

The road not taken

Canadian industries had a choice 10 years ago to innovate and become globally competitive, say U of T's **ROGER MARTIN** and Harvard's **MICHAEL PORTER**. We need a new direction

When we began our study of the Canadian economy in 1990, Canada was the third-richest country in the world (in GDP per capita) and had a dollar valued at 85 cents (U.S.). We released our report, *Canada at the Crossroads*, in 1991 and, a decade later, Canada is the fifth-richest country in the world and has a dollar valued at 65 cents (U.S.), a 23-per-cent international pay cut for all Canadians.

Why the substantial decline? Faced with two paths in 1991, the economy overall chose the less favourable path. This path hewed closely to the Canadian tradition of competing on the basis of lower-cost labour or raw materials and pursuing company strategies of replicating competitors elsewhere.

There is an alternative path — competing on the basis of uniqueness and innovation — which is the only path toward rising relative prosperity for Canada in the global economy. There is no question that Canadian firms can succeed at it. However, lulled by a steadily declining dollar, Canadian firms still face strong temptations toward more of the same.

Perhaps nothing could illustrate the contrast better than the trajectories of two industries that we studied in 1991, newsprint and telecommunications switches. In 1991, newsprint was one of Canada's leading export industries, with both impressive size (\$5.5-billion in sales), and leading world export share (62 per cent). The Canadian industry featured seven large companies, including the world's largest player, Abitibi-Price. The strength of the industry depended on three advantages: low wood fibre cost, low energy costs, and proximity to the world's largest market.

But these static advantages quickly came under pressure with the development of thermomechanical pulping, which facilitated the efficient use of low-cost fibre found in abundant supply in the southern U.S. and Latin America. Moreover, Canada lagged by a decade or more in implementing new processing technologies. Historically lax environmental regulation had also left firms unprepared for the heightening of environmental concerns about the forest products sector worldwide.

Since 1991, prices in the newsprint industry have drifted downward. In terms of world paper production, newsprint has dropped from 39 per cent to 30 per cent, as value-added grades of paper have grown. Meanwhile, Asia's growing appetite for newsprint has spurred investment in Asian production.

Winners in coping with these changes have been the Scandinavian firms, who invested heavily to upgrade themselves and their home industry through the 1990s. At home, they worked together through industry associations and universities to promote innovation. The average worker in the Scandinavian industry has a related university degree. Abroad, they invested heavily in North American assets.

Norway's Norske Skog purchased Canadian newsprint player Fletcher Challenge Canada and is in the process of acquiring Pacifica Papers, another Canadian newsprint company. Swedish/Finnish firm Stora Enso and Finland's UPM-Kymmene also

made major acquisitions abroad.

Unlike the Scandinavian industry, the Canadian pulp and paper sector, exemplified by newsprint, focused primarily on domestic consolidation rather than upgrading and globalizing. It also maintained its focus on the lowest-value-added, slowest-growing part of the marketplace: standard newsprint. And so, one of Canada's historical core industries has lost nine points of global share since 1991.

Today, the newsprint industry depends largely on the devalued Canadian dollar to stay profitable — shaky competitive ground indeed. At 65 cents (U.S.), the Canadian newsprint industry is right at the average of industry cost-competitiveness worldwide. At 85 cents (U.S.), Canada would be the least cost-competitive country in the world by far!

Contrast Canadian newsprint to the telecommunications switch industry. In 1991, the industry was Canada's most important high-technology sector. Nortel enjoyed the leading global market share in the important digital switch segment. Although things looked good for the industry back at the beginning of the 1990s, it was a target for worldwide competitors.

Yet the decade surprised us all. The mar-

ket was transformed from digital switches for handling voice traffic for traditional phone companies such as Bell Canada, to optical transmission systems for handling data and Internet protocol traffic over alternative carrier networks, such as Qwest Corporation's all-fibre network.

Nortel and other members of the nascent Canadian cluster in 1991 could have continued a narrow definition of the industry and focused financial and managerial energy on consolidating it. Had it done so, the Canadian industry would have experienced a drift downward, as did newsprint.

However, the industry acted boldly and aggressively to innovate. Rather than attempt to maintain current positions — through replicating competitors and better management of the status quo — Canadian firms boldly chose innovative strategies with global aspirations, exploiting entirely new markets. They did well thanks to intense R&D, branding and managerial boldness. Despite the current capital markets challenges, Nortel, JDS Uniphase, Celestica and others are positioned to lead the next wave of innovation in the telecommunications equipment market.

At the turn of the millennium, Canada once again faces a fork in the road. If we are

to compete and win on the world stage in the coming century, Canadian firms and governments must turn their backs on a culture of replication, and strive instead for uniqueness and innovation.

Innovation is the key today to global competitive advantage. Government at all levels must enhance Canada's commitment to creating a superior macroeconomic and microeconomic context for competitiveness. And our firms must develop more distinctive strategies based on relentless innovation.

If we all set our aspirations higher, Canada can not only prosper and succeed, but can become a leader in the global economy.

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