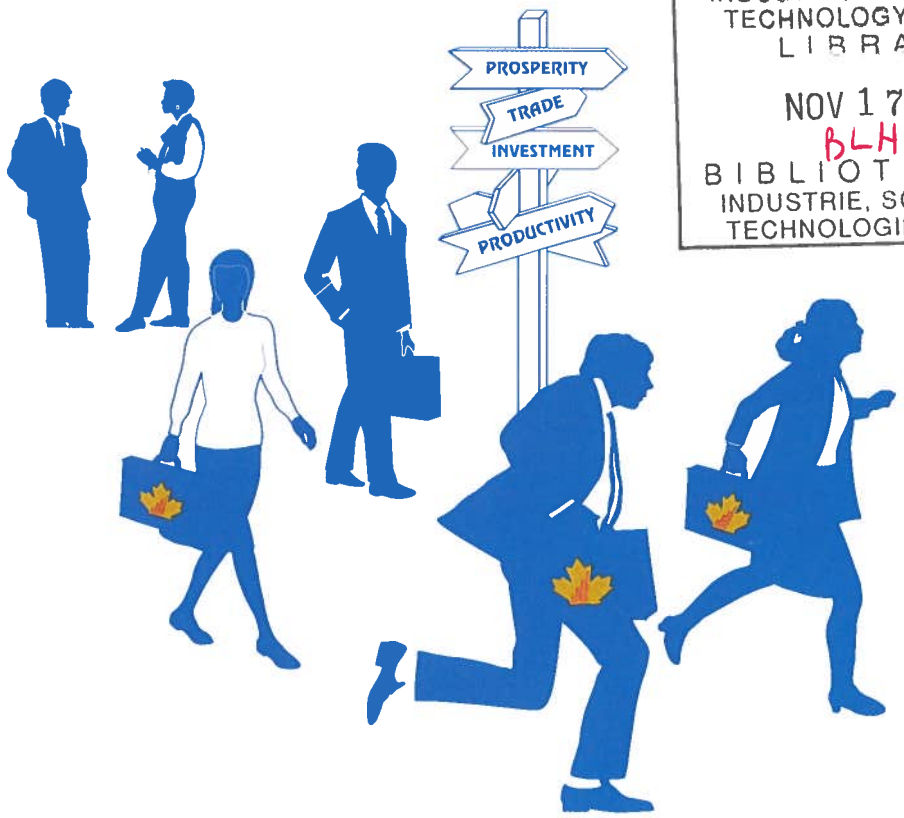
INVESTING IN CANADA

A NEWSLETTER ON CANADA'S INVESTMENT CLIMATE

Vol. 5, No. 1 – Summer 1991

THE COMPETITIVE IMPERATIVE



Globalization is the driving force behind international competitiveness. The global economic, political and business orders are all undergoing significant changes. There is growing interdependence among consumers, producers, suppliers and governments, but also increasing competition between countries, and between corporations.

In this issue we focus on competitiveness, a subject that is generating considerable concern and speculation, as there are indications that Canada is falling behind. Our feature article discusses the different aspects of competitiveness, and reports on research that Investment Canada has undertaken.

For those Canadian firms searching for investment partners abroad in order to increase their competitive edge, we offer some helpful hints excerpted from a publication about planning your first international investment trip.

The 1980s could well be described as the decade of the multinationals. These international companies led the way to an unprecedented increase in the extent of international direct investment. Between 1980 and 1987, direct investment abroad grew at a faster rate than world trade (see Graph 1), which itself grew at a faster rate than world output.

There is a clear imperative driving corporations to invest abroad: it is no longer sufficient for companies to sell within a secure and protected market. With trade and investment barriers falling, companies need to be competitive both in their domestic markets and abroad.

Corporations adopting global strategies have also recognized that trade and investment are largely complementary, and that the nature of competition in most business sectors today requires greater commitment and resources than those necessary for a sales operation.

Canadian competitiveness is the subject of much speculation and concern. While there have been private sector studies on competitiveness, the government has also been addressing this issue. Michael Wilson, the former Minister of Finance, spoke of the challenge of ensuring Canada's prosperity in his Budget Speech of February 26, 1991.

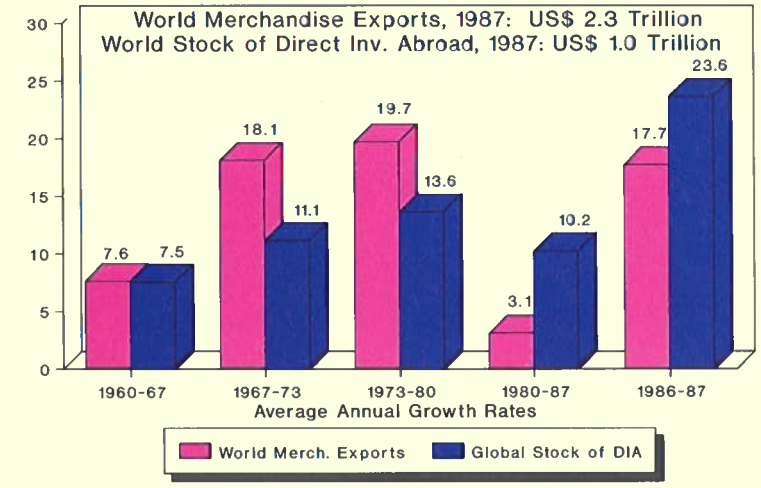
(p. 2) ▼

INSIDE THIS ISSUE

INVESTMENT CANADA INVESTISSEMENT CANADA

THE COMPETITIVE IMPERATIVE ▲ (cont'd from p. 1)

GRAPH 1:
Aspects of Globalization:
(%) Growth in World Trade and Direct Investment Abroad (DIA)



Source: U.S. Dept. of Commerce & Int. Monetary Fund.

Stating that in an increasingly competitive world, "there is no room for complacency and there is no safe hiding place for uncompetitive industries and countries", Wilson announced that as a first step the government would be releasing a discussion paper to help focus public debate toward the building of broader consensus on the problems and the development of solutions.

WHAT IS COMPETITIVENESS?

Any discussion of competitiveness, however, raises questions such as the definition of competitiveness and why is it so important for Canada. This article does not purport to have all the answers to these questions. Rather, it provides an accepted definition of competitiveness, examines a recent study on international competitiveness, and reports on research that Investment Canada has undertaken on competitiveness.

What is meant by competitiveness? Perhaps the most complete definition is that provided by the U.S. President's Commission on Industrial Competitiveness in 1985, when it described the competitiveness of a nation as "the degree to which it can, under free and fair market conditions, produce goods and services that meet the test of international markets while simultaneously maintaining and expanding the real income of its citizens".

With such a definition, success in a competitive environment is measured not only by trade figures, sales or market shares, but also by living standards. This in turn implies that competitiveness depends upon productivity growth, which is the driving force behind increased living standards.

CANADA FALLING BEHIND

One reason competitiveness has become such an issue recently is that Canada's international competitiveness appears to be regressing (see Graph 2). The 1990 issue of the World Competitiveness Report, a yearly publication by the International Management Development Institute and the World Economic Forum, shows Canada slipping from fourth to fifth place in the overall ranking of international competitiveness of the OECD countries.

Additionally, the distance between Canada and the leaders among developed countries in competitiveness—Japan, Switzerland, the United States and Germany—has increased. In other words, Canada is falling behind. While other countries have improved their competitive positions, Canada's has continued at more or less historical levels.

The international ranking in the Competitiveness Report is constructed from a set of 326 criteria on competitiveness covering a wide range of factors. These have been selected on the basis of their relevance and the availability of comparable statistical data. Some criteria have an immediate bearing on current competitiveness (labour costs, for example). Others have a more long-term impact (such as research and development spending).

Some criteria are based on the natural endowments of the country (the quantity and quality of its natural resources), while others (such as labour productivity) have been developed over time by the business community and the public sector. Taken together, these 326 criteria provide broad and comprehensive coverage of the overall competitiveness of each country.

Canada's slippage in relative position is a matter for concern. The country's ability to provide a rising standard of living for its citizens depends upon its comparative international competitiveness. The challenge facing Canada is quite clear-cut. With Canadian competitiveness slipping, it is necessary to pinpoint the factors that have influenced both the past and present performance of Canadian productivity and its related costs, and to identify the changes that must be put in place if Canada is to improve its chances for success on world markets. (p. 3) ▼

THE COMPETITIVE IMPERATIVE ▲ *(cont'd from p. 2)*

INVESTMENT CANADA STUDIES

Investment Canada is involved with two studies concerning aspects of Canadian competitiveness. The first is a study done for Investment Canada by David Slater, past Chairman of the Economic Council of Canada, and a respected authority on macroeconomic policy.

Dr. Slater, whose paper will be a part of the Investment Canada Working Paper series, examines the nature and scope of the linkages between national investment and savings efforts, and productivity and economic growth. Theoretically, high levels of investment savings and capital formation should be associated with periods of high productivity and economic growth.

Dr. Slater's research indicates that investment effort is a necessary, but not sufficient, condition for productivity and economic growth. Improvements to investment and savings efforts must be part of a multifaceted effort to increase Canadian productivity and economic potential, along with other important factors such as innovation, skill development, capacity utilization and market access.

The results highlight the fact that there is no panacea for raising Canada's productivity and economic growth. A wide variety of measures are needed, of which greater investment and savings will clearly be a part.

Investment Canada is also participating in a study that the Economic Council of Canada is undertaking on the complex issue of Canada's competitiveness relative to its major trading partners. The Economic Council's study singles out different aspects of international competitiveness, including labour productivity, total factor productivity (TFP)—which measures the overall productivity of the production process—hourly compensation rates, the level and variability of nominal and real exchange rates, the use of technology, research and development, innovation, capital accumulation, quality of the workforce, quality of management, and the role and influence of multinationals in the country's economy.

MULTINATIONAL ENTERPRISES

The joint Investment Canada-Economic Council project concerns the final topic: the role and influence of multinational enterprises (MNEs) in Canada's economy. Investment Canada's mandate makes it a logical choice to assist the Economic Council in examining how MNEs help to shape Canada's international competitiveness. The study will be done in two phases.

The first phase, which is near completion, examines the role of foreign MNEs in Canada between 1985 and 1988. Phase two of the study will be devoted to analyzing the impact on competitiveness of Canadian-owned MNEs operating in Canada and the rest of the world.

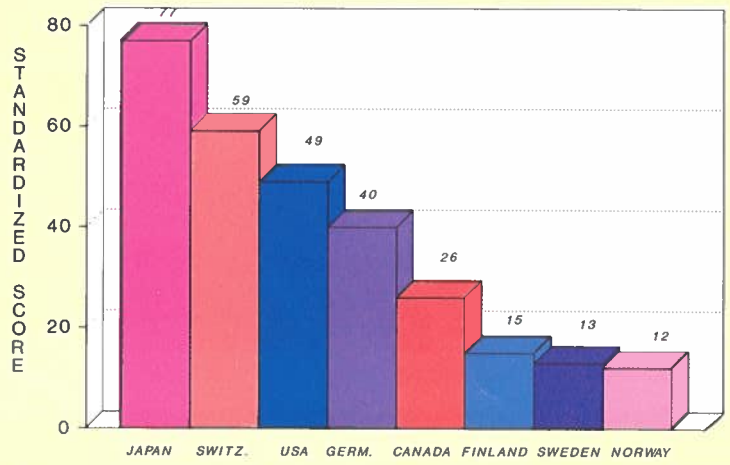
The reason for this study is the immense importance that foreign multinationals have for the Canadian economy, and therefore for Canadian competitiveness. Any study of Canadian competitiveness would not be complete without an analysis of the influence of MNEs, which constitute a crucial link between trade, capital and technology flows.

MNEs collectively account for the vast majority of Canada's total exports and imports, and their importance to Canada in world trade has been increasing. The activities of MNEs also contribute heavily to cross-border capital flows of inward and outward foreign direct investment.

TECHNOLOGY TRANSFER

Finally, there is the vital connection between MNEs and technology transfer. It is prohibitively expensive for Canada, as a small country, to develop leading-edge technologies across a wide range of economic activities. The adoption of technology from multinationals investing in Canada is crucial for Canadian industry. *(p. 4)* ▼

GRAPH 2:
OVERALL COMPETITIVENESS SCOREBOARD



Source: World Competitiveness Report 1990, p.13

THE COMPETITIVE IMPERATIVE ▲ *(cont'd from p. 3)*

Competitiveness is used exclusively in its microeconomic sense as a compact reference to both productivity and trade performance in the joint Investment Canada-Economic Council study. The significance of productivity and trade performance comes from their effects on the level and distribution of the real incomes of Canadians. Higher productivity makes it possible to produce more outputs with fewer resources, thereby allowing Canadians to consume more goods and to sell more abroad.

International trade makes it possible to specialize in the production of certain goods for which Canada has a comparative advantage, while importing others at lower cost. Efficiency in production and trade performance leads to higher standards of living for Canadians. Weaker performances in these areas have negative effects on the living standards of Canadians.

LABOUR PRODUCTIVITY

The concepts of productivity, trade performance and real income are often defined in different ways by different commentators. This study adopts labour productivity (the amount of value-added created by each worker) as the appropriate definition of productivity. This definition is both more reliable and easier to calculate than other definitions, such as total factor productivity.

Labour productivity is a function of two basic factors. The first is the amount of inputs, such as capital and energy, that are used along with labour in the production process. Other things being equal, a worker who uses a great deal of machinery to produce a given output will have a higher productivity than a worker who does not.

How Canada Stacks Up

	1990 Rank	1989 Rank	1986 Rank
Dynamism of the economy	5	3	7
Industrial efficiency	13	4	8
Market orientation	5	4	7
Financial dynamism	10	11	7
Human resources	3	2	4
Impact of the state	6	3	8
Natural endowments	2	2	3
International orientation	15	14	12
Future orientation	16	15	9
Socio-political stability	8	6	7
Overall Rank	**5**	**4**	**7**

The second factor is the efficiency with which inputs are used in the production process. A plant that possesses superior technology, management skill or larger size is likely to have a higher labour productivity. Government policies, such as tariffs that protect firms from foreign competition, are also important determinants of the efficiency of production. The study attempts to assess the importance of each of these factors in determining the labour productivity of foreign and domestically-controlled firms.

TRADE PERFORMANCE

The different definitions of trade performance can be even more confusing than those of productivity. Some commentators focus exclusively on exports, others look only at imports. By contrast, the Investment Canada-Economic Council of Canada study looks at how multinationals shape both sides of the same international trade coin. This recognizes the fact that greater exports allow a country to consume more imports, and that both exports and imports lead to higher living standards.

Efforts to improve Canadian competitiveness will be a major issue in Canada in the coming years. Given the increased importance of investment, issues such as the effect improvements to investment and savings efforts will have on productivity and economic potential, and the role of MNEs in shaping Canada's international competitiveness, must be examined. Investment and increased competitiveness will of necessity continue to be linked together.

– *Geoff Nimmo, Investment Canada*

Geoff Nimmo is a senior policy analyst with the Investment Research and Policy Division.

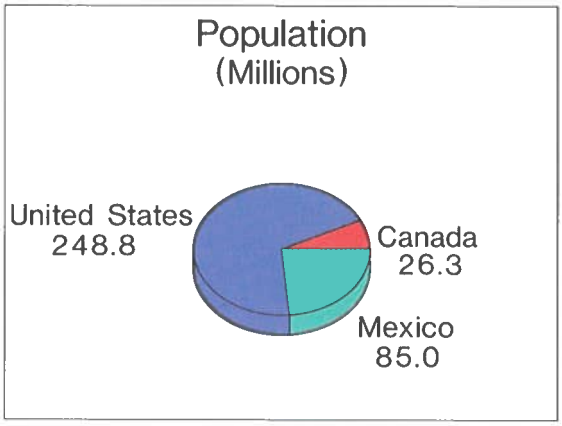
NORTH AMERICAN FREE TRADE AGREEMENT

In a world of increasing competitiveness, our challenge is to ensure that Canada's productivity stays among the highest in the world. A North American Free Trade Agreement (NAFTA) will contribute towards this goal, perhaps modestly at first, but increasingly as our ties with Mexico grow, according to a report released May 1, 1991 by Investment Canada. The three countries commenced formal negotiations this June.

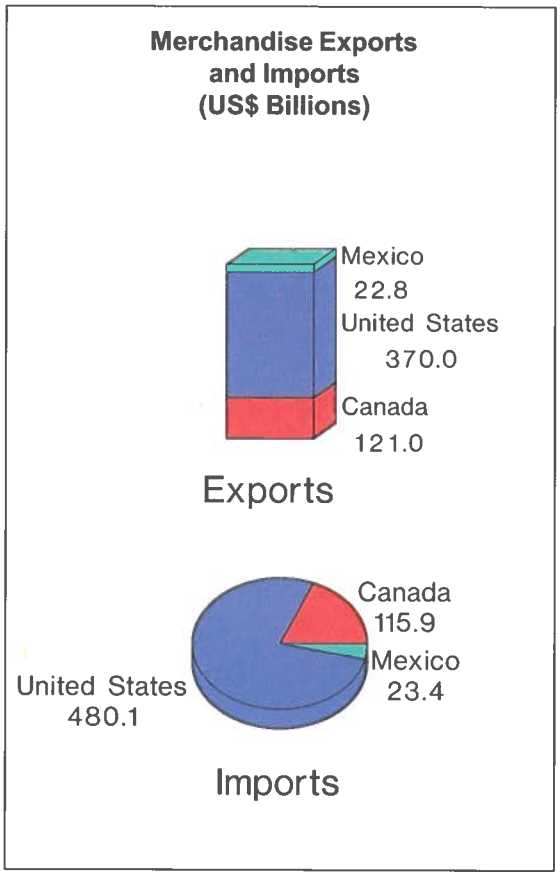
Trilateral free trade will result in much closer and stronger involvement by Mexico in the North American economy, opening up a major new export market for Canada at minimal risk to either domestic sales or our U.S. export market. The report presents "detailed trade and investment data germane to a better understanding of the opportunities and challenges of a NAFTA."

Following the implementation of a NAFTA, Canada would concentrate more on high-skill, high-wage jobs, "where we enjoy a comparative advantage. Mexico, with its abundance of low-skill labour, would concentrate more on labour-intensive activities. In all three countries, business would operate more efficiently and consumers would benefit from greater choice and more competitively priced goods and services."

"Most of Canada's imports from Mexico already enter duty-free, or at relatively low duties. Trade liberalization will not, therefore, result in Mexico overwhelming Canada with a rush of low-cost products," the report states. Mexico, on the other hand, could become a rapidly growing export market for Canada. By the end of the decade, Mexico will have a population of approximately 100 million and its import requirements will be considerable.



Investment Canada's analysis focuses particular attention on Canadian and Mexican competition for the U.S. market, for it is here that Canadian interests would initially be most at stake, whether or not Canada participates in the negotiations. A large part of Canadian exports to the United States would be unaffected by a NAFTA, either because there is no Mexican equivalent or because Mexican exports already enter the United States at very low tariff rates or at tariff rates roughly equivalent to those faced by Canadian exports to the United States.



In some important sectors (automotive, steel, and textile and apparel industries), the competition is already intense and would increase as a result of free trade. Even where markets overlap, however, a NAFTA would simply reflect trends that are already occurring.

The report concludes by noting that expansion of Canada's exports to Mexico, and greater openness to Mexican exports both in Canada and the United States, would be accompanied by greater trilateral investment. To realize new productivity and job opportunities, Canadians would have to be prepared to invest more heavily, both at home and abroad. A trade strategy that taps into the possibilities in Latin America must be supported by business investment strategies. Given the cultural differences and geographic distance, considerable effort by the business sector will be needed to nurture the appropriate commercial ties with Mexico. If this effort is made, the report notes, the long-term opportunities for Canada can be immense.

Copies of the report are available, in English or French, from:

Investment Research and Policy
Investment Canada
P.O. Box 2800
Station D
Ottawa, Ontario
K1P 6A5
Tel: (613) 995-9603
Fax: (613) 996-2515

LOOKING FOR INVESTMENT PARTNERS ABROAD:

YOUR COMPANY PROFILE

- ✓ Basic identifying material about your company such as corporate name, address, telephone, facsimile and telex numbers
- ✓ A brief summary of your product and/or service lines
- ✓ A brief history of the business to date, including current ownership, predecessor companies or other relevant information
- ✓ Names of officers and directors of your company, including business and professional biographical sketches
- ✓ The number of people employed and their major areas of activity
- ✓ A summary of financial information including sales by major product/business lines or areas of activity

YOUR BUSINESS PLAN

- ✓ A description of your company's products, processes or services and the technology involved
- ✓ Business history
- ✓ Organization chart
- ✓ Résumés of senior executives
- ✓ The characteristics that make your products or services competitive
- ✓ Research and development activities
- ✓ A financial statement which demonstrates the performance and strength of your company, and projections. It should point to what others have invested in your firm
- ✓ Market information such as your current market size, growth projections, customer profiles, sales forecasts, pricing, distribution methods, promotions, etc.
- ✓ A review of existing competition, including an evaluation of their products, pricing and market share
- ✓ The methods by which you produce your product or deliver your services
- ✓ A description of your requirement (capital, technology or a partner)

Are you contemplating a business mission abroad? Reaching out for foreign capital and partners is part of the process of adapting to the highly-competitive global marketplace. For many Canadian companies such links are a means of enhancing their operations. The following was excerpted from "Looking for Investment Partners Abroad: Planning Your First International Investment Trip," published under the federal government's Investment Development Program.

The key for such a business mission is adequate planning and preparation. Begin by asking yourself the following:

- ❒ Have you fully investigated what is available in Canada?
- ❒ Are you prepared to commit the time and resources? Finding capital, technology or partners abroad demands an intensive effort, often requiring several trips.
- ❒ Are you ready to deal with the language and cultural differences in your target market?
- ❒ Are you familiar with the business practices in your target market?
- ❒ Do you know whom to approach?
- ❒ Should you engage an intermediary?
- ❒ Do you know which companies to contact, and how to verify their reliability, performance, technology and management?

SOURCES OF ADVICE IN CANADA

- Canadian business associations
- Businesses that have been there
- Legal and financial firms
- Foreign embassies in Canada
- Libraries, universities, community colleges
- Federal business service centres
- Trade and investment departments of provincial and territorial governments

PLANNING YOUR FIRST INTERNATIONAL INVESTMENT TRIP

CANADIAN MISSIONS ABROAD

Most Canadian Missions and provincial trade offices abroad have investment counsellors to help you make contacts, provided they have sufficient notice and documentation. Write to the Canadian Mission in the country, or U.S. region, you have selected. Introduce yourself and your intentions and enclose an itinerary and documents described herein. We recommend your first letter be sent at least three months in advance of your proposed trip.

We also suggest sending a copy of your letter with enclosures to Investment Canada. Investment Canada was created by the federal government to attract business investment to Canada. It works closely with the investment counsellors at Canadian Missions around the world, helping international investors examine investment opportunities in Canada, and helping Canadian companies establish links with potential sources of capital, technology or partnerships.

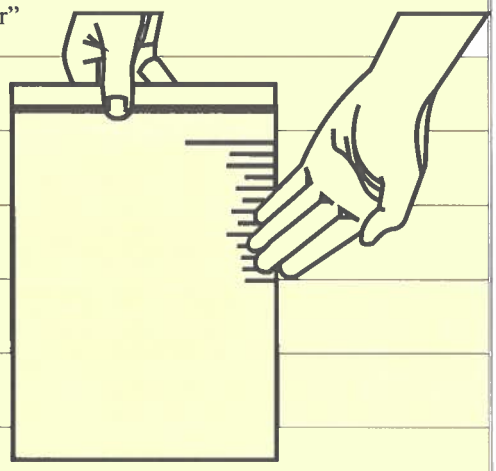
TRAVELLERS' TIPS

- Arrange your itinerary to avoid holidays, feast days and other special periods.
- If you are planning to rent a car overseas, get an international driver's licence before you leave Canada, available from the Canadian Automobile Association.
- Know the normal work hours of destination country, business etiquette, attire, and business and cultural practices.
- Avoid the pitfall of making your schedule too tight. Allow time for jet-lag, traffic, etc.
- Choose a hotel close to the Canadian Mission or companies you intend to visit.

PRE-DEPARTURE CHECKLIST

SUPPORT MATERIALS

- ❒ Business plan or proposal
- ❒ The investment you seek
- ❒ "What's in it for the investor"
- ❒ Company profile
- ❒ Business cards
- ❒ Letters of introduction
- ❒ Complimentary gifts
- ❒ Photograph album
- ❒ Letterhead/stationery
- ❒ Product samples
- ❒ AV projector and slides
- ❒ Compact sound recording unit to record decisions and follow-up actions (check compatibility with local power supply)



TRAVEL DOCUMENTS

- ❒ Valid Canadian passport
- ❒ Visas or entry permits required by destination country
- ❒ Immunizations required by destination country
- ❒ Certificate of vaccinations
- ❒ Confirmed airline and hotel reservations
- ❒ International driver's licence (if you plan to rent a car)

PROSPECTING AT INVESTMENT CANADA

The Investment Prospecting Group was created in May 1989 to assist small and medium-sized Canadian companies in technology-intensive sectors to attract the capital needed for continued growth through equity investments, joint ventures or strategic alliances. In addition, the Group works to convince medium-sized foreign firms in technology-intensive sectors, poised to enter the North American market, that their best entry point is through Canada.

As a result of the Group's work, Shield Diagnostics of Scotland entered a joint venture, in January 1991, with Apotex Scientific (Toronto) for the production of Shield's diagnostics for the North American market. Shield is a high-growth company in the human diagnostic field of biotechnology with proprietary technology for testing for urinary tract infection, and has several new diagnostics in the development pipeline. Apotex has a subsidiary diagnostic company in Toronto (NCS Diagnostics) and a laboratory/diagnostics firm in Arlington, Texas. Production will be in Toronto.

Another example is Medipro Sciences Ltd., a small Canadian company which has developed novel dressings for second and third degree burns and other serious skin wounds. S.S. Pharmaceutical of Japan has taken an equity position in Medipro and the rights for distribution of its products in the East.

Investing in Canada is published quarterly by Investment Canada, the investment development agency of the federal government. The mandate of Investment Canada is to promote investment in Canada, by both Canadians and non-Canadians; to carry out research and provide policy advice on investment matters; and to review major foreign investments to ensure they are of net benefit to Canada.

Editor-in-Chief – Richard Bégin
English Writer/Editor – Lillian Rukas
French Writer/Editor – Vincent Beaulieu
Production – Bernard Cossais
Publishing Officer – Suzanne Le Blanc

Investing in Canada
P.O. Box 2800, Station D
Ottawa, Ontario K1P 6A5
Tel: (613) 995-9525
Fax: (613) 996-2515

The Japanese company, which owns a network of over-the-counter chain drug stores, is the second largest firm of its type in Japan. To date, its primary focus has been on generic drugs for the domestic market. More recently, it has expanded its R&D operations and has been giving greater thought to export opportunities.

Both projects involved the use of independent sector experts to work both with Canadian and foreign firms, and collaborative efforts with Canada's missions abroad, other federal departments and agencies and provincial organizations.

Projects designed to address Canadian investment needs, such as that illustrated by the Medipro case, typically involve four stages:

1. Identifying Canadian investment needs/ opportunities in a sector. This takes the form of profiling Canadian firms and research institutes;
2. Developing an investment prospecting kit, which includes the profiles and an overview of the advantages of doing business in Canada;
3. Identifying foreign firms/investors well-positioned to meet the identified needs;
4. Follow-up both in Canada and abroad aimed at bringing together pre-screened foreign and Canadian companies.

Projects designed to attract foreign firms poised to enter the North American market, such as that illustrated by the Shield Diagnostics case, have a similar methodology. They involve independent private sector experts, are collaborative in nature, and involve most of the steps outlined above. The difference is there is no profiling of Canadian firms or research capabilities.

In its efforts to increase Canada's competitive edge, the Prospecting Group has ongoing projects in artificial intelligence, biotechnology, food packaging, industrial waste-water, medical device, oceans, optoelectronics, and software products sectors. For further information contact:

Dr. C. Farina, Director
Investment Prospecting Group
Investment Canada
P.O. Box 2800
Station D
Ottawa, Ontario K1P 6A5
Tel: (613) 995-0306
Fax: (613) 996-2515