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Business

Q U A R T E R L Y

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PERFORMANCE

Trends

In the second quarter of 2006, employment in the small business sector increased by 103 200 compared with the same quarter of 2005. This figure represented 36.7 percent of overall employment growth, the largest contribution small business has made to job creation since the first quarter of 2004 (62.1 percent).

The number of business bankruptcies continued to fall, reaching 1801 in the second quarter of 2006, a drop of 10.8 percent from the same period in 2005.

In the third quarter of 2006, self-employed workers numbered 2.49 million, a 1.2-percent drop from the same period in 2005. This represents a second consecutive year-over-year decrease following four years of growth.

Total business loans outstanding¹ from chartered banks continued to rise in the second quarter of 2006, reaching \$110.9 billion. This represents an increase of 10.7 percent from the same quarter of 2005. Loans of less than \$1 million accounted for 47 percent of total business loans.

¹ Excluding non-residential mortgages, agricultural loans and customers' liability under acceptances.

SME FDI WORKSHOP:

Building a Better Understanding of SME Financing

The importance of small businesses to economic growth and well-being has long been recognized. Moreover, access to financing can be a critical factor in the growth of small businesses. Governments need good information to ensure that the small and medium-sized enterprise (SME) financing programs and initiatives they put in place are relevant. To this end, the SME Financing Data Initiative (SME FDI) — a partnership of Industry Canada, Statistics Canada and the Department of Finance — provides a comprehensive and impartial means of collecting and analyzing data on both the demand and supply sides of financing for SMEs.

A recent workshop with key stakeholders and potential funding partners re-examined the SME FDI. The goal was to look at the results from its first five years and identify priorities for the next five. The event was co-hosted by Industry Canada and the University of Ottawa School of Management, with support from and senior-level participation by the Business Development Bank of Canada (BDC) and Export Development Canada (EDC).

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Approximately 80 invited guests from various institutions participated:

- representatives from federal departments (Environment Canada, Agriculture and Agri-Food Canada);
- provincial government departments (Ontario, Quebec, British Columbia, and Newfoundland and Labrador);
- regional development agencies (e.g. FedNor, Western Economic Diversification, Atlantic Canada Opportunities Agency and Canada Economic Development for Quebec Regions);
- Crown corporations;
- academic and private sector researchers; and
- representatives from business associations (e.g. Canadian Federation of Independent Business and the Canadian Bankers Association).

The event also attracted international participants from Denmark (Danish Ministry for Economic and Business Affairs), the Organisation for Economic Co-operation and Development (OECD), Sweden (University of Lund), the United States and the United Kingdom.

Participants discussed the importance of understanding financing gaps in Canada, and the challenges of identifying the nature and location of financing gaps. Results from the SME FDI were presented covering topics such as: evaluating financing programs, identifying debt financing gaps, understanding the financial market and understanding borrower attributes.

Workshop participants also explored future directions for the initiative. Possible deeper collaboration with other government departments, the private sector, and the research and academic community was solicited. Participants identified four key priorities for consideration:

- develop longitudinal data to further understanding of the factors that lead to growth, survival and failure of small businesses;
- develop a better understanding of financing gaps, particularly in succession financing;
- improve communication and develop a dissemination strategy that would foster greater linkages between the demand and supply of financing, greater knowledge of investor readiness, and further information at the sub-regional level; and
- increase understanding of obstacles to obtaining financing, including information on the changing financial marketplace, the impacts of an SME's stage of development and urban–rural distinctions.

The SME FDI partners will capitalize on the interest expressed at the workshop to identify new partners to transform these results into an action plan for the initiative over the next five years.

For further information about the SME FDI Workshop, or data and research undertaken by the initiative, please visit www.sme-fdi.gc.ca.

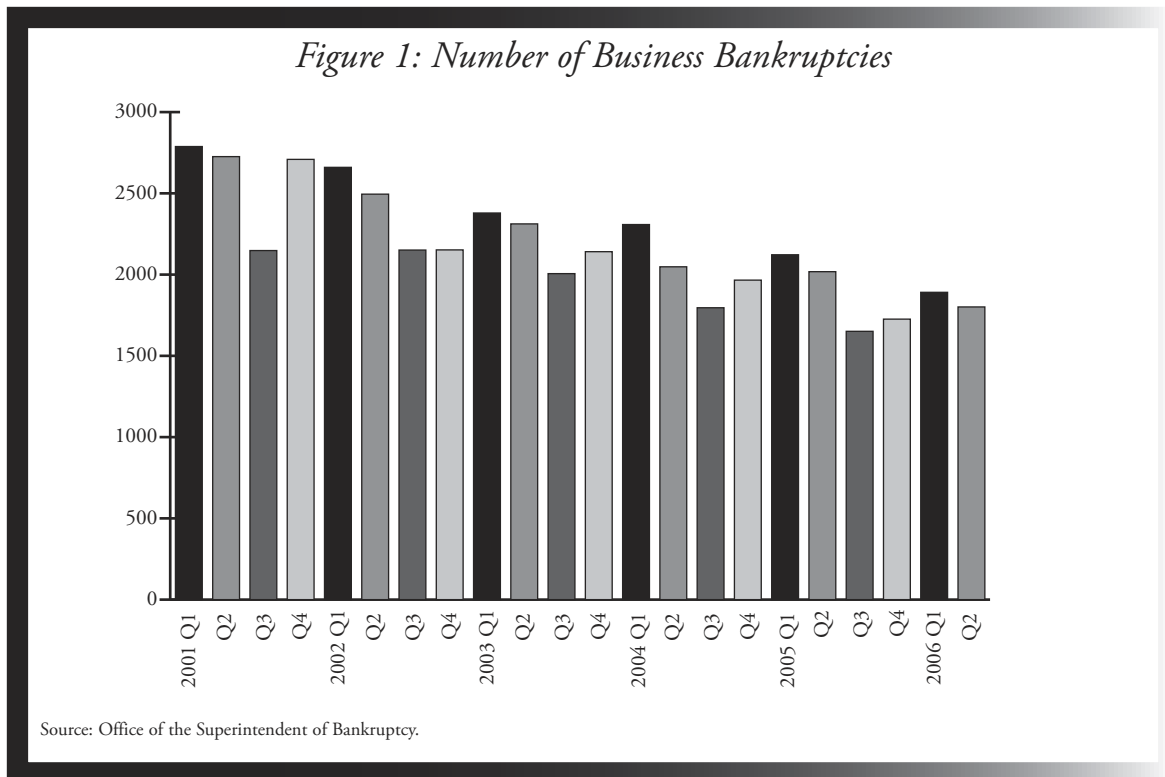
BUSINESS *Bankruptcies*

In the second quarter of 2006, the number of business bankruptcies continued to fall, dropping by 10.8 percent year over year — from 2018 to 1801 (Figure 1). There has not been a year-over-year increase in business bankruptcies in Canada since the fourth quarter of 2001. The current figure also represents a 4.8-percent drop over the first quarter of 2006 (1891 bankruptcies).

Four sectors were responsible for half the business bankruptcies during the second quarter of 2006: construction (316), retail trade (234), accommodation and food services (191), and transportation and warehousing (182). The construction and retail trade sectors were primarily responsible for the year-over-year drop in commercial bankruptcies, each with 77 fewer bankruptcies compared with the second quarter of 2005.

Although the number of business bankruptcies fell, the liabilities in these bankruptcies increased substantially. Total business bankruptcy liabilities in the second quarter of 2006 came to

\$1.6 billion — more than double the \$731 million in liabilities in the second quarter of 2005. However, this sharp rise was primarily caused by a small number of bankruptcies in the finance and insurance sector. In this sector, total liabilities rose from \$7.6 million in the second quarter of 2005 to over \$862.5 million a year later. Excluding the finance and insurance sector, overall liabilities increased by only 1.3 percent compared with the second quarter of 2005, from \$723.6 million to \$732.7 million. Total liabilities in the retail trade sector were also particularly high at \$193.2 million, compared with \$76.4 million in the second quarter of 2005. Such a steep increase naturally exerted upward pressure on the average liability per bankrupt business, which rose to \$886 000 from \$362 000 in the second quarter of 2005. Excluding the finance and insurance sector, the average liability increased by only 14 percent, from \$361 000 to \$412 000 in the second quarter of 2006.



JOB *Creation*

According to Statistics Canada's *Survey of Employment, Payrolls and Hours*, the number of payroll employees continued to increase in the second quarter of 2006 by 281 016 compared with the same quarter of 2005, reaching a total of 13 884 867 (Table 1). This corresponds to annual growth of 2.1 percent, the highest increase in 12 quarters. Although large businesses¹ contributed most to overall job growth with 53.1 percent of net new jobs created, small businesses' contribution continued to increase, reaching 36.7 percent. This represents the largest contribution small business has made to job creation since the first quarter of 2004, when small businesses contributed 62.1 percent of overall job growth.

In the second quarter of 2006, four sectors were the main contributors to job growth: administrative and support, waste management and remediation services (45 322 jobs); health care and social assistance (40 060 jobs); public administration (39 969 jobs) and retail trade (36 537 jobs). The highest growth

occurred in the mining and oil and gas extraction sector, however, with a 13.6-percent increase from the second quarter of 2005 (or 21 851 jobs). The construction sector contributed most to job growth in the small business category, with 16 795 net jobs created. The health care and social assistance sector and the accommodation and food services sector followed with more than 13 000 new jobs each in small businesses.

Two sectors lost jobs. The forestry sector's net loss of 3047 jobs reflects the difficulties this sector has been facing. Small businesses were the most affected, with 1943 jobs lost. The manufacturing sector experienced a net job loss of 19 208. However, all the job loss was in medium-sized and large businesses. The number of small business jobs in manufacturing increased by 3873 from the second quarter of 2005.

¹ Small businesses are defined as having fewer than 100 employees, medium-sized businesses having 100 to 499 employees and large businesses having 500 or more employees.

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Table 1: Year-Over-Year Net Change¹ in Payroll Employment² by Industry, Second Quarter 2006

Quarter	Change		% Contribution to Total Net Change (Number of Employees)								
	%	Jobs	0-4	5-19	20-49	50-99	0-99	100-299	300-499	100-499	500+
Q2 2005	1.2	160 817	-3.8	-5.4	12.2	10.4	13.5	24.3	-20.0	4.3	82.2
Q3 2005	1.4	186 005	3.8	-2.6	14.4	11.1	26.8	18.6	-8.4	10.2	63.1
Q4 2005	1.6	219 582	6.7	-3.7	5.8	8.8	17.6	11.3	-1.3	9.9	72.4
Q1 2006	1.9	251 814	11.2	2.0	10.2	10.2	33.5	7.8	-0.6	7.1	59.3
Q2 2006	2.1	281 016	13.6	4.2	8.8	10.1	36.7	4.9	5.3	10.2	53.1
Industry	Growth (Jobs), Second Quarter 2006										
Forestry	-5.1	-3 047	-122	-941	-457	-423	-1 943	667	-750	-83	-1 023
Mining and oil and gas extraction	13.6	21 851	840	1 160	608	598	3 206	867	2 555	3 422	15 224
Utilities	0.1	144	40	264	-95	53	262	-386	-227	-613	494
Construction	2.9	19 883	9 681	1 200	2 529	3 385	16 795	2 095	3 098	5 193	-2 107
Manufacturing	-1.0	-19 208	735	-86	479	2 745	3 873	-9 657	1 846	-7 811	-15 270
Wholesale trade	0.4	2 683	2 089	567	-337	-1 807	512	-142	224	82	2 087
Retail trade	2.2	36 537	1 130	89	6 080	4 851	12 150	8 185	3 489	11 674	12 712
Transportation and warehousing	1.2	7 295	1 864	291	578	-1 137	1 596	-1 484	301	-1 183	6 884
Information and cultural industries	0.9	3 167	464	99	15	1 220	1 798	-672	-235	-907	2 277
Finance and insurance	1.3	7 641	4 064	2 197	1 482	667	8 410	1 496	2 426	3 922	-4 691
Real estate and rental and leasing	2.3	5 594	2 373	-1 044	787	-184	1 932	-1 916	1 973	57	3 605
Professional, scientific and technical services	1.3	8 827	9 635	-2 217	-269	2 227	9 376	2 993	-2 634	359	-908
Management of companies and enterprises	6.2	5 871	-3 137	-1 927	-1 524	-165	-6 753	645	-105	540	12 084
Administrative and support, waste management and remediation services	6.9	45 322	2 004	4 341	2 221	2 279	10 845	4 988	9 516	14 504	19 972
Educational services	2.9	30 034	819	928	896	530	3 173	-5 021	-3 061	-8 082	34 945
Health care and social assistance	2.9	40 060	409	5 139	5 912	1 550	13 010	5 984	-5 823	161	26 889
Arts, entertainment and recreation	0.8	2 115	1 007	-96	-523	921	1 309	-354	1 054	700	106
Accommodation and food services	1.9	18 059	778	1 435	4 006	6 879	13 098	3 676	384	4 060	901
Other services (excluding public administration)	1.6	8 217	3 807	-162	1 776	3 135	8 556	1 296	-159	1 137	-1 475
Public administration	5.1	39 969	-258	584	657	1 013	1 996	397	1 149	1 546	36 427
Canada total	2.1	281 016	38 226	11 820	24 821	28 333	103 200	13 656	15 024	28 680	149 135

Source: Statistics Canada, *Survey of Employment, Payrolls and Hours*, September 2006.

¹ Year-over-year net change in payroll employment is calculated as the variation between the level of employment in a given quarter and the level in the same quarter a year before.

² *Survey of Employment, Payrolls and Hours* data exclude self-employed workers who are not on a payroll and employees in the following industries: agriculture, fishing and trapping, private household services, religious organizations and military personnel of defence services. The data breaking down employment by size of firm also exclude unclassified industries.



SELF-Employment

According to Statistics Canada's *Labour Force Survey*, the number of self-employed workers in Canada rose from 1.84 million in 1990 to 2.51 million in 2005 — an average annual growth of 2.1 percent. Like the Canadian population as a whole, Canada's self-employed workers are becoming increasingly better educated (see Table 2). Whereas 40.1 percent of self-employed workers had at least a post-secondary certificate or diploma in 1990, this figure rose to 58.5 percent in 2005. People with a university degree are also increasingly opting to work for themselves. Over this 15-year period, the proportion of self-employed workers with a university degree rose from 15.9 percent of all self-employed workers to 25.1 percent. Their number rose by 5.3 percent on average per year. On the other hand, the proportion of self-employed workers who did not graduate from high school dropped by more than half — from 33.1 percent to 15.0 percent.

The improvement in educational attainment was faster for self-employed workers than for employees. Whereas the proportion of people with at least a post-secondary certificate or diploma was smaller for self-employed workers than for employees (40.1 percent as opposed to 40.9 percent) in 1990, 15 years later, self-employed workers were more likely than employees to hold a post-secondary certificate or diploma or a university degree (58.5 percent compared with 56.6 percent).

This improvement in educational attainment was apparent in all categories of self-employed workers. Educational attainment also appears to be associated with the likelihood that self-employed workers will incorporate their businesses. In 2005, 60.4 percent of self-employed with incorporated businesses and paid help, as well as 63.2 percent of those in incorporated businesses without paid help, held a post-secondary certificate or diploma or a university degree. This figure is less than 60 percent for self-employed workers whose businesses were not incorporated.

Table 2: Distribution of Self-Employed Workers¹ and Employees (percentage) by Education Level, Canada, 1990 and 2005

Education Level	Employees		Self-Employed		Incorporated				Unincorporated			
	1990	2005	1990	2005	With Paid Help		Without Paid Help		With Paid Help		Without Paid Help	
					1990	2005	1990	2005	1990	2005	1990	2005
0–8 years	6.6	2.6	12.0	4.5	7.9	3.0	7.3	3.3	12.8	5.2	14.1	5.1
Some high school	19.0	10.8	21.1	10.5	15.8	8.8	16.2	8.4	18.1	9.6	24.8	12.0
High school graduate	23.3	21.0	19.4	19.7	21.5	21.1	20.5	18.5	17.8	19.4	18.4	19.6
Some post-secondary	10.1	9.0	7.5	6.7	8.1	6.7	8.1	6.6	6.1	6.0	7.5	6.8
Post-secondary certificate/diploma	26.7	34.8	24.2	33.4	27.0	33.1	28.3	34.0	23.8	31.1	22.8	34.3
University degree	14.2	21.8	15.9	25.1	19.6	27.3	19.6	29.2	21.4	28.8	12.4	22.3
All levels	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Statistics Canada, *Labour Force Survey*, 2005, special tabulations.

¹ Unpaid family workers are not shown in this table due to their small number.



FINANCING

Foreign Investment Increasing Market Share in Canadian Venture Capital Investment

Venture capital (VC) financing and fundraising activities are widely believed to be important for the growth and survival of companies. However, in recent years, the market share of VC suppliers in Canada has been changing, with foreign investors accounting for a higher proportion of the VC market. According to Canada's Venture Capital and Private Equity Association, the rise in the proportionate share of foreign funds in the Canadian venture capital market reflects the shortage of risk capital available from Canadian domestic sources relative to the quality of available opportunities.¹

Canadian VC Activity, 1996 to 2006

The Canadian VC market has tightened since 2001. Activity fell steadily until 2003, and despite a rise in VC investment activity during 2004–2005, investments are experiencing a downward trend in 2006. The total amount invested during the first half of 2006 reached \$867 million, down 13 percent from the

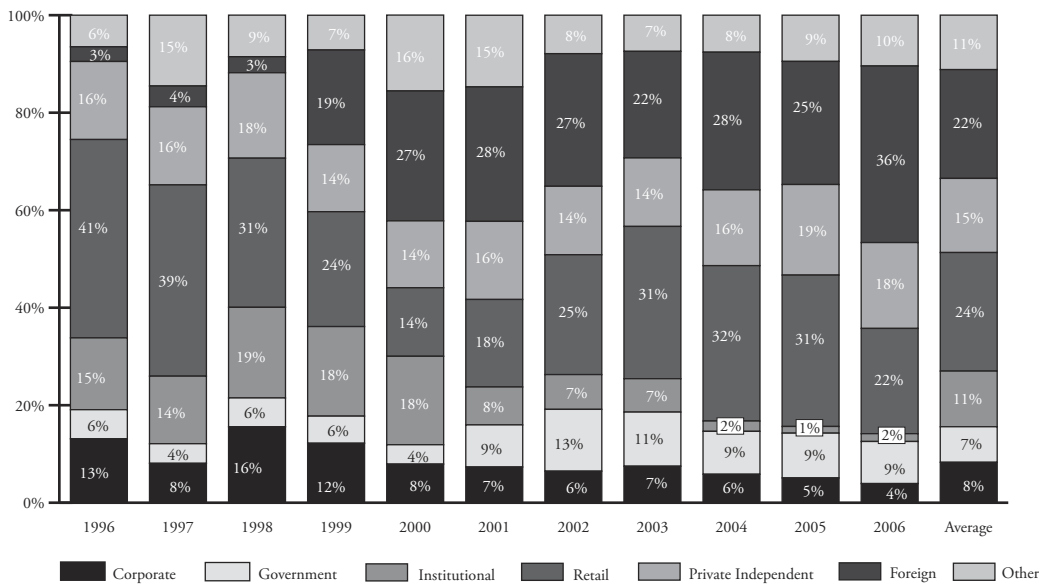
\$1 billion recorded during the same period in 2005. Fundraising activity experienced a sharper decline, from \$1.2 billion in the first half of 2005 to \$879 million in the first half of 2006, or 27 percent.

Importance of Foreign VC Investments

As illustrated in Figure 2, foreign investment in 1999 represented 19 percent of the market, and continued to rise to at least 22 percent of total Canadian VC investment. In the first half of 2006, non-Canadian (primarily U.S.) investors accounted for 36 percent of venture-backed investments to Canadian firms. However, during the second quarter of 2006, foreign investment dropped by 22 percent compared with the \$236 million invested in the same quarter in 2005. While foreign investment is declining, it is not declining nearly as rapidly as Canadian-based VC; hence, the share of foreign investment in Canadian VC investment continues to increase.

¹ Canada's Venture Capital and Private Equity Association, *Canada's Venture Capital Industry More Active in Second Quarter 2006*, news release, August 2006.

Figure 2: Share of Dollars Invested by Investor Type from 1996 to 2006



Source: Thomson Financial.

RECENT *Developments*

OECD–APEC Global Conference on “Removing Barriers to SME Access to International Markets”

The OECD–APEC Global Conference on “Removing Barriers to SME Access to International Markets” was held from November 6 to November 8 in Athens, Greece.

The main goal of the Athens conference was to identify cost-effective mechanisms to remove barriers to SME access to international markets and promote the internationalization of these enterprises. The conference shed light on SME perspectives on the barriers they face when trying to access international markets. Participants also reviewed best practices for support programs put in place by governments, at both

national and local levels, to assist in dealing with these impediments.

For more information on the OECD–APEC conference, please visit www.oecdathens.gr.

The 13th Asia-Pacific Economic Cooperation (APEC) Small and Medium Enterprises Ministerial Meeting

The APEC Small and Medium Enterprises Ministerial Meeting was held in Hanoi, Vietnam, on September 28 and 29, 2006. The Working Group’s main objective is to encourage the development of the small and medium-sized enterprises (SMEs) that create most of the employment in the Asia-Pacific region and are the backbone for the region’s economic growth. Participants aimed to identify the best policies and entrepreneurial practices to strengthen SMEs’ competitiveness for trade and investment in the APEC community.

For more information on the APEC SME Ministerial Meeting, please visit www.apec.org.

Small Business Quarterly Small Business Policy Branch

The *Small Business Quarterly* (SBQ) provides a quick and easy-to-read snapshot of the recent performance of Canada’s small business sector. The SBQ is published by the Small Business Policy Branch of Industry Canada.

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