INDUSTRY

PROFILE

Industry, Science and Technology Canada
Industrie, Sciences et Technologie Canada

Trading Houses

Canada

INDUSTRY PROFILE

TRADING HOUSES

1988

FOREWORD

In a rapidly changing global trade environment, the international competitiveness of Canadian industry is the key to survival and growth. This Industry Profile is one of a series of papers which assess, in a summary form, the current competitiveness of Canada's industrial sectors, taking into account technological and other key factors, and changes anticipated under the Canada-U.S. Free Trade Agreement. Industry participants were consulted in the preparation of the papers.

The series is being published as steps are being taken to create the new Department of Industry, Science and Technology from the consolidation of the Department of Regional Industrial Expansion and the Ministry of State for Science and Technology. It is my intention that the series will be updated on a regular basis and continue to be a product of the new department. I sincerely hope that these profiles will be informative to those interested in Canadian industrial development and serve as a basis for discussion of industrial trends, prospects and strategic directions.

Robert de Cotret

Minister

1. Structure and Performance

Structure

Trading houses are firms which specialize in exporting and importing goods and services. Some provide a full range of services in management, marketing, shipping and financing for their international trading activities. Others act as merchants, agents, export consortia and co-operatives, buying houses and procurement agents or a combination of these businesses. These service companies rely on specialized contacts, knowledge and experience to assist their clients with all the techniques and mechanics of exporting.

Many goods-producing firms have neither the resources nor expertise to sell their products in international markets. This is especially true for small and medium-sized companies. By engaging a trading house, they can take advantage of the traders' network of overseas contacts, frequent trips to those markets, and skill in making successful sales for the client. Trading houses provide these firms with comprehensive export market development and sales services. This profile analyses only firms with a separate identified unit that specializes in trading in goods supplied by both related and non-related companies.

In Canada, trading houses fall into two broad categories — merchants and agents. Merchants actually take title to the goods which they buy and sell for profit. Fifty-six percent of income for small and medium-sized firms, and 60 percent of large company revenues are earned on a merchant basis, which is the riskier form of trading. Agents do not take title to the goods they handle, rather they charge the buyer or seller a commission or flat fee (and sometimes both) for their services. The small and medium-sized trading houses earn 30 percent of their annual income from commissions, while large firms earn 23 percent of their revenues.

A trading house may function as a merchant in some cases, and as an agent in others, depending on client requirements, the type of product, and the preference of the trading house in a particular situation. Most trading houses not only export, they also import and participate in third-country trade where they buy and sell in international markets. They offer services as diverse as financing, personnel development, training for specialized technical business operations, licensing negotiations, technology transfer, major project packaging, market identification and freight forwarding. Trading houses also serve as countertrade, offset or barter managers for their clients when these requirements are imposed by buyers. These trade requirements can be complex and difficult to satisfy, and can be insurmountable for companies trying to export their products. Trading houses, operating in global markets, are organized to help other firms meet these challenges.

Canada

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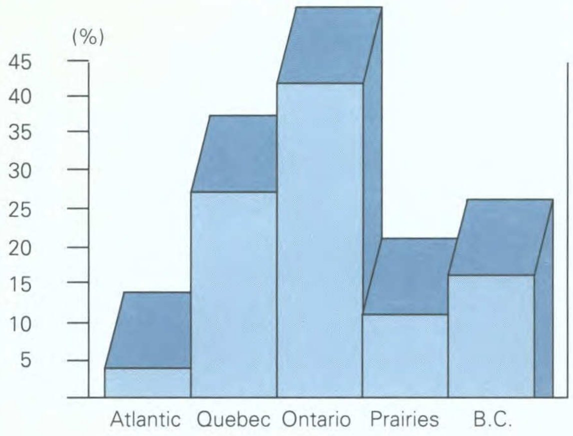


Regional Distribution of Firms — 1988
(Total firms 557)

In 1988, there were 557 active trading houses in Canada, averaging 26 employees each for a total employment of about 10 300, including about 2650 international traders. These highly skilled specialists travel overseas to market and negotiate sales for trading houses. Trading houses handled 15 percent of annual Canadian export sales, worth a total of $18.2 billion in 1987. Of total trading house sales, it is estimated that 62 percent are exported, 16 percent are sold in Canada (usually by the trading house itself), 14 percent are imported and eight percent are sold in third countries (not involving Canadian imports or exports).

In the Canadian industry, small and medium-sized companies are those with less than $50 million in annual revenue and large ones are those with more than $50 million. Eighty-five percent of large trading houses are concentrated in major Canadian business centres, with Ontario, Quebec and British Columbia accounting for 42, 27 and 16 percent respectively. This concentration enables staff to travel easily from international airports. They are also close to a large number of clients while still able to serve others across the country.

Alberta, Manitoba and Saskatchewan share 11 percent of the large trading houses, currently with four, three and one company respectively. The Maritimes have four percent of the national total with one firm in New Brunswick and three in Nova Scotia. There are 60 foreign-controlled trading houses in Canada, predominantly large ones from Asia and Europe, which include Japanese-owned multinational trading companies (Sogo Shoshas).

In some sectors, Canada has not developed large trading houses that provide a full range of marketing, exporting, shipping and financial services. In other countries, resource and commodity exports have traditionally provided a large volume base from which a trading house could grow. However, Canada's large commodity and resource firms, with their considerable international expertise, have tended to serve their worldwide markets directly, rather than use trading houses. Generally, these firms have tended not to diversify into the Canadian trading house business on a commercial basis. Therefore, Canada's largest export industry has not proved fertile ground for the development of diversified indigenous trading houses.

The global trading house industry is dominated by large, predominantly Asian, trading houses. Historically, they were developed as supply and distribution arms for a manufacturing company's goods, with heavy trading in commodity and resource products as well. In the past 40 years, however, these trading houses have diversified to offer their services to other firms on an arm's-length basis. They also engage in worldwide trading activities covering the full spectrum of agricultural and natural resource products, industrial goods and services. These large multinational general trading firms have thousands of employees. Their Canadian subsidiaries alone are staffed by several hundred employees. Their sales volumes are measured in billions of dollars, even for their Canadian operations.

A significant strength among the large foreign-controlled companies is their diverse corporate base. Many have grown out of huge businesses with a home production and distribution base, which they have expanded through international prospecting, mining, manufacturing, technical assistance, marketing and logistics. These foreign companies are major importers, shipbuilders, shipping line owners, and essentially their own bankers.

The small number of large Canadian-owned trading companies have also evolved from the primary producing companies' needs for international marketing expertise. Of the 24 largest trading houses in Canada, 11 are Canadian, nine are Japanese, and four are American.

The emergence of the large Canadian traders on the international scene is relatively recent compared to the long history of the nine huge Japanese trading conglomerates. Today, a growing number of indigenous trading houses offer diverse services to medium and small industrial firms which are unable to sustain international marketing and export trade on their own.

While exporting is their major focus, importing also provides a source of revenue to trading houses. Data on imports are not available.

About 40 percent of Canadian exports to non-U.S. destinations is handled by trading houses. Trading houses are used only to a limited extent in Canada-U.S. trade, accounting for only three percent of our exports there. Manufacturers usually handle exports themselves because the cultures are similar, the market is accessible, and transportation is readily available. By contrast, 78 percent of exports to Japan are handled by trading houses, largely because Japanese trading companies dominate. Discounting both U.S. and Japanese markets, this country's trading houses do 31 percent of Canadian exporting. On a world scale, Canadian trading houses do a significant amount of their exporting to South America (65 percent), Africa (47 percent), the Middle East (35 percent), and the European Community (E.C.) (34 percent).

Trading houses in Canada are both diversified and highly specialized. Large Canadian trading houses specialize in primary products — lumber, metals, minerals, chemicals and agricultural products. Examples of single-commodity firms include XCAN Grain, the co-operative exporter for non-Wheat Board grains in Manitoba; Saskatchewan and Alberta grain handling co-operatives; and B.C. Tree Fruits, the export agent for British Columbia's fruit producers.

Trading house exports consist of fabricated materials (41 percent); primary or crude materials (28 percent); food, feed, beverages and tobacco (28 percent); and end products (finished goods, three percent). Smaller firms (sales of less than $25 million per year) export 76 percent of finished manufactured goods, representing a wide range of products. Large firms (sales of more than $100 million) and medium-sized firms (sales of between $25 million and $100 million) handle one percent and five percent respectively of these exports. Large firms constitute nine percent of the industry, but are responsible for 87 percent of trading house exports. By contrast, 81 percent of trading houses are small (sales of less than $25 million) and account for six percent of trading house exports.

Performance

The Canadian trading house industry has gained strength over the past decade and this trend appears to be continuing. It is difficult to examine the industry over time because of a lack of statistics. However, 1979 trading house export transactions were found to constitute about 10 percent of total Canadian exports. This proportion grew to 13 percent in 1983, and is estimated at 15 percent for 1987. The number of trading houses also increased from about 400 in 1983 to 557 in 1988, while the average number of employees per company has remained stable.

Performance of a trading house depends on its ability to provide services to firms which rely on them for international business transactions. The knowledge, expertise and experience of traders are their most valuable assets. These intangible assets define the trading house as a service company.

The trading industry has developed in Canada for only 15 or 20 years compared to a much longer time in the Federal Republic of Germany (F.R.G.), Japan and France. This historical advantage of foreign competitors may have been one factor that has kept Canadian-owned companies from developing the global conglomerate structure of the Japanese Sogo Shoshas. However, trading houses in Canada account for 15 percent of total exports, and 31 percent of exports to all destinations other than the United States and Japan, compared to the trading houses' shares of exports from Germany and France, which are 30 percent and 25 percent respectively.

2. Strengths and Weaknesses

Structural Factors

The greatest strength of small and medium-sized Canadian-owned trading houses is their success in carving out specialized market niches for themselves, working on a modest scale with comparably sized suppliers of processed and finished products. Their large multinational competitors are not attracted to these niches because they are expensive to pursue, with an uncertain potential payoff in the long term on a scale large enough to complement their existing business. Large Canadian-owned firms also tend to concentrate on bulk and primary products.

Small and medium-sized Canadian-owned trading houses specialize in specific niches. Although finished goods make up only three percent of Canadian exports handled by trading houses, the small and medium-sized trading houses account for 81 percent of this total. Canadian small and medium-sized manufacturers are generally unfamiliar with trading houses and this has limited their participation in exporting finished goods. Successful trading houses of this size in other countries have stronger links to both manufacturers and government agencies, which enhance their credibility and potential to generate business.

There is a large potential market for the services of trading houses in Canada, because small and medium-sized manufacturing firms often experience major difficulties when attempting to export. They often lack the resources, both financial and human, as well as experience in foreign markets and expertise in export practices and techniques. Trading houses offer high-quality international marketing, finance, distribution and communication services, and can meet the needs of these manufacturers far more effectively than they can on their own.

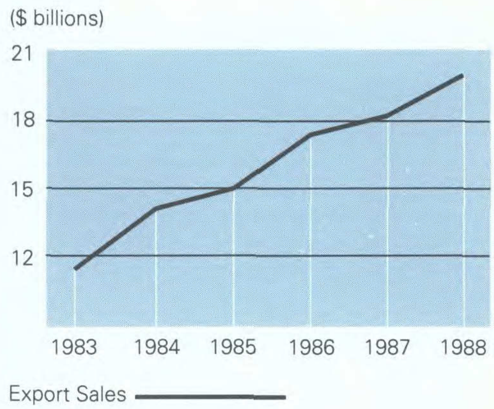
Trading houses also find it difficult to get the co-operation of manufacturers to modify products to satisfy customers abroad. Minor changes in colour, size and adaptations to cultural norms, especially in packaging, are often needed to secure an overseas sale. Resistance by manufacturers to alterations may reflect the general lack of stature and acceptance of trading houses in Canada as trusted partners in international marketing. As a result, Canadian trading houses have often identified markets which they are unable to supply from Canadian sources.

For trading houses firmly established in other countries, financing is also easier to secure because links between financial institutions and the trading house industry are well developed. In France and the United States, for example, banks hold equity positions in existing trading houses, have created new ones, and have entered into joint ventures with others. The Canadian industry is working to overcome a lack of profile among manufacturers, a short track record, and an absence of a tangible asset base. It is adopting a professional accreditation system and steadily developing credibility with government financing agencies and the broader financial community. The lack of tradition and history is as much a disadvantage to trading houses in the United States as it is in Canada.

Canadian-owned trading houses do not have diversified and complex corporate bases like those of the major multinational trading conglomerates. They are, therefore, at a disadvantage for overseas contacts, office support, communications, access to financing, and control of transportation and logistics.

The Canadian trading house industry also faces a challenge in finding competent staff. A joint industry-academic task force on Canadian international trade recently recommended more co-operation among business, post-secondary institutions and government as a way to increase the number of professionals skilled in international trade. Such expertise would make trading houses more capable and effective in worldwide trade, while building on their existing strengths. Improved language skills would also make skilled employees working in international markets more versatile. Language skills are repeatedly emphasized as crucial to successful international trade.

Canadian trading houses currently use sourcing and trade-lead services provided by the government. These services could be strengthened to take advantage of computerized services available in some foreign countries. Computerized systems provide traders with additional information from a variety of international sources on purchases being tendered around the world. Such systems foster international trade and include those produced by the British Overseas Trade Board and the U.S. Department of Commerce and Department of Agriculture.



Trading House Export Sales

Trade-related Factors

Trade restrictions such as tariffs and quotas can indirectly affect the volume of trade handled by trading houses. The implementation of the Canada-U.S. Free Trade Agreement (FTA) will benefit trading houses, particularly through the provisions for national treatment, access of personnel, and the standstill on further non-tariff barriers (NTBs). These provisions, as well as tariff-free access for goods, will benefit trading houses as constraints are relaxed and trade is encouraged.

The NTBs identified as irritants include barriers to the mobility of personnel, currency controls, foreign exchange constraints, import restrictions (quotas), import registration and regulation, export permits, and government procurement procedures, monopolies and subsidies. The foreign exchange issue can sometimes cause a country to avoid a market because the debt level constitutes too high a risk. In other cases, currency regulations necessitate countertrade, offsets or barters and other complex trade negotiations which are also more risky.

Canadian agencies, such as the Export Development Corporation (EDC), the Canadian Commercial Corporation (CCC) and the Canadian International Development Agency (CIDA), have significant roles to play in this industry, particularly as their programs have been modified recently to facilitate activities of trading houses. These programs would be more effective if agencies registered more trading houses, did more to promote the trading house option, and achieved faster turnaround times so that trading houses can enter into overseas negotiations more quickly.

Technological Factors

Technology makes trading house operations more efficient and speeds up communication and capabilities to deliver export services. Trading houses now use computers, telex and facsimile equipment and telephones for constant, rapid communication with suppliers and clients. The ability to exchange timely information is critical to the competitiveness of the industry. It is, therefore, vital for trading houses to keep abreast of advances in international telecommunications.

Electronic Data Interchange (EDI), the electronic transmission of business information, simplifies the communication of all contract and shipping details of a trade deal. Private and public sectors are now working to standardize EDI — an important step to keep systems simple and compatible enough so that they are accessible and affordable to small companies. Application of this technology undoubtedly will be important in speeding international trade transactions and reducing the inefficiencies and inaccuracies of paper tracking systems.

Other Factors

The current exchange rate between Canada and the United States has had a positive impact on American trade. Since 1985, currency realignments affecting Canadian and U.S. dollars relative to European and other foreign currencies have also had a positive effect on trade with Canadian offshore markets.

3. Evolving Environment

Over the past five years the trading house industry has grown both in the number of companies and its share of exports. Its growth is expected to continue. The need to find new offshore markets and to achieve greater economies of scale and other efficiencies, will likely encourage more exporters to seek trading house services to develop new markets and execute sales. Recent international economic development forecasts indicate that the opportunities will be greatest in developing countries, especially in Asia and Latin America. Strengthening prices for minerals, agricultural raw material and some commodities should provide strong opportunities for trading houses. Food and manufactured goods are expected to continue to offer good prospects for expanded trade. Additional opportunities also exist in Japan and the F.R.G.

The FTA is expected to increase the flow of products between Canada and the United States as tariffs are eliminated. Companies are generally expected to become more efficient, competitive and export-oriented. Canadian goods producers who do not currently export may begin to look for new markets in the United States. The extent to which this effort will translate into new business for trading houses is not clear. Despite improved ease of access to U.S. markets, small and medium-sized companies may use trading houses where they lack the trade contacts, expertise, experience and internal resources. Overall, the FTA is not expected to have a major impact on the trading industry because the U.S. market has not been a major market for trading houses.

Further liberalization of trade in the multilateral GATT negotiations (MTN) would create greater opportunities for Canadian exports. Trading houses would also benefit if NTBs that affect trade in services were reduced as a result of the MTN. Overall, tariff and non-tariff reductions as well as NTB negotiations are expected to have a positive effect on trading house business internationally.

4. Competitiveness Assessment

Small, medium and large Canadian-owned trading houses are competitive in the market and product niches in which they have specialized. Unlike multinational global trading companies, they have not developed comprehensive export development, consulting, management, documentation, licence negotiation, packing and shipping, and financing services to a significant degree. Canadian trading houses are unlikely to take market share away from the global trading conglomerates.

In the near term, many trading houses will also be held back by a shortage of skilled personnel to form the basis for business expansion, the lack of scale and financial resources, and underdeveloped links to the manufacturing industries. Nevertheless, as the industry concentrates on its strengths (specialized scope, expert international trade and marketing skills, and strong entrepreneurial initiative) it is likely to continue to succeed and grow. Recent collaboration between resource-based firms and trading houses may result in consortia, established specifically to take advantage of each other's strengths.

The FTA will strengthen the trading house industry modestly by encouraging more Canada-U.S. trade. Small and new exporters may use the services of trading houses. However, because of the similarities between the Canadian and U.S. markets, many exporters may choose to do the trading themselves.

For further information concerning the subject matter contained in this profile, contact:

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Industry, Science and Technology Canada
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(613) 954-2964

PRINCIPAL STATISTICS — SIC(s) COVERED: N/A

	1983	1984	1985	1986	1987	1988
Establishments	N/A	401	N/A	414	477	557
Total staff	N/A	6 000	N/A	N/A	9 703	10 291
Trade staff[1]	N/A	N/A	N/A	N/A	2 487	2 643
Trading house export sales ($ billions)	11.4	14.2	15.0	17.5	18.2	20.1*

TRADE STATISTICS

	1983	1984	1985	1986	1987	1988
Total Canadian exports ($ billions)	88.1	109.5	116.1	116.5	121.5	134.2*
Trading house export sales (% of total export sales)[e]	13	13	13	15	15	15

Destination of total Canadian exports ($ billions)		U.S.	E.C.	Asia	Others
	1983	64.2	6.6	10.0	7.3
	1984	82.7	6.9	11.4	8.5
	1985	90.4	6.7	11.2	7.8
	1986	90.2	7.8	11.2	7.3
	1987	91.8	9.1	12.3	8.3
	1988*	98.2	10.5	16.3	9.2

REGIONAL DISTRIBUTION — 1988

	Atlantic	Quebec	Ontario	Prairies	B.C.
Establishments – % of total	4	27	42	11	16
Employment – % of total	5	24	49	6	16
Exports* – % of total	6	16	49	16	13
Trading house export sales* – % of total	1	3	10	3	3

(continued)

MAJOR FIRMS

Name	Ownership	Location of Major Firms
Agricultural and Food Commodities		
Agro Company of Canada Ltd.	American	Montréal, Quebec
British Columbia Tree Fruits Ltd.	Canadian	Kelowna, British Columbia
Canada Packers Inc. International Trade Division	Canadian	Toronto, Ontario
Cargill Ltd.	American	Winnipeg, Manitoba
C. Itoh & Co. (Canada)	Japanese	Toronto, Ontario
Clouston Foods Canada Ltd.	Canadian	Lachine, Quebec
Continental Grain Co. Ltd.	American	Winnipeg, Manitoba
Fishery Products International	Canadian	St. John's, Newfoundland
Louis Dreyfus Canada Ltd.	American	Winnipeg, Manitoba
Marubeni Canada	Japanese	Toronto, Ontario
National Sea Products Ltd. Intl. Marketing	Canadian	Halifax, Nova Scotia
Northern Sales Co. Ltd.	Canadian	Winnipeg, Manitoba
Northam Food Trading Incorporated	British	Montréal, Quebec
Okura & Company Canada Ltd.	Japanese	Vancouver, British Columbia
Ronald A. Chisholm Limited	Canadian	Toronto, Ontario
Toshiba of Canada	Japanese	Toronto, Ontario
Forest Products, Metals and Minerals		
Canpotex Limited	Canadian	Saskatoon, Saskatchewan
Cansulex Limited	Canadian	Vancouver, British Columbia
Foralix Export Canada Inc.	Canadian	Westmount, Quebec
Green Forest Lumber Ltd.	Canadian	Toronto, Ontario
Lignarex Inc.	Canadian	Sainte-Foy, Quebec
Noranda Forest Sales Inc.	Canadian	Toronto, Ontario
Philipp Brothers (Canada) Ltd.	Canadian	Toronto, Ontario
Plant Forest Products Corporation	Canadian	Vancouver, British Columbia
Thyssen Canada Limited	Canadian	Rexdale, Ontario
Universal Paper Export Co. Ltd.	Canadian	Montréal, Quebec
General Trade		
BHP Trading Canada Ltd.	Canadian	Vancouver, British Columbia
Blue Sky Corporation	Canadian	Vancouver, British Columbia
D.H. Howden	Canadian	London, Ontario
Guillevin International Inc.	Canadian	Mississauga, Ontario
Kanematsu-Gosho (Canada) Inc.	Japanese	Mississauga, Ontario
Ladimex Inc.	Canadian	Westmount, Quebec
Mako Enterprises Ltd.	Canadian	Vancouver, British Columbia
Maritime Group (Canada) Inc.	Canadian	Vancouver, British Columbia
Mitsubishi Canada Ltd.	Japanese	Toronto, Ontario
Mitsui & Co. (Canada) Ltd.	Japanese	Toronto, Ontario
Nissho Iwai Canada Ltd.	Japanese	Vancouver, British Columbia
Norplast Inc.	Canadian	Vancouver, British Columbia
Samsung Company Ltd.	Korean	Toronto, Ontario
Sumitomo Canada Limited	Japanese	Vancouver, British Columbia
Tenpro International	Canadian	Burnaby, British Columbia
The East Asiatic Company (Canada) Inc.	Danish	Vancouver, British Columbia
The Oduro World Enterprises	Canadian	Winnipeg, Manitoba
Toyomenka Canada Ltd.	Japanese	Vancouver, British Columbia

* Estimates for the full year of 1988 were based on Statistics Canada data for the period of January through November.

e Trading house export sales have been estimated, based on 1984 Trading House Task Force Report and 1988 industry consultations by ISTC.

N/A Not available

1 Trade staff is personnel active in international marketing.

Note: 1984 data are from the External Affairs' (EA) 1984 Trading House Task Force Report *Promoting Canadian Exports: The Trading House Option*, data for subsequent years are from ISTC internal analysis based on industry consultation, ISTC Business Opportunities Sourcing System (BOSS), and Statistics Canada trade figures.

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