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CROSS-BORDER INSTITUTE

Dr. William (Bill) P. Anderson received his doctorate in Geography from Boston University in 1984. From 1983 to 1998 he was a member of the Geography faculty, director of the Institute for Energy Studies and an associate member of the Department of Civil engineering at McMaster University.

From 1998 to 2008 he was a professor in the Department of Geography and a lead researcher in the Center for Transportation Studies at Boston University. He arrived July 1, 2008 as Ontario Research Chair in Cross-Border Transportation Policy, founding director of the Cross-Border Transportation Studies Institute and professor in the Department of Political Science at the University of Windsor.

Professor Anderson's main research interests are in transportation studies; international trade and business; Canada-US economic integration; supply chain analysis; and urban and regional economic analysis. He has published 60 journal articles and book chapters and is the author and coauthor of five recent books on economic geography, transportation infrastructure and technologies.

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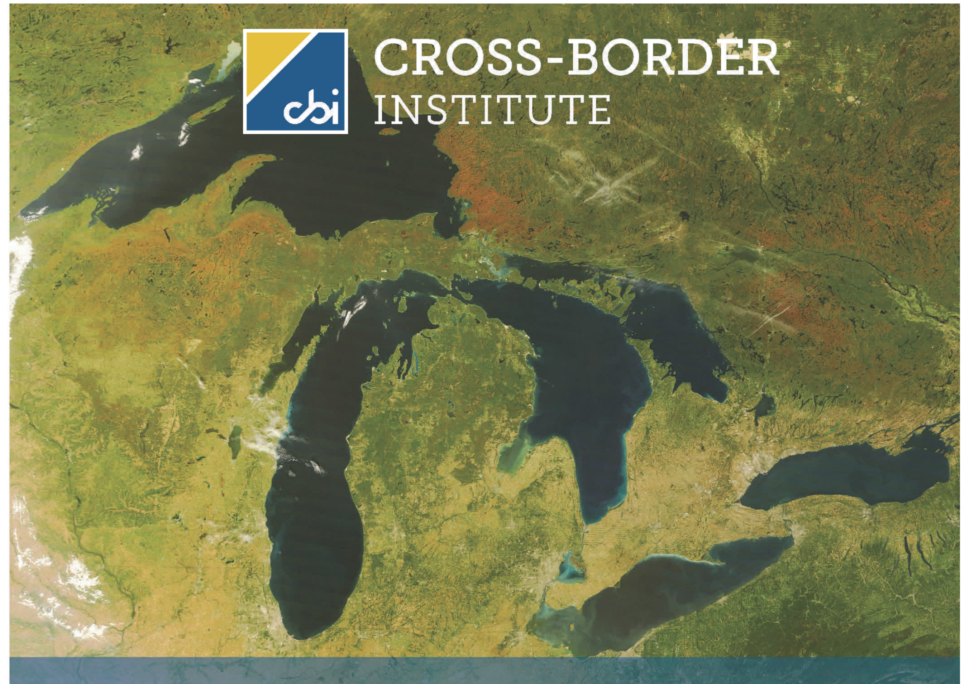

CROSS-BORDER INSTITUTE

THE BORDER AND THE BINATIONAL ADVANTAGE IN THE GREAT LAKES AND ST. LAWRENCE ECONOMIC REGION.

OVERVIEW

The Great Lakes / St. Lawrence (GLSL) region, which includes parts of eight US states and two Canadian provinces, is bound together by a complex web of economic connections but divided by an international border. There is one integrated Great Lakes production complex, but two national regimes of laws, policies and public infrastructure supporting it. There is a common public interest, but there is a perception of rivalry and the lack of an appropriate incentive structure for cooperation. In order to realize its full economic potential, the GLSL must function as one region composed of two nations.

Some suggest that in the interest of economic efficiency we should simply make the border disappear. This outcome is neither likely nor desirable. Coming from different founding philosophies, both nations cherish their political autonomy. For each country, the border makes it possible to enforce laws and policies determined through its democratic processes. Strikingly different policies on firearms, immigration and many other things are only possible if the border acts as a screen to certain goods and people. No matter how friendly and mutually beneficial the relationship between the United States and Canada may be, the border is not going to disappear any time soon.

But the border has costs. The frictions created by traffic delays, border compliance and regulatory inconsistencies retard cross-border commerce. The overarching question addressed by this report is how do Canadians and Americans in the GLSL region enjoy the sovereignty that the border protects while facilitating mutually beneficial economic integration that the border impedes?

Some argue that you can't have it both ways. There is a trade-off between sovereignty and easy cross-border commerce. And since "security trumps trade," the potential for economic integration is limited.

This report rejects that answer. We need to take up the challenge of using policy, technology, infrastructure and education to create a border that provides customs, immigration and security services better than it does today, but with a lot less friction. The onus is not exclusively on governments and border agencies, but also on all the people and firms in the GLSL region. Not only do we need better border crossings, we need to be better border crossers.

Furthermore, this reports argues that rather than seek to eliminate our differences as Canadians and Americans, we must embrace them. The GLSL region can rise to a higher level of proficiency in the global economy not despite its binational character, but because of it. We call this the binational advantage.

BEGINNINGS

The story of how the GLSL emerged as the greatest industrial region the world had ever seen begins with the water. Just as aboriginal people had done before them, French explorers and traders penetrated the interior from their settlements on the St Lawrence through the Great Lakes and their tributary and connecting rivers. Because the waters of the Great Lakes descend from Lake Superior at an elevation of 183 meters all the way down to sea level, there are rapids along the way. The Lachine Canal between Montreal and Lake Ontario, the Welland Canal circumventing Niagara Falls and the Soo Locks between Superior and the lower lakes made navigation possible from Northern Minnesota to the Atlantic. The Erie Canal connected the entire system to New York City. These audacious infrastructure projects endowed the GLSL region with the unique quality of being interior, but not landlocked.

Map of Canada-US border crossings with volume information, including Fort Francis.

Iron and steel became the dominant industrial materials in the 19th century. To make steel you need two things in large quantities: iron ore and coal. Enormous deposits of iron ore were discovered in Northern Michigan and Minnesota from where it could be transported by water (with the help of the Soo Locks) to the lower lakes. There it was combined with coal from the Appalachian region on a huge scale. Additional iron from Northern Quebec was also moved to the new Great Lakes steelmaking centres by water. In addition coal and ore, these centres also had access to main market for steel: the railroads.

As railroads spread into the interior they opened up new territories to commercial agriculture. A dominant rail hub emerged in Chicago, helping to establish it as the great metropolis of the American interior.

Railroads spurred growth in other cities, including Toronto in Canada. There was a virtuous circle of development whereby railroads expanded agriculture, forestry and mining, which in turn expanded the demand for more railroads and the growth of more cities. And all of these things demanded more steel.

But regional economic development didn't end with commodities and steel. Regional entrepreneurs used technological innovation to add value to local resources and produce goods so cheaply that they could dominate global markets. For example, Chicago meat packers used refrigerated rail cars and new systems of production to dominate the market for fresh meat in the US East Coast cities. Henry Ford introduced methods of mass production to make cars not only better but also cheaper, leading to massive expansion in regional production and global demand.

The story of how thousands of manufacturing establishments grew up in scores of industrial cities in the GLSL region is long, complicated and fascinating. The common themes that emerge are infrastructure, innovation and production on a massive scale for external markets.

THE BORDER AND THE EVOLUTION OF THE BINATIONAL ECONOMIC REGION

The 1783 Treaty of Paris between the United States of America and Great Britain delineated the border from the Atlantic Ocean, where Maine abuts New Brunswick, to Lake of the Woods, about 500 kilometers west of Lake Superior (See map). Bodies of water were used to define much of the border, including part of the St Lawrence River, the midlines of all the Great Lakes except Lake Michigan, and the connecting waters of the Niagara, Detroit, St. Clair, and St Marys Rivers. Thus, the GLSL region was divided into its Canadian and American components.

Canada and the US were not always as friendly as they are today. Revolutionary forces invaded Quebec in 1775 and fierce battles were fought across the Niagara and Detroit River frontiers during the War of 1812. Against this backdrop, relations with the US were at the top of the agenda for the new Canadian government after 1867. The main topic of debate was whether Canada's economy should be integrated with the American economy under a system of free trade or protected to develop independently behind tariff barriers. The pro-tariff side won out, making the border an impediment to regional economic integration.

This schism did not prevent economic development from happening, as both the US and Canada emerged as leading industrial nations based largely on the economic activities in the GLSL region. But the Canadian and American industrial heartlands developed in parallel, rather than as an integrated whole. It was not until the 1960s that a process of intense cross-border integration accelerated, spurred on by trade liberalization under the Auto Pact (1965), the Canada-US Free Trade Agreement (1988) and the North American Free Trade Agreement (1994).

Through this process, Canada and the US developed the largest bilateral trade relationship in the world. They also developed a distinctive pattern of trade in intermediate goods. In the manufacturing sector (which dominates trade in the GLSL region) trade is not confined to finished goods but rather involves millions of shipments of materials and component parts in cross-border supply chains. This pattern is well known in the automotive industry but it also prevails in agrifood, machinery, aerospace and others. It has resulted in a uniquely intense form of economic integration with a critical need to move goods quickly, reliably and cheaply through the international border.

Creating a seamless border, however, has proved a challenge. Most crossings are at bridges over the connecting rivers of the Great Lakes. Border infrastructure has not been expanded at pace with the rapid growth in trade since the 1960s, leading to major traffic bottlenecks. While NAFTA is a free trade area, it is not a customs union. This means that even shipments that cross the border tariff free must undergo costly processes of customs administration. In the aftermath of 9/11, security has been ramped up at border crossings, leading to delays, uncertainty and added costs. All of this means that the border is source of significant friction. To the extent that this friction limits cross-border economic integration, the border prevents the GLSL economy from reaching its full potential.

THE GLSL ECONOMY TODAY

After more than a century of rapid economic expansion, the GLSL region entered a period of slower economic growth by the 1980s. On many economic measures, it lags the overall performance of Canada and the United States. For example, between 1998 and 2013, the rate of employment growth in the broadly defined GLSL region1 was only 60% of the same rate in the two national economies combined.

To some extent this can be explained by broad sectoral trends in advanced economies. In both Canada and the US, employment share has been shifting from goods production to services for several decades. In fact manufacturing employment actually declined in both countries over the 1998-2013 period. So the under-performance of the GLSL region may be mostly due to a regional concentration in manufacturing. However, our data analysis indicates that even after controlling for the historical distribution of employment across industries, the regional economy has under-performed. Growth in relatively dynamic industries like professional services, finance and health care has been considerably slower than in other regions. And even manufacturing – where the GLSL has historically outperformed the rest of the world – is lagging behind other American and Canadian regions.

We should not be too quick to draw conclusions based on these results. Slow employment growth in manufacturing may actually reflect rapid productivity growth, whereby fewer people are needed to produce the same quantity of goods. Also, there are islands of economic dynamism within the regions, such as the technology centres of Anne Arbor, MI, Madison, WI and Kitchener-Waterloo ON. Also, the Greater Toronto Area continues to be one of the fastest growing regions (both economically and demographically) in North America.

It is undeniable, however, that the GLSL region is at a crossroads in its economic history. It can continue along its current trajectory and fall further behind in both the North American and global economies. Or it can pursue fundamental, structural changes that make the most of its many economic advantages. Those advantages come in various forms, including advantages of location, natural amenities, workforce skills, educational

1 Here the GLSL region is defined as including all states and provinces that touch the Great Lakes and the St.

Lawrence. In the full report, analysis is repeated for a more narrow regional definition, but results are similar institutions, the ability to attract and integrate global migrants, and others. To this list we can add the binational advantage.

THE BINATIONAL ADVANTAGE

It is common to think of the border as a problem to be overcome. This is natural because border friction is costly. But the border also represents the presence of two great sovereign nations with significant differences. In some cases – for example in the case of inconsistent regulations – those differences represent additional friction. But in many ways, the differences between Canada and the US represent complementarities. Just as two people with complementary skills make good business partners, two nations with complementary characteristics make the GLSL region stronger and better able to compete in the global economy. This is the binational advantage.

Here are a few examples of complementarities:

- Demographics: There are far more people in the US part of the GLSL, but the Canadian population is younger and growing faster. Canadian firms gain from accessing the larger US market, while American firms gain from accessing the more dynamic Canadian market.
- Workforce resources: The US Great Lakes States has one of the largest industrial labour forces in the developed world. But the provinces of Ontario and Quebec enthusiastically welcome migrants from around the world who bring technological and entrepreneurial skills that may be in short supply in the States.
- Out-of-synch business cycle: In the years since the Great Recession there have been periods when the Canadian economy did better than the US, and years (like right now) when the US economy did better than Canada. Thus the binational advantage is a moderating effect on demand in the GLSL region.
- Public Services: One of the most obvious differences between Canada and the US is in the mixture of taxation, regulation, infrastructure and public services offered by the public sector. Different kinds of economic activities have different public sector needs. Some will be served better in Canada, others in the US. Entrepreneurs and investors can "vote with their feet" to locate where their needs are best met.

Taking advantage of these complementarities is complicated by the less than complete liberalization of economic relations. For example, NAFTA allows for very limited labour mobility, so it is not possible to directly access needed skills that are present across the border. But creative firms will find ways to realize the binational advantage. For example, trade in services provides a means of accessing those critical skills.

MAKING A BETTER BORDER

Naturally, the border is always a factor. The good news is that with technologies that are already available, combined with policy innovation, the border need not diminish the binational advantage.

This report does not contend that complete elimination of border functions is a necessary end state in the GLSL region or in North America more generally. That would require a level of policy harmonization that may never be achieved and may not even be desirable. More modest goals for border improvement will be sufficient to fully achieve the binational advantage.

One such goal is that the Canada-US border should become inconsequential with regard to three types of business decisions: location decisions, sourcing decisions and market entry decisions. The border should not be a sufficient impediment to prevent a firm from locating some facilities in the US and others in Canada in order take advantage of market, skills, public sector or other complementarities. Nor should it prevent a firm from purchasing inputs of goods or services from across the border. Nor should it prevent a firm from expanding its market by selling its goods and services across the border. This goal does not require that border costs fall to zero, only that they are low enough so as not to be a deciding factor in those business decision.

How close are we to this goal? That's hard to say, but we know that we are not there yet. Econometric analysis suggests that Canada-US trade is much lower than it would be if the border were costless. Detailed studies show that cross-border trucking costs are much higher than for comparable domestic shipments. There is a wealth of anecdotal evidence that cross-border movement of people for business purposes is a major source of friction.

But there is reason to be optimistic. Customs, immigration and security functions consist mostly of the exchange of information, and technologies to transfer information wirelessly and securely have exploded in recent years. As an example, a major security concern is that contraband may be placed on a truck carrying a legitimate load while en route to the border. GPS and other tracking technology can verify that the truck neither stopped nor deviated from its approved route between a secure facility of origin and the border. Creating this type of virtual secure corridor is especially suited to supply chain movements over relatively short distances that are typical of trade in the GLSL region. Other technologies – vehicle to vehicle and vehicle to infrastructure communication, RFID systems, sensors, TV white space wi-fi – can be harnessed for border application. Canadian and American border officials are open to creating the type of policy innovation necessary to exploit these technologies.

Still, you can't drive a truck across a virtual bridge. The focus of trade flows in the GLSL region at a few key crossings means that adequate infrastructure is needed to provide the fast and reliable movement of goods and people necessary to realize the binational advantage. Infrastructure solutions are expensive, contentious and maddeningly slow to accomplish, but they are necessary. The Herb Gray Parkway and Gordie Howe International Bridge projects jointly represent a historic achievement to secure the economic future of the GLSL region.

Artist's rendering of Gordie Howe Bridge