



At a Crossroads: Canadian Defence Policy and the Canadian Defence Industrial Base

The Canadian Defence Industry and the Defence Market Place

The Canadian defence industry is an innovative and export oriented sector of the Canadian economy. It consists of well over 600 small, medium and large enterprises spread throughout Canada and punctuated by strong regional clusters and niche capabilities. These firms create high wage jobs and many also have a commercial market focus.

A recent study by Innovation, Science and Economic Development Canada and Statistics Canada found that, in 2014, the Canadian defence industry accounted for:

- 63,000 jobs;
- Approx. \$10 billion in annual sales, 60% of which came from exports, which is 20% higher than the Canadian manufacturing average;
- Employee compensation nearly 60% above the Canadian manufacturing average; and
- Nearly a third of employees working as engineers, scientists, researchers, technicians and technologists.

These findings are particularly important when you consider the market context in which defence companies operate. The global market place for defence goods and services is managed and highly regulated—in no way does it approach a “free market”. Almost all governments manage their defence sector for both national security and domestic economic reasons. This is the main reason defence is exempt or carved out from international trade agreements.

Canada, by contrast, is an outlier in this regard—governments in this country have not managed the Canadian defence market nor collaborated with domestic industry anywhere near to the extent of our allies. This presents an opportunity to improve Canada’s defence posture.

Defence Industrial Policies: Three Case Studies

The UK’s *Defence Growth Partnership*, its defence industrial policy, was unveiled in 2012. It is a formal partnership between the British defence industry and the government to “deliver a truly competitive, sustainable and globally successful UK defence sector...that will secure a thriving UK defence sector delivering security, growth and prosperity for our nation.”

This year the Australian Department of Defence issued its *Defence Industry Policy Statement, 2016*. This document is founded on the idea that “close collaboration between Defence and industry is critical to meet the challenges of the future and deliver the Government’s ambitious program of works” and that “the Defence and industry partnership of the future will be instrumental in delivering and supporting the future Australian Defence Force.”

The U.S. does not have a formal defence industrial policy set out in a single document. Instead, the Americans have a very elaborate, multifaceted and sophisticated defence industrial policy that involves everything from massive private sector R&D support to management of the structure and competitive intensity of the American industry. A high percentage of their acquisitions are classified as “U.S. Eyes Only”. The Americans also invoke “Buy American” legislation and provisions. As a result, most major platforms are purchased from domestic suppliers.

RECOMMENDATION OF CANADA’S DEFENCE INDUSTRIES: The Canadian defence industry urges the Minister’s Advisory Panel on the Defence Review to recommend that the defence white paper commits to developing, in collaboration with industry, a made in Canada defence industrial policy designed to address Canada’s unique security challenges and economic opportunities. This would serve to strengthen Canada’s defence posture, as well as link two of the government’s key priorities, the Defence Review and the Innovation Agenda, ultimately bolstering Canadian prosperity.

The Link between Defence Policy and the Defence Industrial Base

There is a critical link between the defence of Canada, Canada's international defence posture and the Canadian defence industrial base. This linkage needs to be understood and considered in the Defence Review. The efficacy of any defence policy is highly dependent on the ability to procure defence equipment and services.

Having security of domestic supply in key defence technologies and services is understood by our allies as important to their independence of action and national security. This should be a serious consideration in defence policy thinking in this country. Canadians often assume that if we buy from our allies we can always count on them to deliver what we need, when we need it and at the price we expect. That assumption could be costly if tested in a crisis when we need what our allies need at the same time.

This concept of independence of action also applies to how Department of National Defence (DND) sustains its military equipment. Over the past decade there were a series of procurements in which foreign Original Equipment Manufacturers were contracted to provide both the equipment and maintenance of the fleets over their lifecycle, largely outside of Canada. This arrangement weakens the government's leverage if there is a need to move Canadian Armed Forces (CAF) equipment to the front of the line when repairs, life extensions or capability enhancements are required. By contrast, when the CF-18 fighter aircraft was purchased 35 years ago, the government of the day required specific intellectual property and technical data packages be transferred to Canada. This decision contributed to a robust military aircraft In Service Support (ISS) and Maintenance, Repair and Overhaul (MRO) capability that now accounts for 20 per cent of the entire defence sector as a percentage of sales. This wise government decision three decades ago has permitted synergies with Canada's commercial ISS and MRO market and has opened export markets for Canadian firms.

Capability development is critical not only for the CAF, but also for the industry that supports the CAF in delivery of that capability. This concept was the foundation behind the National Shipbuilding Strategy. Canada needs to nurture its defence industrial base, as our allies do, or it will atrophy, with adverse implications for Canada's independence of action and CAF operational effectiveness.

The Re-Capitalization Opportunity

The CAF is in the midst of its first major re-capitalization in over a generation. This began more than ten years ago when the DND received its largest funding increase in three decades.

It is only in recent years, however, that that funding infusion is having an impact on DND's equipment re-capitalization. Much more is to come in the future. Two projects alone, the Canadian Surface Combatant and the Next Generation Fighter—which taken together are valued at \$35 billion or more for the equipment purchase alone—will basically shape the defence industrial base in this country for the next thirty years. This needs to be clearly understood by the government. How the government handles these procurements will re-shape the defence industrial base in Canada for the foreseeable future. This shaping should not occur by unintended consequences. The re-capitalization of the CAF represents a once in a generation opportunity if Canada adjusts its thinking about defence procurement and its relationship to Canadian sovereignty and economic interests.

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Key Documents:

1. Report of the Special Adviser to the Minister of Public Works and Government Services, *Canada First: Leveraging Defence Procurement Through Key Industrial Capabilities*. February 2013 (<http://www.tpsgc-pwgsc.gc.ca/app-acq/documents/eam-lmp-eng.pdf>)
2. Government of Australia, Department of Defence, *Defence Industrial Policy Statement 2016* (<http://www.defence.gov.au/whitepaper/Docs/2016-Defence-Industry-Policy-Statement.pdf>)
3. HM Government, Department of Business, Innovation and Skills and Department of Defence, *Defence Growth Partnership, 2014* (<http://www.defencegrowthpartnership.co.uk/>)
4. Christyn Cianfarani, Globe and Mail Report on Business, *Military procurement can help break Canada's innovation logjam*, April 21, 2016. <http://fw.to/MGen6uM>