SOCIAL POLICY AND THE KNOWLEDGE ECONOMY: NEW CENTURY, NEW PARADIGM

Thomas J. Courchene

The emerging societal order, characterized by the knowledge-based economy (KBE), is calling for a new and challenging social policy paradigm. Long-standing social priorities such as early childhood development, education and health have now become the drivers of information-era growth and competitiveness, especially in terms of research and innovation. Likewise, the factors propelling global city regions (GCRs) to the economic forefront in the KBE "are likely to be universities, health research centers and R&D labs on the one hand, and socio-cultural policies that accommodate the creative class on the other," writes IRPP Senior Scholar Tom Courchene. Under the former resource-based model people migrated to where the jobs were, whereas in the KBE era businesses and jobs will cluster where the talent is. This is part and parcel of the 21st century social policy paradigm, the most exciting dimension of which is that investing in the development of citizens is the key to ensuring both social cohesion and economic competitiveness.

Caractérisé par l'économie du savoir, l'ordre sociétal émergent nécessite en matière de politique sociale un paradigme inédit et stimulant. En cette ère de l'information, des priorités de longue date comme le développement de la petite enfance, l'éducation et la santé sont devenues des moteurs de croissance et de compétitivité, surtout en recherche et en innovation. Quant aux vecteurs qui propulseront les cités-régions internationales à l'avant-plan de cette économie du savoir, ce seront vraisemblablement les universités, les centres de recherche en santé et les laboratoires de recherche et développement, prédit le chercheur principal de l'IRPP Tom Courchene, mais également les politiques socioculturelles destinées à la « classe créative ». Si l'ancien modèle économique fondé sur les ressources imposait aux gens de se déplacer pour trouver du travail, les entreprises et les emplois de l'économie du savoir se regrouperont là où se concentrent les talents. Ce phénomène sera partie intégrante du paradigme des politiques sociales du XXIe siècle, dont l'aspect le plus stimulant résidera dans l'investissement consenti au développement des citoyens, facteur clé de cohésion sociale tout autant que de compétitivité économique.

It is surely paradoxical that the advent of the so-called new economic order has led to the catapulting of the social envelope to policy centre stage. To be sure, part of the reason is that, with knowledge and human capital increasingly at the cutting edge of competitiveness, social policy is progressively becoming indistinguishable from old-style economic policy in terms of fostering growth and innovation. Nonetheless, much of what has come to be viewed as received wisdom in terms of the relative roles of social and economic policy needs to be revisited and rethought in light of the transformative nature of what will henceforth be referred to as the knowledge-based economy or era (KBE). Accordingly, the purpose of this essay is to articulate the essence of the KBE social policy paradigm for 21st century Canada.

Toward this end, attention will be directed initially to the core framework and implications that arise from the truly exciting development that underpins this new social policy paradigm, namely the emergence of information- and knowledge-empowered citizens as creative agents of, and for, societal progress on the economic, social and democratic fronts. Indeed, the knowledge/information

revolution will privilege human capital in much the same way as the Industrial Revolution privileged physical capital. Hence, the analytical core of KBE social policy centres around the roles of education, skills and knowledge for enhancing competitiveness, for raising living standards, and for ameliorating income distribution concerns. Beyond this core, however, there are a series of corollaries that will serve to map out the larger contours of the paradigm, including imperatives relating to institutional infrastructure, to the maintenance of our east-west societal glue in the face of the north-south shift in our trading axes, and to the rise of cites as arguably the pre-eminent jurisdictions of the new order. To an important degree, what characterizes the KBE is that traditional economic policy is now increasingly international, whereas social policy not only remains primarily domestic but, as well, is increasingly the stuff of nation-building.

The remainder of the essay then briefly applies this framework/paradigm to a wide range of policy areas and programs, particularly in those realms where it serves to rewrite earlier social and economic policy orthodoxy, including education, income distribution, taxation, medicare, EI, federalism, infrastructure, and even a common currency. What is rather remarkable is that in virtually all cases a KBE-consistent social policy perspective is arguably also first-best economic policy. The exciting news here is not just that good social policy is good economic policy: it is also that *both* social and economic policy in the KBE will benefit from adopting a human capital or "citizens first" perspective to the challenges of the twenty-first century.

A second and related corollary has been best expressed by Dani Rodrik in his influential monograph *Has Globalization Gone Too Far?* namely, how do we ensure that increasing international economic integration does not lead to increasing domestic social disintegration? The presumed solution is to embed this globalization within a domestic and international framework that at the same time advances social cohesion and lends democratic legitimacy to globalization, much like the so-called "compromise of embedded liberalism" in the post-war period essentially enmeshed the earlier round of international openness within the context of the blossoming of the domestic welfare state.

Under the assumption that preserving and promoting economic competitiveness and social cohesion are the appropriate guideposts for assessing Canada's policy success in the KBE, a dedicated approach to investing in citizens' education and skills will bridge the gap between the economic and social spheres. Specifically, with knowledge progressively at the cutting edge of wealth creation and competitiveness, with enhancing skills and education as the key not only to achieving high living standards but also to addressing income inequality and social solidarity, and with information empowerment as the *sine qua non* of meaningful citizenship, it follows that a commitment to a human capital future for Canadians is emerging as the principal avenue by which to promote *both* cohesion and competitiveness. This is the analytical core underpinning the new social policy paradigm and, indeed, of public policy generally in the knowledge/information era.

While this perspective is the centrepiece of the new social policy paradigm, one can articulate a series of corollaries or challenges that will serve to elucidate other facets of the paradigm. The first of these is that in several key areas traditional economic policy *is* becoming less important and certainly less challenging relative to social policy. One reason for this is that an increasing number of these policy areas are being passed upward to the supranational level — trade policy for NAFTA and the European Union, monetary policy and currency choice for the Euroland, etc. Another is that for other important areas either there are often international standards that are progressively driving domestic policy (e.g., the Bank for International Settlement's *capital-adequacy* rules for global banks, inflation targeting for central banks) or there are pressures for harmonization arising from the shift from the shallow integration of the GATT regime to what Sylvia Ostry calls the "deep structural integration" or sovereignty-intrusive requisites of the WTO regime.

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of the domestic welfare state. To a large degree, this too is a challenge that must be addressed by KBE social policy, writ large, including the role of civil society both domestically and internationally.

Arguably the most pressing implication for Canada flowing from the Rodrik challenge is that related to preserving and promoting our east-west human-capital and social-policy "railway" now that virtually all provinces are linked, trade-wise, more to the US than to their sister provinces. Call this the third corollary.

A fourth directs attention to the pivotal role of infrastructure and institution-building. It is not an overstatement to assert that in the KBE the institutional and infrastructure challenge relates primarily to social policy, not to economic policy. Compare banking and education. I know with certainty that a decade from now I will still have access to state-of-the-art banking services. One would hope that our policy authorities would ensure that, wherever possible, these services would be provided by Canadian-based financial institutions. But, if not, the Internet will guarantee me the requisite access. However, I have no such guarantee when it comes to education and, more generally, to Canada's social policy infrastructure. These services are, in general, not tradeable so that we cannot easily access other nations' social infrastructure. Moreover, unlike the case for provision of services like banking, there are no direct pressures to emulate best-practices elsewhere in the world, and in any event since social infrastructure is typically embedded in national norms and values it would not transport easily across national boundaries. Hence, in terms of health, welfare, education, training, EI, etc., we must rely on our own inate ingenuity in designing these institutions. While Canadians have on many occasions demonstrated their ability to be institutionally creative in the face of domestic or international challenges, we nonetheless need to recognize that federalism can also be a valuable ally in this undertaking. Specifically, the dynamic social/institutional learning arising from provincial experimentation with the design and delivery of these public goods, services and infrastructures can serve (and in the case of medicare obviously have served) as critical catalysts in the evolution of state-of-the-art social institutions and infrastructure. There is a larger point to be made in this context, namely that our social institutions and infrastructure will effectively define who we are and who we desire to be as Canadians, individually and collectively, in the knowledge era, which of course further underscores the importance of the KBE social policy paradigm.

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A final but hardly exhaustive corollary is illustrative of the sweep of the KBE social policy paradigm. Specifically, cities and especially the so-called global city regions (GCRs) will tend to come under the social policy umbrella because they are the dynamic centres of dense concentrations of knowledge, human capital, health/bio-technological/industrial R&D, etc. that drive economic activity, innovation and exports. Richard Florida in his book *The Rise of the Creative Class* builds on this to articulate a "creative capital theory of growth." He notes that access to talented and creative people is to modern business what access to coal and iron ore were to steelmaking. Cities that score well in terms of Florida's 3Ts — technology, talent, and tolerance (where the latter is measured by the amenities and opportunities available for every lifestyle) — will become places where the creative class will cluster. More to the point, companies will then be drawn to these same cities to access the concentrations of the creative class. This vision of the dynamics of KBE innovation and growth differs markedly from the last paradigm's vision in (at least) two important ways. First, it reverses the causation: businesses and jobs will cluster where the creative class clusters, rather than people moving to where the jobs are. Second, while not downplaying the influence of economic variables such as taxation in terms of attracting talented people, the larger attracters are likely to be universities, health research centres and R&D labs on the one hand and socio-cultural policies that accommodate the creative class on the other. This *is* a paradigm shift.

By way of a one-sentence summary of the essence of the KBE social policy paradigm, I offer the following "mission statement" (drawn from *A State of Minds: Toward a Human Capital Future for Canadians*):

> *Design a sustainable, socially inclusive and internationally competitive infrastructure that ensures equal opportunity for all Canadians to develop, to enhance and to employ in Canada their*

skills and human capital, thereby enabling them to become full citizens in the information-era Canadian and global societies.

Others may prefer the wisdom of Lester Thurow, who said in an article that appeared in *The Toronto Star* in January 1993:

If capital is borrowable, raw materials are buyable, and technology is copyable, what are you left with if you want to run a high-wage economy? Only skills, there isn't anything else.

Either way, investing in Canadians is investing in Canada's future. In other words, the KBE social policy paradigm is first and foremost an investment paradigm.

At the heart of the social policy paradigm must be the dual recognition that increasing Canadians' education and skills holds the secret for boosting competitiveness and living standards, on the one hand, and that ensuring equality of opportunity for all Canadians to access education/skills enhancement is essential to ameliorate the income polarization that is arising because of the increased returns to human capital investment, on the other. This is a tall order indeed because the requisite policy package will be comprehensive, complex, interactive and multi-jurisdictional, let alone frequently charting unknown policy waters. In contrast, and of necessity, the ensuing discussion can only be partial and selective.

The Gazette, Montreal

Infants and toddlers at a Montreal day care: In the 21st century, social policy will be shaped by the needs of knowledge-based economies, none more pressing than the health, nutrition, care and education of children.

The most challenging part of this package and the one that most reflects traditional social policy relates to the income distribution implications of the KBE. If Canada is intent on embracing a human-capital future for *all* Canadians, then this has to begin with our children. In *A State of Minds* I proposed a charter of human capital rights for Canada's children. Along similar lines, Tom Kent, in his *Social Policy 2000: An Agenda* (published in 1999 by the Caledon Institute), calls for issuing every newborn a "certificate of opportunity." Among its features, Kent would include the following provisions:

The certificate would state the rights of the child and, briefly, the subsequent rights and responsibilities of citizenship. It would offer the ...commitment of the government of Canada, in cooperation with provincial governments...to do all in its power to protect the individual's security, to foster health, to secure good living standards, to make possible for each individual a full opportunity to develop and use his or her capacities. In this...respect, the certificate might be seen as a kind of passport for early access to the services of a child centre.

Kent recognizes that such a certificate might find its greatest benefit in relation to First Nations children precisely because it is not designed specifically for them: "[These certificates] offer a non-discriminatory way to lessen the child poverty from which they greatly suffer, to reinforce their cultures and to empower...their own

communities." As a final comment on these certificates of opportunity or human-capital charters, their importance transcends the particular level of the budget associated with them. They will become powerful societal symbols in their own right, reminders to one and all that access to a human capital future must be open to all, i.e., it must become a "mind of state" as it were in pursuit of Canada becoming a state of minds.

This child charter would be an integral component and driver of a societal commitment to early childhood development as the necessary precursor to the ability to access education/skills opportunities. In this regard, the frequent squabbles over whether day-care/child-care tax credits or vouchers should depend on the structure of the family or of the employment status of family members miss the essential point, namely that any such (*presumably* income-tested) vouchers are the entitlement of the child irrespective of the characteristics of the child's family.

While Canada has not embraced this children's rights or opportunities approach, we have nonetheless been creative in policies related to other aspects of early child development. For example, the Canada Child Tax Benefit is a policy masterstroke: it makes a huge dent into child poverty; it encourages labour force attachment because it converts the children's component of welfare into a negative income tax; it respects the provinces since they are free to re-allocate equivalent welfare monies into priorities relating to children in working poor families; and it streamlines policy roles since Ottawa now looks after the kids and the elderly, leaving the provinces to design integrated programs for dealing with the adults, e.g., transitions from school, training and welfare to work.

At the post-secondary education (PSE) level, Canada is at or near the top of national rankings in terms of the percentage of citizens enrolled in universities or colleges. Intriguingly, because Canada lags the US in terms of university attendance, the 2004 federal budget undertook several further initiatives to increase university attendance, especially for Canadians from disadvantaged backgrounds. These include the Canada Learning Bond as well as a subsidy for first-year university for students from low-income families. While both of these measures are welcome in terms of increasing the equality of opportunity for PSE access, for all-too-many Canadians the real PSE barriers can only be addressed by early childhood initiatives as elaborated earlier.

A final but hardly exhaustive corollary is illustrative of the sweep of the KBE social policy paradigm. Specifically, cities and especially the so-called global city regions (GCRs) will tend to come under the social policy umbrella because they are the dynamic centres of dense concentrations of knowledge, human capital, health/bio-technological/industrial R&D, etc. that drive economic activity, innovation and exports. Richard Florida in his book *The Rise of the Creative Class* builds on this to articulate a "creative capital theory of growth."

What would further advance both equity and efficiency at the PSE level would be for the provinces to ensure transparent and formal transition procedures between colleges and universities. By way of example, the University of California system reserves dedicated places in upper years to transfer students from state and community colleges, the reward for which is that on many occasions the top graduating student did not begin studies in the Cal system. Canada needs this integration because the two systems still operate as cultural solitudes for too many students. Within the university system a case can be made on both access and excellence grounds for greater diversity — world-class research-oriented universities at one extreme and dedicated teaching universities (perhaps some two-year transfer institutions as well) with much lower tuition at the other.

The remainder of the analysis addresses a variety of policy areas as they relate to the KBE social policy paradigm, beginning with medicare and EI, the two areas that pose the greatest challenges to the paradigm.

Medicare: Health care is emerging as one of the leading-edge sectors in the KBE for innovation, research and exports as well as employing high-level human capital. To achieve this potential as a dynamic engine of growth medicare will need an infusion of physical, financial and human capital on a scale that will not be possible if we continue to view medicare primarily as a social policy endeavour. In "Medicare as a Moral Enterprise," an 2004 IRPP *Policy Matters*, I argued that the health sector will progressively be characterized by specialized diagnostic and treatment centres that will be cost-effective, flexible, innovative as well as state of the art in terms of quality. Following the Kirby Report, our publicly funded health-care system should be truly agnostic as to whether these specialized centres will privately, publicly or third-sector operated.

While this is medicare's key role in the KBE social policy, current reality is quite different. For reasons alluded to in "Hourglass Federalism" (in the April 2004 issue of *Policy Options)* medicare is crowding out virtually all other provincial

spending, including investment in the areas of KBE social policy. This is unsustainable: either Ottawa comes on board as a full financial partner (say, 25 percent of funding, as recommended by Tom Kent) or the provinces will have to privatize the funding via taxes, premiums, user fees or de-listing diagnostic and treatment services. This must occur because, public opinion notwithstanding, education/human capital clearly trumps medicare as a spending and societal priority in the KBE. In turn this is so because medicare (as distinct from public health and wellness) is primarily about *consumption* whereas the KBE paradigm is primarily about *investment* and, therefore, underpins our ability to continue to provide world-class health care in the future. Intriguingly, the Ontario budget's de-listing of several services (eye examinations, physiotherapy, chiropractic) and its imposition of dedicated premiums integrated with the income tax system, on the one hand, and the proposed summer federal-provincial meeting to develop the parameters for Ottawa's financial role in the health sector, on the other, probably signal the beginning of the meaningful evolution of 21st century medicare.

Employment Insurance: EI (formerly UI) in its current form is clearly offside vis-à-vis the KBE. Nearly 20 years ago, in 1986, the Newfoundland *Royal Commission on Employment and Unemployment* listed a dozen or so reasons why UI had outlived its usefulness, such as "the system undermines the intrinsic value of work," "the system undermines the importance of education," and several concerns relating to how one and all could manipulate the system (including job rotation and the prevalence of the then 10-42 work/UI syndrome). The Royal Commission recommended scrapping UI and replacing it with an income-tested guaranteed annual income. At the very least, the existing EI regulations need to be converted to insurance principles to ensure that long-term benefit periods do not flow from short-term labour force attachment. It is disheartening to note that as this is being written Ottawa has undone the earlier reforms that tightened up the 10-42 system. It is even more disheartening to realize that the result will be that individuals will be passed back and forth between federal UI and provincial welfare and/or make-work programs rather than being offered opportunities to invest in their skills.

Economic policy: In general, what passed as good economic policy under the previous paradigm is also good economic policy in the KBE. And Canada's performance of late has been stellar: the FTA/NAFTA has arguably been very successful; the export-import neutral GST has allowed us to continue to run a larger government than the US and still remain competitive; *Business Week* has referred to our fiscal achievements (seven consecutive surpluses and now the lowest debt-to-GDP ratio of the G-8) as the "Maple Leaf Miracle"; and Canada's inflation-targeting strategy has delivered consistently lower inflation rates than in the US and has earned international accolades (although my view remains that the shift toward a human capital future in an increasingly integrated North America will eventually call for a common currency with the Americans). Yet some challenges remain: for example, even though we have made considerable headway in reducing income taxes, the reality is that our tax rates on high-level and mobile human capital need to be reduced in order to level the international playing field.

At the heart of the social policy paradigm must be the dual recognition that increasing Canadians' education and skills holds the secret for boosting competitiveness and living standards, on the one hand, and that ensuring equality of opportunity for all Canadians to access education/skills enhancement is essential to ameliorate the income polarization that is arising because of the increased returns to human capital investment, on the other.

Under the old paradigm, social policy tended to play second fiddle to economic policy. Essentially, the view was that Canada should have as generous a social policy envelope as was possible, where "possible" meant that the magnitude and incentives of the social policy should not undermine Canada's competitiveness. Under the KBE, this is still a concern, but what is new is that this is now a two-way street. Apart from the fact that much of KBE social policy is itself competitiveness-enhancing, the proverbial shoe is now on the other foot: among the range of options acceptable for any given economic policy decision, choose that option that most advances citizens' abilities to develop and enhance their skills and human capital. This too is a paradigm shift.

Federalism: Given that much of the constitutional responsibility for implementing the KBE rests with the provinces, the federal-provincial fiscal balance must be such that the provinces have access to sufficient revenues. Relatedly, equalization remains the key program for ensuring that all Canadians can have access to reasonably comparable public goods and services. Beyond this, and beyond the earlier-mentioned need to encourage provincial experimentation, there is a need to accommodate some of the policy spillovers arising from the combination of NAFTA integration and the KBE. The AIT and SUFA are creative intergovernmental instrumentalities for preserving and promoting our

east-west economic and social unions respectively. And in tandem they are ensuring the mutual recognition of accreditation and qualifications across provinces thereby securing our east-west human capital union. Moreover, the new Council of the Federation must, among other roles, work to internalize the many horizontal policy spillovers/externalities that arise across provincial programs. Given that much of the responsibility for KBE social policy rests with the provinces, they need to embrace these and other "pan-Canadian" principles/approaches if they wish to forestall citizens from demanding a larger federal role in the paradigm.

Cities: This is a convenient juncture to return to the role of cities and particularly global city regions (GCRs) in the KBE. With their dense concentrations of human capital and R&D as well as their role as national nodes in international knowledge networks, our GCRs are pivotal to our collective socio-economic future. Indeed, how we fare in North America and beyond will in no small measure depend on how our GCRs perform relative to US GCRs. And herein lies a delicate challenge. Under the behind-tariff-walls paradigm, GCRs were convenient and obvious places to redistribute from. In the KBE, these GCRs will need to retain more of the tax revenue raised within their boundaries if they are to succeed in head-to-head competition with their international competitors. Moreover, their political star is also rising: GCRs and perhaps cities generally will become more fully and more formally integrated into our system of intergovernmental relations. The nature of the KBE makes it so.

Internationalization of the KBE: Canada is hardly unique in wrestling with the dictates of the KBE. Already, aspects of the social envelope are being internationalized: the labour-force "rider" in NAFTA and the concern over "social dumping" in the EU may well be harbingers for an international system that will progressively bring key components of social policy under the rubric of trade policy and perhaps the WTO, all of which will serve to complicate the design and delivery of domestic social policy. At the highest level of aggregation, the KBE is ushering in remarkable shifts in the traditional north-south global power structure since human capital is distributed much more equally across countries than is physical or financial capital. Finally, the dark side of all of this is that criminals and terrorists alike also have been empowered by the information revolution, with devastating results. One implication of this for the KBE social policy paradigm is that the pre-9/11 peace dividend has effectively vanished, so that social policy now faces increased competition for access to the public purse.

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Readers will recognize that several key aspects of the KBE social policy paradigm are absent from the foregoing analysis: the many roles that immigration can and has played in our socio-economic, cultural and demographic evolution; the challenges inherent in extending full access to this paradigm to individual First Nation citizens and at the same time preserving their traditional collective rights; and the myriad of ways that both equity and efficiency can be enhanced in terms of a broad range of social programs like benefits for golden-agers, homelessness, financing education/health, etc. Nonetheless, the foregoing analysis hopefully does suffice to signal that we are truly at an historic crossroads where investing in individuals (and making the rest of policy consistent with this emphasis) is central to success on both the economic and social fronts. The fact that reference in the above has been to a KBE social policy paradigm, or to a paradigm shift, is entirely deliberate since designing and implementing KBE social policy will be a daunting task because it calls for a rethinking of so many policy areas let alone a restructuring of federal and provincial bureaucracies in order to reflect these new priorities and policies.

The exciting reality is that this century represents the policy coming-of-age of citizens. If Laurier could proclaim that the 20th century would belong to Canada, embracing a KBE social policy paradigm will allow us to proclaim that the 21st century will belong to Canadians.

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