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Increased Import Competition from China Helped Slow the Decline in Canadian Manufacturing Productivity between 2005 and 2010

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The Centre for the Study of Living Standards (CSLS) today released a report entitled “*Does Import Competition Reduce Domestic Innovation? Evidence from the 'China Shock' and Firm-Level Data on Canadian Manufacturing.*”

The report finds that the increasing share of Chinese imports to Canada reduced growth in R&D spending and total factor productivity within Canadian manufacturing firms. More specifically, increased Chinese imports can explain about 7 per cent of the total decline of \$1.36 billion (2007 CAD) in R&D expenditure in Canadian manufacturing between 2005 and 2010. The impact is relatively small as most of the decline in R&D spending occurred within small, less-productive firms who accounted for a small share of the total R&D expenditure in manufacturing.

The increased share of Chinese imports also translated in lower profit margins for smaller and less productive firms. As some of these firms were forced to exit the market, a positive reallocation effect took place as employment shifted towards more productive firms, more than offsetting the negative effect on R&D spending and productivity by the smaller firms. Overall, our estimates imply that had there been no increase in the share of Chinese imports in the total domestic market for manufacturing goods between 2005 and 2010, the aggregate TFP level in manufacturing would have declined by 1.26 per cent per year instead of the actual 1.09 per cent per year.

The findings imply that rising Chinese import competition affected firm innovation and outcomes (i.e. productivity, employment, survival). Moreover, the findings imply that the size

distribution of firms was affected by the increased share of Chinese imports. Given these effects, a further discussion on appropriate policy responses to trade liberalization would be desirable.

The report is posted at <http://www.csls.ca/reports/csls2019-03.pdf>.

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The Centre for the Study of Living Standards (CSLS) is a national, independent, Ottawa-based not-for-profit research organization. Its primary objective is to contribute to a better understanding of trends and determinants of productivity, living standards, and economic wellbeing in Canada through research.