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SMALL BUSINESS

# Financing Profiles

SME Financing Data Initiative December 2011

## Small and Medium-Sized Enterprises in Tourism Industries

Andrea Pierce, Small Business Branch, Industry Canada

### HIGHLIGHTS

- Small and medium-sized enterprises (SMEs) operating in tourism industries accounted for 8 percent of SMEs in Canada in 2007.
- On average SMEs in tourism industries were younger (i.e., fewer years in operation) and more growth-oriented than their non-tourism counterparts.
- Majority business owners in tourism industries were significantly more likely to be female or be a visible minority compared with owners in other industries.
- Compared with SMEs in non-tourism industries, those in tourism industries were less likely to request external financing (15 percent versus 18 percent in 2007) and less likely to be approved for external financing (93 percent versus 96 percent in 2007).
- Debt financing was the most common type of external financing sought. In 2007, SMEs in tourism industries typically received smaller average amounts of debt financing compared to other SMEs ($239 000 versus $264 000).
- Of the main tourism industries, SMEs in the accommodation industry required the most capital but had the most difficulty obtaining financing.
- SMEs in tourism industries faced similar pricing loan conditions (interest rates) but unfavourable non-pricing loan conditions compared to others SMEs.
- The average tourism SME generated less revenue, less profit and had less retained earnings than its non-tourism counterpart.

### INTRODUCTION

Tourism activities play an important role in the Canadian economy, accounting for approximately 2 percent of Canada's overall gross domestic product and having as much economic impact as the fisheries, forestry and agriculture sectors combined. In 2010, tourism activities provided over 594 500 jobs and represented 3.5 percent of employment in Canada (Statistics Canada, 2011). Small businesses (fewer than 100 employees) are of critical importance to tourism in Canada as they account for close to 98 percent of businesses in the sector. Though there has been substantial research on small and medium-sized enterprises (SMEs) in tourism, information on their financing needs and obstacles is limited.

Access to financing is one of the most critical factors for growth for SMEs; however, in many cases they have difficulties obtaining the financing they need. Obtaining financing can be particularly difficult for SMEs in tourism because they are often viewed by financial institutions as relatively risky compared to SMEs in other industries (Council of Tourism Associations of British Columbia, 2006). According to consultations with tourism business owners in Ontario, one of the most significant impediments to improving, modernizing and/or expanding operations for businesses in tourism industries—particularly for SMEs—is the availability of financing (Ontario Tourism Competitiveness Study, 2009).

Given the importance of financing to the success and growth of a business, this report was produced to investigate the financing activities of SMEs in tourism industries and identify, if any, the unique financing needs and obstacles of this group. Using data from the SME Financing Data Initiative *Survey on Financing of Small and Medium Enterprises* from Statistics Canada, this report provides an overview of the business characteristics and recent financing activity of Canadian SMEs in tourism industries in comparison with Canadian SMEs in non-tourism industries.

### *Data and Definitions*

This report uses the comprehensive database of the SME Financing Data Initiative *Survey on Financing of Small and Medium Enterprises*, which was first released in 2000. The Statistics Canada survey, generally conducted every three years, measures the demand for, and sources of, financing for Canadian SMEs. The database includes information on the financing application process, firm profiles and demographic characteristics of SME ownership. This report is based on the 2004 and 2007 survey results. The representative samples consist of 13 042 respondents in 2004 and 15 808 respondents in 2007.

For the purpose of this report, an SME is defined as a business with fewer than 500 employees and less than $50 million in annual revenues. Excluded from this target population are non-profit and government organizations, schools, hospitals, subsidiaries, co-operatives and, financing and leasing companies.

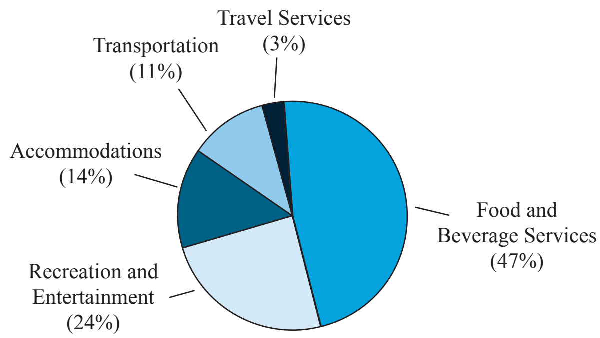
A tourism SME is defined as a business that meets the above SME criteria and operates in a tourism industry. A list of tourism industry groups was outlined based on the *Canadian Tourism Satellite Account* (CTSA). According to CTSA, a tourism industry is one that “would cease or continue to exist only at a significantly reduced level of activity as a direct result of an absence of tourism” (Statistics Canada, 2010a). The Appendix provides the complete list of the NAICS codes included in the tourism grouping. It should be noted that for the purpose of this report, all small and medium-sized businesses operating in these tourism industries were considered SMEs in tourism industries.

In 2004, the unweighted sample consisted of 1689 respondents in tourism industries and 10 788 respondents in non-tourism industries and in 2007 it included 1732 respondents in tourism industries and 14 069 in non-tourism industries. These observations were weighted to represent the whole economy.

## DISTRIBUTION BY INDUSTRY

Tourism businesses are distributed across five main industry groups: food and beverage services, recreation and entertainment, transportation, accommodation and travel services. In 2007, 8 percent of the estimated 2 million employer and non-employer SMEs in Canada operated in one of these tourism industries. As illustrated in Figure 1, the majority of SMEs in tourism industries operated in the food and beverage services industry (47 percent) followed by the recreation and entertainment industry (24 percent). Accommodation represented 14 percent of SMEs in tourism industries, transportation accounted for 11 percent, while travel services made up 3 percent.

**Figure 1**
**Distribution of Small and Medium-Sized Enterprise in Tourism Industries, 2007**



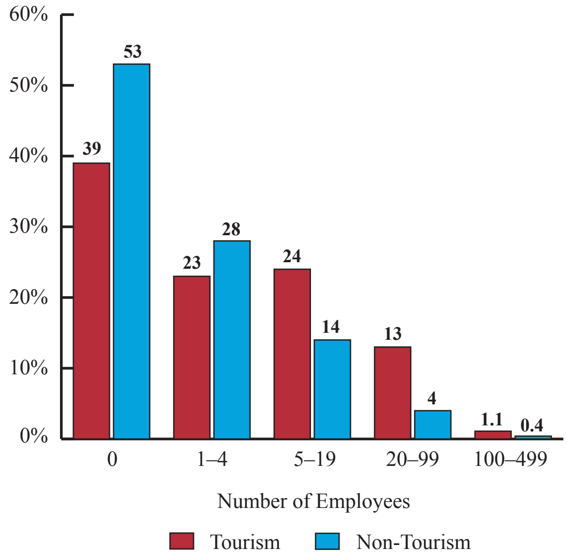

Source: SME Financing Data Initiative, Statistics Canada, *Survey on Financing of Small and Medium Enterprises*, 2007.

## SIZE AND LOCATION

***The majority of tourism small and medium-sized enterprises were small (less than 100 employees)***

The majority (99 percent) of SMEs in tourism industries were considered small (fewer than 100 employees). Figure 2 demonstrates that SMEs in tourism industries were less likely to be micro-businesses (fewer than 5 employees) compared with SMEs in non-tourism industries, (62 percent versus 81 percent) but were more likely to employ 5 or more workers (38 percent versus 18 percent).

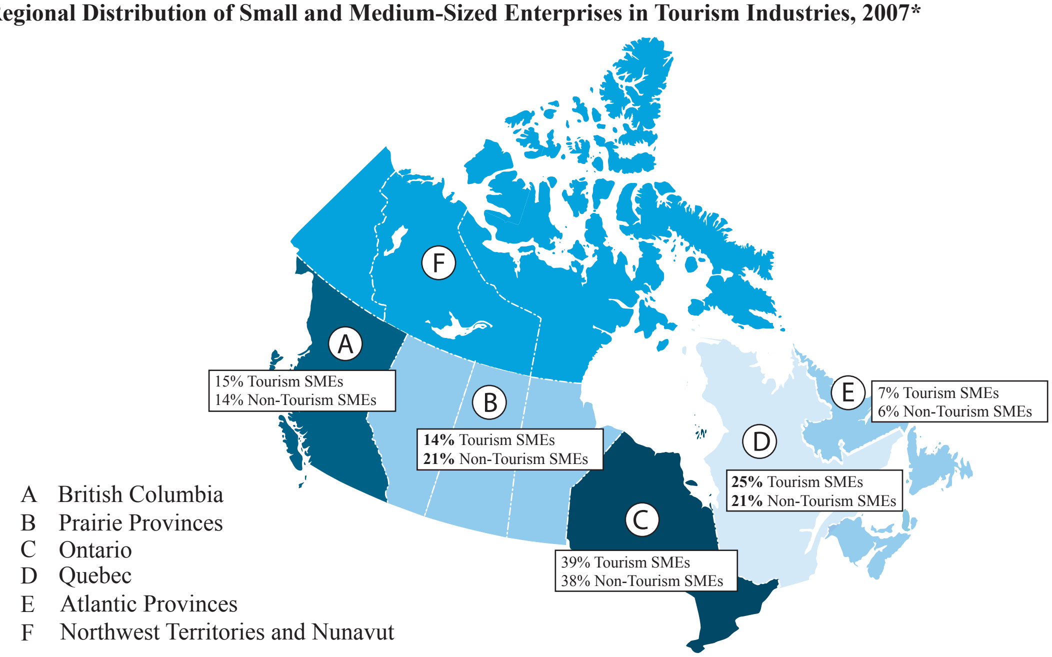
**Figure 2**
**Distribution of Small and Medium-Sized Enterprises in Tourism Industries by Size, 2007***




* Bold values denote statistically significant difference at 5 percent.
Source: SME Financing Data Initiative, Statistics Canada, *Survey on Financing of Small and Medium Enterprises,* 2007.

The regional distribution of SMEs in tourism industries is fairly proportional to the distribution of all SMEs across Canada. SMEs in tourism industries were located in every region of the country but were primarily concentrated in Ontario (39 percent) and Quebec (25 percent). In Quebec, the concentration of SMEs in tourism industries was much higher than the concentration of SMEs in non-tourism industries in 2007. On the other hand, in the Prairies, the concentration of SMEs in tourism industries was much lower than the concentration of SMEs in non-tourism industries (see Figure 3).

**Figure 3**
**Regional Distribution of Small and Medium-Sized Enterprises in Tourism Industries, 2007***




* Bold values denote statistically significant difference at 5 percent.
Distribution for the Territories and Nunavut are not available due to low frequency of response.
Source: SME Financing Data Initiative, Statistics Canada, *Survey on Financing of Small and Medium Enterprises*, 2007.

## BUSINESS CHARACTERISTICS

### *Tourism small and medium-sized enterprises were typically younger and more growth-oriented*

Table 1 presents a comparison of business characteristic between SMEs in tourism industries with SMEs in non-tourism industries. In 2007, SMEs in tourism industries were typically younger than their non-tourism counterpart. As shown in the Table 1, 11 percent of SMEs in tourism industries had been selling goods and services for one to two years compared with 8 percent of SMEs in non-tourism industries. In contrast, 68 percent of SMEs in tourism industries had been selling goods and services for over six years compared with 73 percent of SMEs in non-tourism industries.

**Table 1**
**Business Characteristics, 2007***

| Business Characteristics | Tourism SMEs (%) | Non-Tourism SMEs (%) |
|---|---|---|
| *Year Firm Started Selling Goods* | | |
| Between 2002 and 2004 (1–2 years old) | **11** | **8** |
| Between 1999 and 2001 (3–5 years old) | 21 | 19 |
| Prior to 1999 (6 or more years old) | **68** | **73** |
| *Stage of Development (as identified by the owner)* | | |
| Start-up | 5 | 4 |
| Fast Growth | **16** | **9** |
| Slow Growth | **48** | **38** |
| Maturity | **27** | **37** |
| Decline | **5** | **11** |
| *Growth Intentions* | | |
| Intend to expand business within next 2 years | **45** | **40** |
| Current financing sufficient to fund expansion plans | **46** | **59** |

* Bold values denote statistically significant difference at 5 percent.
Source: SME Financing Data Initiative, Statistics Canada, *Survey on Financing of Small and Medium Enterprises,* 2007.

Although being relatively young, few SMEs in tourism industries reported being in the start-up stage of business. The majority of businesses in tourism industries identified themselves as being in the slow growth stage of business (48 percent). Interestingly, tourism business owners were more likely than non-tourism business owners to identify their business sales as experiencing either fast growth or slow growth but were less likely to identify their business sales as declining or experiencing no growth (“maturity”).

Not only were SMEs in tourism industries more likely to be in the fast growth stage of business but they were also found to be more growth-oriented than their non-tourism counterpart. As shown in Table 1, in 2007 45 percent of SMEs in tourism industries had intentions to expand the size or scope of their business in the next three years, while only 40 percent of SMEs in non-tourism industries reported the same intentions. Despite being more growth oriented, SMEs in tourism industries were less likely than those in non-tourism industries to have sufficient financing to fund their expansion plans.

## OWNER CHARACTERISTICS

***Tourism small and medium-sized enterprises owners were more likely to be female and twice as likely to be a visible minority compared with non-tourism small and medium-sized enterprises owners***

An individual's characteristics and background are important determinants of entrepreneurial activity. In 2007, there were notable differences in demographic characteristics between tourism and non-tourism entrepreneurs.

Previous literature has shown that the tourism sector is a major employer of women (Canadian Tourism Human Research Council, 2009; and Statistics Canada, 2010b). According to 2007 survey results, more than half of businesses in both tourism and non-tourism industries were majority male-owned (51 percent for tourism industries and 65 percent for non-tourism industries); however, compared with businesses in non-tourism industries, those in tourism industries were significantly more likely to be majority female-owned. Specifically, 26 percent of SMEs in tourism industries were majority female-owned, whereas only 16 percent of SMEs in non-tourism industries were majority female-owned. This finding is also consistent with the *Small Business Financing Profiles – Women Entrepreneurs* (Industry Canada, 2010), which highlighted that majority female-owned SMEs were more likely to be concentrated in the service sector, particularly in the tourism sector.

In 2007, the mother tongue of an SME owner operating in a tourism industry was less likely to be English and more likely to be French or a language other than English or French compared with a non-tourism SME owner (see Table 2). This coincides with a greater concentration of recent immigrant owners and visible minority owners in the tourism industry than in the non-tourism industry. Specifically, 18 percent of tourism owners were a visible minority and 4 percent were recent immigrants (within the last five years). In contrast, only 9 percent of non-tourism owners were visible minorities and 3 percent were recent immigrants.

The majority of owners in both tourism and non-tourism industries were between the ages of 50 and 64 (45 percent for both). Despite being similar in age to SME owners in non-tourism industries, SME owners in tourism industries had less managerial experience than their non-tourism counterpart. As shown in Table 2, 67 percent of tourism owners had more than 10 years of managerial experience, while 72 percent of non-tourism owners had the same amount of experience.

**Table 2**
**Owner Characteristics, 2007***

| Owner Characteristics | Tourism SMEs (%) | Non-Tourism SMEs (%) |
|---|---|---|
| *Gender* | | |
| Majority Male Ownership | **51** | **65** |
| Majority Female Ownership | **26** | **16** |
| Equal Ownership | **23** | **19** |
| *Background* | | |
| Visible Minority (other than Aboriginal) | **18** | **9** |
| Aboriginal | 3 | 2 |
| Disabled | 2 | 2 |
| Recent Immigrant (within last 5 years) | **4** | **3** |
| Held by family members | 64 | 65 |
| *Mother Tongue* | | |
| English | **54** | **68** |
| French | **24** | **18** |
| Other | **22** | **14** |
| *Age* | | |
| Less than 30 | 2 | 3 |
| 30–39 | **14** | **12** |
| 40–49 | 26 | 28 |
| 50–64 | 45 | 45 |
| 65 and over | 13 | 13 |
| *Managerial Experience* | | |
| Over 10 years | **67** | **72** |

* Bold values denote statistically significant difference at 5 percent.
Source: SME Financing Data Initiative, Statistics Canada, *Survey on Financing of Small and Medium Enterprises,* 2007.

## OBSTACLES TO BUSINESS GROWTH

***Small and medium-sized enterprises in tourism industries were more likely to report obtaining financing as an obstacle to business growth***

The tourism industry operates in a unique and challenging environment, constantly adapting to changing demographics, economic conditions, health and safety issues and environmental concerns. As a result, achieving growth targets for an SME in the tourism industry can be challenging. Current issues facing the tourism industry include, but are not limited to, seasonality of industry demand, new competition from emerging economies, exchange rates, border infrastructure, increased fuel costs, air access, labour shortage and concerns over global security (Canadian Tourism Commission, 2009a; and Industry Canada, 2008).

Among SME owners surveyed in 2004, the most frequently identified obstacle for both tourism and non-tourism business was the level of taxation. Low profitability, insurance rates and instability of consumer demand were more common concerns for businesses in tourism industries than those in non-tourism industries in 2004 (see Table 3).

In 2007, the most frequently cited challenge reported by SMEs owners was rising business costs followed by finding qualified labour. Over half of tourism SME owners (59 percent) identified business costs as an obstacle to growth and almost half (39 percent) cited concerns about finding qualified labour.

Interestingly, in comparison with SMEs in non-tourism industries, SMEs in tourism industries were significantly more likely to cite obtaining financing as an obstacle to business growth in both 2004 and 2007 (see Table 3). In 2007, across the tourism industries, SMEs in the accommodation industry were the most likely to identify obtaining financing as an obstacle (32 percent), followed by the recreation and entertainment industry (29 percent). Conversely, none of the businesses in the transportation industry identified obtaining financing as an obstacle (SME Financing Data Initiative, Statistics Canada, 2007).

**Table 3**
**Perceived Obstacles to Business Growth, 2004 and 2007***

| Obstacles | | 2004 Tourism (%) | 2004 Non-Tourism (%) | 2007 Tourism (%) | 2007 Non-Tourism (%) |
|---|---|---|---|---|---|
| External to the Firm | Finding Qualified Labour | **32** | **37** | 39 | 42 |
| | Instability of Consumer Demand | **42** | **36** | 30 | 33 |
| | Government Regulations | 35 | 34 | 31 | 27 |
| | Environmental Regulations/Compliance | | | 11 | 12 |
| | Level of Taxation | 50 | 47 | | |
| | Increasing Competition | | | 37 | 40 |
| Internal to the Firm | Obtaining Financing | **25** | **20** | **25** | **16** |
| | Management Capacity | 12 | 14 | 12 | 11 |
| | Rising Business Costs | | | 59 | 56 |
| | Low profitability | **47** | **38** | | |
| | Insurance Rates/Premiums | **42** | **36** | 36 | 34 |

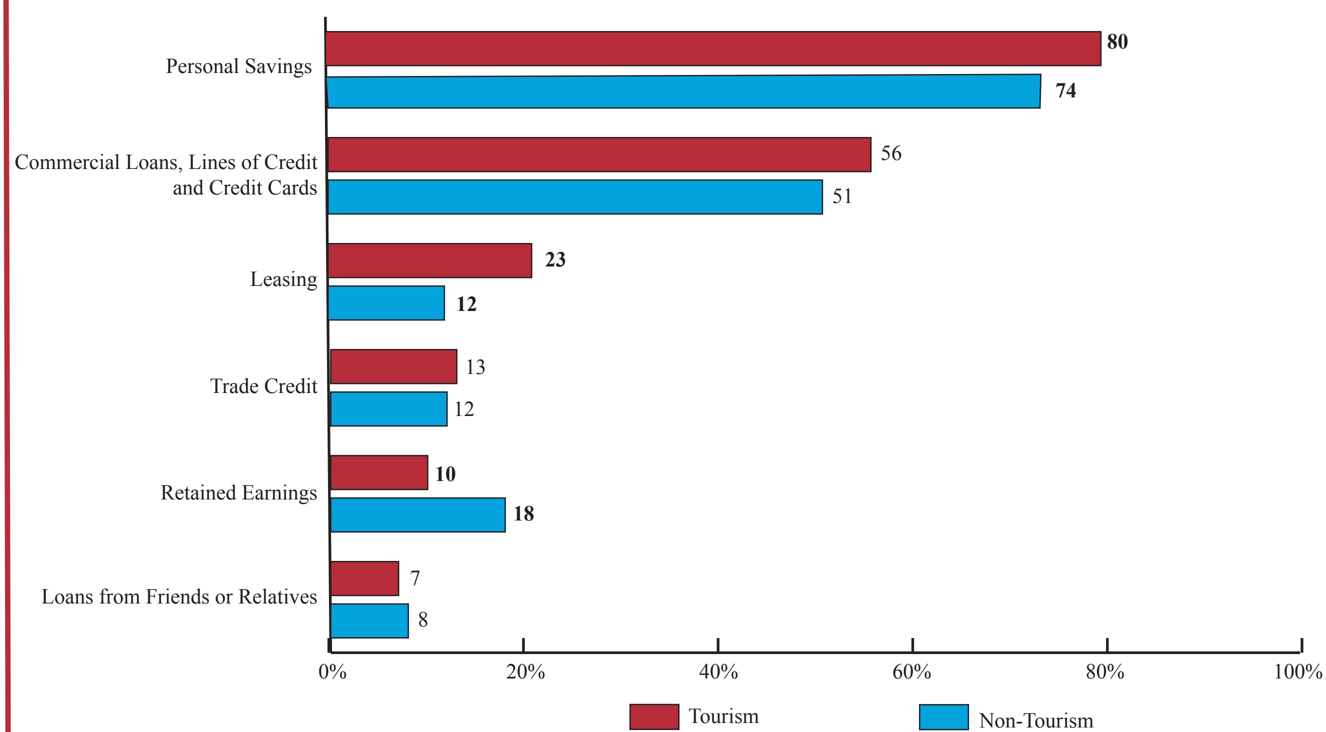
* Bold values denote statistically significant difference at 5 percent.
Source: SME Financing Data Initiative, Statistics Canada, *Survey on Financing of Small and Medium Enterprises*, 2004 and 2007.

## CAPITAL STRUCTURE

***Tourism small and medium-sized enterprises are very reliant on personal savings to financing their business***

An important factor for growth and development of a business is financing. SME owners typically look to informal sources of financing, such as personal loans and personal savings, when starting a business or funding day-to-day operations. Figures 4 and 5 list the top six sources of financing used by the average SME to start-up and operate a tourism company compared with the average SME in a non-tourism industry in 2007. For both types of SMEs, the main source of financing during business start-up was personal savings, with more SMEs in tourism industries using this source (80 percent versus 74 percent for SMEs in non-tourism industries). Compared with SMEs in non-tourism industries, SMEs in tourism industries were significantly more likely to make use of lease financing and significantly less likely to use retained earnings (see Figure 5).

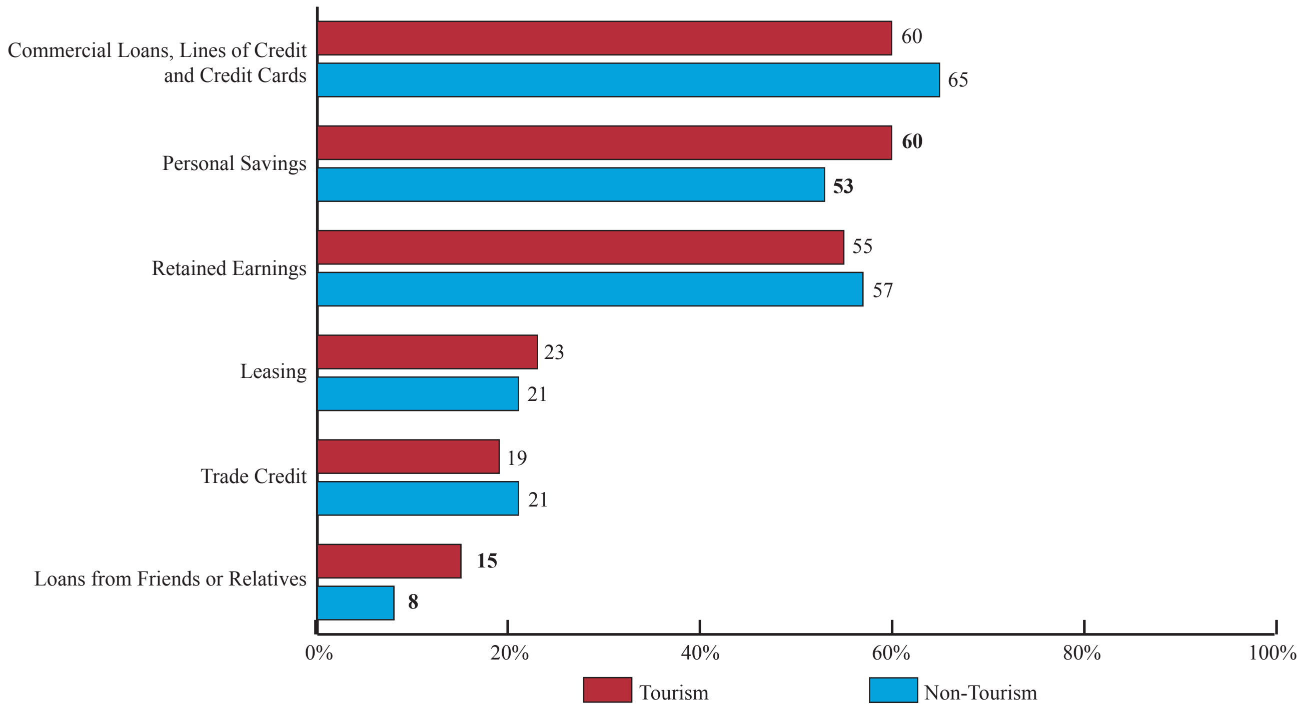
**Figure 4**
**Top Six Important Sources of Financing Used During Start-up, 2007***




* Bold values denote statistically significant difference at 5 percent.
Note: Start-up is defined as the period prior to the sale of goods and services. Sources of financing include any source used, regardless of whether it was authorized or obtained in a previous year. Multiple responses were possible.
Source: SME Financing Data Initiative, Statistics Canada, *Survey on Financing of Small and Medium Enterprises*, 2007.

As shown in the Figure 5, the main sources of financing used to keep the business in operation differ slightly from those sources used during start-up. In 2007, commercial loans, lines of credit and credit cards surpassed personal savings as the most common type of financing used for day-to-day business. Figure 5 also shows that SMEs in tourism industries were still very reliant on personal loans and informal financing to keep their business in operation. Specifically, SMEs in tourism industries were just as likely to use personal savings as they were to use commercial credit and they were significantly more likely to use personal savings than their non-tourism counterpart. Moreover, SMEs in tourism industries were almost twice as likely as SMEs in non-tourism industries to use informal financing (loans from friends and family) to financing their ongoing operations. This could be an indication that SMEs in tourism industries have more difficulty obtaining credit from financial institutions than SMEs in non-tourism industries and as a result they need to turn to alternate means of financing their business (i.e., personal savings and informal financing).

**Figure 5**
**Top Six Important Sources of Financing Used to Keep Business in Operation, 2007***




* Bold values denote statistically significant difference at 5 percent.
Note: Sources of financing include any source used, regardless of whether it was authorized or obtained in a previous year. Multiple responses were possible.
Source: SME Financing Data Initiative, Statistics Canada, *Survey on Financing of Small and Medium Enterprises*, 2007.

## FINANCING ACTIVITY

***Small and medium-sized enterprises in tourism industries were less likely to seek financing and less likely to be approved***

In order to determine if SMEs in tourism industries have more difficulty accessing financing than their non-tourism counterpart, the following section examines the recent financing activity of these businesses.

As presented in Table 4, SMEs in tourism industries were less likely to request external financing, both in 2004 and 2007. Debt financing was the most common type of external financing requested by SMEs in both tourism and non-tourism industries. In 2007, SMEs in tourism industries were slightly less likely to seek debt financing compared with SMEs in non-tourism industries (10 percent versus 13 percent).

As shown in Table 4, SMEs in tourism industries were not only less likely to request external financing, they were also less likely to be approved[1] for external financing. Specifically, in 2004, 87 percent of SMEs in tourism industries were approved for external financing compared with 91 percent of SMEs in non-tourism industries. In 2007, the approval rate for SMEs in tourism industries increased to 93 percent but was still below the 96 percent reported by SMEs in non-tourism industries. In particular, SMEs in tourism industries were less likely to be approved for debt financing and significantly less likely to be approved for government loans or grants in 2007.

**Table 4**
**Financing Request and Approval Rates, 2004 and 2007***

| Type of Financing | | 2004 Tourism (%) | 2004 Non-Tourism (%) | 2007 Tourism (%) | 2007 Non-Tourism (%) |
|---|---|---|---|---|---|
| Any External Financing | Request Rate | 23 | 24 | **15** | **18** |
| | Approval Rate | **87** | **91** | **93** | **96** |
| Debt Financing | Request Rate | 19 | 19 | **10** | **13** |
| | Approval Rate | **81** | **88** | 91 | 94 |
| Lease Financing | Request Rate | **2** | **3** | 4 | 5 |
| | Approval Rate | 97 | 96 | 93 | 93 |
| Equity Financing | Request Rate | **0.5** | **1** | 1 | 1 |
| | Approval Rate | 70 | 44 | 72 | 70 |
| Trade Credit | Request Rate | **9** | **12** | 8 | 9 |
| | Approval Rate | 95 | 89 | 100 | 99 |
| Government Loan or Grant | Request Rate | 2 | 3 | 3 | 3 |
| | Approval Rate | — | — | **69** | **81** |

*Bold values denote statistically significant difference at 5 percent.
Note 1: Request and approval rates are Industry Canada calculations using the whole sample. Approval rates exclude observations in which loans were withdrawn or are still under review.
Note 2: "—" indicates that estimates were suppressed to meet confidentiality requirements of the *Statistics Act* or for low data quality reasons.
Source: SME Financing Data Initiative, Statistics Canada, *Survey on Financing of Small and Medium Enterprises*, 2004 and 2007.

[1] It should be noted that approval rates presented in Table 4 do not distinguish between full and partial approval. In other words, a request for financing was considered "approved" as long as some amount (not necessarily the full amount) was approved. Moreover, approval rates do no consider scale and each request for financing was given the same weight in the calculations. That is, a request for $500 carried equal weight to a request for $50 000.

***Of the main tourism industries, accommodation had the highest external financing request rate***

Given the diversity of the industries within the tourism sector, Table 5 demonstrates the request and approval rates by industry within tourism. In 2007, the highest external financing request rate was in the accommodation industry (21 percent), followed by the recreation and entertainment industry (18 percent), both having a higher request rate than the overall tourism average (15 percent). On the other hand, the external financing request rates for the food and beverage industry (13 percent) and the transportation industry (10 percent) were below the tourism average.

The most common type of external financing sought by all industries was debt financing, with the exception of travel services, which had equal request rates for debt financing and government loans or grants. The accommodation industry had the highest debt financing request rate (13 percent) of all industries.

As shown in Table 5, the approval rates for external financing in the recreation and entertainment industry (100 percent) and for the accommodation industry (94 percent) were higher than the tourism average (93 percent) in 2007. On the other hand, approval rates for the food and beverage (90 percent) and transportation industries (78 percent) were lower than the tourism average.

**Table 5**
**Financing Request and Approval Rates, by Tourism Industry, 2007**

| Type of Financing | | Accommodation (%) | Food and Beverage (%) | Recreation and Entertainment (%) | Transportation (%) | Travel Services (%) |
|---|---|---|---|---|---|---|
| Any External Financing | Request Rate | 21 | 13 | 18 | 10 | 16 |
| | Approval Rate | 94 | 90 | 100 | 78 | — |
| Debt Financing | Request Rate | 13 | 10 | 9 | 9 | 9 |
| | Approval Rate | 95 | 86 | 100 | 83 | — |
| Lease Financing | Request Rate | 6 | 4 | 5 | 2 | 7 |
| | Approval Rate | 91 | 91 | 100 | — | — |
| Equity Financing | Request Rate | 4 | 2 | 0 | 0 | 1 |
| | Approval Rate | — | 69 | — | — | — |
| Trade Credit | Request Rate | 9 | 9 | 6 | 4 | 7 |
| | Approval Rate | 100 | 99 | 100 | 100 | — |
| Government Loan or Grant | Request Rate | 4 | 2 | 6 | 0.1 | 9 |
| | Approval Rate | 85 | 73 | 74 | — | — |

Source: SME Financing Data Initiative, Statistics Canada, *Survey on Financing of Small and Medium Enterprises*, 2007.
Note: "—" indicates that estimates were suppressed to meet confidentiality requirements of the *Statistics Act* or for low data quality reasons.

## Debt Financing

***Tourism small and medium-sized enterprises were less likely to be fully approved for the debt financing they requested in 2007***

Given that debt financing is the most popular type of external financing sought by SMEs, further investigation of this type of financing is warranted. Table 6 presents the average approved debt amounts for SMEs in both tourism and non-tourism industries to examine the magnitude of debt requests. As shown, regardless of the type of debt requested (short-term or long-term), the average amount approved for SMEs in tourism industries was lower than that approved for SMEs in non-tourism industries.

Based on the size of loan approved, it is not possible to determine whether SMEs in tourism industries were more likely than SMEs in non-tourism industries to be fully or partially denied debt financing or whether

SMEs in tourism simply requested smaller amounts of debt financing. To investigate this, the ratio of total amount of financing approved-to-requested is considered. As shown in Table 6, this ratio was slightly lower for SMEs in tourism industries than for those in non-tourism industries in 2004 (86 percent for tourism and 88 percent for non-tourism). In 2007 however, this ratio decreased dramatically for SMEs in tourism industries to 67 percent, indicating that on average, SMEs in tourism industries received only 67 percent of the amount of debt financing they requested. This was significantly lower than the 93 percent ratio observed for SMEs in non-tourism industries.

**Table 6**
**Approval Debt Financing Amounts**

| Type of Debt Financing | 2004* | | 2007 | |
|---|---|---|---|---|
| | Tourism | Non-Tourism | Tourism | Non-Tourism |
| Average Long-Term Approved | $185 000 | $195 000 | $254 000 | $273 000 |
| Average Short-Term Approved | $48 000 | $87 000 | $126 000 | $190 000 |
| Average Total Debt Approved | $97 000 | $129 000 | $239 000 | $264 000 |
| Approved/ Requested Total Debt | 86% | 88% | 67% | 93% |

* 2004 amounts exclude extreme outliers.
Note: Figures are Industry Canada calculations using only the observations in which both request amount and approved amount are included. Approval amounts exclude observations in which the response was "don't know" or "refused."
Source: SME Financing Data Initiative, Statistics Canada, *Survey on Financing of Small and Medium Enterprises*, 2004 and 2007.

To verify that SMEs in tourism industries had a more difficult time accessing financing, Table 7 illustrates the full and partial approval rates for SMEs in tourism and non-tourism industries in 2007. As shown, SMEs in tourism industries were less likely to be authorized for the full amount they requested (82 percent compared with 89 percent for SMEs in non-tourism industries). Moreover, SMEs in tourism industries were significantly more likely than SMEs in non-tourism industries to be only partially approved (10 percent versus 5 percent) and also more likely to have their request turned down (9 percent for tourism and 6 percent for non-tourism).

**Table 7**
**Result of Debt Financing Request, 2007***

| Debt Financing | Tourism (%) | Non-Tourism (%) |
|---|---|---|
| Full Amount Authorized | **82** | **89** |
| Partial Amount Authorized | **10** | **5** |
| Request Turned Down | 9 | 6 |

* Bold values denote statistically significant difference at 5 percent.
Source: SME Financing Data Initiative, Statistics Canada, *Survey on Financing of Small and Medium Enterprises*, 2007.

### *The accommodation industry required the most debt financing but had the most difficulty obtaining it*

In order to determine if any particular tourism industry had more difficulty accessing financing, Table 8 presents approved debt financing amounts by tourism industry in 2007. As noted in the table, the accommodation industry had the highest average debt financing amount approved (both short-term and long-term) of all industries in tourism. Despite this, the accommodation industry also had the lowest total debt approved-to-requested ratio at 42 percent. This suggests that SMEs in the accommodation industry required the most financing but had the most difficulty being approved for the full amount they requested compared with SMEs in other tourism industries.

There are a number of reasons why securing financing can be challenging for a business in the accommodation industry. The seasonal nature of the tourism sector in Canada means many accommodation businesses have short operating seasons in which they must generate the majority of their revenues to cover their costs. The industry is faced with low profit margins, fluctuating sales and high bankruptcy rates (Canadian Tourism Commission, 2009b). These businesses are also extremely vulnerable to external events such as, economic, political and health issues. Dealing with these circumstances requires accurate forecasting and leaves little room for management error.

**Table 8**
**Approved Debt Financing Amounts by Tourism Industry, 2007**

| Type of Financing | Accommodation | Food and Beverage | Recreation and Entertainment | Transportation |
|---|---|---|---|---|
| Average Long-Term Approved | $595 000 | $172 000 | $137 000 | $502 000 |
| Average Short-Term Approved | $211 000 | $94 000 | $133 000 | — |
| Average Total Debt Approved | $546 000 | $157 000 | $183 000 | $566 000 |
| Approved/Requested Total Debt | 42% | 86% | 99% | 99% |

Note 1: Data for the Travel Services Industry is not available due to low frequency of response.
Note 2: "—" indicates that estimates were suppressed to meet confidentiality requirements of the *Statistics Act* or for low data quality reasons.
Source: SME Financing Data Initiative, Statistics Canada, *Survey on Financing of Small and Medium Enterprises*, 2007.

Additionally, businesses in the accommodation industry require significant capital for their real estate component, including buildings, operating systems, furniture and equipment. In many cases these assets are specialized or built in to the building, making them hard to realize in the event of liquidation. Moreover, due to high attrition rate and changing preferences in the industry, the liquidation values of these assets are low—often less than 25 cents in the dollar (Council of Tourism Associations of British Columbia, 2009).

All of these factors cause lenders to be conservative when lending to these businesses. A recent study conducted by PKF Consulting (2011) on behalf of Industry Canada found that 13 percent of the lending companies surveyed (chartered banks, private sources and finance and trust companies) indicated that they did not lend to the accommodation industry in 2010. Of those 13 percent, half noted that the influencing factor for not lending was the perceived risks associated with the sector.

The study also showed that of the active lenders to the accommodation industry, many imposed certain lending restrictions in order to mitigate their exposure to risk. For example, 67 percent of the companies said they restricted hotel financing to certain hotel asset types and the same number said that they only finance hotels in certain regions or markets. Furthermore, 42 percent indicated that they limited the amount lent per hotel asset and 33 percent said they had a ceiling to the overall amount lent to the industry. This therefore indicates that due to the nature of the industry, businesses in accommodation have difficulties generating confidence in lenders. This may help explain why they have more difficulty securing the full amount of financing they require compared with businesses in other tourism industries.

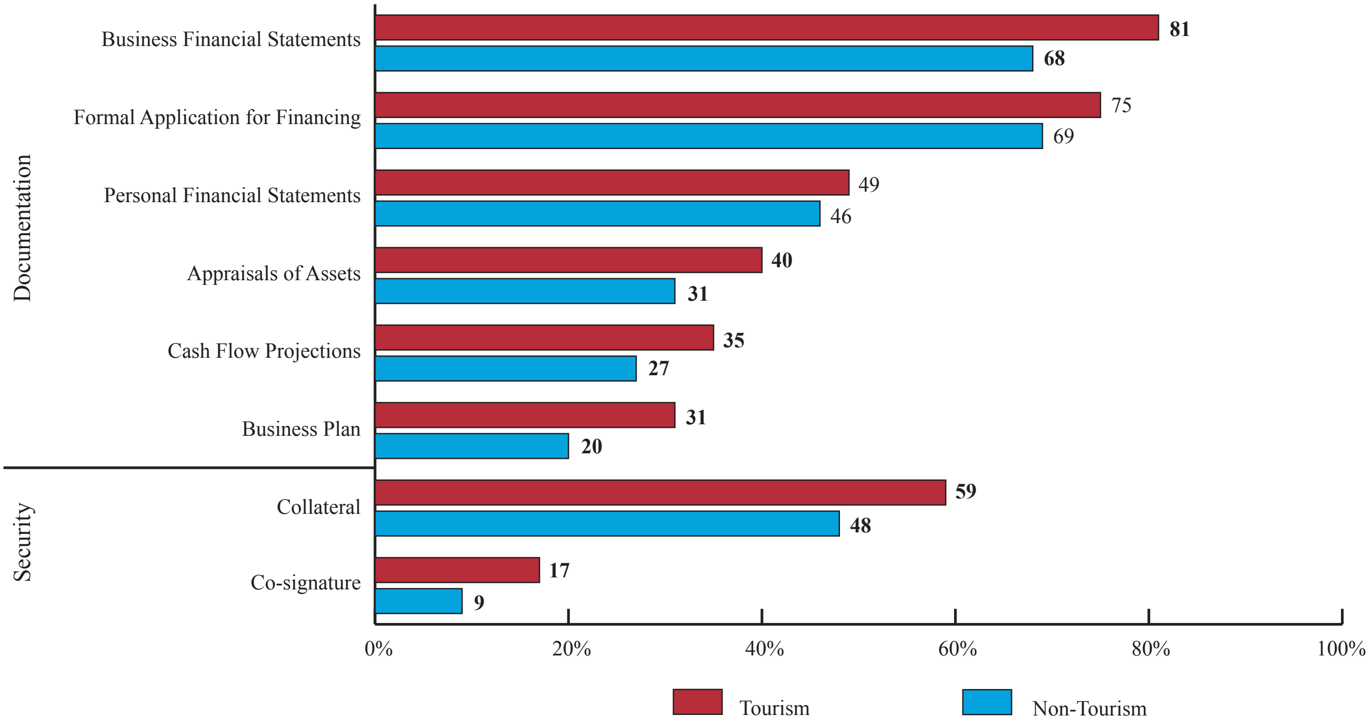
## Financing Terms and Conditions

***Small and medium-sized enterprises in tourism industries faced less favourable non-pricing loan conditions but similar pricing loan conditions compared with small and medium-sized enterprises in non-tourism industries***

When a business is perceived as being relatively risky, it is not unusual for a lender to provide less favourable loan conditions. In 2007, compared with non-tourism businesses, those in tourism industries faced more stringent non-pricing loan conditions (documents and security required to obtain the loan) but similar pricing loan conditions (interest rates). Specifically, SMEs in tourism industries were significantly more likely than SMEs in non-tourism industries to be required to provide business financial statements, appraisals of assets, cash flow projections and a business plan to secure debt (see Figure 6). Moreover, a higher percentage of SMEs in tourism industries were required to pledge collateral or to provide a co-signature in order to obtain requested credit compared with SMEs in non-tourism industries.

Conversely, Table 9 illustrates that SMEs in tourism industries paid similar interest rates to SMEs in non-tourism industries in both 2004 and 2007. This is contrary to what would be expected for a relatively risky industry. Moreover, SMEs in tourism industries had a longer interest term on their loan compared with non-tourism.

**Figure 6**
**Documents and Security Required During Loan Application Process, 2007***




* Bold values denote statistically significant difference at 5 percent.
Note: Multiple responses were possible.
Source: SME Financing Data Initiative, Statistics Canada, *Survey on Financing of Small and Medium Enterprises*, 2007.

**Table 9**
**Average Interest Rate and Length of Terms, 2004 and 2007**

| | | 2004 | | 2007 | |
|---|---|---|---|---|---|
| | | Tourism | Non-Tourism | Tourism | Non-Tourism |
| Short Term (excluding credit cards) | Average Overall Interest Rate | 6.1 | 6.1 | 7.0 | 7.2 |
| Long Term | Average Overall Interest Rate | 6.3 | 6.0 | 7.2 | 7.4 |
| | Average Length of Term (months) | 85.1 | 77.4 | 68.6 | 63.3 |

Source: SME Financing Data Initiative, Statistics Canada, *Survey on Financing of Small and Medium Enterprises*, 2004 and 2007.

## Reasons for Not Applying for Financing

***Small and medium-sized enterprises in tourism industries were more likely not to request financing because the process is too difficult and time consuming***

As found earlier, SMEs in tourism industries were less likely to request financing than those in non-tourism industries, but what is the reason for this? As shown in Table 10, in 2004 the primary reason for not applying for financing was because financing was not needed; however, fewer SMEs in tourism industries cited this reason.

**Table 10**
**Reasons for Not Requesting Financing, 2004***

| | 2004* | |
|---|---|---|
| | Tourism (%) | Non-Tourism (%) |
| Financing not needed | **87** | **91** |
| Thought request would be turned down | 6 | 5 |
| Applying for financing is too difficult | **7** | **5** |
| Applying for financing is too time consuming | **5** | **3** |
| Cost of debt financing is too high | **5** | **3** |

* Bold values denote statistically significant difference at 5 percent.
Source: SME Financing Data Initiative, Statistics Canada, *Survey on Financing of Small and Medium Enterprises*, 2004.

Six percent of SMEs in tourism industries and five percent of SMEs in non-tourism industries did not apply for financing because they thought they would be turned down. These businesses are known as discouraged borrowers because although they required financing they were discouraged from requesting it for fear of being rejected.

SMEs in tourism industries were more likely not to have requested debt because the application process was too difficult or time consuming. This is likely a reflection of having to provide more documents and security to obtain their loan compared with SMEs in non-tourism industries.

Additionally, SMEs in tourism industry were more likely not to have sought financing because they felt that the cost of debt was too high. Interestingly, this finding is not consistent with the findings on interest rates, which showed no statistically significant difference in rates paid between SMEs in tourism industries and those in non-tourism industries.

## FINANCIAL PERFORMANCE

***The poor financial performance of small and medium-sized enterprises in tourism industries may help explain their difficulties in accessing financing***

Using anonymized tax file data linked by Statistics Canada, Table 11 presents a summary of financial statement figures for the average tourism SME in comparison with the average non-tourism SME. In both 2004 and 2007, the average SME operating in a tourism industry had substantially lower total revenues, profit and retained earnings compared with the average SME operating in a non-tourism industry.

Additionally, from 2004 to 2007, average current assets increased for both types of businesses; however the increase was smaller for SMEs in tourism industries. The result was a widened gap between the industries in terms of assets.

This poor financial performance suggests that businesses in tourism industries have more financial difficulties, which could be a result of the industry's challenging environment or it could indicate poor financial management. In any event, this performance may help to explain why businesses in tourism have more difficultly obtaining financing.

**Table 11**
**Selected Financial Statement Figures (to the closest thousand), 2004 and 2007***

| | 2004 | | 2007 | |
|---|---|---|---|---|
| | Tourism SMEs | Non-Tourism SMEs | Tourism SMEs | Non-Tourism SMEs |
| Total Revenue | **$685 000** | **$951 000** | **$775 000** | **$1 167 000** |
| Total Expenses | **$676 000** | **$908 000** | **$745 000** | **$1 086 000** |
| Net Income/Loss before tax | **$10 000** | **$43 000** | $30 000 | $81 000 |
| Current Assets | **$101 000** | **$327 000** | **$138 000** | **$476 000** |
| Fixed Assets** | $368 000 | $302 000 | $496 000 | $469 000 |
| Total Assets | $469 000 | $629 000 | $634 000 | $946 000 |
| Current Liabilities | $161 000 | $224 000 | **$177 000** | **$294 000** |
| Total Liabilities | $396 000 | $423 000 | $496 000 | $591 000 |
| Retained Earnings | **$39 000** | **$144 000** | **$73 000** | **$211 000** |
| Total Shareholder Equity | **$73 000** | **$206 000** | $138 000 | $354 000 |

* Bold values denote statistically significant difference at 5 percent.
** Fixed assets include total tangible assets, intangible assets, long term investments and other long term assets.
Source: SME Financing Data Initiative, Statistics Canada, *Survey on Financing of Small and Medium Enterprises*, 2004 and 2007.

## SUMMARY AND DISCUSSION

Tourism is an important sector that supports SMEs and provides employment to Canadians across the country. Given the increasingly important role that tourism plays in the Canadian economy, it is critical to investigate SMEs in tourism industries to determine their unique characteristics. This report has presented a profile of SMEs in tourism industries and examined their differences compared with SMEs in non-tourism industries in terms of business and owner characteristics, access to financing, financing terms and conditions and obstacles to business growth.

The findings showed that SMEs in tourism industries have unique business characteristics compared to SMEs in non-tourism industries. Specifically, businesses in tourism industries were typically younger and more growth-oriented. Additionally, SMEs in tourism industries were more likely to be majority female-owned.

Compared with SMEs in non-tourism industries, those in tourism industries were less likely to request external financing and also less likely to be approved for external financing. It was also found that SMEs in tourism industries faced similar pricing loan conditions but less favourable non-pricing loan conditions.

After measuring the ratio of total amount of debt approved to total amount of debt requested, it is clear that SMEs in tourism industries had more difficulty obtaining financing than their non-tourism counterparts, especially in 2007. In particular, the accommodation industry, which required the most financing, had the most difficulty, receiving less than half of the debt financing they requested in 2007. The seasonality and risks associated with the industry as well as poorer financing performance relative to other sectors, may explain why businesses in tourism industries have more difficulties accessing financing.

In conclusion, the results presented in this report reveal that SMEs in tourism industries face unique challenges when it comes to access to financing, especially in the accommodation industry. Given the lack of research on the financing activities of businesses in the tourism sector, further research may be required to determine why these financing obstacles exist and what can be done to overcome them.

## NAICS included in Tourism Grouping

| NAICS | Description |
|---|---|
| **Air Transportation** | |
| 4811 | Scheduled Air Transport |
| 4812 | Non-scheduled Air Transport |
| **Rail Transportation** | |
| 4821 | Rail Transportation |
| **Water Transportation** | |
| 4831 | Deep Sea, Coastal and Great Lakes Water Transportation |
| 4832 | Inland Water Transportation |
| **Bus Transportation** | |
| 4851 | Urban Transit Systems |
| 4852 | Interurban and Rural Bus Transportation |
| 4854 | School and Employee Bus Transportation |
| 4855 | Charter Bus Industry |
| 4859 | Other Transit and Group Passenger Transportation |
| **Scenic and Sightseeing Transportation** | |
| 4871 | Scenic and Sightseeing Transportation, Land |
| 4872 | Scenic and Sightseeing Transportation, Water |
| 4879 | Scenic and Sightseeing Transportation, Other |
| **Taxicabs** | |
| 4853 | Taxi and Limousine Service |
| **Travel Services** | |
| 5615 | Travel Arrangement and Reservation Services |

| NAICS | Description |
|---|---|
| **Recreation and Entertainment** | |
| 51213 | Motion Picture and Video Exhibition |
| 7111 | Performing Arts Companies |
| 7112 | Spectator Sports |
| 7115 | Independent Artists, Writers and Performers |
| 7121 | Heritage Institutions |
| 7131 | Amusement Parks and Arcades |
| 7132 | Gambling Industries |
| 7139 | Other Amusement and Recreation Industries |
| **Hotels** | |
| 7211 | Traveller Accommodation (except 721114-Motels) |
| **Motels** | |
| 721114 | Motels |
| **Camping** | |
| 721211 | RV (Recreational Vehicle) Parks and Campgrounds |
| **Other Accommodation** | |
| 721212 | Hunting and Fishing Camps |
| 721213 | Recreational (except Hunting and Fishing) and Vacation Camps |
| 721198 | All Other Traveller Accommodation |
| **Food and Beverage Services** | |
| 7221 | Full-Service Restaurants |
| 7222 | Limited-Service Eating Places |
| 7224 | Drinking Places (Alcoholic Beverages) |

Note: NAICS 5321 Automotive Equipment Rental and Leasing is considered a tourism industry but was excluded from the survey population because it classifies as financing and leasing companies.

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## SME Financing Data Initiative

*Small Business Financing Profiles* is an ongoing series of articles on specific segments of the marketplace and a component of Industry Canada's reporting efforts on SME financing.

Consistent with recommendations in 1999 from the Task Force on the Future of the Canadian Financial Services Sector, the SME Financing Data Initiative is a comprehensive data collection program on SME financing in Canada. In partnership with Statistics Canada and Finance Canada, Industry Canada reports on the supply of, and demand for, small and medium-sized business financing to provide a complete picture of SME financing.

As part of the initiative, Statistics Canada administers a series of national surveys on small and medium-sized enterprises (*Survey on Financing of Small and Medium Enterprises*) and financial providers (*Survey of Suppliers of Business Financing*). Industry Canada supplements these surveys with the *Credit Conditions Survey* and additional research into niche areas of SME financing.

For further information on the SME Financing Data Initiative and access to statistical findings and reports, visit www.sme-fdi.gc.ca. For information regarding the methodology of the *Survey on Financing of Small and Medium Enterprises*, visit Statistics Canada's website at www.statcan.ca.

For further information on this article, email info@smefdi-prfpme.gc.ca.

### Reviewers

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