

CHAPTER 1

Introduction: Getting to a Four-Day Work Week Through Faster Productivity Growth

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A recent study from the Angus Reid Institute found that a majority of Canadian adults feel it's a good idea to make a 30-hour work week standard in Canada (Globerman, 2020). This finding is hardly surprising. Leisure time is valuable, and most people prefer more of it to less. A more interesting line of questioning might have asked respondents how much monetary compensation they would be willing to forego in order to negotiate a four-day work week with their employers, rather than their current five-day work week. In the absence of increases in labour productivity, businesses operating in competitive markets could not afford to reduce work hours by approximately 20 percent while continuing to offer employees the same levels of compensation.¹

Globerman and Emes (2020) report that the average annual number of hours worked per worker in Canada in 2018 was about 80 hours (or 4.5 percent) less than in 2000. Over that same period, average annual compensation (adjusted for inflation) increased by about 13 percent. This finding suggests that while Canadian workers certainly value more leisure, they also value a higher material standard of living. Therefore, it is a reasonable inference that Canadian workers would be unambiguously better off if they could work four days a week rather than five days a week while earning at least the same (or an even higher) level of compensation associated with a five-day work week.

Achieving the feat of making higher incomes while working fewer hours will require Canadian workers to be more productive, since the

¹ More will be said about the empirical relationship between changes in compensation and changes in labour productivity later in this essay.

amount that employers in competitive markets will be willing to pay workers will increase only if the value of output produced by per hour of work also increases. Simply put, if the average Canadian worker chooses to work fewer hours, the value of the output produced per hour worked must increase commensurately if average compensation per worker is to remain constant in inflation adjusted dollars.²

Globerman and Emes (2020) estimate that decreasing hours worked from a 40-hour, 5-days-per-week schedule to a 32-hour, 4-days-per-week schedule would have entailed a reduction of approximately 341 annual hours worked during 2018 for the average Canadian worker. Given this reduction, if inflation-adjusted compensation increases by 2 percent per annum from 2018-2030, the average Canadian worker could move to a 4-day workweek by 2030 and enjoy a real average annual income that would be about 1.5 percent higher than the real average annual income earned in 2018.³ This, in turn, implies that labour productivity would need to increase by about 2 percent per annum if this labour market outcome is to be achieved.

As suggested by the data reported in table 1, a 2 percent per annum increase in labour productivity would represent a substantial acceleration in Canada's productivity performance compared to its more recent performance. Indeed, it would represent almost a doubling of the rate of growth of labour productivity achieved over the period 2010-2016, but a more modest 33 percent increase compared to the 2010-2014 period. While a 2-percent per annum increase in labour productivity therefore appears to be a reach given recent productivity growth rates, it is relevant to point out that Canada's annual rate of growth of labour productivity over the long period from 1961-2012 averaged two percent (Baldwin, Gu, Macdonald and Yan, 2014). This is certainly not to say that achieving a durable increase in productivity growth will be easy. Rather, it is to say that it would be a serious public policy mistake to accept Canada's recent productivity growth performance as immutable and underestimate the

² While the precise relationship between increases in productivity and increases in compensation has become somewhat controversial, the available evidence for Canada identifies a strong linkage between labour productivity growth and real wage growth over time (see Gu, Macdonald, and Yan, 2014).

³ These calculations were made pre-Covid-19. Given the marked negative impact the pandemic has had on full-time employment and real wages in 2020, the increase in real average annual compensation required to offset the assumed reduction in average hours worked might be slightly different than the estimated 2 percent per annum. Nevertheless, the point remains that increases in real wages are required to offset any reduction in hours worked if total compensation is to remain unchanged.

Table 1: Labour Productivity Growth in Canada's Business Sector

1997-2010	2010-2014	2010-2016
1.3	1.53	1.05

Source: Gu and Wilcox, 2018.

benefits of moving back to a productivity growth path that Canadians, for many years, took to be quite achievable.

Restoring Canada's labour productivity growth performance back to its long-run trend will require a variety of public policy initiatives starting with government officials acknowledging the importance of improving labour productivity to the economic and social well-being of Canadians. While much has been written about initiatives to improve productivity growth rates, and while no simple formula has been identified, there is some agreement among economists on at least a few steps that should be taken to achieve the goal of faster productivity growth. Perhaps most important is to promote innovation and entrepreneurship along with the capital investment that is complementary to innovation and entrepreneurship (Gold, 2016).

As is true for productivity growth more generally, there is no simple formula to promote innovation and entrepreneurship. In particular, innovation reflects complicated social and economic interactions that economists are far from fully understanding.⁴ Nevertheless, there are some basic public policy initiatives that are broadly seen as helpful to encouraging innovation and entrepreneurship and, therefore, crucial to encouraging faster productivity growth. The various essays in this volume identify and discuss a number of important such initiatives.

While it can be fairly said that the Canadian government has tried to promote innovation and entrepreneurship from a "top-down" perspective, a strong argument can be made that government efforts to do so have had predictably unfavourable results.⁵ Rather, the process of improving productivity growth would be better served by removing government-imposed barriers to innovation and entrepreneurship. Such barriers take a

⁴ For a comprehensive discussion of the complexity of the innovation/entrepreneurial process, see Cross (2020).

⁵ Cross (2020) and Globerman and Emes (2019) argue this point forcefully.

variety of forms including the large and continually growing size of government which, in turn, increases competition with the private sector for critical inputs such as capital and skilled labour.

The government competes away financial and other inputs from the private sector directly through taxation, and indirectly by borrowing money, which increases the cost of capital for private businesses. Relatively high tax rates, especially on capital gains, reduce the willingness of businesses to invest in innovative ventures by diminishing the after-tax rewards to risk-taking. When accompanied by government rhetoric excoriating successful entrepreneurs for failing to pay their “fair share” of taxes, high marginal tax rates contribute to a culture where commercial success is punished, rather than rewarded. In such circumstances, would-be Canadian innovators and entrepreneurs have an incentive to leave Canada for other locations, particularly the United States, where commercial success begets both greater financial rewards and social approval.⁶

Government regulations and other restrictions on competition suppress the commercialization of new technology, either by direct fiat or by creating a business environment where poor productivity performance is not punished by the loss of business to more innovative rivals.⁷ While some regulations are justifiable using a social benefit-cost framework, there is also substantial red tape that obliges companies to use resources, including management time, that could be deployed more beneficially to raise Canadians standards of living if invested in commercializing new technology.

Certification requirements and related regulatory obstacles to labour market mobility are typically justified as protecting consumers from underqualified and even dangerous providers of services. In many cases, the obstacles are more accurately understood as barriers to entry that protect incumbent providers from more efficient competitors. Similarly, financial regulations that require extensive disclosure of information on the part of start-up companies seeking to raise capital impose entry costs that effectively protect incumbents from the threat of entry by new firms.

A wide range of industries in Canada enjoy legal protection from competition, both from internal and external sources. For example, provincial governments have restrictions that limit or block the importation of goods and services from other provinces, while the federal government

⁶ Cross (2020) highlights the importance of cultural attitudes towards commercial success as an influence on innovation and entrepreneurship and compares attitudes in Canada unfavourably to those in the US.

⁷ From their extensive review of the relevant literature, Bloom, Van Reenan, and Williams (2019) conclude that competition typically increases innovation, especially in markets that initially have low levels of competition.

imposes tariffs on a range of products and limits foreign direct investment across a range of industries from commercial banking to telecommunications and broadcasting. Tariff and non-tariff barriers harm productivity by weakening competitive discipline on incumbent domestic firms, as do legal barriers to inward foreign direct investment. Given the relatively small domestic market, interprovincial barriers to trade discourage specialization of production by limiting the size of the domestic market available to Canadian companies. The resulting sacrifices of economies of scale and efficiency gains associated with learning-buy-doing have been shown to be important reasons for Canada's productivity gap relative to US producers (Head and Ries, 1997).

The impact of the Covid-19 pandemic on future productivity growth rates in Canada or, indeed, in other countries, is uncertain but potentially profound. Certainly, a significant portion of existing physical capital assets in sectors such as commercial real estate, retailing, and transportation are arguably less productive in their current uses going forward, and possibly permanently so, as a consequence of the pandemic. Likewise, the demand for human capital in specific activities such as travel and retail management and consultancies will likely be lower in the future, while it will be higher for other types of human capital in activities drawing on, for example, artificial intelligence and supply chain logistics.

It is inadvisable for government bureaucrats to direct the allocation of capital and labour in response to the changes that have been set in motion or, perhaps, accelerated by the Covid-19 crisis. Top-down economic planning is a particularly bad idea in periods of rapid economic change. The discrete changes that seem to be occurring strengthen the basic argument of Cross (2020) and others that government-imposed restrictions on private markets to allocate productive resources should be reduced to permit the emergence and growth of businesses that are better suited to prosper commercially in the "new environment," while allowing businesses that are poorly suited to leave the marketplace and allow their inputs to be used more efficiently in other activities and businesses.

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