

## Mackenzie Institute Conference: Canada's Defence Perspectives 2020-2050

### Panel 4: Improving Canada's Defence Procurement Strategy in the 21st Century

Panel Remarks

March 30th, 2016 14:00, Fairmont Chateau Laurier, Ottawa, Ontario

#### **Check Against Delivery**

Good afternoon. I want to thank the Mackenzie Institute for inviting me to be part of this panel today.

The topic we have been asked to address is timely. It is timely not because issues with defence procurement in Canada seem timeless, but rather because the Trudeau government is undertaking two major policy reviews simultaneously, one on defence and the other on innovation. So I want to use my time today to link these big government initiatives in the context of today's discussion about defence procurement, recapitalization, and the concept of using procurement to leverage economic benefit for the country - a Defence Procurement Strategy.

Let's start with the Defence Review. Defence reviews are about three fundamental things: defence policy, force size and structure, and funding. Decisions on these matters are for the government to make, based on input from the Canadian Armed Forces (CAF) and from experts like those in the room today. In industry we take defence policy, force structure and funding as givens and we work within that box.

Historically defence reviews in this country have not dealt much with the processes or industrial dimensions of military procurement, in contrast to similar exercises undertaken in other nations--the Australians, for example, have just published a Defence White Paper that has a companion document on defence industrial policy.

Nevertheless, it goes without saying that no defence policy can be executed effectively if procurement isn't working well--in other words if the CAF isn't getting from industry the equipment and services it needs on time and on budget.

There is general consensus that defence procurement in Canada is not working well. To some that would be an under-statement.

The standard critique of Canadian defence procurement goes something like this: it takes too long to procure even relatively non-complex technologies and systems, not to mention the complex ones; the procurement system is too risk averse, is premised on transferring as much risk as possible to business, and is mind bogglingly complex and burdensome; accountability in defence procurement is too diffuse; the costing and budgeting for defence procurements are too rigid; what is desired by the CAF is sometimes not

aligned with what can be produced by the private sector at any price and the idea of deliberately targeting and organically growing Canadian capability for delivery into procurements - a pipeline of innovation - seems almost unpalatable. This has manifested itself in the lapsing and re-profiling of capital funds. A consequence of this, if it weren't for the export market, would be a much larger-scale atrophy of the sector and an economic story that follows what we have seen in other domestic sectors over the last few years.

The government has committed to streamlining defence procurement to resolve some of the problems and they seem to be looking for ideas in this connection. The Defence Review is one obvious locus for this discussion. And industry, which deals day to day with the existing defence procurement processes, procedures, rules and habits of mind, is perhaps better placed than most to offer some pragmatic advice on how to simplify and improve defence procurement; we also, as a matter of course for our own businesses, often engage in what is called business process re-engineering. We hope the Defence Review--which the government has said will be consultative and transparent-- deals with defence procurement issues to some extent, and we in industry look forward to being a constructive part of that conversation.

In tandem with the Defence Review is the government's Innovation Agenda, a key priority for the Minister of Innovation, Science and Economic Development. In fact the Innovation Agenda is really the core of this government's economic policy. And they are right to focus on improving Canada's innovation performance, because we know this is central to productivity growth and improved standards of living.

Canada has followed the standard policy menu to stimulate innovation for nearly a generation now--reducing significantly marginal tax rates on capital and labour; investing in university based research; investing in post-secondary education and up-skilling workers; opening markets to international trade and investment; providing generous R&D tax incentives to business. Sadly, the results of this approach have been disappointing. Canada's productivity growth level remains stagnant at around 1 per cent. Our weak economy-wide innovation performance--as measured by low private sector R&D spending and weak investment in machinery, equipment and information technology, for example--are major sources of this relatively poor performance.

It seems obvious that new approaches to innovation policy are needed. The Trudeau government appears to be looking for innovative policies for their Innovation Agenda. One potentially promising approach to drive innovation that has not been used by Canadian governments for this purpose is the buying power of governments, in other words procurement.

In the defence realm we know that many of our allies have used military procurement for decades to drive innovations in their economies. One would be hard pressed to argue that the British, American, French, Israeli or even Swedish economies, for example, would be as nearly innovative as they are today had they not approached military procurement with a focus on developing key defence technologies and innovations at home, and then exporting them abroad.

Canada has not really been in that game. But now we have a new tool in the policy tool box as part of the Defence Procurement Strategy leveraging objectives - Industrial and Technological Benefits or ITBs, and in particular the Value Proposition part of that regime - that can be an instrument of innovation policy, and needs to be thought of and applied in that way. If the Value Proposition is utilized, especially in major defence capital projects, as an instrument to drive innovation, the government will be able to incentive R&D in, and intellectual property transfer to Canada, both of which are major drivers of innovation. This tool is in its infancy, but it needs to be used systematically and strategically going forward to enhance innovation in the Canadian defence industrial base.

I want to emphasize that we are not talking here about creating an innovative domestic defence industry out

of nothing and it doesn't require "clean sheet" design. It means getting smart about what's out there and who has it at the right technology maturity level and either taking risk if it's in Canada, or setting up the conditions to incent it being moved here for the long haul. What I am talking about is building upon a solid innovation foundation that already exists in the defence sector. A recently completely ISED-Statistics Canada survey concludes, for example, that the Canadian based defence industry generates 60 per cent of its revenues from exports, which is 20 per cent higher than the overall Canadian manufacturing industry. An export intensity like that is an indicator of an innovative industry, especially given the highly regulated and protected international marketplace within which defence companies operate. It says our companies are winning business in protected foreign markets because we are leading edge and innovative.

In addition, the same survey reported that more than 30 per cent of employment in the Canadian defence industry is concentrated among highly skilled engineers, scientists, researchers, technicians and technologists, and the sector outpaced the overall Canadian manufacturing average in employee compensation. Again, all of which are innovation indicators.

My message to you today is that we have actually two distinctly different outlooks for 2020-2050 depending upon our perspective and the choices we make over the next 4 years. We can do things in the same way we have been for some time now: we can choose to remain largely risk averse. We can continue to view defence procurement in a silos within Government - insignificantly chipping away at unilateral inefficiencies. We can treat defence, procurement and the innovation agenda as completely de-coupled concepts. I would suggest that the perspective on the future with that outlook will be the same as today, certainly in our sector.

Alternatively, there is another outlook for 2020-2050. We can acknowledge that we have a big opportunity in front of us right now one that is good for the military, the government, industry and the Canadian economy generally. If we start now, by 2020 we might have a strategy in place. A strategy that marries the Defence Review and the Innovation Agenda, providing the opportunity to make practical changes to improve the process of defence procurement, while at the same time enhancing innovation in the Canadian defence sector. It is a marriage of defence policy and economic policy, what some might call "defence industrial policy". It is truly the "strategy" part of the Defence Procurement Strategy. If we have one in 2020 when the Canadian Surface Combatant project, or the Next Generation Fighter program or even the procurement of next the generation of sensor or space technologies start execution, our perspective might be more optimistic. It is around that sense of optimism that a defence industrial policy will deliver new products and services which, in parallel, we will be capable of selling into the export market. These same products and services will be evolved in service and will live for those next 30 years over.

I'd invite you to think on which outlook for 2020-2050 you want to see, and maybe more importantly, which one you want your children to be a part of.

Thank-you.