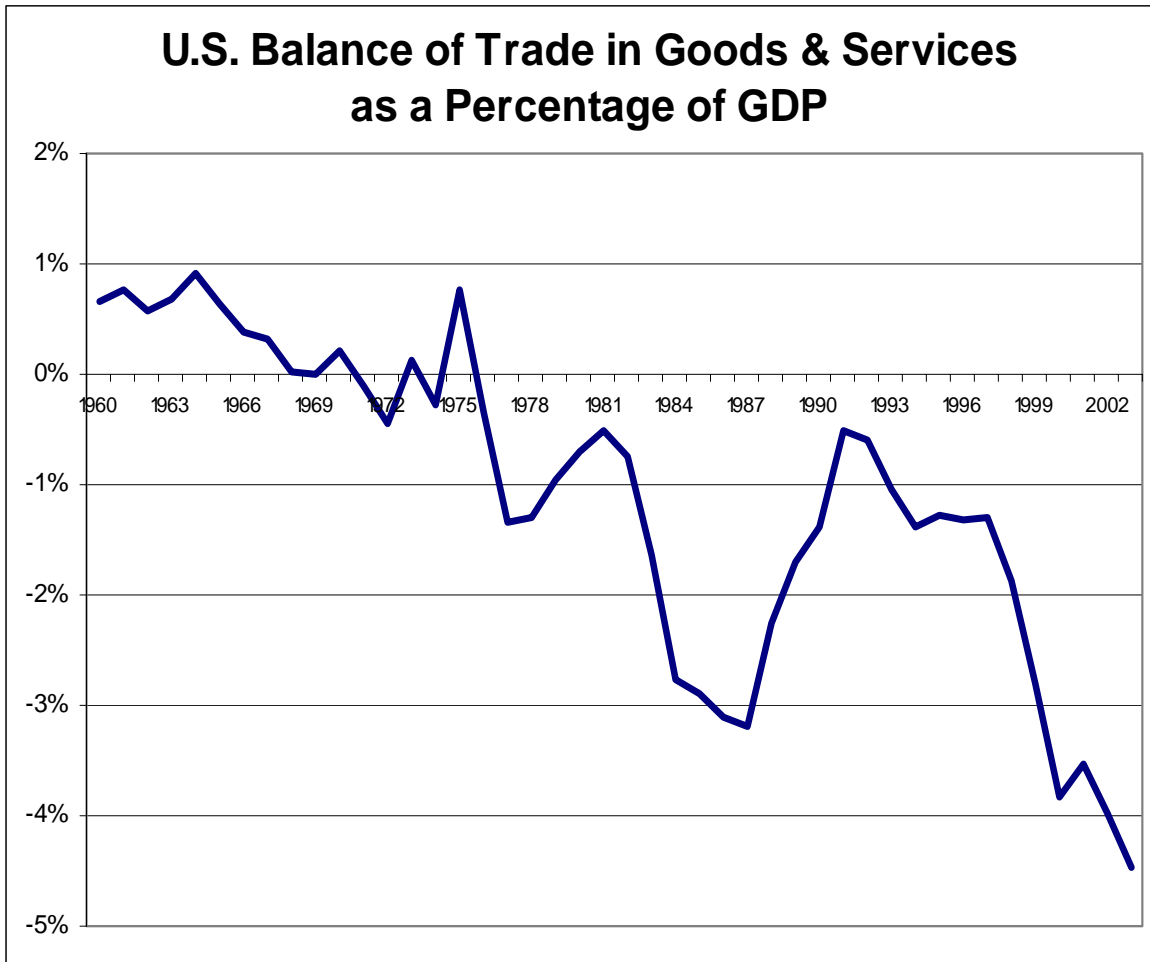
adopted in the United States in 2001, 2002 and 2003?

The answer is Yes and No. Canada like the United States has instituted tax cuts over the last several years. But unlike the United States, Canada targeted its tax breaks more toward the middle class and left the top rate in place. Canada's tax cuts were also more modest and were calibrated to keep the nation's budget surpluses at a relatively constant percentage of GDP.

Perhaps the best measure of the size of a tax cut is the degree to which it causes revenues to fall as a percentage of GDP. In Canada, central government revenues as a percentage

of GDP fell by 1.15 percentage points between 2000 and 2003. That compares with a whopping 4.2 percentage point drop in the share of GDP collected as federal revenues in the United States during the same time period.

This loss of revenue had a dramatic impact on the federal deficit and therefore should have been highly stimulative. During calendar year 2000, both nations enjoyed budget surpluses. The U.S. Surplus at 1.9% of GDP was about three times the size of the Canadian surplus by the same measure. By calendar year 2003, the U.S. budget surplus had turned into a deficit equaling nearly 4% of GDP



while the size of Canadian surplus remained relatively unchanged.

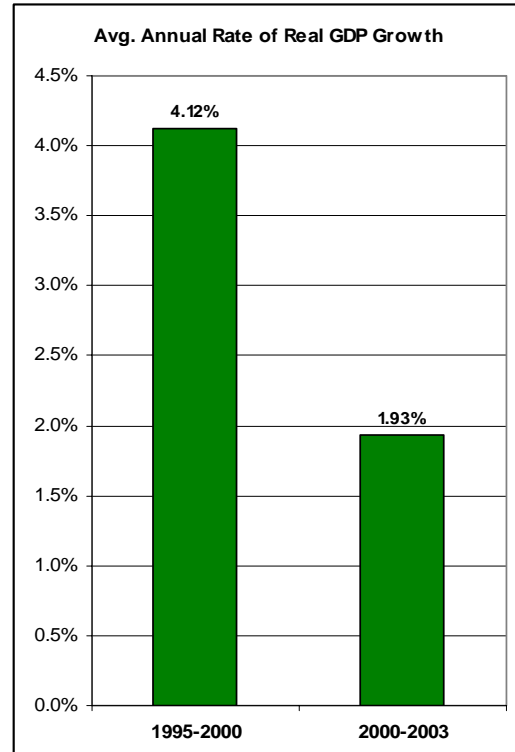
If the experience of these two countries over the past three years is any indication, smaller tax cuts targeted toward middle income tax payers is more simulative than large tax cuts targeted at upper income taxpayers.

How Much Did Trade Imbalance and Outsourcing Affect Relative Job Performance?

There has been growing concern in the United States that the trade imbalance and the outsourcing of U.S. production overseas are major factors behind the “jobless recovery.” Since 2000 the U.S. trade deficit has continued to grow dramatically despite shifting economic fundamentals that should result in a steadily improving balance of trade.

Weaker Economy Should Equal Less Demand for Foreign Goods

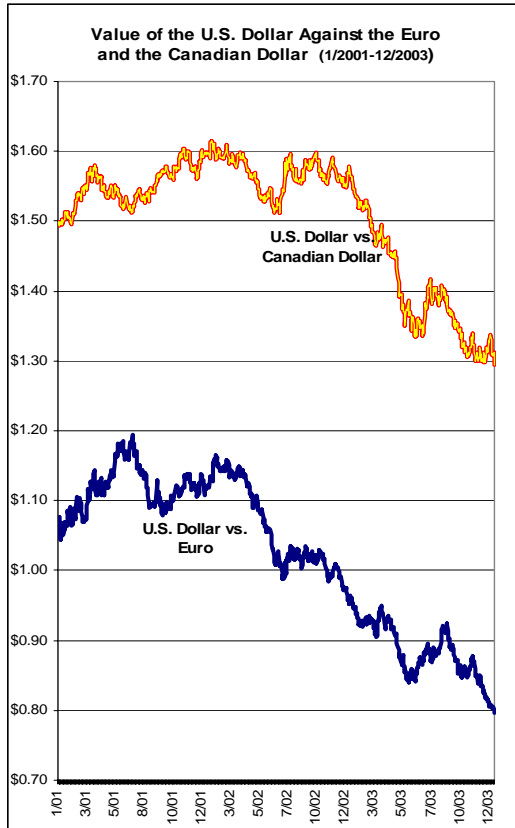
Among those fundamentals was the significant slowdown in U.S. economic growth that began in the spring of 2001. During the five years between 1995 and 2000, the U.S. economy grew at an average annual rate of 4.2%. Since 2000 the economy has grown at an annual rate of 1.9%. There are obvious downsides to this turn around in the pace of economic activity, but one of the benefits of that turnaround should have been a reduction in the purchase of foreign produced goods and improvement in the balance of trade.



Weaker Dollar Should Make American Made Products Cheaper Overseas, Foreign Products Less Attractive Here

Another fundamental that should have significantly helped U.S. trade balances was the decline in the dollar. Since January 2001 the dollar has dropped by 25% against the Euro, 13% against the Canadian dollar and 6% against the Japanese Yen.

Again, the decline in a currency is a double edged sword. While it makes foreign goods more expensive to consumers at home, it should make domestically produced products more affordable and more attractive to consumers overseas. While the recent decline in the dollar has succeeded in making some products, for example gasoline, much more expensive, it has not generated any apparent expansion



in the sale of U.S. goods and services outside the United States.

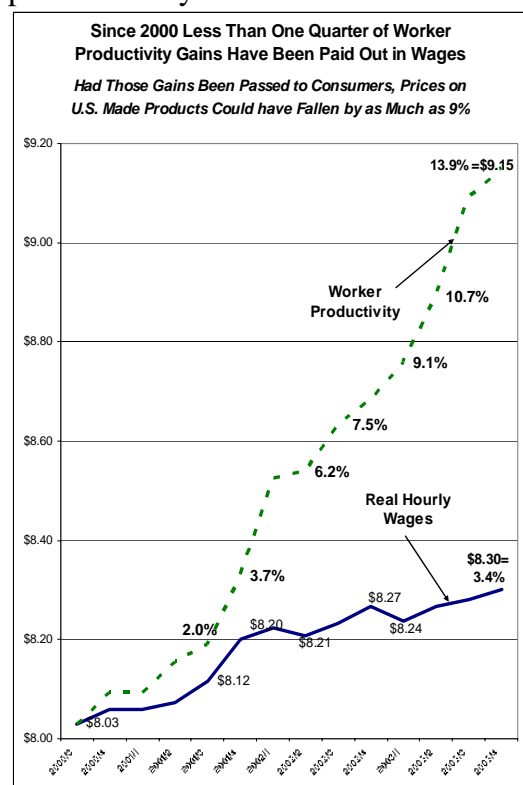
Productivity Has Little Apparent Impact on U.S. Competitiveness

Finally, productivity growth is generally considered a very positive sign for an economy as long as there is a growth in demand to consume the additional products that increased productivity can make available. The great strides in productivity that occurred in the 1920s could not be absorbed on international markets because they did not have sufficient export earnings to buy American products, and they could not be absorbed within the United States since they had not been passed on to workers in the form of increased wages.

The United States enjoyed very strong growth in productivity during the 1990s and that trend has continued during the first three years of this decade. But like the 1920s, only a small fraction of worker productivity growth has been given to workers in the form of higher wages.

Between the third quarter of 2000 and the last quarter of 2003, hourly output per worker increased by nearly 14%. During that same period, average real hourly wages paid to American workers increased from \$8.03 to \$8.30—an increase of only 3.3% or less than one quarter of the increase in worker productivity.

That means that American producers had the flexibility to reduce the prices they charged for American made products by as much as 9%.



Statistics indicate that they did neither. While the consumer price index indicates that there was only moderate upward pressure on prices, they also provide little evidence of falling prices on any significant number of products or services. Likewise, trade data does not show any increase in exports, much less the kind of increase that one might expect to find from a substantial reduction in the prices charged for U.S. products. The remarkable increases in corporate profits in recent quarters may provide some evidence to how the gap between worker productivity and wages was absorbed.

Even in Combination These Factors Have Not Slowed the Deterioration of the U.S. Trade Deficit

None of these supposedly powerful indicators of how well a nation will compete in international markets and against foreign products in its own market has appeared to help the U.S. hold back its huge and growing trade deficit. Our position since 2000 has deteriorated on virtually every front. U.S. Exports of goods has declined by 8% since 2000 while imports have grown by 3%. The balance of trade in services, once considered this nation's strong suite has also showed deterioration. The export of services was essentially flat over the period while imports of services have grown by more than 11%.

Altogether the \$489 billion, 2003 trade deficit was **30% higher** than the 2000 deficit.

Of even greater concern is the prospect of further deterioration in U.S. trade balances with the rest of the world.

The January 2004 deficit was more than 7% higher than for the same month in 2003. If that trend were to continue for the remainder of 2004 the trade deficit would exceed \$525 billion for calendar year 2004, **40% higher** than just four years earlier.

Canada Continues to Ring Up Trade Surpluses

While the United States has experienced persistent trade deficits in recent years, Canada has experienced persistent surpluses. This in large part because of the large surplus Canada runs in its bilateral trade relationship with the U.S. Between 2000 and 2003, total Canadian export of goods declined by 7% but unlike the United States, imports also declined and by nearly as much as exports.

While the overall balance of trade in Canada has deteriorated to some extent over the past three years the nation still retains a trade surplus of nearly \$60 billion Canadian dollars equaling more than 5% of GDP. Canada has managed to maintain a surplus of this size despite a significant appreciate in the Canadian dollar against the U.S. dollar and virtually no growth in worker productivity. While the latest employment report in Canada did indicate some softening of the labor market it was the first negative report in more than 6 months.

Canada has managed to cope with many of the same problems confronted by policy makers here in the U.S. and appear to be grappling with them that is providing much greater hope for those searching for work.