The Canadian Distinctiveness into the XXIst Century - La distinction canadienne au tournant du XXIe siècle

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Canadian Business:
‘No, I’m from Canada’

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THOUGH IT WAS TEMPTING—AND PROBABLY WOULD HAVE BEEN MORE
teresting—to do a parody of the recent very popular beer com-
mercial, this essay will address Canadian distinctiveness in business.
Having said that, however, there are a few business images to reflect
upon:

• It is possible to establish a world class business based upon
the snowmobile.
• Canadians were destined to lead in telecommunications
because it was cold outside. Better to stay inside and talk on
the phone.
• We had to do something with all the rocks, trees, and
beavers.

Instead, because at a tender stage in my professional life I was coun-
seled only to speak about those subjects of which I at least had a
passing knowledge, I am going to talk about the exciting subject of the
financial services industry and consider whether there is a distinct
Canadian view of it. There are a few caveats I would like to make
before beginning.

First, in regard to the use of terms such as ‘Canadian’ and
‘American,’ I am aware that, leaving aside matters of race and gender,
there are differences between individuals from Québec, the East Coast,
Alberta, and the West Coast and that the term ‘Canadian’ means more
than simply the Torontonian view. I would also like to emphasize,

* The views expressed are those of the author and should not be attributed, directly
or indirectly, to his employer, Royal Bank of Canada, or any other organization.
though it may seem otherwise at times, that there are differences between people of Atlanta, New York, and Los Angeles. The use of ‘American’ is for ease of reference only.

I have had the good fortune to work for the last decade for two extremely large financial institutions. One is based in the United States, with Canadian operations that were sold a few years ago. The other one is based in Canada with U.S. operations and aspirations of expanding them. In the first case, I seemed to spend significant time explaining that things were different in Canada. Recently, I seem to have made the same effort to consider whether there are differences between Americans and Canadians.

This paper has its genesis in two short stories that I should like to relate. The first one has to do with the negotiation of a potential joint venture with a South American businessman. He strongly preferred working with us because, as he put it, “Canadians actually listen.” The second story concerns a friend who had been sent to Europe to run a somewhat mediocre operation. This friend had been successful in improving the business over a two-year period, or as he put it, “two years less a day,” and was looking forward to his return to Canada, notwithstanding the vastly different business culture that he had learned to function within. When he explained to his successor that the culture was different and would require adjustments, his successor, who happened to be from the U.S., explained that my friend would not have to worry because he would— as he put it— “whip these people into shape.”

What I have learned, though it is impossible to define, is that a distinct Canadian approach to business can be attributed, I will argue, to the role of government regulation in business and the need to preserve distinctiveness in the face of globalization. The subject of financial services reform over the last five years provides an unusual opportunity to compare American and Canadian approaches to similar issues. The United States government passed in late 1999 the Gramm-Leach-Bliley Act on financial privacy and pretexting, also referred to as the Financial Services Modernization Act. This legislation repealed the Glass-Steagall Act, which had been in place since the 1930s and had significantly restricted and compartmentalized financial services in the United States. The new legislation removed almost all barriers contained in the old legislation. In Canada, after adopting a new regulatory framework in 1992, reviewing two proposed bank mergers, and holding several inquiries into the state of the Canadian financial services industry, the Canadian federal gov-
ernment released, in 1999, the White Paper entitled *Reforming Canada’s Financial Services Sector – A Framework for the Future*, to serve as the basis for new legislation that is expected in the near future.

The two documents are noteworthy because they deal with several identical matters. For example, they both deal with ownership restrictions, regulatory approvals, and business powers. In the area of ownership restrictions, the Canadian White Paper would limit the ownership to 20 per cent of the voting equity. This would effectively preclude large institutions from either acquiring or merging with each other. The U.S. legislation contains no equivalent restrictions. Indeed, the U.S. legislation encourages ownership of virtually any ‘financial’ business, regardless of size, provided no anti-trust matters arise. In Canada, the approval process for mergers or investments or acquisitions of financial institutions are subject to the prior approval of the Minister of Finance and a long process of regulatory scrutiny involving public consultations, the Competition Bureau, and Office of the Superintendent of Financial Institutions [OSFI]. The regulatory process obliges the Minister to consider the public interest and, if appropriate, impose conditions on the proposed transaction. The U.S. legislation, on the other hand, effectively contains a deemed approval requirement. The Canadian proposals will preserve the long standing restrictions against banks selling insurance in bank branches or participating in the auto-leasing business. There are no similar restrictions under the *Gramm-Leach-Bliley Act*. There are of course many other components in the two regulatory schemes, but I suggest that the subjects I have noted are sufficient to make the point that the regimes are different.

The shape of the financial services industry that could emerge in the two countries has been, and will continue to be, a source of keen debate. The Canadian proposals are likely to perpetuate the status quo – that relatively large banks that compete in a relatively small, fragmented market will find it increasingly difficult to compete against much larger competitors. The market capitalization of Royal Bank is about two times larger than the largest non-bank financial institutions. On the other hand, the largest U.S. bank is eight times larger, by market capitalization, than Royal Bank. Under the U.S. legislation, further consolidation among financial institutions is likely, with the result that already large institutions will become larger and more efficient. If one is concerned about the competitiveness of Canadian institutions compared to international ones, these trends could be disturbing.
But the point here is not to speculate about the future of the financial services industry. Instead, the issues worth pursuing are both to recognize that the Canadian and American regulatory regimes are dramatically different and then to consider what these differences suggest about Canadian attitudes towards business.

According to the Canadian proposals, changes to the financial services sector were needed to:

- Enhance competition thus making the sector more vibrant;
- Empower consumers in order to provide an important discipline to competition and make the sector more responsible to their needs;
- Strengthen the relationship between financial institutions and the communities they serve in order to make the sector healthier;
- Increase flexibility so that the regulatory framework would more effectively balance the need for safety and soundness with the need to facilitate competition and innovation.

All these changes were driven by, among other things, technological and demographic changes.

When the Gramm-Leach-Bliley Act became law, a number of comments were made by various commentators and politicians:

- "This day we can celebrate as an American day."
- "Eliminating barriers to financial services competition will allow American companies to better compete in the global economy."
- "The Act will help the American financial services system play a leading role in propelling our economy into the 21st, continuing the longest peacetime economic expansion in our history."
- "When Glass-Steagall became law, it was believed that stability and growth came from government overriding the function of free markets."
- "We are here to repeal Glass-Steagall because we have learned government is not the answer. We have learned that freedom and competition are."
- "The world changes and Congress and the laws have to change with it."
- "Voters believe that reform is vital to America’s ability to maintain its position as a financial superpower in the global markets."
The differences between the two approaches are apparent. For example:

a) In the area of competition:
   Canada – competition must be balanced against other needs of the community
   US – competition will benefit all stakeholders

b) In connection with consumers:
   Canada – consumers must be ‘empowered’ to foster competition.
   US – consumers will benefit from competition

c) The view of the market:
   Canada – community based
   US – global

The purpose for describing these differences is to show that the Canadian regulatory environment, at least in connection with financial services, has led Canadians to develop a particular skill set in business. As an aside, I concede that there may well be a ‘chicken and egg’ dimension with respect to the causal relationship.

In my experience, at least in financial services, to function in the Canadian market, several skills and strategies are required:

• a consultative approach to negotiations driven by the need to function in a regulatory environment characterized by discretion as opposed to explicit rules;
• a focus on business problem-solving;
• a broad approach to issues that reflects the need to address broader community concerns; and
• a view that business arrangements are an exercise in building something.

These skills emerge from the necessity of having to work in a small, relatively closed market that is heavily influenced by government intervention and economic trends emerging from outside the country. The extent of interdependence that arises from these relationships obliges business people to look at issues in a broad sense. It also limits the scope of initiatives for any individual organization in terms of solving a business problem.

Within Canada, at least in terms of financial services, these skills have led to the creation of a strong and vibrant financial services
industry. And that is a critical element in the Canadian economy. The pressing question, then, is whether these skills will allow Canadians to continue to prosper in the context of globalization. For my purposes here, I can offer these thoughts. If globalization — if it is capable of definition — implies a free, open market, then this will be different from the Canadian experience. On the other hand, if globalization leads to a market of interdependent competitors, then the skill set that I described before will probably be useful. The larger issue is whether the Canadian economy can generate sufficient wealth, in a timely way, to retain talented business people.