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SELLING BEYOND THE U.S.

Do Recent Immigrants Advance Canada's Export Agenda?

At a Glance

- Analysis of more than 15,000 Canadian small and medium-sized enterprises (SMEs) shows that those with a majority owner who is a recent immigrant are more likely to export than other businesses, and are particularly more likely to export to non-U.S. markets.
- Non-U.S. exporting businesses with an immigrant majority owner are among the fastest-growing Canadian SMEs, but are less operationally efficient than other exporting businesses.
- Among recent immigrants who export, knowledge-based immigrant exporters represent the strongest potential in non-U.S. markets.

EXECUTIVE SUMMARY

In the face of a protracted stagnant Canada–U.S. trade relationship, Canadian businesses of all sizes are being encouraged to target fast-growing markets in developing countries. However, a major concern is that they may be hampered by their limited foreign language skills and cultural knowledge, as well as their lack of trusted relationships and knowledge of how to do business in these markets. However, commentators and policy-makers suggest that these barriers are not insurmountable because Canada has a diverse pool of immigrants upon which it may draw. Still, despite significant immigrant flows from source countries such as China and India over the last decade, Canada's trade remains largely concentrated in the United States. This raises a fundamental question: Do recent immigrants directly contribute to Canadian export activity?

To address this question, we investigate the export orientation of over 15,000 Canadian SMEs. Specifically, we test the hypothesis that Canadian SMEs with a majority owner who is a recent immigrant are more likely to export to non-U.S. markets, compared with Canadian SMEs owned by non-immigrants or immigrants who have lived in Canada for more than five years. We also examine the growth rates, profitability, access to business networks and financing, and industrial and geographic concentrations of exporting SMEs, comparing those owned by recent immigrants with other businesses. In doing so, our analysis provides new evidence about the export orientation of businesses owned by recent immigrants, and also offers new insights into their strengths and weaknesses. Therefore, this study provides a solid platform for the formulation of coherent export promotion policies as it relates to immigrants in Canada.

RECENT IMMIGRANT BUSINESS OWNERS ARE MORE LIKELY TO EXPORT OUTSIDE THE U.S.

When choosing between the Canadian market and non-U.S. markets, we found that recent immigrant business owners are 1.6 times more likely to select non-U.S. markets over the Canadian market than non-immigrant business owners. If the choice is between U.S. and non-U.S markets, then recent immigrant business owners are more than two times more likely to select non-U.S. markets over the U.S. market than non-immigrant business owners.

IMMIGRANT-OWNED BUSINESSES EXPORTING TO NON-U.S. MARKETS ARE FAST-GROWING

Our assessment of the performance of Canadian SMEs reveals that businesses owned by recent immigrants that export to non-U.S. markets are among the fastest-growing SMEs. Over the period 2007–11, their profits grew at an average annual rate of 21 per cent compared with a 2 per cent decline for their non-immigrant counterparts. On a whole, immigrant exporters that sell to the U.S. and non-U.S. markets have realized an average annual net profit growth rate of 16 per cent (21 per cent for non-U.S. markets minus 5 per cent for the U.S. market). By contrast, non-immigrant exporters have realized an average annual net profit growth rate of just 1 per cent (3 per cent for the U.S. market minus 2 per cent for non-U.S. markets).

HOWEVER, IMMIGRANT EXPORTERS TO NON-U.S. MARKETS ARE LESS EFFICIENT

It is important to note that the superior growth in the profits of non-U.S. immigrant exporters does not translate into superior rates of return from business operations. In general, U.S. immigrant exporters and non-immigrant exporters generate higher profits when they undertake the same levels of investment in assets or become exposed to similar risk factors (such as unanticipated changes in foreign exchange rates) over the course of doing business abroad. This suggests that, in general, non-U.S. immigrant exporters are less operationally efficient than U.S. immigrant exporters and non-immigrant exporters, and less effective in managing the risks involved in international business. However, if the most operationally efficient companies are expected to export to non-U.S. markets, which are relatively difficult and costly to serve, then immigrant ownership may actually confer advantages (i.e., social ties abroad, foreign language skills, and cultural knowledge) that partially compensate for the relatively low operational efficiency of non-U.S. immigrant exporters, at least in the short term.

MOST IMMIGRANT EXPORTERS TO NON-U.S. MARKETS ARE LIKELY COMPETING ON PRICE, NOT INNOVATION

We found that most non-U.S. immigrant exporters are recently established wholesale/retail traders with limited business connections in Canada. In contrast, U.S. immigrant exporters are generally more established and better connected businesses that operate in knowledge-based and manufacturing industries. In addition, research and development (R&D) spending accounts for a larger share of the expenditures of U.S. immigrant exporters than non-U.S. immigrant exporters. This difference in R&D spending rates suggests that non-U.S. exporting businesses owned by immigrants have adopted a fundamentally different business model than the immigrant owners of knowledge-intensive exporting businesses that sell to the U.S. market. More specifically, the relatively low R&D spending rates and dominant industry choice (wholesale/retail trade) of non-U.S. immigrant exporters suggest that they are more likely to compete on the basis of a low-pricing strategy than a premium-pricing strategy that emphasizes product features. This suggests that non-U.S. immigrant exporters may be more vulnerable to price competition than U.S. immigrant exporters. A notable exception is knowledge-intensive non-U.S. immigrant exporters whose business model appears to be founded on an innovation-based strategy.

QUEBEC AND ONTARIO HAVE THE HIGHEST SHARE OF IMMIGRANT EXPORTERS BEYOND THE U.S.

Ontario, British Columbia, and Quebec account for more than four-fifths of Canada's immigrant population. In general, exporting businesses that are owned by immigrants are more concentrated in Ontario and Quebec than in other provinces. In Quebec, just over 40 per cent of immigrant businesses export to non-U.S. markets. British Columbia has the smallest share of non-U.S. immigrant exporters. However, given the disproportionately large share of immigrant-owned exporting businesses in dominant Ontario and Quebec industries (i.e., wholesale/retail trade and knowledge-based as opposed to forestry), the industrial structure of British Columbia may be less conducive to export activity for immigrant-owned businesses than that of Ontario and Quebec.

MOST IMMIGRANT-OWNED BUSINESSES REPRESENT LIMITED LONG-TERM EXPORT POTENTIAL

While the propensity of recent immigrant-owned businesses to export to non-U.S. markets is relatively high, the magnitude of their contribution to exporting activity in Canada is limited for several reasons. First, most non-U.S. immigrant exporters are recently established, less operationally efficient firms with limited business connections in Canada. Second, their business model does not appear to be founded on an innovation-based strategy that emphasizes new products as opposed to product price. This means they may be vulnerable to price competition in non-U.S. markets over the long term. However, these shortcomings primarily apply to a dominant group of non-U.S. immigrant exporters in the wholesale/retail trade sector.

A SELECT GROUP OF KNOWLEDGE-BASED IMMIGRANT EXPORTERS REPRESENTS IMPORTANT POTENTIAL IN NON-U.S. MARKETS

In contrast, medium-sized immigrant exporters in the knowledge-based sector that export beyond the U.S. market are particularly promising. This is because their business model appears to be founded on an innovation-based strategy that enables them to compete on the basis of introducing new products rather than offering lower prices. At the same time, this innovation-based strategy predisposes them to formidable financing challenges in the Canadian private debt and equity markets. Therefore, the financing of innovative immigrant exporters that sell to non-U.S. destinations warrants special attention when formulating export promotion policies in Canada. Despite the current policy focus on boosting activity in non-U.S. markets, the bulk of Canada's trade is still to the United States. Policy-makers should also consider the potential of knowledge-intensive immigrant exporters that sell to the U.S. market.

INTRODUCTION

For decades, tapping into export markets beyond the U.S. has been an objective for Canadian businesses and policy-makers. This objective has become an imperative given that Canada–U.S. trade has been stagnant over the past decade while developing country markets grew rapidly. As a result, policy-makers and analysts have called on businesses of all sizes to go beyond the U.S. market, especially to fast-growth, developing country markets.[1] Canadian companies have started to export to fast-growth markets, with 16 per cent of exports to these markets in 2012. However, overall, trade is still overwhelmingly concentrated in the U.S. market.[2]

Canada has consistently attracted and admitted immigrants from fast-growth markets. China, for example, is the number one source country for Canadian immigrants: almost 33,000 permanent residents were admitted to Canada from China alone in 2012.[3] Yet, Canada's export pattern has not reshaped to reflect the significant immigration flows from China or other key source countries such as India, which have occurred over the last decade.

1 Foreign Affairs, Trade and Development Canada, *Global Markets Action Plan.*

2 Sydor, *The Internationalization of Canadian SMEs.*

3 Citizenship and Immigration Canada, *2012: Canada's Record-Breaking Year for Immigration.*

Canadian companies that go beyond the U.S. market face multiple challenges related to foreign languages, cultures, social networks, and the cost of doing business. However, many commentators and policy-makers have argued that these challenges are not insurmountable given Canada's diverse immigrant population. Why then has Canada not been able to effectively leverage the foreign language skills, and the cultural knowledge and networks of recent immigrants that originate from fast-growth developing economies?

Key Definitions

Recent immigrants and non-immigrants: Recent immigrants are immigrants who have been living in Canada for up to five years. By default, non-immigrants are defined as immigrants who have been living in Canada for more than five years.[1]

Small and medium-sized enterprise (SME): A Canadian private firm with fewer than 500 employees and annual revenue less than C$50 million.

Immigrant-owned business: A SME whose majority owner is a recent immigrant.

Non-immigrant-owned business: A SME whose majority owner is a non-immigrant.

U.S. immigrant exporter: A recent immigrant-owned business that sells to the U.S. market only.

U.S. non-immigrant exporter: A non-immigrant-owned business that sells to the U.S. market only.

Non-U.S. immigrant exporter: A recent immigrant-owned business that either sells to non-U.S. markets only, or both the U.S. market and non-U.S. markets.

Non-U.S. non-immigrant exporter: A non-immigrant-owned business that either sells to non-U.S. markets only, or sells to both the U.S. and non-U.S. markets.

1 This classification scheme was adopted because data are only available for immigrants who have been living in Canada for up to five years. By focusing on Canadian businesses that are specifically owned by recent immigrants rather than immigrants in general, we may underestimate their contribution to exporting activity in Canada. At the same time, we are better placed to effectively capture how the unique characteristics of immigrant business owners impact their export market decisions well before they assimilate into mainstream Canadian society.

RESEARCH OBJECTIVES

At present, we do not have a clear picture of the actual role that recent immigrants play in Canadian export activity. (See box "Key Definitions" for our definition of recent immigrants, among other key terms used in this study.) One of the key objectives of this study is to examine whether the export market decisions of Canadian immigrant business owners reflect their global experience and connections outside of Canada. Specifically, we intend to address the following question: Are Canadian SMEs with a recent immigrant majority owner more likely to export to countries beyond the U.S., compared with SMEs owned by non-immigrants (as defined by immigrants who have lived in Canada for more than five years)?

We are generally interested in Canadian SMEs because they exhibit a pattern of internationalization that is consistent with Canada's export agenda as defined in Canada's 2013 *Global Markets Action Plan*.[4] Importantly, this plan places considerable emphasis on the growth of exports in emerging markets. This requires that SMEs play a far more significant role as exporters in emerging markets than is currently the case. Currently, small businesses disproportionately account for the value of exports to emerging and developing country markets, including India, Egypt, Turkey, and South Korea.[5] In addition, they have been making steady inroads into BRIC countries (Brazil, Russia, India, and China) as a group.[6] Furthermore, exports account for a larger share of the sales of Canadian small businesses than their medium or large counterparts. However, large firms account for about two-thirds of the value of exports.[7]

There is evidence that Canadian SMEs that export to BRIC countries generally experience a boost in their performance.[8] At the same time, the most experienced and innovative Canadian SMEs are better positioned to

4 Foreign Affairs, Trade and Development Canada, *Global Markets Action Plan*.

5 Industry Canada, *Canadian Small Business Exporters*.

6 Ibid.

7 Ibid.

8 Sui and Goldfarb, *Not for Beginners*.

survive after entering BRIC countries.[9] To the extent that international business experience and innovative capacity increase with company age and size, well-established medium to large companies are likely to have a competitive advantage over recently established small firms in fast-growth developing country markets. Arguments along this line suggest that recently established immigrant-owned small businesses that target non-U.S. markets are unlikely to significantly advance Canada's export agenda. However, more systematic evidence is necessary since the role of recent immigrant businesses in trade in general, and exporting activity in particular, is incompletely understood.

This study addresses questions of both theoretical and practical importance, making it relevant to industry leaders, policy-makers, and academic researchers. The questions addressed include:

1. What factors influence the decision of Canadian SMEs to participate in non-U.S. markets?
2. What are the key elements of the export strategy of immigrant-owned SMEs? We examine their characteristics (i.e., majority owner's gender and business experience), and potential strengths and weaknesses, including access to networks and financing, innovation, size, export performance, and profitability.
3. Do immigrants help Canada to establish stronger trade linkages in non-U.S. markets?
4. What factors should policy-makers consider when formulating export promotion policies that pertain to immigrants?

RELATED STUDIES AND THE CONTRIBUTIONS OF THIS STUDY

Much of what we currently know about the role of immigrants in export activity, and how to target export markets, comes from prior country-level studies on the relationship between immigration and aggregate bilateral trade flows.[10] Like our study, previous studies along this line start out with the notion that immigrants may systematically differ from non-immigrants in terms of their preferences, language and cultural skills, and their access to networks in their countries of origin. Importantly, these studies generally found a statistically significant (partial) correlation between immigrant presence and trade flows to and from the immigrants' countries of origin. This has been shown for a number of countries, including the United States,[11] the United Kingdom,[12] and Canada.[13]

Immigrant presence in Canada strengthens the export orientation of Canadian SMEs and enables Canada to develop new trade linkages beyond the United States.

One may infer from the existing evidence that immigrants foster trade linkages between their host countries and the countries from which they originate. However, the existing evidence does not convincingly show that immigrants in Canada or elsewhere promote trade through direct involvement in trade activity or international business. Therefore, it remains unclear whether immigration policy is actually a potent tool for redirecting Canadian trade flows.

This study primarily contributes to the existing literature by providing more direct evidence about the role that immigrants play in trade promotion in general, and exporting in particular. Specifically, we examine firm-level Canadian data for more than 15,000 SMEs to determine the effects of immigrant ownership on export orientation. We found that SMEs with a majority owner who is a recent immigrant are more likely to export to countries beyond the U.S. compared with SMEs owned

9 Sui and Goldfarb, *Not for Beginners*.

10 Downie, *How Immigration Expands Canadian Markets*; Girma and Yu, "The Link Between Immigration and Trade"; Gould, "Immigrant Links to the Home Country"; Head and Ries, "Immigration and Trade Creation"; Wagner, Head, and Ries, "Immigration and the Trade of Provinces."

11 Gould, "Immigrant Links to the Home Country."

12 Girma and Yu. "The Link Between Immigration and Trade."

13 Downie, *How Immigration Expands Canadian Markets*; Wagner, Head, and Ries, "Immigration and the Trade Provinces."

by non-immigrants or immigrants who have lived in Canada for more than five years. This suggests that immigrant presence in Canada does not merely strengthen the export orientation of Canadian SMEs, but also enables Canada to develop new or stronger trade linkages beyond the U.S. than would otherwise have been the case. Thus, prior studies that found a positive correlation between immigration and total trade flows between countries may actually point to the potential of immigrants to directly impact a country's cross-border trade flows and/or its existing trade relationships with other countries.

The influx of immigrants in a country may lead to changes in its cross-border trade flows and/or its existing trade relationships with other countries.

More generally, a positive correlation between immigration and total trade flows between countries suggests two possibilities along the following lines: (1) people primarily migrate to foreign countries with pre-existing trading relationships with their home countries; and (2) immigrants create new or stronger trading relationships between their host countries and the countries from which they originate. The first case suggests that *trade causes immigration*. Meanwhile, the second case suggests that *immigration causes trade*; that is, the influx of immigrants in a country will lead to a change in its cross-border trade flows and/or its existing trade relationships with other countries. Our finding is more consistent with the second case. Altogether, this suggests that immigrants have an important role to play in Canada's export agenda. As such, this study contributes to the formulation of the policies required to advance this export agenda by providing new insights into the strengths and weaknesses of immigrant-owned exporting businesses.

OUR DATA AND METHOD

A non-technical explanation of the data and methodology is provided here; however, Appendix A provides more technical details about the methodology, data, definition of variables, and the results of our regression analysis.

As mentioned above, one of our key objectives is to determine whether immigrant-owned SMEs are more likely to export goods and services to non-U.S. markets compared with their non-immigrant-owned counterparts. Our method allowed us to estimate the impact of immigrant ownership on the likelihood that Canadian SMEs will export to non-U.S. markets as opposed to selling either to the domestic market only or exporting only to the United States. We controlled for other factors (such as access to inter-firm networks, R&D intensity, company age and size) to isolate the effect of immigrant ownership on export market decisions. In addition, since the survey data that we used include trade in goods and services, our coverage of the exporting activity of Canadian SMEs in general and immigrant-owned businesses in particular, is more comprehensive than prior studies that used data on trade in goods only.

For the purpose of this study, we define a SME as a private firm with fewer than 500 employees and annual revenue of less than C$50 million. This definition is consistent with that of Industry Canada and Statistics Canada. Based on data availability, we define a SME to be immigrant-owned if its majority owner is an immigrant who has been living in Canada for up to five years. (See box "Key Definitions.")

We drew on the following confidential data sources:

- Statistics Canada's 2007 Survey on Financing of Small and Medium Enterprises;
- T2 Corporation Income Tax Return, and the General Index of Financial Information (GIFI).

These databases have been linked by Statistics Canada's Centre for Data Development and Economic Research (CDER). Based on the data available for 2007, we have a sample of more than 15,000 Canadian SMEs. Immigrant-owned SMEs account for almost 3 per cent (442) of this sample.

LIMITATIONS

We acknowledge that this study has a number of limitations that are primarily due to data unavailability. First, our analysis of immigrant-owned businesses is restricted to Canadian SMEs with immigrant majority owners who have lived in Canada for at most five years. However, it is possible that immigrant business owners who have lived in Canada beyond five years may be better positioned to significantly contribute to export activity; hence, our focus on recent immigrants may potentially underestimate the extent to which immigrants are participating in export markets. At the same time, we also recognize that it will become increasingly difficult to disentangle the unique contributions of immigrants versus Canadian-born individuals as the process of assimilation unfolds over time. So this five-year restriction may in fact enable us to better capture how the unique characteristics of immigrant business owners affect their export market decisions well before they assimilate into mainstream Canadian society.

Second, although Statistics Canada's latest Survey on Financing of Small and Medium Enterprises is available for 2011, it does not provide data on multiple business ownership.[14] Since only the 2007 survey contains data on multiple business ownership, we primarily focus on 2007. Our analysis essentially provides a snapshot of the impact of immigrant ownership on the export market decisions of Canadian SMEs, but it does not tell us whether immigrant-owned businesses will continue to target the same export markets over time. At the same time, we do not have a compelling reason to expect major changes in their export market decisions over time.

Third, we know from prior studies that it is worthwhile to jointly study exports and foreign direct investment (FDI) because they may serve as complements or substitutes.[15] However, data limitation precluded such an analysis. In addition, although we treat Canadian SMEs that sell exclusively to the domestic market as non-exporters, they may very well operate as importers. As importers, they may enable both exporters and non-exporters in Canada to operate more efficiently by supplying cheap raw materials and other productive inputs that have been sourced abroad. Therefore, it is important to understand the importing activity of immigrant-owned SMEs in Canada. However, data limitation precluded an analysis of the import orientation of Canadian SMEs owned by recent immigrants.

Fourth, our data do not enable us to determine whether recent immigrant-owned businesses primarily export to the countries from which their owners originate. Ideally, we would like to know, for example, whether immigrants from India disproportionately account for newly established or existing businesses that primarily export to India. This type of information would considerably strengthen evidence in support of the view that immigrant presence in Canada directly promotes trade in general, and exporting in particular.

Our analysis essentially provides a snapshot of the impact of immigrant ownership on the export market decisions of Canadian SMEs.

Finally, we cannot rule out the possibility that the export data are overstated for Canada–U.S. trade, and understated for Canada's trade with non-U.S. countries. For instance, this may occur in cases where the full value of exported goods and services is credited to the U.S., but only a fraction of those goods and services actually represents added value (e.g., the entire value of a car is credited as an export each time it crosses into the U.S., even if only a part has been added in Canada). Furthermore, exports from Canada to non-U.S. countries may be partially credited to the U.S. where it merely serves as a trans-shipment point. The understatement of Canada's trade with non-U.S. countries is often evident in discrepancies in the officially recorded values of two-way trade between Canada and non-U.S. countries. For example, Mexico's official imports from Canada far exceed Canada's recorded exports to Mexico.

EXPORT MARKET DECISIONS OF IMMIGRANT AND NON-IMMIGRANT BUSINESSES

In this section, we will primarily examine whether recent immigrant-owned businesses systematically differ from their non-immigrant counterparts in terms of their export market decisions. As suggested above,

14 We need data on multiple business ownership to determine whether SMEs belong to inter-firm networks. These networks are created if entrepreneurs own and/or manage several businesses at the same time.

15 Head and Ries, "Overseas Investment and Firm Exports."

recent immigrants may have an advantage over non-immigrants in terms of foreign language skills, cultural knowledge, and access to networks in their non-U.S. countries of origin.[16] Therefore, we predict that *recent immigrant-owned businesses are more likely to export to non-U.S. markets (as opposed to the Canadian or U.S. market) than non-immigrant-owned businesses, all else being equal.*

To determine whether the data actually support this prediction, we will first broadly compare immigrant- and non-immigrant-owned businesses based on a number of export measures. However, we acknowledge that the evidence from such broad comparisons may not be comprehensive because there are material differences (e.g., company age, value of assets, business experience of owners) between immigrant and non-immigrant businesses and their owners. Therefore, we will extend our analysis by drawing on the key results from our regression analysis. (See Appendix A.) The statistical evidence from our regression analysis is more comprehensive because it ensures that immigrant and non-immigrant businesses are comparable by controlling for material differences at the level of the owners, firms, the industry, and the location in which they operate.

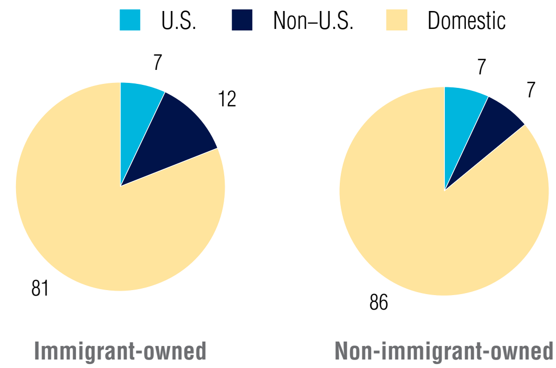
Most Canadian businesses are focused on the domestic market, but immigrant-owned businesses are more likely to target non-U.S. markets.

Chart 1 indicates that both immigrant and non-immigrant businesses are focused largely on the domestic market. However, immigrant-owned businesses are more likely to target non-U.S. markets than businesses owned by non-immigrants, as Chart 1 illustrates.

When it comes to international markets, we found that 12 per cent of immigrant-owned businesses are exporters that sell goods and services to non-U.S. markets compared with 7 per cent for non-immigrant businesses. However, the share (7 per cent) of immigrant and

16 Head and Mayer, *What Separates Us?*; Head and Ries, *Immigration and Trade Creation.*

Chart 1
Canadian SMEs' Market Decisions, 2007
(percentage share by destination)



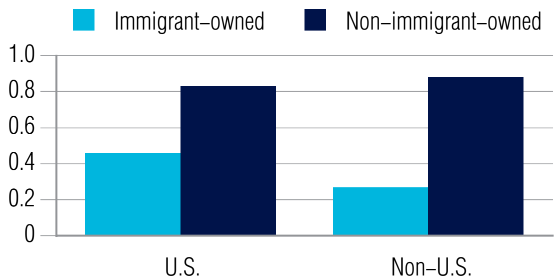
Sources: The Conference Board of Canada; Statistics Canada, *Survey on Financing Small and Medium Enterprises*, 2007.

non-immigrant businesses that export to the U.S. is the same. (See Chart 1.) Altogether, these results are consistent with our prediction that immigrant exporters are more likely to sell to non-U.S. markets than their non-immigrant counterparts.

Immigrant exporters are low-value exporters in both U.S. and non-U.S. markets. On average, non-immigrant exporters sell almost twice as much as immigrant exporters—C$830,000 compared with C$460,000—in the U.S. market. (See Chart 2.) But when non-immigrant exporters sell to non-U.S. markets, the average value of their exports is more than three times that of immigrant exporters—C$880,000 compared with C$270,000. This suggests that while immigrant exporters are low-value exporters in the U.S. market, they are even more so in non-U.S. markets. However, exports account for more than two-thirds of the sales of non-U.S. immigrant exporters compared with roughly a half for non-U.S. non-immigrant exporters. Meanwhile, exports account for the same share of sales (roughly two-fifths) for U.S. immigrant and non-immigrant exporters. (See Chart 3.)

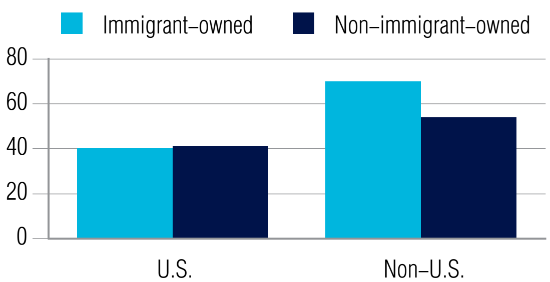
Interestingly, non-immigrant exporters seem to use their human resources more efficiently to generate value from their exporting activity in either U.S. or non-U.S. markets; specifically, the average value that

Chart 2
Value of Exports, 2007
($ millions)



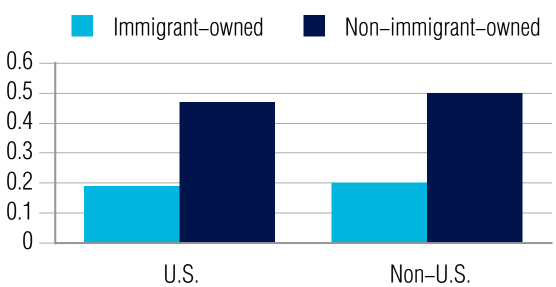
Sources: The Conference Board of Canada; Statistics Canada, *Survey on Financing Small and Medium Enterprises*, 2007.

Chart 3
Export Intensity, 2007
(percentage of sales)



Sources: The Conference Board of Canada; Statistics Canada, *Survey on Financing Small and Medium Enterprises*, 2007.

Chart 4
Value of Exports per Employee, 2007
($ millions)



Sources: The Conference Board of Canada; Statistics Canada, *Survey on Financing Small and Medium Enterprises*, 2007.

Table 1
Selected Factors That Impact the Market Decisions of Canadian SMEs

	U.S. vs. Domestic	Non-U.S. vs. Domestic	Non-U.S. vs. U.S.
Immigrant owner	~	+	+
Access to inter-firm networks	+	~	~
Located in urban centre	~	+	~
R&D (share of total spending)	+	+	~
Company size (value of assets)	+	+	~
Company age (years)	+	~	~

Note: A plus sign indicates a significant and positive relationship, a minus sign indicates a significant and negative relationship, and a tilde (~) indicates statistical insignificance. Please see Table 1 in Appendix A for more detailed regression results.
Sources: The Conference Board of Canada; Statistics Canada, *Survey on Financing Small and Medium Enterprises*, 2007.

employees contribute to the exports of non-immigrant businesses is more than twice that of immigrant businesses. (See Chart 4.)

Up to this point, our broad comparison of immigrant and non-immigrant businesses suggests that immigrant businesses are:

- more likely to export to non-U.S. markets;
- more export-oriented in general (exports represent a larger share of their sales);
- disproportionately low-value exporters in both U.S. and non-U.S. markets, but more so in the latter;
- more dependent on the sales generated from non-U.S. markets;
- less operationally efficient in terms of their use of employees in their export operations.[17]

The following will extend our analysis by focusing on the first result above. Specifically, we will examine whether immigrant exporters are more likely to sell to non-U.S. markets than otherwise comparable non-immigrant exporters.

All else being equal, we found that immigrant exporters are more likely to sell goods and services to non-U.S. markets than non-immigrant exporters. (See Table 1.)

17 This is consistent with their relatively low export value per employee.

Specifically, if immigrant and non-immigrant business owners are similarly faced with a choice between selling to non-U.S. markets and the Canadian market, our findings indicate that immigrant business owners are 1.6 times more likely than their non-immigrant counterparts to select non-U.S. markets over the Canadian market.[18] (See Table 1 in Appendix A.) If the choice is between the U.S. and non-U.S. markets, immigrant business owners are more than two times more likely to select non-U.S. markets over the U.S. market. Other factors such as business connections also influence export market decisions. (For other findings, see box "Selected Factors Other Than the Immigrant Status of Owners That Influence Export Market Decisions.")

Selected Factors Other Than the Immigrant Status of Owners That Influence Export Market Decisions[1]

- **Business connections matter:** The odds of becoming a U.S. exporter[2] as opposed to a non-exporter are 55 per cent higher when SMEs belong to an inter-firm network rather than operating as stand-alone enterprises.
- **Innovation matters:** A one percentage-point increase in R&D spending as a share of total expenditures increases the odds that SMEs will sell to non-U.S. markets by 5 per cent.
- **Manufacturers are more likely to export:** The odds of becoming an exporter as opposed to a non-exporter are generally lower for non-manufacturing SMEs relative to manufacturing SMEs. This is not surprising because some non-manufacturing SMEs may actually be non-trading service-based firms. At the same time, many services are tradable across borders. However, the export activity of firms that offer tradable services may not be adequately captured if they operate through foreign affiliates—so that exports are treated as foreign direct investment (FDI)—or if their value-added activities are embedded in the overall value of trade in manufactures.
- **Location matters:** When SMEs are based in Ontario and Quebec, rather than other provinces, they are more likely to become exporters that sell to U.S. and non-U.S. markets. Thus, these provinces seem to have conditions or industries that are more conducive to export activity. Meanwhile, the odds of becoming a non-U.S. exporter instead of a non-exporter are 49 per cent higher when SMEs are based in an urban centre rather than a rural area.
- **Company size matters:** An increase in the asset value of SMEs by one dollar increases the odds that they will sell to the U.S. and non-U.S. markets by 1.5 and 2 per cent, respectively, as opposed to the domestic market.
- **Company age is not critical:** An additional year of business operation does not significantly increase the likelihood that SMEs export either to U.S. or non-U.S. markets as opposed to selling to the domestic market.

1 See Table 1 in Appendix A.

2 We conveniently use the term "U.S. exporters" to refer to Canadian SMEs that export only to the United States.

PERFORMANCE OUTCOMES

We have established that immigrant exporters are more likely to sell to non-U.S. markets than otherwise comparable non-immigrant exporters; however, this raises another related question: Do non-U.S. immigrant exporters outperform other exporters on average? To address this question, we will evaluate the performance of immigrant and non-immigrant exporters based on the following three measures:

- profitability
- growth rate of profits
- "profit stability" or risk-adjusted profitability

To evaluate the profitability of exporters, we examine their return on assets (ROA) between 2007 and 2011. This is the average profit per dollar invested in assets. Importantly, this performance measure captures whether the companies are using resources efficiently in the markets in which they operate. When we look at exporters to non-U.S. markets, we found that the average ROA of non-immigrant exporters is more than twice the average ROA of their immigrant counterparts; specifically, for every C$1.00 that is invested in assets, non-U.S. non-immigrant exporters realized C$2.39 in profits on average compared with C$1.18 for non-U.S. immigrant exporters. (See Chart 5.) However, immigrant exporters that sell to the U.S. market outperform non-immigrant exporters on average—for every one Canadian dollar that is invested in assets, U.S. immigrant exporters realized C$2.65 in profits on average compared with C$1.83 for U.S. non-immigrant exporters. As our

18 Table 1 in Appendix A reports a log odds ratio of 0.954. Taking the antilog with respect to base e (i.e., $e^{0.954}$) yields an odds ratio of 2.60. Since an odds ratio of 1 implies equal chances, the additional gain in the odds ratio is 1.60.

results below indicate, these top-performing U.S. immigrant exporters are apparently highly innovative businesses in the knowledge-based sector.

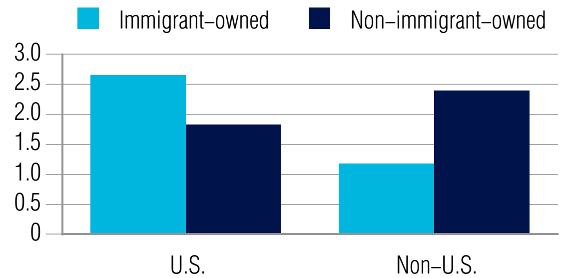
The profits of immigrant exporters that sell to non-U.S. markets grew the fastest but were the least profitable and the least stable. Charts 5 to 7 show the average profits, profit growth, and profit stability for immigrant-owned versus non-immigrant-owned exporters.

To evaluate the growth performance of exporters, we examined the average rates at which their profits grew. In principle, if revenue from exports is growing at a faster rate than the costs associated with the deployment of assets and employees in export operations, we expect to see an increase in the growth rate of profits over time. Drawing on the financial results of companies for the period 2007–11, we found that immigrant exporters that sell to non-U.S. markets have grown the fastest on average, at a rate of 21 per cent annually on average. (See Chart 6.) In contrast, the profits of non-U.S. non-immigrant exporters declined by 2 per cent annually on average. (See Chart 6.) On a whole, while immigrant exporters that sell to U.S. and non-U.S. markets have realized an average annual net profit growth rate of 16 per cent (21 per cent for non-U.S. markets minus 5 per cent for the U.S. market), non-immigrant exporters have realized an average annual net profit growth rate of just 1 per cent (3 per cent for the U.S. market minus 2 per cent for non-U.S. markets).

While the ROA profitability measure captures the extent to which companies are efficiently using resources in the markets in which they operate, it does not capture the extent to which they are compensated for the degree of risk that they assume when they serve one market versus another. To capture differences in the degree of risk across markets, we adjusted the ROA profitability measure.[19] This yields what may be called a "profit stability" profitability measure; or more directly, a *risk-*

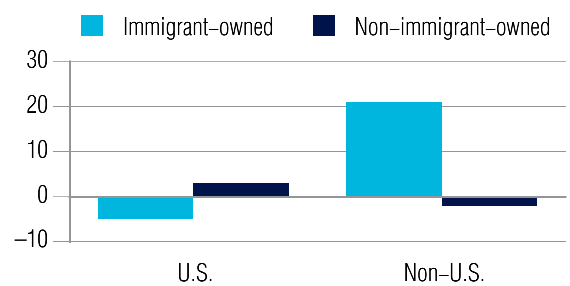
19 Specifically, we divided average ROA by the standard deviation of ROA for the period 2007–11. Standard deviation of ROA is a measure of the variation around the average ROA value. It serves as proxy for risk. A higher (lower) standard deviation implies higher (lower) degree of risk, which is observed as greater (lower) variability in profits for a given period. All else being equal, the risk-adjusted ROA values will decrease (increase) as the standard deviation of ROA increases (decreases).

Chart 5
Average Profits, 2007–11
(average profit per dollar invested in assets)



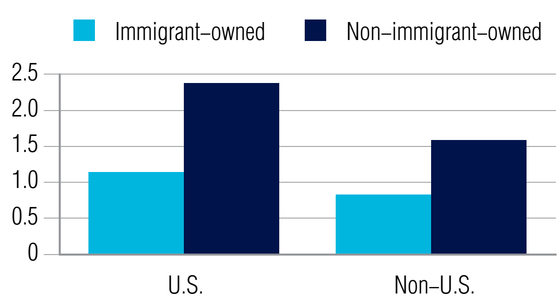
Sources: The Conference Board of Canada; Statistics Canada, *Survey on Financing Small and Medium Enterprises*, 2007.

Chart 6
Average Annual Profit Growth Rate, 2007–11
(per cent)



Sources: The Conference Board of Canada; Statistics Canada, *Survey on Financing Small and Medium Enterprises*, 2007.

Chart 7
Average Profit Stability, 2007–11
(average profit per dollar invested in assets adjusted for risk)



Sources: The Conference Board of Canada; Statistics Canada, *Survey on Financing Small and Medium Enterprises*, 2007.

adjusted ROA profitability measure, which we define as the average profit on a dollar invested in assets per unit of risk.

We found that immigrant and non-immigrant exporters that sell to non-U.S. markets have average profit stability (an average risk-adjusted ROA) of C$0.83 and C$1.59, respectively. (See Chart 7.) This suggests that non-immigrant exporters are better compensated than immigrant exporters for the risks that they assume in non-U.S. markets. We also found that non-immigrant exporters that sell to the U.S. market outperform their immigrant counterparts in terms of risk-adjusted profitability; specifically, the non-immigrant and immigrant exporters have an average risk-adjusted ROA of C$2.38 and C$1.14, respectively. (See Chart 7.) Altogether, these results suggest that non-immigrant exporters manage the risks involved in international business more effectively than immigrant exporters, and the former are rewarded for doing so in terms of higher average profitability adjusted for risk.

DO NON-U.S. IMMIGRANT EXPORTERS HAVE A VIABLE BUSINESS MODEL?

The superior growth performance of immigrant exporters that sell to non-U.S. markets is a notable finding. It is consistent with a prior study which found that newly established immigrant-owned exporting companies outperform other immigrant-owned domestic companies in Canada as well as newly established non-immigrant-owned exporting companies in terms of the average rate of growth in revenue, profits, employment, and average wage.[20] However, that study did not indicate which export markets primarily account for these superior growth outcomes. Our study suggests that these outcomes may be partially attributed to immigrant exporters that sell to non-U.S. markets. Furthermore, as we illustrate below, recently established immigrant-owned SMEs disproportionately sell more goods and services to non-U.S. markets compared with immigrant-owned SMEs that have been in business for more than a decade.

Although non-U.S. immigrant exporters are among the fastest growing Canadian SMEs, their superior growth performance does not translate into superior rates of return from business operations. In general, U.S. immigrant exporters and non-immigrant exporters usually generate more profits when they undertake the same levels of investment in assets, or become exposed to similar risk factors—such as unanticipated changes in foreign exchange rates—over the course of doing business abroad. Ideally, business owners and managers should pursue both high growth rates and high rates of return.[21] However, if both of these performance outcomes are not attainable at a particular stage of business development, then business owners and managers should primarily focus on generating high rates of return from business operations.[22] This strategic focus will enable firms that are initially slow growing to eventually scale up their operations to achieve both high growth rates and high rates of return. Therefore, the high growth-low return outcome for non-U.S. immigrant exporters gives cause for concern; specifically, they are at risk of not achieving the desired high growth-high return performance outcome over the long term.

A relatively large proportion of immigrant exporters to non-U.S. markets are essentially wholesale/retail traders with limited business connections in Canada.

For several reasons, the relatively low operational efficiency of non-U.S. immigrant exporters calls the viability of their business model into question. A major concern is that they are low-value exporters. (See Chart 2.) As low-value exporters, they are perhaps not sufficiently compensated for the additional assets and employees that must be deployed, and the additional risks that must be assumed, when expanding into non-U.S. markets. However, the relatively low operational efficiency of non-U.S. immigrant exporters is not only limited by their low export values. On average, they are more recently established than U.S. immigrant exporters, and they also

20 Neville and others, "Do Young Firms Owned by Recent Immigrants Outperform Other Young Firms?"

21 Davidsson, Steffens, and Fitzsimmons, "Growing Profitable or Growing From Profits?"

22 Ibid.

Table 2
Characteristics of Immigrant and Non-Immigrant Businesses and Their Owners, 2007 Average

	Immigrant				Non-immigrant
	Exporting to U.S. markets only	Exporting to non-U.S. markets	Non-exporting	All businesses	All businesses
Firm characteristic(s)					
Female ownership (share of total)	n.a.	31	18	19	29
Company age (years)	12	7	9	9	16
Number of employees	20	8	4	5	7
Assets (C$ millions)	1.5	1.9	2.9	2.7	2.2
Revenue (C$ millions)	2.1	0.4	1.4	1.3	1.9
R&D (share of total spending)	25	6	4	5	3
Urban (per cent of total in urban centre)	92	96	83	84	75
Access to inter-firm networks (per cent of total)	19	2	3	3	7
Owner characteristic(s)					
Owner's business experience, including experience outside of Canada (years)	n.a.	26	15	15	20

n.a. = not available due to Statistics Canada's confidentiality policy on small sub-samples.
Sources: The Conference Board of Canada; Statistics Canada.

generate relatively low average revenue from their export operations despite their relatively large asset base. We will also show that a relatively large proportion of non-U.S. immigrant exporters are essentially wholesale/retail traders with limited business connections in Canada. Furthermore, we assert that their business model makes them more vulnerable to price competition compared with both U.S. and non-U.S. immigrant exporters in the knowledge-based sector.

THE CHARACTERISTICS, RESOURCES AND STRATEGIC OPERATIONS OF IMMIGRANT- AND NON-IMMIGRANT BUSINESSES

Up to this point in our analysis, we have evaluated the export market decisions of immigrant and non-immigrant businesses, as well as their implications for performance. In this final part of our analysis, we will provide greater insights into the characteristics of non-immigrant businesses.[23]

Female Immigrant Owners Target Non-U.S. Markets

On a whole, immigrant businesses have a lower share of female ownership—19 per cent compared with 29 per cent—relative to non-immigrant businesses. (See Table 2.) However, when we looked at immigrant businesses that sell to non-U.S. markets, we found that almost one-third of them have a female majority owner. This is much higher than the one-fifth share of domestically focused immigrant-owned businesses. (See Table 2.) This could mean that female immigrant owners face fewer barriers in non-U.S. markets than in the Canadian market.

Recently Established, Small, and Less Operationally Efficient Immigrant Businesses Disproportionally Export to Non-U.S. Markets

On a whole, recent immigrant businesses are almost 10 years old on average.[24] (See Table 2.) Non-immigrant businesses are more than one-and-a-half times older

23 The descriptive statistics for female ownership and business experience are based on less than one-third of the observations in our sample. Descriptive statistics for all other owner and firm characteristics are based on the full sample.

24 Although recent immigrants have been in Canada for up to five years, they may become majority owners in established Canadian businesses. This explains why it is possible for recent immigrants to own businesses that are more than five years old.

than immigrant businesses. While immigrant exporters that sell to non-U.S. markets have been in business for less than 10 years on average, their owners appear to have substantial business experience outside of Canada. Meanwhile, immigrant exporters that sell to the U.S. market have been in business for more than 10 years on average. (See Table 2.) What is clear is that recently established immigrant exporting businesses disproportionately sell goods and services to non-U.S. markets.

On average, we found that immigrant businesses are smaller than non-immigrant businesses in terms of the number of employers (five compared with seven) and revenue (just over C$1 million compared with almost C$2 million). However, the average immigrant business has almost C$3 million in assets compared with just over C$2 million for the average non-immigrant business. (See Table 2.) If the average immigrant business has more assets but generates lower revenue than the average non-immigrant business, it is possible that the former is not operated as efficiently as the latter.

Immigrant ownership may confer advantages in non-U.S. markets, such as social ties or language skills that may partially compensate for company size, inexperience, or weaker R&D activity.

When we look at immigrant exporters as a group, we find that the asset value of an average non-U.S. immigrant exporter is roughly 21 per cent higher than that of an average U.S. immigrant exporter; yet the average non-U.S. exporter generates less than one-fifth of the revenue of the average U.S. exporter. (See Table 2.) Altogether, these results suggest that less operationally efficient, young, and small immigrant exporters disproportionately sell goods and services to non-U.S. markets. However, this finding warrants explanation because it appears to be at odds with prior research that suggests that the most operationally efficient firms will export to difficult export markets.[25]

In terms of the degree of difficulty and cost of doing business, Canadian firms are likely to find the U.S. market easier and potentially less costly to deal with than non-U.S. markets because the former is large, close to Canada, and similar in terms of language, culture, and legal and regulatory institutions. This implies that the most operationally efficient Canadian firms are expected to sell to non-U.S. markets, yet the findings of this study indicate the opposite: recently established immigrant-owned SMEs disproportionately sell to non-U.S. markets. Furthermore, as detailed below, these non-U.S. immigrant exporting businesses constitute a relatively large share of wholesale/retail traders with limited business connections in Canada. However, if immigrant-owned exporting businesses lack the capabilities that engender operational efficiency, how are they able to sell to the supposedly more demanding non-U.S. markets?

We suggest that less operationally efficient immigrant-owned firms may export to non-U.S. markets over the short term because immigrant ownership confers advantages (i.e., social ties abroad, foreign language skills, cultural knowledge) that may partially compensate for firm characteristics that are associated with high productivity (e.g., R&D activity, company age and size). This is consistent with our finding that immigrant ownership has a greater positive effect than company age and R&D intensity on the likelihood that Canadian SMEs will sell to non-U.S. markets as opposed to either the domestic or U.S. market. (See Table 1 in Appendix A.) More practically, recent immigrant business owners with limited business connections in either Canada or the U.S. may perceive few, if any, commercial opportunities in the North American market; if so, they will be motivated to export to non-U.S. markets where they are likely to have stronger social and business ties.

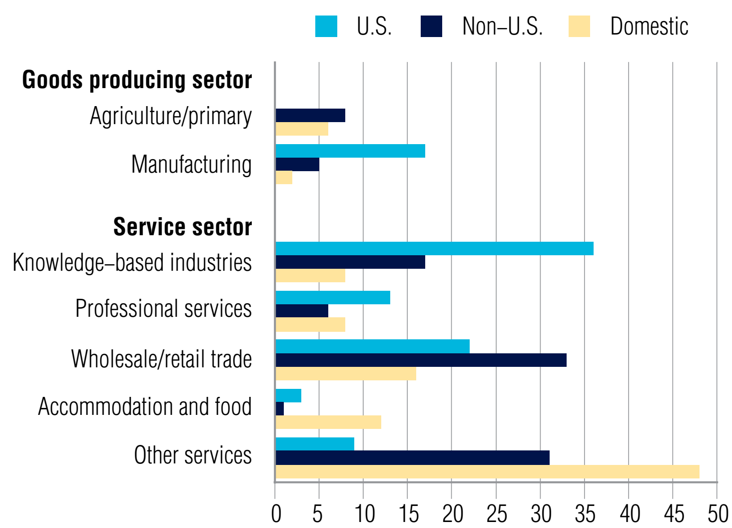
25 Arnold and Hussinger, "Export Behavior and Firm Productivity in German Manufacturing"; Bernard and Jensen, "Exporters, Jobs, and Wages"; "Exceptional Exporter Performance"; "Why Some Firms Export"; Clerides, Lach, and Tybout, "Is Learning by Exporting Important?"; Wagner, "The Causal Effects of Exports on Firm Size and Labor Productivity."

The Most Innovative Immigrant Exporters Sell to the U.S. Market

In practice, innovative businesses are characterized by their capacity to generate new ideas about how to make novel products and services or improve existing ones. One way to identify an innovative company is to assess the share of its revenue that is generated from new products or services.[26] However, due to data limitations we were unable to apply such an output-based measure of innovative capacity. Therefore, we applied an input measure to proxy innovation. Specifically, we used the share of R&D spending in total expenditures as a measure of the innovative capacity of the companies in our sample.

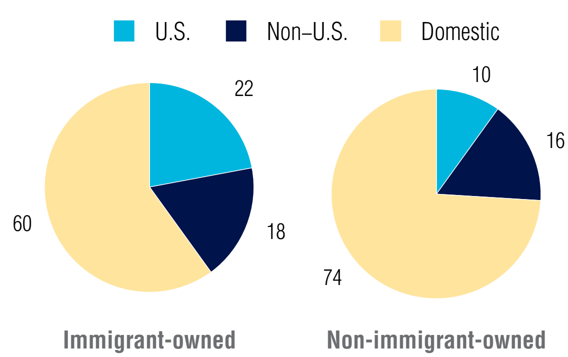
On average, we found that R&D spending accounts for a larger share of the expenditures—5 per cent compared with 3 per cent—of immigrant businesses relative to non-immigrant businesses. (See Table 2.) But this higher average share of R&D spending among immigrant businesses is primarily attributed to U.S. immigrant exporters. The share of their spending budget that is allocated to R&D activities is roughly four times larger than that of non-U.S. immigrant exporters. (See Table 2.) The differences in R&D spending rates across immigrant-owned businesses that export partly reflect differences in the nature of competition in the industry in which they operate. Although a relatively large group of non-U.S. immigrant exporters operate in knowledge-based industries, non-U.S. immigrant exporters are overwhelmingly concentrated in the wholesale/retail trade and other services.[27] (See Chart 8.) Insofar as above-average R&D spending rates are required to sustain international competitiveness in the knowledge-based and manufacturing industries, the relatively high R&D intensity of U.S. immigrant exporters is consistent with their relatively high participation rates in these industries—22 and 34 per cent respectively (see charts 9 and 10)—compared with either non-U.S. immigrant exporters or non-immigrant exporters in general. In the wholesale/retail trade sector where lower R&D spending rates are expected relative to the knowledge-based and manufacturing industries, non-U.S. immigrant exporters account for the largest share—just over one-fifth (see Chart 11)—of immigrant-owned businesses.

Chart 8
Share of Immigrant-Owned Businesses Active in Each Market, by Sector, 2007
(per cent)



Sources: The Conference Board of Canada; Statistics Canada. Survey on Financing Small and Medium Enterprises, 2007.

Chart 9
Share of Immigrant and Non-Immigrant Owned Businesses Active in Each Market, Knowledge-Based Industries, 2007
(per cent)



Sources: The Conference Board of Canada; Statistics Canada. Survey on Financing Small and Medium Enterprises, 2007.

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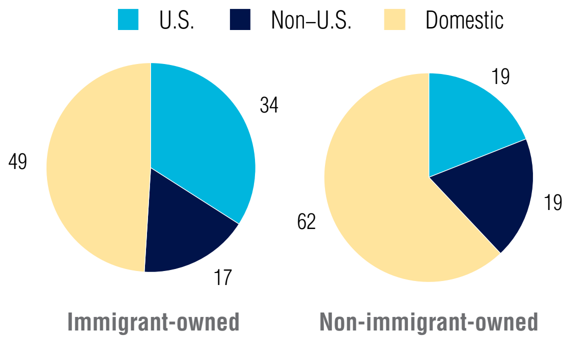
26 Therrien and Mohnen, “How Innovative Are Canadian Firms?”

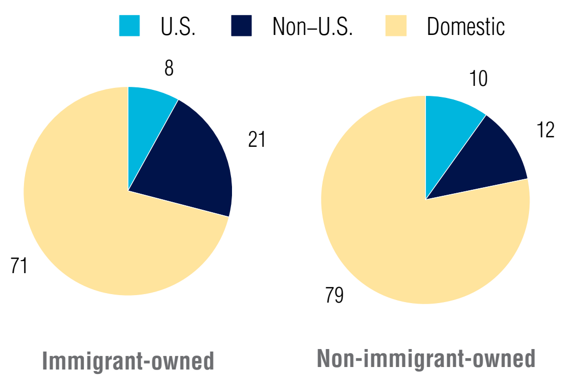
27 We recognize that a relatively large share of non-U.S. immigrant exporters operate in a variety of service-based industries (shown as “Other services” in Chart 8). However, since our data do not adequately reflect the nature of these services, we will focus on wholesale/retail trade throughout this study. This emphasis is appropriate since the wholesale/retail trade sector accounts for the largest share of non-U.S. immigrant exporters.

Chart 10
Share of Immigrant and Non-Immigrant Businesses Active in Each Market, Manufacturing, 2007
(per cent)



Sources: The Conference Board of Canada; Statistics Canada. Survey on Financing Small and Medium Enterprises, 2007.

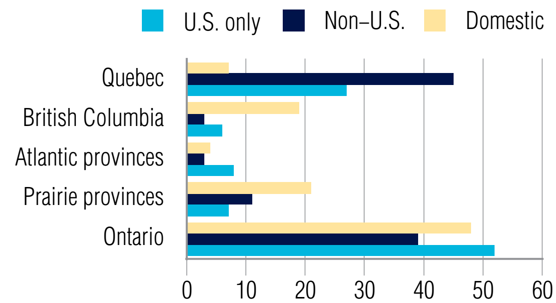
Chart 11
Share of Immigrant and Non-Immigrant Businesses Active in Each Market, Wholesale/Retail Trade, 2007
(per cent)



Source: The Conference Board of Canada. Survey on Financing Small and Medium Enterprises, 2007.

The relatively low R&D spending rates and dominant industry choices (such as the wholesale/retail sector) of non-U.S. immigrant exporters relative to U.S. immigrant exporters suggest that non-U.S. immigrant exporters may be primarily competing on the basis of a low-pricing strategy than a premium-pricing strategy that emphasizes product features. This low-pricing strategy may involve the marketing and sale of low-margin, as well as low-tech or maturing products and services in less developed countries. In contrast, the R&D and industry choices of U.S. immigrant exporters suggest they are more innovative businesses that are involved in the production, marketing, and sale of high-margin, high-tech, or newly developed products and services in the technologically advanced U.S. market. This suggests that non-U.S. and U.S. immigrant exporters are not merely selling to different export markets; more importantly, they seem to be operated by immigrant owners who have adopted fundamentally different business models. A notable exception is knowledge-intensive non-U.S. immigrant exporters whose innovation-based business model appears to be similar to that of U.S. immigrant exporters as a group.

Chart 12
Share of Immigrant-Owned SMEs Active in Each Market, by Province of Origin, 2007
(per cent)



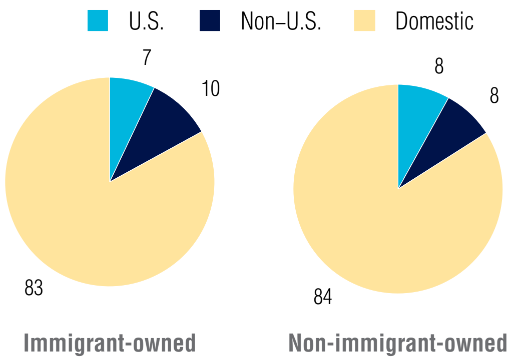
Sources: The Conference Board of Canada; Statistics Canada. Survey on Financing Small and Medium Enterprises, 2007.

QUEBEC AND BRITISH COLUMBIA HAVE THE LARGEST AND SMALLEST SHARES, RESPECTIVELY, OF NON-U.S. IMMIGRANT EXPORTERS

Ontario accounts for just over half of Canada's immigrant population, while British Columbia and Quebec together account for almost one-third.[28] We found that Quebec accounts for slightly more than two-fifths of non-U.S. immigrant exporters in Canada, while Ontario

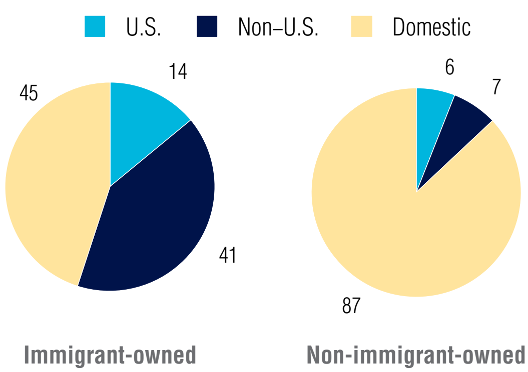
28 Based on the 2006 Census, there are 6.2 million foreign-born individuals or immigrants in Canada in 2006—Ontario, British Columbia, and Quebec account for 54.9, 18.1, and 13.8 per cent, respectively. (Statistics Canada, "Immigration to Canada.") More recently, the immigrant population is estimated at 6.8 million in the 2011 Census—Ontario, B.C., and Quebec account for 54.9, 18.1, and 13.8 per cent, respectively. (Statistics Canada, *Immigration and Ethnocultural Diversity in Canada*.)

Chart 13
Share of Immigrant- and Non-Immigrant-Owned SMEs Active in Each Market, Ontario, 2007
(per cent)



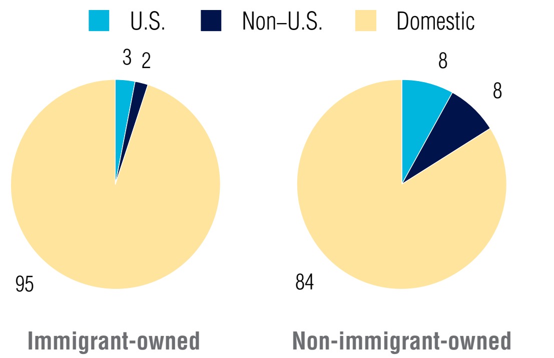
Sources: The Conference Board of Canada; Statistics Canada. Survey on Financing Small and Medium Enterprises, 2007.

Chart 14
Share of Immigrant- and Non-Immigrant-Owned SMEs Active in Each Market, Quebec, 2007
(per cent)



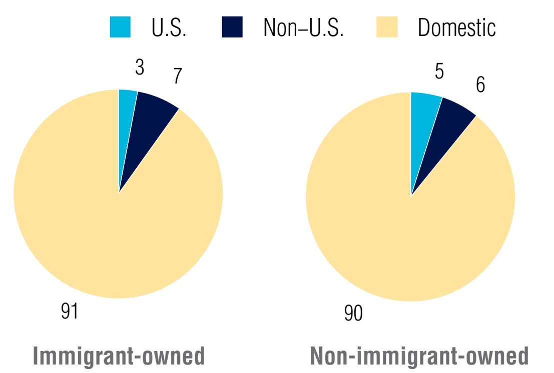
Sources: The Conference Board of Canada; Statistics Canada. Survey on Financing Small and Medium Enterprises, 2007.

Chart 15
Share of Immigrant- and Non-Immigrant-Owned SMEs Active in Each Market, British Columbia, 2007
(per cent)



Sources: The Conference Board of Canada; Statistics Canada. Survey on Financing Small and Medium Enterprises, 2007.

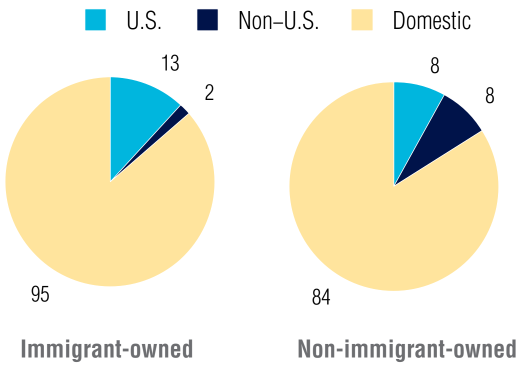
Chart 16
Share of Immigrant- and Non-Immigrant-Owned SMEs Active in Each Market, Prairies, 2007
(per cent)



Sources: The Conference Board of Canada; Statistics Canada. Survey on Financing Small and Medium Enterprises, 2007.

accounts for just over one-third. (See Chart 12.) B.C. accounts for less than one-twentieth of non-U.S. immigrant exporters in Canada. Alternatively, the share of immigrant-owned businesses in Quebec that export to non-U.S. markets is just over four and twenty times larger than the shares of immigrant-owned businesses in Ontario and B.C., respectively. (See charts 13, 14, and 15.) Meanwhile, the share of immigrant businesses in Quebec that export to the U.S. is two and more than four times larger than the shares of U.S. immigrant exporters in Ontario and B.C., respectively. (See charts 13, 14, and 15.) With the exception of B.C., non-U.S. immigrant exporters account for a larger share of total immigrant-owned businesses than non-U.S. non-immigrant exporters across provinces. (See charts 13 to 17.)

Chart 17
Share of Immigrant- and Non-Immigrant-Owned SMEs That Export to Different Markets, Atlantic, 2007
(per cent)



Sources: The Conference Board of Canada; Statistics Canada. Survey on Financing Small and Medium Enterprises, 2007.

The disproportionately low representation of non-U.S. immigrant exporters in B.C. is puzzling. One possible explanation is that the geography and industrial structures of Ontario and Quebec offer conditions that are more conducive for exporting to non-U.S. markets. Ontario is particularly appealing because it is home to Canada's major information and communications technology (ICT) clusters. For example, some of Canada's leading ICT clusters are in the Greater Toronto Area (GTA), Ottawa, and the region that encompasses Kitchener, Waterloo, Cambridge, and Guelph.[29] Meanwhile, Quebec has a relatively strong position in the wholesale/retail trade sector.[30] Furthermore, the major urban centres in Ontario and Quebec not only accommodate the growth of the knowledge-based and wholesale/retail industries, but also seem to attract immigrant exporters since more than 90 per cent of U.S. and non-U.S. immigrant exporters are based in urban centres as opposed to rural areas. (See Table 2.) Meanwhile, the forestry industry alone accounts for almost one-third of B.C.'s exports.[31] Therefore, everything else being equal, recent immigrant businesses are likely to find exporting more difficult in B.C. than in Ontario and Quebec due to the differences in industrial structure.

NON-U.S. IMMIGRANT EXPORTERS HAVE LIMITED ACCESS TO BUSINESS NETWORKS IN CANADA

Business networks or clusters constitute a variety of shared or pooled resources, including financial capital, employees, and machinery and equipment. Business owners may particularly benefit from ties to these networks during the early years of operations when it is difficult or costly to mobilize the resources necessary to grow their ventures.[32] Importantly, young and small firms that are connected to business networks are more likely to survive relative to their stand-alone counterparts.[33] Furthermore, when family members are heavily involved in such business clusters, connected companies may have relatively low financing and operational costs because they may undertake transactions on the basis of mutual trust rather than formal contracts.

To determine whether Canadian SMEs have access to such business networks, we investigated whether their owners were multiple business owners or portfolio entrepreneurs during the period of study.[34] Portfolio entrepreneurs are enterprising individuals who are not necessarily interested in owning and growing a single business into a large firm over time; instead, they are interested in owning and strategically growing a cluster of businesses that may offer related products or services, and potentially span two or more industries. By owning multiple businesses, portfolio entrepreneurs enable their companies to have access to inter-firm networks or business clusters.

29 Wolfe, "Knowledge, Learning and Social Capital in Ontario's ICT Clusters."

30 Statistics Canada, "Retail and Wholesale Trade."

31 B.C. Stats, *Annual B.C. Origin Exports*.

32 Harrison, Mason, and Girling, "Financing Bootstrapping and Venture Development in the Software Industry"; Malmström, "Typologies of Bootstrap Financing Behavior in Small Ventures"; Mason and Harrison, "An Overview of Informal Venture Capital Research"; Thorne, "Alternative Financing."

33 Rosa, "Entrepreneurial Processes of Business Cluster Formation and Growth."

34 Birley and Westhead, "A Comparison of New Businesses"; Kolvereid and Bullvåg, "Novices Versus Experienced Founders"; Rosa, "Entrepreneurial Processes of Business Cluster Formation."

On a whole, we found that a larger share of non-immigrant businesses—7 per cent compared with 3 per cent—have access to inter-firm networks in Canada relative to immigrant businesses. (See Table 2.) When we look at immigrant businesses as a group, we found that almost one-fifth of immigrant exporters that sell to the U.S. have access to inter-firm networks. (See Table 2.) This is almost 10 times and slightly more than 6 times the proportion of non-U.S. immigrant exporters and immigrant non-exporters, respectively, with inter-firm network connections. By having limited business ties in Canada, non-U.S. immigrant exporters are likely to find it difficult or costly to source both the financial and non-financial resources that are required to profitably expand their export operations. This is a cause for concern since non-U.S. immigrant exporters are disproportionately young and small.

Immigrant exporters to the U.S. are concentrated in the knowledge-based sector and, therefore less likely to be able to pledge tangible assets as collateral for loans.

NON-U.S. IMMIGRANT EXPORTERS HAVE BETTER ACCESS TO BANK FINANCING

On average, a larger proportion of immigrant businesses—84 per cent compared with 71 per cent—apply for a bank loan relative to non-immigrant businesses. (See Table 3.) The loan approval rate of immigrant businesses is 70 per cent, which is almost 10 per cent higher than that of non-immigrant businesses. (See Table 3.) While roughly four-fifths of U.S. and non-U.S. immigrant exporters apply for a bank loan, about two-thirds and three-quarters of U.S. and non-U.S. immigrant exporters, respectively, are approved for loans by Canadian banks. (See Table 3.) What is clear is that a larger proportion of U.S. immigrant exporters than non-U.S. immigrant exporters are denied a bank loan when they apply for one. On the surface, this difference in denial rates is puzzling because Canadian exporters are likely to seek financing from their banks with the expectation that they will qualify for a loan guarantee under Export Development Canada's Export Guarantee Program (EGP).[35]

Table 3
Access to Finance From Canadian Financial Institutions, 2007
(per cent)

Markets	Loan application rate	Loan approval rate
Immigrant		
U.S.	85	67
Non-U.S.	79	75
Domestic	85	60
Total	84	70
Non-immigrant		
Total	71	62

Sources: The Conference Board of Canada; Statistics Canada. Survey on Financing Small and Medium Enterprises, 2007.

Canadian exporters with C$5 million or more in export sales are likely to qualify for an EGP loan guarantee. Importantly, this focus on export value is consistent with prior studies that suggest that export promotion programs should primarily target medium-sized firms that are already exporting.[36] In practice, however, small Canadian exporters may qualify for an EGP loan guarantee if exports account for at least 15 per cent of their sales. This suggests that both U.S. and non-U.S. immigrant exporters are likely to qualify for EGP loan guarantees based on the current export-related criteria. However, Canadian financial institutions, acting independently of Export Development Canada, ultimately decide whether to provide loans to exporters with EGP loan guarantees. Given the lower loan approval rate of U.S. immigrant exporters relative to non-U.S. immigrant exporters (see Table 3), it is possible that Canadian financial institutions are less willing to lend to U.S. immigrant exporters with EGP loan guarantees.

35 Export Development Canada, *Export Guarantee Program*.

36 Fernandes and Mattoo, *Leave Export Promotion to Goldilocks*; Freund and Pierola, *Export Superstars*; Sui and Goldfarb, *Not for Beginners*.

The fundamental problem is that U.S. immigrant exporters are concentrated in the knowledge-based sector. As potentially innovative businesses, they are likely to hold a relatively large share of their assets in the form of intangible assets (i.e., intellectual capital); hence, they are not in a position to pledge business assets if loan approval is contingent on meeting collateral requirements. Furthermore, there is considerable uncertainty about whether they can successfully commercialize their novel product ideas, and generate a regular stream of cash flow within a given period.[37] For these reasons, bank financing is not an appropriate form of financing for innovative U.S. immigrant exporters.[38] A more appropriate form of financing is private equity from business angel investors and venture capital firms.[39] This in turn implies that innovative U.S. immigrant exporters are unlikely to significantly benefit from the bank-based EGP.

In this snapshot, recent immigrant business owners are more inclined to sell to non-U.S. markets than their non-immigrant counterparts.

In contrast, non-U.S. immigrant exporters typically operate in the wholesale/retail trade sector, and are therefore likely to hold a relatively large share of their assets in the form of tangible assets that may be pledged as collateral in support of their loan applications. Furthermore, there is less uncertainty about the future prospects of the wholesale/retail trade sector relative to the knowledge-based sector. For these reasons, non-U.S. immigrant exporters are more likely to receive bank loans under the EGP than innovative U.S. immigrant exporters.

CONCLUSIONS AND IMPLICATIONS

In this study, we examined whether recent immigrant business owners may significantly contribute to Canada's export agenda. A key goal stated by the Canadian government is to increase Canada's exports to fast-growth, non-U.S. markets. If recent immigrants have an advantage over non-immigrants in terms of foreign language skills, cultural knowledge, and access to networks in their non-U.S. countries of origin, then the former are better positioned to sell to non-U.S. markets. We have presented systematic evidence suggesting that recent immigrant business owners are in fact more inclined to sell to non-U.S. markets than their non-immigrant counterparts. More generally, our study indicates that non-U.S. immigrant exporters are:

- among the fastest growing Canadian SMEs. For the period 2007–11, the profits of non-U.S. immigrant exporters grew at an average annual rate of 21 per cent compared with 2 per cent for their non-immigrant counterparts;
- among the least profitable Canadian SMEs, despite their superior growth performance;
- more dependent on export activity for revenue generation relative to U.S. immigrant exporters and non-immigrant exporters in general;
- low-value exporters relative to U.S. immigrant exporters and non-immigrant exporters in general;
- younger and smaller than U.S. immigrant exporters and non-immigrant exporters in general;
- less connected to business networks in Canada compared with U.S. immigrant exporters and non-immigrant businesses in general;
- treated more favourably by Canadian financial institutions relative to U.S. immigrant exporters;
- predominantly wholesale and retail traders as opposed to U.S. immigrant exporters which are predominantly innovative businesses in the knowledge-based and manufacturing industries;

37 The borrowing limit (maximum authorized loan) that banks set for companies is traditionally tied to their operating cash flow as measured by Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA). Thus, knowledge-intensive ventures with little, if any, earnings from operations effectively have a borrowing limit of zero.

38 Even if Canadian banks were willing to finance innovative firms in the knowledge-based industry, they generally lack the in-house skill and expertise required to carry out due diligence at the level of venture capital firms. Ultimately, Canadian banks are precluded from financing excessively risky investments under banking regulations that are designed to safeguard the banking system.

39 Citizenship and Immigration Canada, *Start-Up Visa*.

- urban-based operations like U.S. immigrant exporters;
- predominantly based in Ontario and Quebec;
- operated by a relatively large share of female owners compared with either U.S. immigrant exporters or non-immigrant businesses in general.

IMMIGRANT OWNERSHIP MAY HELP LESS OPERATIONALLY EFFICIENT SMES TO EXPORT TO NON-U.S. MARKETS IN THE SHORT TERM

The finding that small, recently established, and less operationally efficient immigrant businesses disproportionately export to non-U.S. markets is a puzzling one. This finding is fundamentally at odds with prior research that points to operational efficiency or high productivity as a precondition for exporting to difficult foreign markets. To the extent that exporting to non-U.S. markets is more difficult and costly than exporting to the U.S., this suggests that immigrant ownership may actually confer advantages (i.e., social ties abroad, foreign language skills, cultural knowledge) that partially compensate for the relatively low operational efficiency of non-U.S. immigrant exporters in wholesale/retail trade. However, owner-specific advantages along this line may not adequately compensate for low productivity over the long term. As a result, the participation of less operationally efficient non-U.S. immigrant exporters in non-U.S. markets may be short-lived.

A FEW ESTABLISHED MEDIUM TO LARGE INNOVATIVE NON-U.S. IMMIGRANT EXPORTERS MAY ADVANCE CANADA'S EXPORT AGENDA

We found that recent immigrants account for 3 per cent (almost 30,000) of Canadian SMEs. Some may suggest that recent immigrants may play a more substantial role in export activity if they have a higher participation rate in business start-ups in Canada. However, the findings in this study suggest that it is not the proliferation of young and small, immigrant-owned export businesses that will substantially advance Canada's export agenda over the long term; rather it is the existence of a few medium to large innovative non-U.S. immigrant exporting businesses.[40]

40 Fernandes and Mattoo, *Leave Export Promotion to Goldilocks*; Freund and Pierola, *Export Superstars*; Sui and Goldfarb, *Not for Beginners*.

Financing Challenges Faced by Innovative Non-U.S. Immigrant Exporters

It is noteworthy that non-U.S. immigrant exporters are generally more likely to receive bank loans than U.S. immigrant exporters. However, we established that the former are predominantly wholesale/retail traders, while the latter are predominantly innovative businesses in the knowledge-based sector. It perhaps makes little, if any, difference to Canadian banks whether the most innovative immigrant exporters sell to the U.S. or non-U.S. markets. Canadian banks will generally avoid innovative businesses in the knowledge-based sector given the high degree of uncertainty that surrounds their future prospects, and the unavailability of marketable tangible assets that may be pledged as collateral. Thus, innovative immigrant exporters are expected to have a relatively high loan rejection rate as a group. This in turn implies they are unlikely to significantly benefit from the current bank-based Export Guarantee Program. Instead, they are more likely to benefit from access to private equity from business angel investors and venture capital firms.

The financing of innovative immigrant exporters to non-U.S. markets warrants special attention when formulating export promotion policies in Canada.

CONTRIBUTION OF RECENT IMMIGRANT BUSINESSES TO CANADA'S EXPORT AGENDA

We generally acknowledge that recent immigrant businesses have been contributing to Canada's overall export agenda based on their participation in both the U.S. and non-U.S. markets. In particular, we recognize that they have the potential to help Canada expand its horizon beyond the U.S. market because they are generally more likely to export than non-immigrant businesses and, when they do, they are more likely to sell to non-U.S. markets. However, the magnitude of their contribution to Canada's export agenda has been limited by a number of factors.

First, although recently established immigrant exporters are among the fastest growing companies in Canada, they are also among the least operationally efficient companies. Second, their business model is not generally founded on an innovation-based strategy that supports competition based on product novelty as opposed to product price. As a result, they may be vulnerable to price competition in the non-U.S. markets over the long term. However, we are quick to point out that these shortcomings primarily apply to non-U.S. immigrant exporters that belong to the wholesale/retail trade sector. In contrast, medium to large non-U.S. immigrant exporters in the knowledge-based sector appear to be more promising, although their innovation-based strategy predisposes them to formidable financing challenges in the Canadian private debt and equity markets. For this reason, the financing of innovative non-U.S. immigrant exporters warrants special attention when formulating export promotion policies in Canada. However, a more comprehensive approach also calls for attention to knowledge-intensive immigrant exporters that sell only to the U.S. market.

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Appendix A

Export Market Decision Regression Analysis

METHODOLOGY

A multinomial logit model is used to evaluate the export market decision of business owner *i* for a set of owner-firm characteristics and macroeconomic conditions. The model has the following structure:

$$ln[Prob(Market_i = j) \div Prob(Market_i = 0)] = \alpha' X_i$$

where the categorical dependent variable is the log odds of exporting to $Market_i$ relative to a given reference market (i.e., $Market_i = 0$). We consider two reference-market cases. In the first case, we define the reference market as the domestic market or "not exporting," and the alternative market choices as the U.S. and non-U.S. markets. In the second case, the reference market is the U.S., and the alternative choice is non-U.S. markets. X_i is a vector of owner and firm characteristics, and macroeconomic conditions that impact the firm's export market decisions. Finally, α is a vector of coefficients, or log odds ratios, to be estimated. Therefore, the odds ratios are obtained by taking the antilogarithm of reported estimates with respect to base e.

The variables included in the multinomial regression model are summarized as follows.

DEPENDENT VARIABLE: CATEGORICAL DEPENDENT VARIABLE (MARKET CHOICES)

- **U.S.**—A firm's export market choice is defined as the "U.S. market" if it exports only to the United States.
- **Non-U.S. market**—A firm's export market choice is defined as "non-U.S. market" if it exports to at least one non-U.S. country or region (i.e., Latin America, Europe, or Asia), and/or exports to both the U.S. and non-U.S. countries.
- **Domestic market**—A non-exporter's market choice is characterized as "domestic market."

INDEPENDENT/CONTROL VARIABLES

Owner characteristics:

- **Immigrant**—A binary variable with value 1 if the business owner is a recent immigrant (i.e., living in Canada for up to five years), and 0 otherwise.
- **Visible minority**—A binary variable with value for 1 if the business owner is non-white in colour/race without regard for the place of birth, and 0 otherwise. The definition of a visible minority excludes individuals of Aboriginal origin.

Firm characteristics:

- **Company age**—Age of the company at the time of the 2007 survey.
- **Company size**—Measured in terms of the value of assets.
- **R&D intensity**—R&D spending as a percentage of total expenditure.

- **Access to inter-firm network**—A SME belongs to an inter-firm network if it is owned by someone who also owns and/or operates at least another business; that is, the owner is a multiple-business owner or a portfolio entrepreneur. Thus, access to an inter-firm network is defined as a binary variable with value 1 if the SME owner is a portfolio entrepreneur, and 0 otherwise.

Macroeconomic conditions:

- **Sector/industry category**—Goods producing sectors (agriculture/primary industries, manufacturing); service sectors (knowledge-intensive industries, professional services; wholesale/retail trade; accommodation and food services).
- **Provinces/provincial region and the territories**—Atlantic provinces (New Brunswick, Prince Edward Island, Nova Scotia, Newfoundland and Labrador); British Columbia; Ontario; Prairie provinces (Alberta, Saskatchewan, and Manitoba); Quebec, and the Territories (Northwest Territories, Nunavut, Yukon).
- **Urban**—A binary variable with value 1 if the business is located in an urban centre, and 0 otherwise.

The variable denoting immigrant ownership is the principle independent variable; therefore, all other variables essentially constitute control variables. We did not include female ownership or business experience in the regression analysis because this information is available only for less than one-third of the observations in our sample.

DATA

To empirically evaluate the export market decisions of immigrant- and non-immigrant-owned SMEs, we draw on the following data sources: Statistics Canada's Survey on Financing of Small and Medium Enterprises, T2 Corporation Income Tax Return, and the General Index of Financial Information (GIFI). These confidential microdata files provide both financial and non-financial data on incorporated Canadian owners and firms. Based on the data available for the year 2007, we have a sample of 15,794 Canadian SMEs (immigrant-owned SMEs, 442; non-immigrant-owned SMEs, 15,352). Statistics Canada randomly selected 1 per cent of the estimated population of Canadian SMEs in 2007 (1.6 million) to be part of this survey.

RESULTS

TABLE 1
Export Market Decisions: Estimates (Log Odds Ratios) From the Multinomial Logit Model

Dependent variable **Market Choices** is a categorical variable that has three outcomes:

- **U.S.**—A firm's export market choice is defined as the "U.S. market" if it exports only to the United States.
- **Non-U.S. market**—A firm's export market choice is defined as "non-U.S. market" if it exports to at least one non-U.S. country or region (i.e., Latin America, Europe, Asia), and/or exports to both the U.S. and non-U.S. countries.
- **Domestic market**—A non-exporter's market choice is characterized as "domestic market."

Table 1
Export Market Decisions: Estimates (Log Odds Ratios) From the Multinomial Logit Model

	U.S. vs. Domestic		Non-U.S. vs. Domestic		Non-U.S. vs. US	
Immigrant-owned	–0.165	(0.363)	0.954***	(0.340)	1.119**	(0.445)
Visible minority	–0.289	(0.257)	–0.123	(0.200)	0.167	(0.309)
Access to inter-firm networks	0.437**	(0.191)	0.052	(0.221)	–0.385	(0.270)
Urban	0.042	(0.194)	0.399*	(0.207)	0.358	(0.268)
R&D intensity	0.037***	(0.010)	0.048***	(0.012)	0.011	(0.010)
Company size (assets)	0.015**	(0.007)	0.020**	(0.010)	0.005	(0.010)
Company age	0.007	(0.004)	0.004	(0.004)	–0.003	(0.005)
Industries						
Accommodation/food	–2.992***	(0.330)	–3.489***	(0.361)	–0.497	(0.479)
Agriculture/primary	–1.307***	(0.238)	–1.337***	(0.273)	–0.029	(0.344)
Knowledge-based	–0.979***	(0.164)	–0.601***	(0.153)	0.378*	(0.207)
Professional services	–1.322***	(0.181)	–1.038***	(0.177)	0.284	(0.238)
Whole/retail trade	–1.059***	(0.186)	–1.022***	(0.185)	0.037	(0.244)
Other services	–2.138***	(0.229)	–2.042***	(0.222)	0.096	(0.307)
Provinces/Territories						
Atlantic provinces	–0.465**	(0.222)	–0.220	(0.200)	0.245	(0.282)
British Columbia	–0.139	(0.204)	–0.082	(0.200)	0.056	(0.267)
Prairie provinces	–0.866***	(0.212)	–0.528**	(0.214)	0.338	(0.284)
Quebec	–0.465**	(0.189)	–0.014	(0.182)	0.451*	(0.245)
Territories	–0.523*	(0.314)	–0.653*	(0.363)	–0.130	(0.458)
Constant	–1.267***	(0.213)	–1.831***	(0.241)	–0.564	(0.302)

No.	11,111	Wald Chi–squared	428.776
Log pseudo-likelihood	–353,664	Pseudo R–squared	0.079

Note: standard errors are in parentheses. The reported estimates in this table are log odds ratios. To properly interpret these estimates, one has to first convert log odds ratios into odds ratios. This may be done with a standard exponent calculator, where the base is *e* (approximately 2.718) and the exponent or power is the reported estimate in question. To see how this works, consider the estimate of 0.954 that is reported for the effect of immigrant-ownership on the likelihood that Canadian SMEs will sell to non-U.S. markets as opposed to the domestic market (first entry in the second column of the table). Using an exponent calculator, one may confirm that a log odds ratio of 0.954 is equal to an odds ratio of 2.60. Since an odds ratio of 1 implies equal chances, the additional gain in the odds ratio is 1.60 when the firm is immigrant-owned as opposed to non-immigrant owned. Thus, we conclude that immigrant business owners are 1.6 times more likely than non-immigrant business owners to select non-U.S. markets over the Canadian market.
*p < 0.1, **p < 0.05, ***p < 0.01
Sources: The Conference Board of Canada.

Appendix B

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Selling Beyond the U.S.: Do Recent Immigrants Advance Canada's Export Agenda?

by Sui Sui and Horatio M. Morgan

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