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student review

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Quarterly
Student Magazine
Fall 2014

Arab Spring Reforms Remain Ineffectual

IN THIS ISSUE:

- Weaker loonie hurts Canadians more than it helps
- First Nations education
- Burger King-Tim Horton's merger

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Website: fraserinstitute.org
E-mail address: claire.jones@fraserinstitute.org

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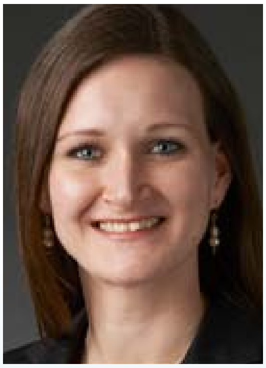


Dear Readers,

The fall 2014 edition of *Canadian Student Review* features a range of interesting articles on topics such as the effects of a weakening Canadian dollar, the price of public health care, whether or not the Arab Spring has resulted in more economic freedom for the Middle East, and reforming Canada's personal income tax rates.

We are also including a recent video we have produced on the Canadian Consumer Tax Index, which tracks the total tax bill of the average Canadian family over the past 50 years, and an infographic on First Nations education. We'd love to hear what you think about these visual illustrations of our work.

You will also find details of our student seminars which will take place across Canada this fall. These lively seminars provide a forum for discussion on a range of topical issues, and are a great way to network with peers and leading policy experts.

I hope you enjoy reading these articles, and are having a great start to the new semester.

Best,

Claire Jones
Editor, *Canadian Student Review*

Contents


TAX

Weaker Loonie Hurts Canadians More Than It Helps

This week the Canadian dollar dropped below 90 cents US. Good news, say some economists, for the Canadian economy. But in reality, the negative impact of a weaker loonie will likely outweigh any benefits.

It's a myth that devaluation of the Canadian dollar broadly stimulates the economy and leads to prosperity. In fact, a weaker loonie triggers higher domestic prices, which hit consumers in the wallet, and higher importing and financing costs, which hurt businesses and government. You can read more about this in the analysis *Economic Consequences of the Lower Canadian Dollar.*

For example, certain commodities—such as gasoline—are priced in US dollars. So when the loonie drops, people pay more at the pumps.

The cost of doing business will also increase. Canadian businesses import 55 per cent of their machinery and equipment. When faced with higher prices, businesses will buy less machinery and equipment, and consequently limit production, which may limit employment opportunities and hurt worker wages.

Canadian governments, meanwhile, will pay more when managing debt denominated in US dollars, particularly provincial governments and their utilities (i.e. natural gas or electricity), which issue the most bonds denominated in non-Canadian currency.

However, there are benefits—albeit overstated, in some cases.

Exporters benefit from a lower exchange rate. Why? Because Canadian exporters exchange goods for US dollars, so when the loonie is relatively low, those US dollars, when repatriated, buy more Canadian dollars.

But even for exporters, the benefits of a lower exchange rate are likely to be limited, because market demand is the primary driver of exports—not the relative strength or weakness of the loonie.

Moreover, exporters may rely too heavily on a depreciating dollar, which can lead to investments that only make sense with a weaker loonie.

Canadian natural resource industries should benefit most from a lower Canadian dollar. Oil and gas firms, for example, export much more than they import, so a weaker loonie will boost their bottom line.

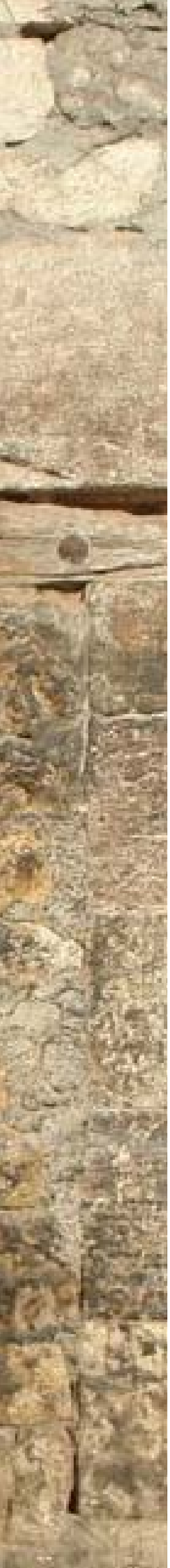
For individual Canadians, anyone invested abroad will pocket more Canadian dollars when those investments are brought back home.

However, this is a dubious benefit to the Canadian economy because it rewards people for not investing in Canada, and consequently, lowers the value of all assets in the country. ■

Philip Cross was formerly Chief Economic Analyst at Statistics Canada. He now writes a bi-weekly op-ed for the National Post and other papers.

First Nations schools		Provincial schools
$13,524 Per student		$11,646 Per student
✗	Core curriculum	✓
✗	Attendance requirements	✓
✗	Teacher certification	✓
✗	Provincially recognized diplomas	✓
<40%	Graduation Rates	>75%

Arab Spring Reforms Remain Ineffectual Due to Lack of Economic Freedom



Despite the promise of the Arab Spring, most nations in the region have failed to reform their economies, largely leaving elite privilege in place. You can read more in this new essay, *Institutions and Economic, Political, and Civil Liberty in the Arab World,* which spotlights Arab countries and the need for increased economic freedom and free market reform that will enable citizens to make their own economic decisions outside the influence of government or crony capitalist elites.

Denial of economic freedom helped launch the Arab spring—it began in Tunisia when a vegetable and fruit seller set himself on fire to protest police bullying in the public market. His freedom to sell his wares was repeatedly denied, yet restrictions on economic freedom still plague the region.

Much of the population in the region believes the Arab world underwent significant "neoliberal" free market reforms in the first decade of this century, a perception reinforced by praise from international institutions.

Yet, according to policy data, crony capitalism, disguised as reform, marked the period, with ruling families in countries such as Tunisia and Egypt grabbing state assets under the guise of privatization.

This period of phony crony reform is a huge impediment to future reform because many citizens believe free markets have been tried and failed.

Free market reform is vital to the success of the Arab Spring. If the old economic structures remain in place, the elite will, for their own benefit, maintain the power to deny opportunity to the people.

Charles Roffy

Johnathan Rashad

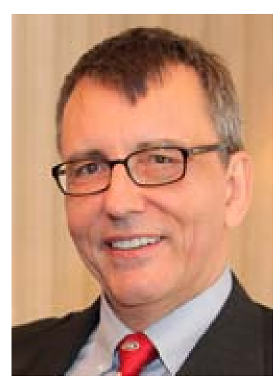
Despite large-scale protests, no new economic vision emerged from the Arab Spring

While protesters in many countries demanded civil freedoms, democracy and an end to elite privilege, no new economic vision for the region emerged from the Arab Spring. And many protesters are simply pining for the unproductive government jobs they had heretofore been denied.

Nonetheless, there are signs of progress in Jordan, Morocco, and Tunisia, where economic and political reforms are underway. But obviously, the region faces other obstacles to economic progress, including the limited economic role of women and the waves of violence (and resulting refugee crisis) sweeping through countries such as Iraq and Syria.

While the situation in parts of the Arab world remains bleak, economic freedom is a vital component in the region's overall recovery.

Fred McMahon is a Fraser Institute Resident Fellow and holder of the Dr. Michael A. Walker Research Chair in Economic Freedom. He manages the Economic Freedom of the World Project at the Fraser Institute.



The VIDEO Gallery

Canadian Consumer Tax Index 2014

Canadian families spend more money on taxes than on food, clothing, and shelter combined.

See the video HERE

Bigstock

A typical Canadian family with two parents and two children will pay up to $11,786 for public health care in 2014. This comes from our new study, *The Price of Public Health Care Insurance,* which helps Canadians better understand health care costs and the value they receive for their tax dollars.

Health care in Canada is not free—while Canadians may not pay directly for medical services, they pay a substantial amount of money for health care through taxes.

In fact, most Canadians are unaware of the true cost of health care because they are not billed for any portion of physician and hospital services covered by tax-funded health care insurance. Moreover, general government revenue—not a dedicated tax—

bankrolls health care, while health care premiums (where applied among provinces) cover only a fraction of health care costs.

However, using data from Statistics Canada and the Canadian Institute for Health Information, the study estimates the amount of taxes Canadian families will pay for public health insurance in 2014, and by how much it has increased over the last decade.

For example:

In 2014, the average single individual earning roughly $42,000 will pay $4,381 for public health care insurance.

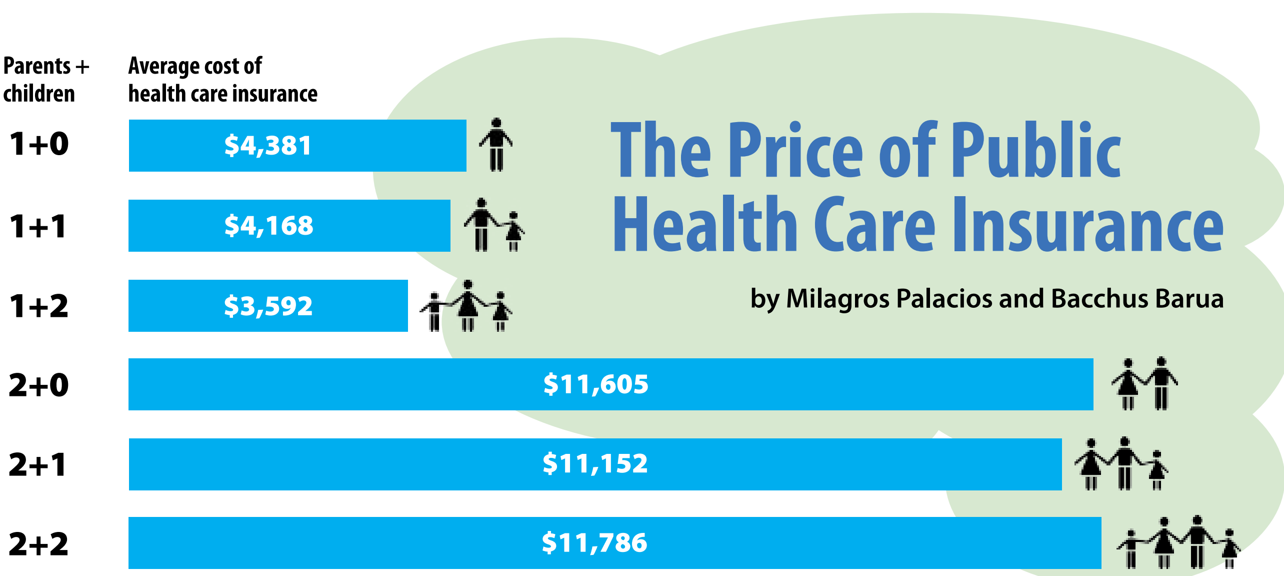
A family of two adults and two children earning approximately $118,000 in 2014 will pay $11,786 for public health care insurance.

And what about the cost of health care insurance among income groups?

The 10 per cent of Canadian families with the lowest income will

The Price of Public Health Care Insurance

by Milagros Palacios and Bacchus Barua



pay an average of $523 for public health care insurance in 2014.

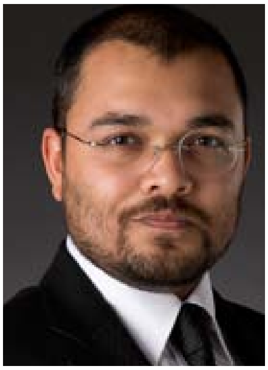
In 2014, the 10 per cent of Canadian families with an average income of $57,818 will pay an average of $5,522.

And families among the top 10 per cent of income earners in Canada will pay $37,239 for public health care insurance.

Finally, between 2004 and 2014, the cost of health care insurance for the average Canadian family (all family types) increased by 53.3 per cent, dwarfing increases in income (34.7 per cent), shelter (40.7 per cent), clothing (33.4 per cent) and food (15.6 per cent).

The cost of health care in Canada is rising and it's ordinary Canadians and their families who pay the bill.

Any debate about health care in Canada has to acknowledge the real cost Canadians pay through taxes. Once Canadians know how much health care actually costs them, they can then decide if the system delivers good value for their money. ■



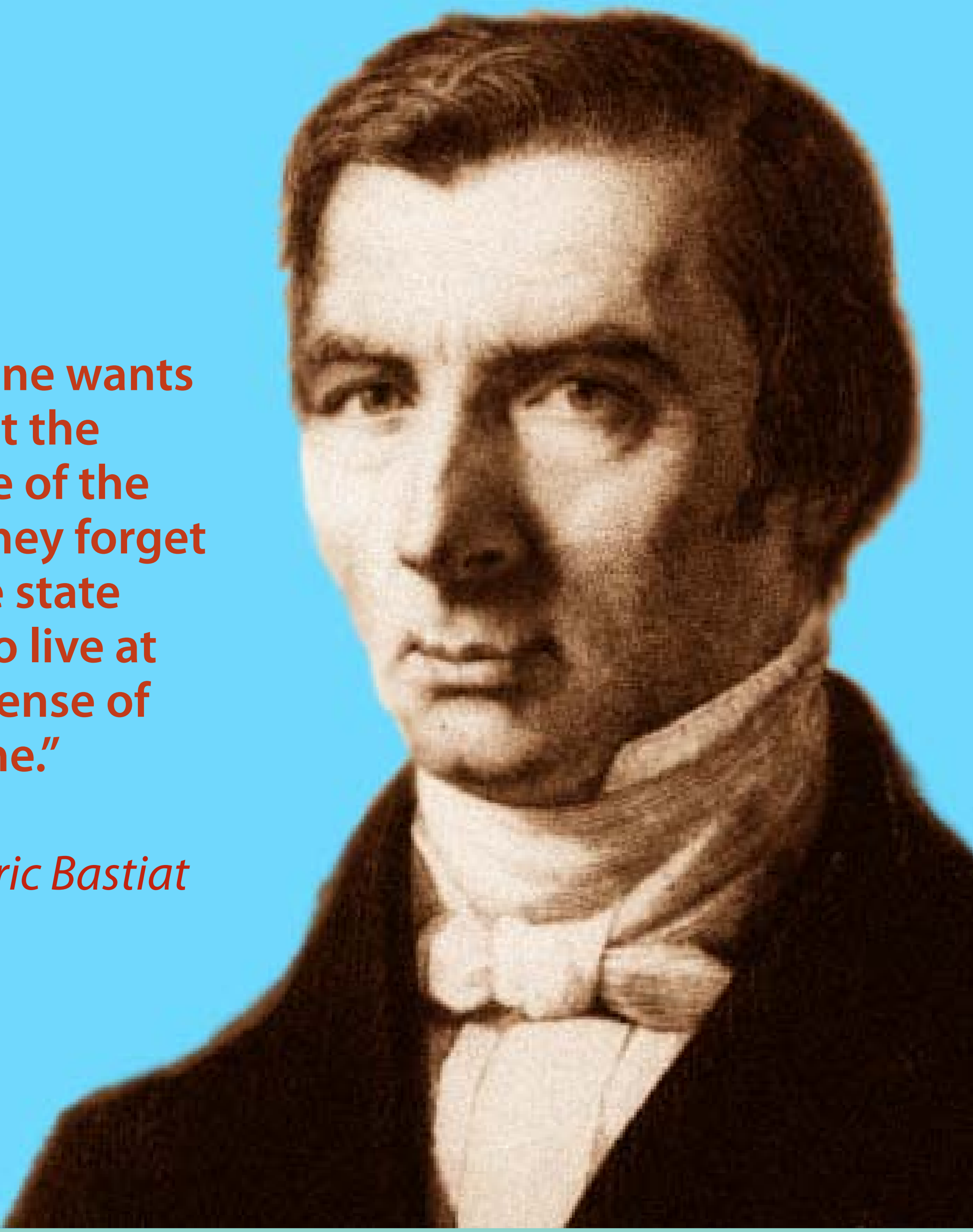
Bacchus Barua

Milagros Palacios

Bacchus Barua is a Senior Economist in the Fraser Institute's Centre for Health Policy Studies.

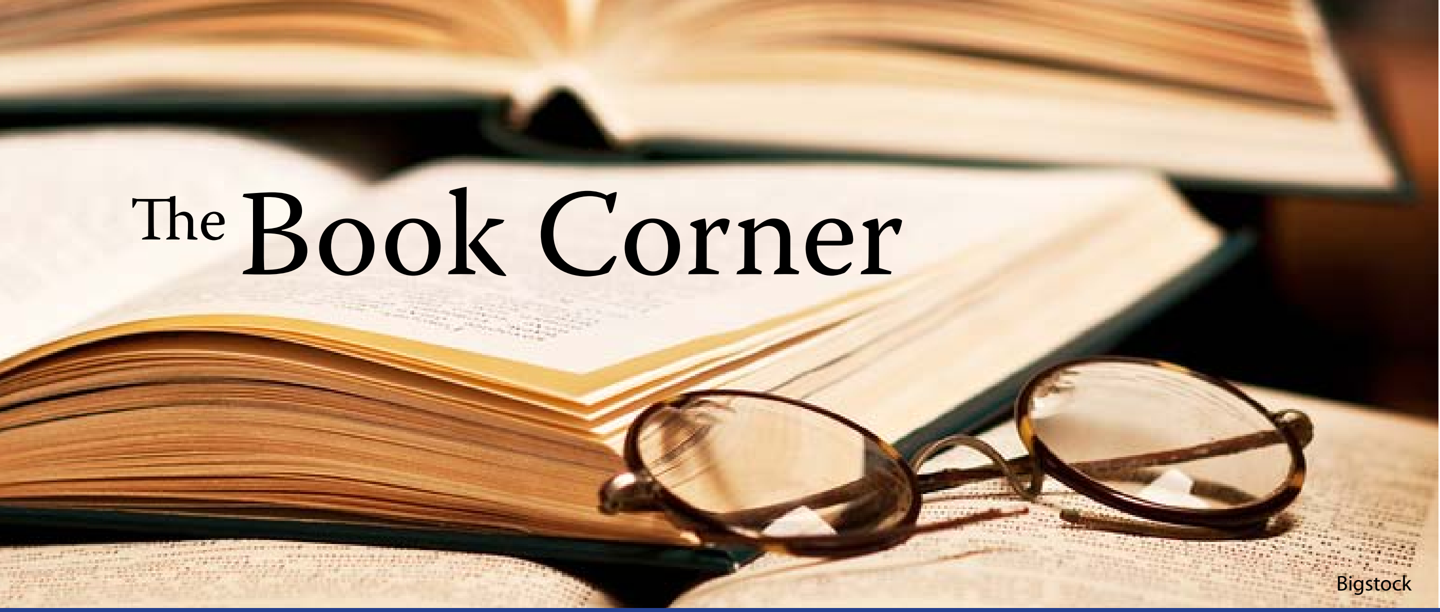
Milagros Palacios is a Senior Research Economist at the Fraser Institute.

THE QUOTE WALL



"Everyone wants to live at the expense of the state. They forget that the state wants to live at the expense of everyone."

—Frédéric Bastiat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The Book Corner

Fraser Institute researcher-recommended books on free market policies and economics

WHO NEEDS JOBS?

Spreading Poverty or Increasing Welfare

Pierre Lemieux

In his new book, Pierre Lemieux reveals one of the most pervasive misapprehensions driving government economic policy. He explains why jobs are costs, not benefits; and why, consequently, we need as few of them as possible. Using economic analysis, he illustrates how jobs are not the goal of economic life, and how creating jobs should not be the aim of public policy. He demonstrates why federal programs that seek to create jobs are almost guaranteed to be unnecessary and expensive, and how they undermine productivity throughout the economy.

In one anecdote, he tells how the chainsaw destroyed logging jobs—and made Americans much better off. He argues that successful policies that allow technological change to occur may destroy some jobs, but also create other jobs, and thus improve the standard of living.

He also looks at how income and prosperity are created (by businesses producing what consumers demand), proposes solutions to the unemployment problem, and gives readers the knowledge they need to make sense of the many theories and comments about jobs from North American politicians and economists.

The book is an introduction to the economic way of thinking, and is accessible to the everyday reader with straightforward, non-technical language. With his clear approach, Lemieux takes this controversial and complex topic and makes it understandable, using economic analysis and powerful, real world examples.

Pierre Lemieux

Pierre Lemieux will discuss Who Needs Jobs? Spreading Poverty or Increasing Welfare *at the Fraser Institute's Explore Public Policy Issues student seminar in Montréal on February 14, 2015.* ■

Canada's Personal Income Tax Rates: Time for Reform

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Both economic theory and empirical research show that there is a relationship between marginal tax rates and economic performance. A marginal tax rate refers to the extra tax an individual will owe to the government for engaging in a little more of the taxed activity. Marginal tax rates determine the amount of tax a person must pay for the *additional* dollar he or she earns. This affects individual decisions like whether to accept a new job, choosing working hours, or whether to increase investment in human capital via education.

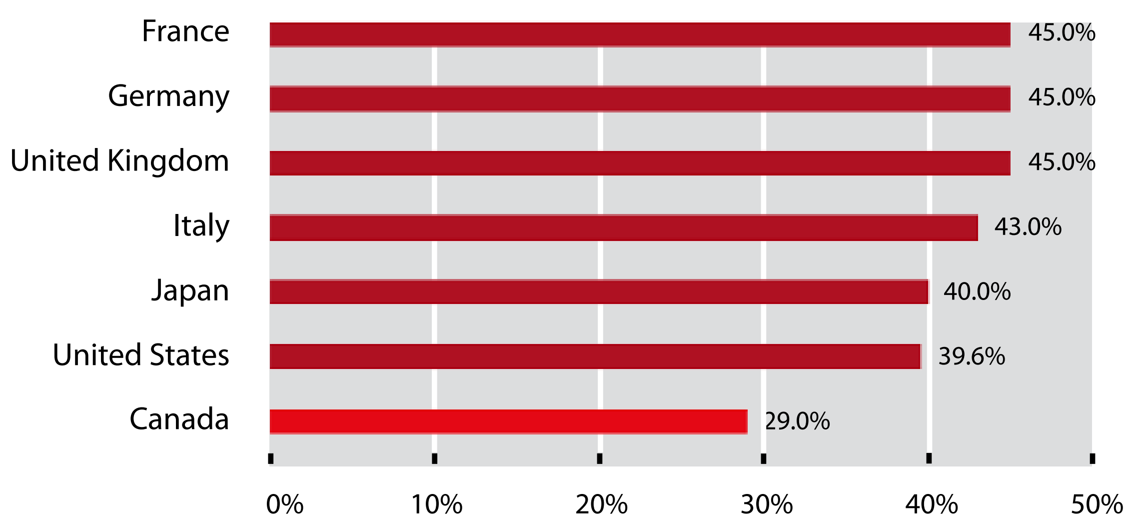
In a study published by the Fraser Institute, Murphy, Clemens and Veldhuis (2013) summarized the literature on how marginal tax rates influence economic growth, employment, saving, entrepreneurial activities, investment, and other economic indicators. In particular, they found that there is no real dispute about the adverse economic effect of high and increasing marginal tax rates. Their study also demonstrates that Canada has relatively high marginal personal income tax rates—especially after accounting for the income levels at which they apply—among G-7 countries. This lack of competitiveness is particularly acute in Ontario, Quebec, and Nova Scotia.

Canadian governments continue to impose new and higher taxes

Despite the evidence that high marginal tax rates stunt growth, Canadian governments continue to impose new and higher taxes. In the federal and provincial budgets of the last few years, there were a number of tax increases. British Columbia lowered its personal income tax exemption from $11,354 (2012) to $10,276 (2013) and $9,868 (2014), but introduced a new tax rate for those earning more than $150,000 per year in 2013. Ontario introduced a new tax bracket in 2012 to increase its top rate to 19 percent. Then in 2014 the government lowered the threshold for this rate but increased its top tax rate to 20.5 percent with another bracket, which led to a more complicated tax system and increased the burden for high-income earners. New Brunswick has increased all four of its marginal tax rates for two consecutive years, and its top marginal tax rate increased by 25% over this period. All of these changes decrease the competitiveness of Canada's personal income tax system.

In Canada's federal structure, both the federal and provincial governments levy personal income taxes. Prior to 2000 most provinces based their personal income tax on the "basic federal tax." By 2001, all provincial governments were allowed to establish their own tax rates and brackets. We now have a federal and provincial system with different rates and income thresholds. The system is progressive with tax rates increasing with income.

Figure 1: Federal/ Central Top Personal Income Tax Rates for G-7 Countries, 2013



Tax reform would stimulate saving, investment, entrepreneurship, and employment

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Figure 1 compares the federal marginal income tax rates with other G-7 countries. Canada's top federal rate is competitive relative to the other countries. France, Germany, and the United Kingdom all have top income tax rates at 45 percent, while the United States has a top income tax rate of 39.6 percent. The threshold of the top rate for each country is different.

But looking just at the federal tax rates yields an incomplete picture. Provincial tax regimes vary. Alberta has a flat tax rate of 10 percent on all income of $17,786 and above. Ontario has a deeply progressive income tax with seven brackets ranging from 5.05 percent to 20.53 percent. Nova Scotia has the highest top marginal income tax rate of 21 percent, which is more than double the lowest top rate in Alberta (10 percent). Quebec is another province with a heavy tax burden at all income levels, especially for lower and middle-income earners. The province's marginal tax rates start from 13.53 percent at $11,305 and climb to 20.97 percent at $136,270 and above.

The distribution of income taxation between the different levels of government in Canada is less tilted in favour of the federal government than in other countries. Canadians tend to pay a lower share of their total income taxes to the federal government, and a greater share to provincial governments relative to citizens in other federal states. Consequently, any assessment of Canada's tax competitiveness must give full consideration to the combined federal-provincial income tax burden.

Figure 2: Combined Federal and Provincial Marginal Personal Income Tax Rates for $136,270, 2014

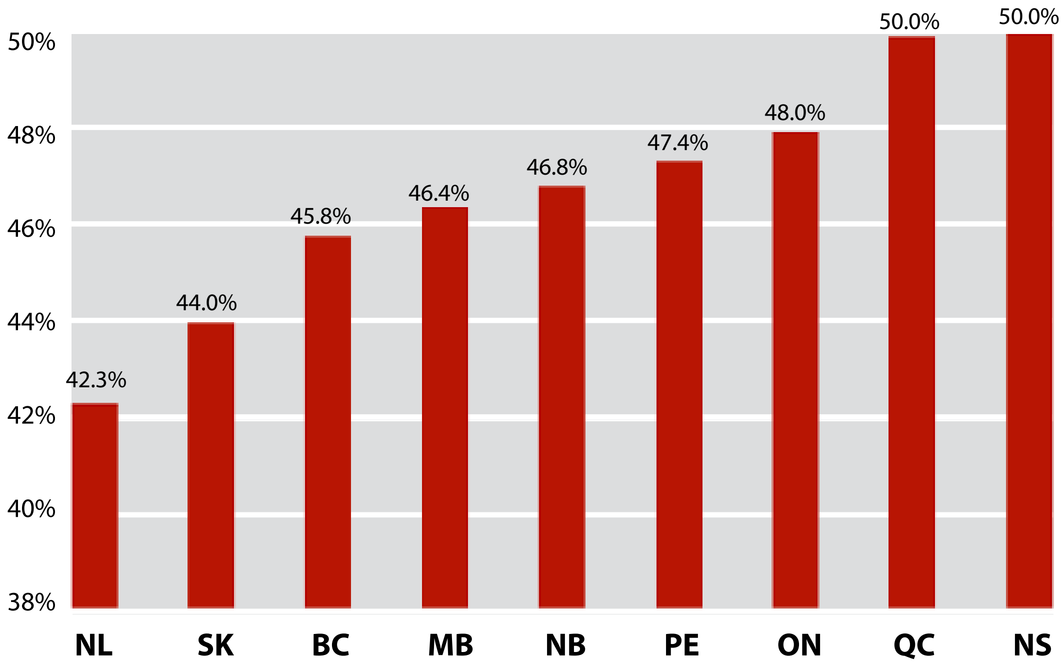

Figure 2 shows that the combined federal and provincial marginal tax rates are greater than 40 percent in every province. Quebecers and Nova Scotians experience the highest combined marginal tax rates of nearly 50 percent at the $136,270 income level. At this income level, every Canadian province has a higher combined marginal tax rate than any American jurisdiction (Speer, Palacios, and Ren, 2014).

As the empirical and theoretical literature shows, the high and progressive tax regime has very negative effects. It is time to reform provincial tax codes, especially in Quebec, Ontario, and Nova Scotia. These three provinces suffer from the highest top marginal rates which apply to the highest income earners, and may discourage their ability to generate maximum returns for their investment and create jobs.

As Murphy, Clemens, and Veldhuis state in their 2013 study (P7), "the principles for income tax reform are straightforward: The objective should be to flatten rates and broaden the tax base (by reducing or eliminating tax credits, deductions and other special privileges)."

Tax reform would not only improve Canada's tax competitiveness, it would also stimulate economic activities such as saving, investment, entrepreneurship, and employment. By reducing the complexity of the tax system and the compliance costs, the government can reduce marginal tax rates for a wider range of people. If provincial governments followed effective reforms, Canada could be in a competitive position and attract capital, investment, and skilled workers from around the world.

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Feixue Ren is an intern in the Government Budgets and Fiscal Policy department at the Fraser Institute. She holds a MA of Economics from Lakehead University, and is a PhD candidate in Economics for the University of Ottawa.

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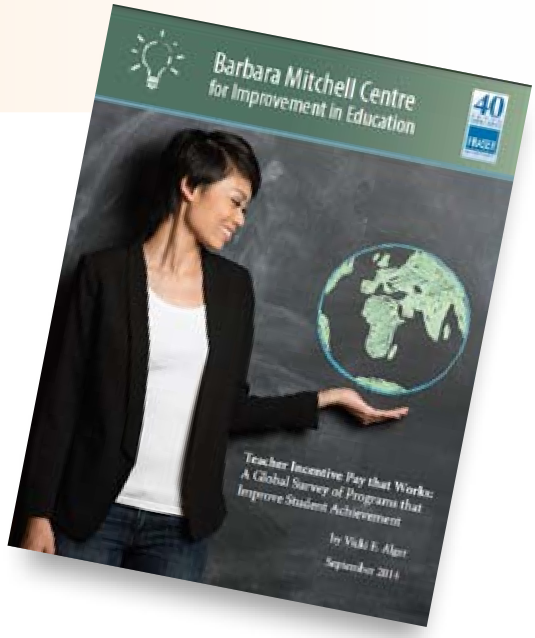
HOT TOPICS!

Burger King-Tim Horton's deal a reminder that business taxes matter

News that Burger King and Tim Horton's are merging and that the new company will be headquartered in Canada has taken the business and political world by storm. US politicians and left-of-centre groups denounced the transaction as "tax dodging" and warned of a public backlash against the well-known burger chain. Canadian politicians have refrained from saying much about the deal but spoke positively about the country's corporate tax regime. What are we to make of this late-summer kerfuffle?

Politicians are talking about taxes because taxes are at the heart of this deal (although other factors are also at play). It's called a "tax inversion" whereby an American company merges with a foreign one and in so doing, reincorporates abroad to take advantage of lower taxes. It's a powerful reminder that competitive business taxes matter.

Read the full commentary
HERE



Teacher Incentive Pay that Works

Teacher compensation in Canada is stuck in a time warp. It is determined by a rigid salary schedule based on tenure and advanced degrees—factors that have little if any positive impact on student achievement. Outside of the teaching profession, surveys suggest that close to three-fourths of Canadian employees already receive performance-based and variable pay. In fact, compensation based on results is the rule rather than the exception at more than eight out of 10 companies worldwide because this approach is one of the most effective strategies for attracting and retaining top talent.

Countries other than Canada realize that education practices of the past cannot meet the needs of a competitive 21st century world. Consequently, the number of countries implementing incentive pay for teachers is proliferating after decades of increasing education funding overall with no commensurate improvement in student achievement.

Read the study HERE

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