

REPORT ON FOREIGN DIRECT INVESTMENT

[FDI]

OPERATIONS IN ATLANTIC CANADA

For

Atlantic Canada Opportunities Agency

BY

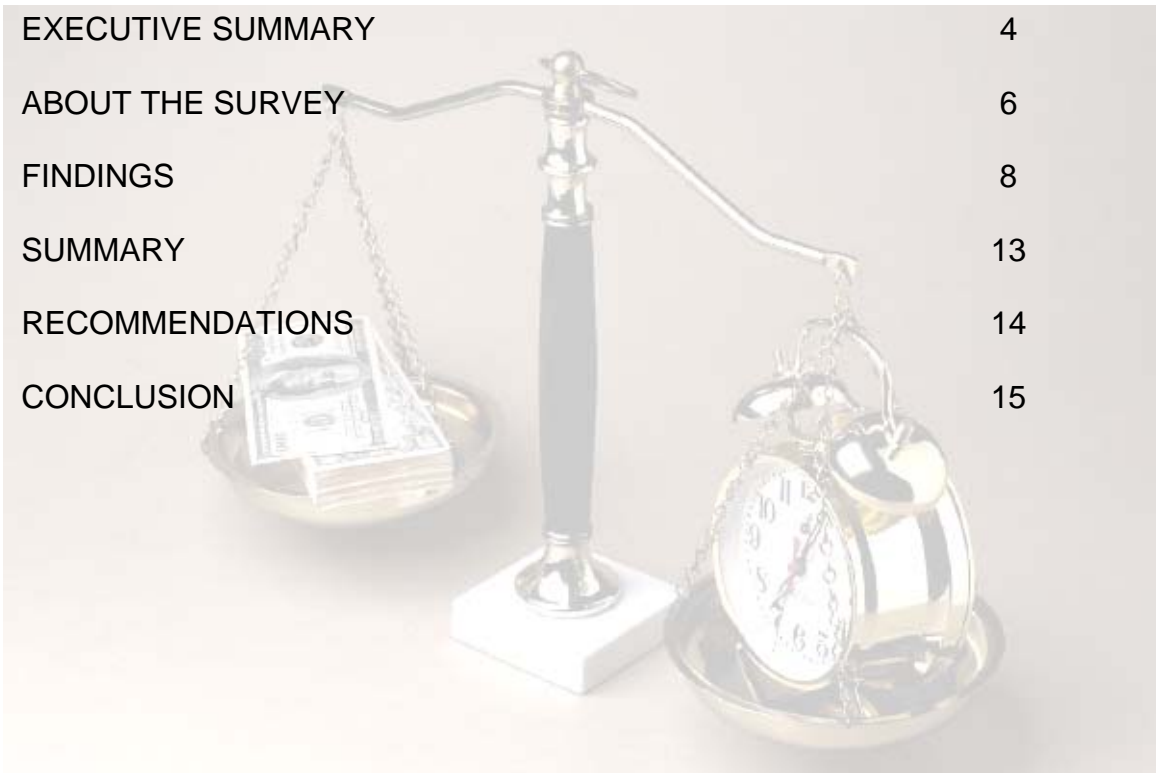
HIGH IMPACT SOLUTIONS

535 Montgomery Street
Fredericton, NB E3B 2X6
506 – 450-3710

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INTRODUCTION

High Impact Solutions is pleased to present the findings on foreign direct operations in Atlantic Canada. We gratefully acknowledge the assistance and support of the Atlantic Canada Opportunities Agency throughout this engagement.

In our opinion this reports provides excellent insight into the senior managers' experience with their foreign operations resident in this region.



EXECUTIVE SUMMARY

High Impact Solutions is pleased to present the findings of “A Survey of Foreign Direct Investors in Atlantic Canada to Support ACOA’s Investment Marketing Activities.”

Following is a synopsis of the Survey. A more detailed analysis and explanation is provided in the sections of the Report following the Executive Summary.

Out of a possible 76 targeted foreign-owned companies established in Atlantic Canada we received 62 responses or an over 80% response rate. Of these, fifty-one companies completed the survey in its entirety.

All of the input was constructive and for the most part positive, though some foreign owned firms are finding challenges to doing business in Atlantic Canada.

The manufacturing sector represented 50% of the replies with the customer contact centre sector accounting for 29.03% and information technology businesses coming in third at 12.90%. Processing companies were 2% and ‘other’ amounted to 3%. It consisted of aerospace repair and overhaul and other service companies.

By Province, 50% of the respondents were from New Brunswick, 32.35% from Nova Scotia and 8.82% each from Newfoundland and Labrador and Prince Edward Island.

We asked the FDI’s why they chose Atlantic Canada. Of the 59 companies that answered this question 24 or 40.68% cited the cost of doing business as key. 15.25% said it was the workforce and 13.56% attributed it to the raw materials. 10.17% said it was the access to the North American market with 5.08% citing nearness to the US. No company considered proximity to Europe as a reason. Only 2% of the companies openly cited incentives as the primary reason. However many companies did allude to incentives as being important.

98.18% of the respondents said that the region had met or exceeded their expectations and 90% of the respondents said that they would recommend Atlantic Canada as a site for new foreign investment.

18 Companies or 29% of the respondents are so pleased with the region that they are prepared to offer a testimonial to ACOA.

Perhaps the most exciting findings are that 16 companies plan to expand their operations in the next five years and that 14 companies also believe that other

business processes or operations of their firms could logically be expanded to Atlantic Canada. This represents an immediate opportunity for ACOA and the four Provinces that can be acted upon immediately.

In terms of the challenges, air connections and costs of air travel to and from our region remain. For manufacturers distance to market and transportation costs are concerns. The movement of goods back and forth across the border was not cited as an issue. However one company cited that it was becoming more onerous a process for US executives entering Canada and that this often leaves a negative first impression.

Other issues range from increasing challenges to finding the right people to accessing capital and financing, to union issues. Others cited a failure on the part of government to support their businesses by buying locally.

Almost 41% of the companies that took part in the survey said that the cost of doing business was the most important reason for choosing Atlantic Canada. With the rising value of the Canadian dollar companies have at the same time said that this advantage has been significantly diminished.

Over 15% stated that the quality and availability of the workforce was their primary reason for locating in the region. Many firms also believe that pressure on the workforce demand has somewhat hurt the work force availability and cost.

The findings of the survey present immediate opportunity for generating new qualified leads, offer new marketing material through third party corporate testimonials and through the overwhelmingly positive experience, statistically supported, that the FDI's have collectively experienced in Atlantic Canada.

At the same time the survey has revealed that there are challenges including the depreciation of the primary reason for locating here, the cost of doing business. Signs of labour compression and rising costs need to be addressed. Finally the age-old problem of air access and cost as well as the overall cost of transportation continues to be an issue.

ABOUT THE SURVEY

In early April 2005 we developed a target list of FDI's from ACOA's 2002 APEC Report. This formed the basis from which the actual contact list was developed.

Also, in early April we developed and finalized with ACOA the survey questions, of which there were fourteen. We intentionally kept the survey short to obtain maximum results. It took the respondents six to eight minutes to complete. This proved effective in that virtually all of the respondents completed the survey in its entirety.

Further, we utilized a 'url' to enable the respondents to complete the survey electronically and at a time of their choosing. This turned out to be tremendously popular as all but one of the participants chose to use it.

Originally we started with a 2002 list of 104 companies described as foreign owned. Eliminating Tier II companies subsequently reduced the list. Tier II companies were the companies that are engaged in mining, fishing, seal harvesting, oil and gas exploration and support, oil storage facilities and retail sales.

Subsequently 88 companies were targeted. Forty-two were located in New Brunswick, six located in Newfoundland, Nova Scotia had thirty-five and PEI had five.

To this we added 12 more FDI's that were identified by High Impact Solutions and not on the original list. These were either established since 2002 or missed from the original 2002 study.

In the course of actually contacting the companies we learned that ten companies were not foreign owned.

Ultimately we arrived at a population of 76 truly foreign owned Tier I companies to be surveyed.

It should be noted that of the 62 companies that completed the survey, not all completed every question. The percentage comparisons are based on the actual number of companies that answered the individual question.

The survey was conducted between April 21st and May 12th. There were sixty-two respondents representing 82% participation. Of the sixty-two replies fifty-one were completed in full.

Of the respondents 50% were from New Brunswick while 32.35% were from Nova Scotia. Newfoundland and Labrador and Prince Edward Island's responses represented 8.2% each.

Thirty-one companies or 50% were in manufacturing while 29.03% were in the customer contact centre industry with 12.90% in Information Technology. 3.23% were in the processing industry. The remaining 4.84% were in 'other' and consisted of aerospace repair and overhaul and the service sector.



FINDINGS

In general terms the findings presented herein are both revealing and full of opportunity. In some cases they verify what we thought we knew while in others, they dispel beliefs that we might have thought that they had about Atlantic Canada.

There are some immediate opportunities that should be acted upon. These appear in the 'Recommendations' section and relate to opportunity for business expansion as well as the attraction of new business functions of the established companies.

At the same time there are challenges to doing business in the region.

By question what follows are the findings and major comments of the respondents.

Question. ***“Prior to locating in Atlantic Canada did your company have a preconceived notion of the region?”***

Fully 60% or 36 companies that answered the question said 'No'. Of the 40% or 24 companies that said 'Yes' the comments were generally like the excerpted following few.

“ Back in the late 1990's we perceived it as a low cost and low turnover area. All of Atlantic Canada was low cost due to the exchange rate back then, and within Canada, Atlantic Canada was the lowest.”

“Hardworking, low cost, but difficult to access by air.”

“Good HR resource pool-innovative-inexpensive area to locate-some government support structures in place.”

“Positive but with geographical implications.”

“Highly educated population, customer service focused and relatively high unemployment rate. Reasonable cost of living standards”

There were also some companies who had prior knowledge of the region through having been from here, having done business with companies here and subsequently bought them or developed joint ventures with them.

Question. ***“Has your Atlantic Canada operation lived up to your expectations?”***

81.82% or 45 responses said 'Yes' and 9 of them or 16.36% said that they exceed expectations. We believe that this result in itself is a testimonial that ACOA should include in its external marketing of the region.

Most of the comments related to the quality of the workforce, a solid work ethic and a cost effective location with competitive wage rates.

Many of the comments were tempered with cautionary thoughts that included an erosion of the cost advantage given the increased value of the Canadian dollar. One of the call centres noted that they felt the region was saturated with call centres and this was driving up labour costs. Others were concerned about the cost of airfare and the difficulty getting to and from Atlantic Canada by air.

Question. "***What was your primary reason for locating in Atlantic Canada?***"

24 of the 59 companies that replied to this question, or 40.68% said the 'Cost of doing business' was the primary reason for locating in the region. 15.25% named the workforce, 18.64% named the proximity to North American marketplaces. No one named proximity to Europe as a reason for locating here. The proximity to raw materials was fourth at 13.56%.

By sector the findings were as follows. For 'Manufacturing' 25% chose 'cost of doing business' while 21% said 'access to the North American market' was the primary reason. 18% said 'proximity to raw materials' was the most important reason.

For the Customer Contact Centres, 61% cited the 'cost of doing business' as the most important reason with 28% naming the 'quality and availability of the workforce' as the primary reason.

The Information Technology sector said that the 'cost of doing business' was the most important reason coming in at 75%. Twenty-five percent named the workforce.

By Province the figures break down as follows.

- New Brunswick
 - Cost of doing business 57%
 - Workforce 9%
 - Nearness to US 9%
- Newfoundland and Labrador
 - Cost of doing business 50%
 - Workforce 33%
- Nova Scotia
 - Cost of doing business 29%
 - Proximity to raw materials 29%

Workforce 14%
Access to North American market 14%
Prince Edward Island
Cost of doing business 40%
Incentives 40%
Workforce 20%

While only 2% admitted to incentives being the main reason many mentioned incentives as an important secondary reason for choosing Atlantic Canada

Question. ***We asked the foreign companies to elaborate on the workforce as to productivity, skills, availability, turnover and language capability. We provided five categories of ratings.***

They were, 1. superior, 2. somewhat better, 3. about the same, 4. somewhat poorer, and 5. very poor.

Over 77% rated Atlantic Canada as superior or somewhat better in terms of low employee turnover. This was the highest percentage positive comment received in the section.

66% said that the quality of the workforce was either superior or somewhat better than other locations outside of Atlantic Canada.

49% felt that the productivity of their Atlantic Canadian workforce was either superior or somewhat better than other locations.

From the perspective of workforce availability 41.51% felt that the region was somewhat better and 9.43% believed it to be superior.

On the subject of workforce availability and breaking by sector 67% of the customer contact respondents said that the Atlantic Canadian workforce was either somewhat better than or superior to other locations in which they operated. For manufacturing the figure was 40% and for IT, it was 50%.

In terms of workforce quality, respondents by sector were as follows. A remarkable 94% of respondents in the customer contact field felt that the quality of the Atlantic Canadian workforce was either somewhat better than or superior to other locations. For IT, that number was 71% and for manufacturing, it was 40%.

By Province, and on the subject of workforce availability, 55% of the New Brunswick respondents felt that the availability was either somewhat better than

or superior to other locations. In Nova Scotia that figure was 47% with Newfoundland and Labrador coming in at 33% and PEI at 20%."

As to language capability some respondents commented negatively. But rather than referring to the bilingual [French/English] competence, they alluded to poor English grammar. 62.75% believed the language capability was about the same.

Question. **Overall operational costs.** 66% felt that the costs in terms of competitiveness were superior or somewhat better.

Question. **Transportation costs.** 45% of the companies that responded to this question believed that our costs were somewhat poorer, [read higher] than other locations.

Question. **Regulatory red tape.** 62% thought we were 'about the same' as other places. 26% actually believed that we were somewhat better than other locations.

Question. **We asked the FDI's about corporate tax structures in Atlantic Canada.** Fully 75% were of the opinion that the region's corporate tax rates were about the same or better than other jurisdictions. Over 30% felt ours were more competitive than elsewhere. The problem appears to be an "outsiders' perception which seems to be the opposite to that of an 'insiders' reality.

Question. **"Do you have plans to expand your existing Atlantic Canadian business in the next five years?"** The response to this question was that a remarkable 26% or 16 companies have plans to expand. This represents immediate opportunity for the Atlantic Canada Opportunities Agency.

But even more exciting is the revelation to the following question.

"Are there other processes or functions that the current existing business function of our company that could logically be expanded into Atlantic Canada?" 14 companies have advised that there are indeed such processes or functions that could be added.

Question. **"Is Atlantic Canada's corporate tax level competitive?"** 63.04% or 29 companies felt that the corporate tax rate was competitive. The same companies were of the opinion that the perception was that our corporate taxes were not competitive.

Interestingly over 90% acknowledged that though our personal income tax rates were high, it was irrelevant to their decision to locate in Atlantic Canada.

The survey revealed that foreign companies are facing many challenges to their businesses in Atlantic Canada. We received 34 comments on the question

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“What, if any, were the barriers and difficulties you encountered in investing in Atlantic Canada?”

The major areas of concern are;

- Air access and cost
- Transportation issues for manufacturers and distance to markets
- Small decreases in the quality of labour starting to be noticed
- Perception of high corporate taxes

Question. ***“If you had a positive experience with Atlantic Canada and your decision to locate here, would you be prepared to provide a testimonial to that effect that ACOA could use?”***

EIGHTEEN COMPANIES OR 29% ARE SO PLEASED WITH ATLANTIC CANADA THAT THEY ARE PREPARED TO PROVIDE A TESTIMONIAL. We were impressed with the number of firms that were pleased to do this. The companies with three exceptions wish to be contacted directly for their testimonial. In some cases they will refer to ‘head office’ for the comment.

Question. ***We asked for comments on the Canadian government investment policy and regulatory requirements.*** Comments were mixed. They ranged from no opinion to positive and negative opinions.

We received positive feed back on the subject of incentives. Generally speaking it was felt that both levels of government provided effective financial support. The interest free deferred repayment type program was considered useful and a responsible way of providing support. Atlantic Canadian incentives were considered as good as any in Canada. One respondent noted that they were not as good as American incentives.

SUMMARY

The FDI's in Atlantic Canada have had and continue to have a successful business experience here. So much so that 98% of them say that the region has met or exceeded their expectations. Indeed 90% would recommend Atlantic Canada as a site for other foreign companies to expand into. In fact 18 companies or 29% of the respondents are prepared to offer a testimonial that ACOA may use.

Over 80% believe that their Atlantic Canada experience has been superior or somewhat better than experiences in other jurisdictions.

Actionable findings are that 26% or 16 companies have plans to expand in the next five years. This represents an opportunity for ACOA to ensure the expansions take place and that they employ as many Atlantic Canadians as possible.

Further 14 other companies believe that there are other business functions or processes of their company that could logically be expanded into Atlantic Canada. This is another finding that ACOA can capitalize upon by immediately.

In terms of taxes our personal tax rates, though considered high, were irrelevant to their decision to locate in Atlantic Canada. Our corporate tax rates were relevant but they were observed to be competitive with other locations and therefore not a deterrent to their operations. They did acknowledge though that the 'perception' is that they are much higher than in other locations.

On the negative side or at least in terms of challenges there are indeed some issues that require further study and action.

Our competitive cost advantage is eroding. The quality and quantity of the skilled work force is decreasing. Getting to and from Atlantic Canada by air continues to be a challenge. Corporate taxes are considered competitive yet the perception is that they are high.

A final outcome of the survey was the identification of 12 additional foreign companies and the identification of 10 previously considered foreign companies as, in fact, being domestic.

RECOMMENDATIONS

From a marketing perspective ACOA should use the overwhelmingly positive impression that the FDI's have of their Atlantic Canada experience and their hearty endorsement of the region in both local and external marketing initiatives.

ACOA should immediately develop a plan of action with the 14 companies that have stated that other components of their business could move to Atlantic Canada.

ACOA should develop a plan of action aimed at the 16 companies that intend to expand their existing business functions in the next five years.

ACOA should immediately follow-up with all companies that indicated they were prepared to provide testimonials that can be used for marketing purposes.

Continue to get the competitive corporate tax message out to prospective investors and offer comparative examples to US jurisdictions you are targeting for investment.

Consider the development of a coordinated aftercare program directed to the foreign firms in Atlantic Canada. This would be effective in a range of areas. First it could identify new business opportunities from expansions and the addition of different business processes. Second it could facilitate the retention of these businesses and identify issues that may be emerging before they become a problem.

A word of caution is in order. The survey was conducted in "strict confidence" as indicated in the introductory letter signed by M. Serge Langis, Director General, Trade and Investment and reiterated during our phone contact and should be observed. It would be inappropriate to share specific information gathered in this survey with outside agencies and / or governments without the permission of the company that submitted it.

CONCLUSION

This survey and the nature of the questions, the quality and quantity of the responses have truly provided excellent intelligence to the Atlantic Canada Opportunity Agency. This is much more than a sampling of the FDI's. Indeed it is feedback from nearly all the Tier I FDI's resident in Atlantic Canada.

The challenge now is to act upon the findings to ensure that maximum employment potential and wealth generation is assured.

It has been our pleasure to have worked on this most interesting assignment.

