Asia Pacific Foundation and Canadian Manufacturers & Exporters' Convening

Ontario and the Asia Pacific Gateway: Interests and Perspectives

Ontario Investment Service – International Marketing Centre -- June 19-20, 2006

The opening sessions on June 20 began with an introductory panel with Paul Evans, Yuen Pau Woo and Deborah Turnbull. They laid out the broad vision of the interrelated Asia Pacific Gateways and overlapping municipal/provincial/federal jurisdictions involved. The panel noted:

- The "factory Asia" phenomenon and its implication for global supply chain and production networks;
- The Asia Pacific Gateway is a response to the dynamics in Asian trade and a call for Canada to develop sufficient capacity to adapt to Asia's development;
- The need to not just "think big," but "really big" – that we should not be developing for current needs but future demand;
- The Gateway is not simply a Vancouver or a Western Canadian strategy, but a "national strategy;"
- The impact of the Gateway would be akin to the way the St. Lawrence Seaway and Canadian Pacific Railway had transformed economies across Canada.

Four questions were posed to the participants:

1) What are the broader dimensions of the Gateway beyond physical infrastructure? Goods and people will use the infrastructure but what will accompany this trade? What are the transformative effects? These have ramifications for innovation, competitiveness, education and values.
2) What are the financing and labour issues associated with the different dimensions of Gateway? What does this mean for Canadian businesses?
3) What is the Ontario dimension of Gateway? Specifically, for Toronto financial services, manufacturers and transportation providers.
4) What is the framework for public-private partnership in Gateway projects?

Transportation and Supply Chain Management Panel

John Kaldeway, of the Greater Toronto Airports Authority, said Toronto Pearson Airport handles around 47% of Canada's international passenger traffic (excluding trans-border travelers) and an average of 330,000 cargo tons per year, although annual capacity is 1M tons. The number of direct service routes has been growing, and expanding this market through Open Skies Agreements is a top priority. The airport is currently talking with Chinese carriers about bringing in more flights from Shanghai and Beijing. The greatest challenge facing the airport is the ability to react to competition. Kaldeway stressed the airport's current financial regime, which includes 30% of landing fees paid to the government, is hindering its ability to compete with US airports.

Pat Sinnott, Senior Vice President, Canadian Tire Corporation, spoke about the need for a national Canada-Asia Gateway strategy that includes both the west coast and east coast ports. One of the key reasons for this lies in the need to have a balanced flow of loaded transportation equipment eastbound and westbound.

Mr. Sinnott pointed out that since 60-70% of the population of Canada is situated east of the Manitoba border, approximately 70% of all containers entering the Port of Vancouver are destined to "ship-to" locations in central Canada. Demand in Western Canada combined with export demand is not sufficient to fill the containers that empty in central Canada for a return to the Port of Vancouver. Therefore, as the Asian-sourced volumes destined to central Canada increase as expected over the next several years, the imbalance will increase unless more product enters Canada through the Port of Halifax. An example was presented which showed how using the Port of Halifax mitigates a substantial proportion of what will otherwise become a significant and expensive challenge. In addition, the Port of Halifax is badly needed to increase Canada's port throughput capacity.

Canadian Tire currently imports about 60,000 TEU (20ft. equivalent unit ocean containers) a year, mainly through the Port of Vancouver. The company has been increasing its use of the Port of Halifax and owns or leases approximately 3,000 domestic, 53ft containers to balance shipments across the country.

Andrew Fuller, of CN Rail, pointed to an exhaustive review four years ago of the railway's overall operation from a supply chain perspective. The goal was to achieve inter-modal excellence. CN has been building capacity through construction, new routes, and mergers and acquisitions. The railway will add 3,000 railcars to meet capacity demands for the new Prince Rupert port. CN is also raising efficiency by using a reservations system for containers, improving train design and operating extended hours. Halifax is a top priority for CN as it sees strong demand and growth potential. Fuller noted two existing challenges: 1) wasted capacity due to empty containers moving across the railway, and 2) lack of product integration along the supply chain.

Discussion:

- The problem of empty containers is shared by ocean carriers and ports in Asia. Bulk shippers to Asia have the same backhaul problem with ships on which they export more commodities than they import. More commodities are becoming containerized, using otherwise wasted container capacity.
- Retailers are not accustomed to using Halifax and much depends on whether ocean carriers call at the port and it takes a long time for ocean carriers to change their routing. One participants noted that it was more difficult to move goods out of Halifax harbour than to bring them in. Participants expressed doubt as to the strength and attractiveness of Halifax in light of the heavy investment by the US Government in US East Coast port infrastructure.
- There are prospects of India developing greater connections with Canada. Although an air agreement with India was completed last year, there are currently no direct flights between Canada and India. There are opportunities for air cargo service between the countries.
- Other corridors and locations may have a role in a national Gateway strategy. These include the St. Lawrence Seaway, the Northwest Passage, Sault Saint Marie (as an intermodal transport centre) and the Ports of Montreal and Churchill. However, CN's Fuller said that Sault Saint Marie lacks the critical mass that is required for an intermodal

transport centre to be financially feasible. It was reported that the Northwest Passage may be only 20 years away from opening to commercial shipping.

Financial Gateway Panel

Neil Tait, of BMO Financial Group, said Canada must have a "made in Canada" strategy for China developed by government, industry and export trade associations. We need a collective Canada "buy in" strategy. BMO's North American clients in China are weighted heavily in favour of the US rather than Canada. There is a lack of Canadian business in China due to the lack of links between the two countries. Tait noted that the Prime Minister has not yet engaged China with a state visit. We do not have a position from the PM on where he stands in our relationship with our second-largest trading nation, a relationship that has been nurtured by his predecessors over the past 40 years starting with PM Trudeau. Canada needs a collective strategic plan for China as Canada can offer much that China needs, notably resources.

Marvin Hough, of Export Development Canada (EDC), said Canada has slipped in key Asia Pacific and emerging markets. He feels that Canadian businesses investing in emerging markets are not keeping pace with their competitors as the integrative trade phenomena continues to evolve. In India, now a major focus for EDC, it is often no longer competitive to bid for engineering projects from Canada: partnerships with Indian firms are necessary for success. In the context of the integrative trade environment, EDC has taken a more flexible approach to its criteria and now focuses on “Canadian benefits” rather than the previous approach of only focusing on the “Canadian content” in an export transaction. With respect to foreign direct investment, EDC is taking a number of steps to more fully support transactions, particularly those involving Canadian direct investment abroad. For example, a recent agreement with Sinosure, China’s export credit insurance agency, will assist Canadian affiliates in China to obtain credit insurance and other financial support to grow their business. The agreement will also help Chinese firms which invest in Canada and export out of Canada to receive financial support.

Janis Koyanagi, of the Toronto Stock Exchange, said the market can attract listings by smaller Chinese firms because of its lower costs compared to New York and London. The TSX has a business development team in China and is positioning itself as a gateway to North American capital. She pointed out that there are opportunities for Chinese firms to gain listing via reverse takeovers and capital pool companies. The three barriers for Chinese investors in Canadian equities are: 1) the time differences, 2) currency exchange, and 3) access to trade equities in China.

Discussion:

- Canada’s large Chinese immigrant population can facilitate China-Canada investment. Many Chinese students who return home serve as a valuable bridge to the Canadian market as they are familiar with Canadian practices. Some Chinese-Canadians base their business in Canada and manufacture in China. Chinese institutions are gaining interest in Canadian capital markets.
- Government and business should work together to refine a Canadian strategy toward Asia. There is a lack of the focus which is critical to bringing the needed elements --

people, infrastructure, finance -- together. Tait of BMO stressed that there must be a collective "Canadian story" which Canada uses to market itself.

Ontario's Asia Pacific Strategy: Implications for Gateway

The Hon. Joe Cordiano, Ontario's Minister of Economic Development and Trade, said Gateway must be broader than just the expansion of infrastructure: it involves the way in which we do business and compete internationally. Canada has a long way to go to become a global trader. He believes the small size of Canada's global trade footprint is a legacy of the country's free trade agreements in North America. Canada must catch up in Asia Pacific markets, among others. He suggested that Canadians are not sufficiently exposed to the rest of the world because of a lack of international travel.

Cordiano reviewed the government's efforts in developing increased investment and education links with China. He focused on China's appetite for zinc, nickel and copper, of which northern Ontario has plentiful supply. On a recent mission to China, 30 agreements were signed, which Cordiano attributed to successful leveraging of relationships with government officials. He said Ontario could do more in Japan, the world's second-largest economy. Currently, bilateral trade in products and services stands at $1B a month. Cordiano discussed Ontario's auto strategy which would see the province producing more cars than any other North American jurisdiction. He emphasized the strategy for gaining a greater share of global trade and investment is to set up in-market centres and agents to increase collaboration and build partnerships.

Discussion:

- There are currently no trade agreements with China or India. There was some concern that Ontario is pursuing its overseas activities alone rather than partnering with other provinces or with the federal government. Cordiano said that anything to bring focus will help. However, he pointed out that Ontario must pick its markets according to its strengths, notably the automotive sector.
- Cordiano emphasized that the only way Ontario manufacturers will survive is to focus on innovation, human capital, technology and capital. He stressed that advanced manufacturing and the automotive sector will remain as key competitive advantages for Ontario. However, he suggested that not all manufacturers in Ontario will survive as global manufacturing shifts.

Advanced Manufacturing and Innovation Strategies:
Asian Challenges and Opportunities

Paul Beamish, of the Richard Ivey School of Business at the University of Western Ontario, said Canadian companies must integrate into mega global companies or be left behind. Despite Canada's connection to the advanced US market, Canadian companies tend to over-rely on the resource sector. He pointed to a lack of study tours and overseas exposure by Canadian companies. There is an incredible amount of innovation happening outside of Japan that Canadians are failing to notice. He argued that Canadians must travel more and increase their engagement in Asia.

Vincent Guglielmo, of the Automotive Parts Manufacturers Association, reviewed various automotive parts industry trends and argued that Canadian firms must have an Asian strategy, aimed at obtaining the best quality parts at the lowest cost. The China market has been experiencing high margins but these are falling quickly. India is moving toward manufacturing and that it is only five years behind China. He stressed that the Eastern European market is very important as it is becoming able to compete with China. One recurring problem is that Canadian companies refuse to engage and move up the value chain.

Fernando Pisano, of P&P China Automotive Corporation, emphasized the intellectual property rights challenges faced in China and said that companies can expect to lose their IP rights as soon as they export products to China. He estimated it will be at least 10 years before IP protection is sufficiently enforced in China. In devising business strategies, Pisano stressed that relationships are just as vital as written contracts.

Harold Hoschen, of iFire Technology, argued that in practice each country in Asia is different and requires a different strategy. He pointed out that there are many supply chains located entirely within the region, such as the television production clusters in China that produce 90% of world's TV sets. Companies must focus on their employees as ultimately intellectual capital rests with them.

Human Dimensions of Gateway: Education, Tourism, Arts and Culture

Jeff Melanson, of the Royal Conservatory of Music (RCM), said there are huge opportunities in China due to a lack of music education standards. RCM, the largest music curriculum education supplier in North America, has a major business selling its system in China. However, RCM faces stiff competition from its British counterpart which benefits from a reputation built in its colonial past. RCM has developed a China strategy and is engaging in cultural diplomacy efforts through the Hong Kong Economic and Trade Office and the Hong Kong Trade Development Council.

Michael Kraft, of Lingo Media Inc., said that small publishers can compete in China. The English as a Second Language book market presents a huge opportunity for foreign firms that can develop good content for the Chinese market. He noted that relationships in China are very important and that establishing a local physical presence is the biggest challenge for Canadian firms in the cultural industries. However, the Canada brand name is highly regarded, and publishers can benefit from that reputation.

Harry Hamazaki, of the Ontario Tourism Marketing Partnership, said Chinese tourists are among the highest spenders in the world. He noted that Approved Destination Status (ADS) for Canada is still pending even though this country was one of the first to begin the application process. Fifty countries have leapfrogged Canada in gaining ADS status. Hamazaki pointed out three obstacles to ADS: 1) the Lai Changxing case, 2) Canada's position on Falun Gong, and 3) confusion in immigration policies that handicap the drive for ADS. He argued for the need for Canadian tourism and hospitality operators to become familiar with Chinese tourists' requirements (e.g. food preferences).

Sara Diamond, of the Ontario College of Art and Design (OCAD), said China was ready to move from emulation to original design as a key to value-added production. Well-designed products are at the heart of industrial success. Diamond said the Chinese government had mandated annual growth of 10% in new media education and said there are potential partnership opportunities as complex art gains popularity. Art builds human relationships, Diamond said. The challenge is finding ways to integrate art, science and engineering.

Discussion:

- Canada has been too impatient with its overseas marketing activities. The lure of the huge US market sees some Canadian players withdraw from Asia after only a brief attempt at becoming established. Ontario trade offices overseas were shut down due to short-term lack of business only to reopen later. In the interim, Australia benefited from Ontario's absence.
- There are aspects of Canadian culture and design that are marketable in Asia. Diamond of OCAD said that despite Canada being a poor ambassador of culture compared to Northern Europe, Canada's strong sense of sustainable design and architecture is gaining popularity in China.
- The tourism sector is unprepared to receive Chinese tourists in large numbers. There was agreement that Ontario is not prepared in terms of helping the sector adapt to the needs of Chinese tourism. Preparedness might include developing interpreters and multilingual signage and a "how to" manual on Chinese hospitality and service standards.