



INVESTMENT ATTRACTION: The challenges ahead of small communities to attract Foreign Direct Investment (FDI)

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Abstract

The world is changing, and the global market is shrinking. Countries are seeking to build new partnerships to attract new foreign direct investments. Amid uncertainties in various global markets, investors are seeking safer investing markets. As per FDI Intelligence's 2017 report, Ontario was ranked 'top 3', making it the best target for foreign capital investments in North America. But are countries like Canada and their rural communities ready to accept the challenge of FDI? The white paper summarises the various factors that affect FDI decisions and highlights the challenges faced by rural communities in Canada in attracting foreign direct investment. The paper concludes that small communities are required to take collaborative approach and partner with other communities to attract FDI. It also summarises the discussion held at the Hot Button Workshop at EDCO 2018 with several rural community city managers and senior staff members. In this regard, the white paper suggests some solutions that can help make rural communities FDI ready.

Introduction

Financial markets tend to be globally integrated; due to which, the exchange controls and market access is more liberated. This kind of integration has been conducive to a milieu in which economies compete against one another to achieve more share and participate more in the global market. The evolving market participation has introduced new financial instruments that broaden access to market and lessen the transaction costs which itself urge more investors to invest in foreign markets. The technological advances in communications and data analysis have further enhanced foreign market participation and foreign direct investment (FDI) (OECD, 2008).

FDI is an investment through which the investor owns at least 10 percent of the voting parity in the management of a given enterprise located in another economy. There are two

ways that individuals and companies could create foreign direct investments; firstly, by investing in the financial capital of a company that is already operating in another country or by investing in a new project dealing with production in Canada by a foreign country. Both ways generate profit for investors in the investing economy (Miele 76).

FDI, be it inward or outward, is a driving key to economic growth in economies. It expands competitiveness in both the host (recipient) and home (investing) economy. The investments by foreign enterprises in production sector increase employment and national income. It also boosts the opportunity to transfer technology and know-how as knowledge and expertise between economies (OECD). FDI boosts the living standard of the economies in the long run.

Considering the merits of FDI for local economies, the developing and developed economies are reaping the benefit of the global economic opportunities. In this regard, the *Canadian Direct Investment Abroad* (CDIA) takes place in diverse sectors including mining, financial services, wholesale and retail trade, energy and manufacturing (Miele 76). Several Canadian firms as international players include *Brookfield Asset Management INC.*, *Power Corp*, *Manulife Financial Corp.*, and *Nexon Inc.*, to name a few (Krzepkowski & Mintz). However, when it comes to inward FDI, which is the direct investment by foreign investors in Canadian companies or projects, it could be argued that Canada is behind the other economies in attracting FDI (ibid; Miele 76).

Different provinces have initiated plans and programs to improve their attraction to FDI. Ontario as an example is one of those provinces that have implemented strategies to represent Canada as a secure place to carry out business. Ontario's municipalities have initiated strategic

plans to urge foreign investors to invest in their communities. Attracting foreign investors is not an easy task and will not be an overnight accomplishment. Smaller municipalities have an additional task to overcome the challenges to attract FDI. The focus of this research paper is to identify the challenges and make recommendations on how to handle these challenges in the long run.

Foreign Direct Investment in Ontario

There are several factors that affect FDI. Despite some factors such as production sites shifting towards clusters (where firms outsource production of specialized components to experts), developing economies attracting inflow of global FDI, multinational firms turning their attention and interest to “new growth” or emerging economies, Canada’s performance in attracting FDI has exceeded its overall economic weight (Moloney et al. 14). According to a 2017 report by *FDI Intelligence*, the Province of Ontario attracted 8% of the FDI in North America. Attracting a total of 128 FDI projects, Ontario ranked as the ‘top 3 destination’ for capital investment in North America (Ontario, Canada ‘top 3’ destination). Ontario attracted a total of \$4.5 billion in investments in the year 2016.

Another report, *2017/2018 American Cities of the Future Report*, recognised various cities of Ontario as potential investing cities. Besides other cities, Toronto, Mississauga, Ottawa, Brampton, London, Hamilton, Oakville, and Markham made it to the top list (Ontario cities as FDI cities). Among all the names, Toronto ranked fourth overall in North America. Toronto contributes to nearly 19% of Canada’s GDP (ibid). 35% of largest of 800 corporations have their headquarters based in Canada; two-thirds of this number is based in Toronto. Toronto’s 72%

share of inward FDI comes from sales, marketing, and business service activities (Mullan). Mississauga strengthens Ontario's position in attracting FDI. Located in the Greater Toronto Area, Mississauga tops the ranking in FDI's in mid-size cities in North America. FDI in Mississauga is focused on the tools, industrial machinery, and equipment sector (ibid). As per the report, Canadian cities such as Toronto, Montreal, Vancouver, and Mississauga have shown the most notable movement in FDI in the last few years (ibid). Ottawa is also gaining momentum in establishing itself as a business-friendly tech hub. Nearly 1750 tech companies are established in Ottawa making it one of the top hubs for technology innovation (Ontario cities as FDI cities). Besides the top names, other cities such as Brampton, London, Guelph, Hamilton, Oakville, Markham, Waterloo, Cambridge, Windsor, Burlington, and Niagara Falls have also been recognised for various reasons and as potential FDI sites. Each city has its unique feature making it FDI friendly.

Figure 1. Ontario FDI Ranking Mid, Small, and Micro Cities

ONTARIO FDI RANKING			
NAME	SIZE	RANKING	SECTORS
Brampton	Mid-size	10	Business-friendly, Growing transit network
London	Mid-size	6	Business-friendly, manufacturing companies
Hamilton	Mid-size	8	Transportation hub, Leader in Innovation
Oakville	Small	5	High skilled workforce
Markham	Mid-size	7	High-Tech hub
Guelph	Small	10	Human capital and lifestyle
Waterloo	Small	7	Global think tank
Cambridge	Small	6	Part of Innovation corridor
Windsor	Small	1	Skilled workforce
Burlington	Small	10	Talent and location
Niagara Falls	Micro	3	Strategic location
Brantford	Micro	1	Uniquely positioned
Sarnia	Micro	8	Chemical industry
Sudbury	Micro	10	Mining
Chatham-Kent	Micro	7	Strategic location
Kingston	Small	6	Human capital
Pickering	Micro	10	Seaton community and Innovation corridor

Source: Invest Ontario: Ontario cities recognized as FDI cities of the future

A total of 421 cities across North America and South America were ranked based on five categories: economic potential, business friendliness, connectivity, human capital and lifestyle, and cost-effectiveness. Ontario scored an overall high with 20 cities dominating the business-friendly category (ibid). Termed as Canada's economic powerhouse, Ontario attracts attention from the FDI community globally. The City of Toronto and the Greater Toronto Area geographically located within Ontario generate more than \$310 billion annually, making Ontario the centre for financial and investment opportunities (ibid). Ontario's leading advantages lie in offering low corporate taxes, a skilled workforce, and a diverse economy. Ontario's strength also lies in its 20 cities that are FDI ready and have unique characteristics to attract FDI. A 2015 report on Global Opportunities Index (GOI) ranked Canada as the top investment destination in the western hemisphere and positioned it sixth globally (Canada top investment destination).

Figure 2. Global Opportunity Index Ranking

	Economic Fundamentals	Ease of doing Business	Quality of Regulations	Rule of Law
Canada (7.73)	6.14	8.00	8.00	8.80
U.S. (7.14)	6.45	7.42	6.30	8.40
Mexico (5.34)	5.27	5.89	5.50	4.70

Source: Invest Ontario: Canada top investment destination in the western hemisphere: 2015 GOI

Canada was one of the only countries to feature in three of the four categories with a score of eight points and more. According to the report, 'the ease of doing business' factor is very high in Canada. KPMG points out that Canada's competitive tax rates for businesses, the effectiveness of policy making, Canada's tariff export-related programs, Canada's strategy to

provide a tariff-free zone for industrial manufacturers, and its ability to offer protection of investor rights and protection of property rights makes it an attractive destination with site selectors for FDI (ibid).

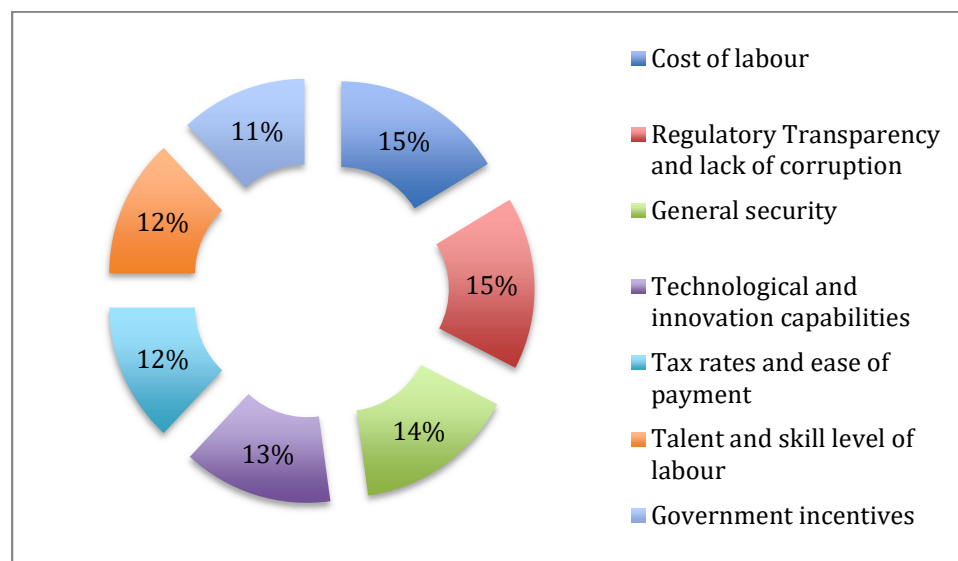
How to be FDI ready?

It is essential to understand the top factors that determine or influence FDI decisions. According to A.T Kearney's report (2016) Foreign Direct Investment (FDI) Confidence Index, the most critical factors that affect the FDI decision-making process are:

1. Market size
2. Cost of labour
3. Transparency of regulations and policies

As per Kearney's report, the other top factors that affect FDI decision-making process include:

Figure 3 Top Factors Influencing FDI Investments



source: A.T Kearney's Report 2016

The factors that play a crucial role in influencing FDI decisions are the cost of labour and regulatory transparency. Ontario's diverse and multicultural population teamed up with the high-quality human resource is considered as a considerable asset for establishing businesses in Ontario. Ontario has 68% of post-graduate skilled talent, the highest in any OECD country (Why Ontario).

Ontario's initiatives in technology and innovation in the sectors of automotive, aerospace, chemical and biochemical, green energy, industrial automation and robotics, life sciences, and mining are putting Ontario on the FDI map globally.

A.T Kearney points out that FDI decisions are also related to geographical areas. Executives from Asia consider the cost of labour and stable and secure environment as a critical decision factor, European executives consider country's market size as a crucial decision factor, whereas North American executives focus on skilled labour. The report also suggests that the sectors also influence FDI decisions. Service-sector firms planning to invest, consider transparency of government regulations, and market size as their focus in contrast to industrial firms who focus more on labour cost and the secure environment as its deciding factor (ibid). Mercer's report ranks Canadian cities Calgary, Montreal, Toronto, Ottawa, and Vancouver high on personal safety (4 out of Top 5 North American). Political stability, economic stability and banking regulations, socio-cultural environments, and health also contribute to other factors that make cities or countries FDI ready.

Small Communities: Challenges

It is pertinent to understand the role of rural communities in Canada and question if they are FDI ready. The concept of rural communities are defined by two dimensions (State of rural Canada 2):

1. Low density
2. Long distance to density

Although the report determines and defines the rural communities, it states that policy practitioners need to acknowledge that rural communities are unique, and no two rural communities will be the same or have the same problems. There is diversity in the rural community across Canada with each community having its geography, history, own set of challenges and opportunities. The uniqueness of the communities makes the policy development and attracting FDI process complex and challenging. Canadian rural communities have noticed a rapid growth and change in the last 30 years (ibid). Rural communities have had a decline in their manufacturing and primary industries, there has been social and economic restructuring, demographic is ageing, and the youth are leaving the rural communities and moving to cities. The recent changes have impacted the rural communities, making it challenging for them to attract FDI. Rural communities lack skilled and talented labour, resulting in no interest from FDI. According to a report by Canadian Council of Learning (ibid 5):

1. Rural communities have a 16.4% high school drop out rate as compared to the urban communities (9.2%)
2. The average level of education is lower in the rural communities
3. Among the 34 OECD countries, Canada has the largest urban-rural gap

As a policy decision, investing in rural communities would require a creative and unique approach. It is imperative that rural communities form clusters to build upon their strengths. Rural communities have the advantage of networks, and they need to use that to their benefit. The challenge is also with the existing traditional form of policy. To resolve this challenge, the Canadian Council of Learning report suggests adopting a place-based approach. The approach includes identifying the strengths and niches of a place and further developing it to its full capacity by building on the expertise and experience of the local people. The inclusion of all levels of government would be required to bring in this change.

Another challenge faced by the rural communities' in attracting FDI is its existing infrastructure and services. Site selectors would not consider rural communities as their first choice, as they lack sufficient infrastructure to support the inflow of FDI. Large-scale industries that are keen to invest have a high demand for housing, social services, broadband connectivity, and access to high-quality health services, and connection to main highways for easy transportation, and educational facilities for their workers. The limited availability of these facilities creates a hurdle in attracting FDI into the rural communities.

Small Communities: Solutions

Rural Ontario's strength lies in its farms. Ontario has more than 25% of all the farms in Canada (ibid). Rural communities need to capitalise on their local assets and seek creative ideas to grow in their existing opportunities. Rural sectors strengths lie in manufacturing, mining, forestry, and agricultural sectors. Rural communities need to acknowledge that they will always face tough competition globally, and from the urban cities within Canada. Finding a niche for

their region or teaming up with a municipality that already has had some success with FDI would be a start in a positive direction.

The solution to attract FDI lies in collaboration and cooperation at the regional level to compete at the global level. Building on local strength involves greater inter-municipal and government stakeholder collaboration on economic development at the regional level. One of the strategies includes urging entrepreneurship and innovation by using business incubators namely eco-tourism, biopharmaceutical and biofuels in Northern Ontario as well as rural agricultural communities. These partnerships among local communities beget harmonised regional economic development strategies that bring about human capital, promote entrepreneurship, clustering, and remarkably promote a region to global investors (AMO 21). Individually the rural communities lack the factors to attract FDI, but if teamed up, they can establish themselves as regional or municipal partners to attract FDI in the region. The communities strategy to approach FDI should include clustering of businesses, developing corporate economic plans, and rather than competing with each other, they should work together as one team to accomplish FDI goals.

Knowledge and creative industries also build a city-region brand by forming clusters and regenerating urban neighbourhoods. Such regional alliances consist of *Communitech*, *Toronto Region Research Alliance*, *Invest Hamilton Niagara*, *East Economic Development Commission*, *Southwestern Ontario Marketing Alliance*, and *Toronto Global*. For instance, the Ontario East Economic Development Commission (OEEDC), as the first economic development-marketing organisation in Ontario, promotes partnership and regional co-operation among communities to carry out economic development activities. The OEEDC also provides knowledge to other

entities to form regional organisations, which come in different forms. However, their common goal is to increase their opportunities for investment, business retention and growth. One of the organisations is *Waterloo Region Economic Development* (WRED) that markets the competitive advantages of the Waterloo Region to the world, to attract businesses, investment and talent to the Region. WRED introduces the competitive advantages of the Waterloo Region to the global market and streamlines connection between regional businesses and entrepreneurs and foreign business networks as well as international markets. It makes the global economies aware of the Waterloo Region as a hub for business opportunity; developing business and holding meetings with foreign investors to streamline FDI procedures; managing data to support making decisions in terms of FDI process; and promoting public-private partnerships to enhance resources and collaboration to develop FDI in the region (OEED; Parsons Ltd.).

Conclusion

Globally, Canada's position in the FDI market is strong, and Ontario has established itself as a leader in attracting FDI; however, the rural communities in Canada are struggling to draw FDI attention. With the changing market and stiff competition, FDI attention is shifting to Asian economies and investors are willing to invest in upcoming economies, raising a risk to the rural communities. Canada needs to strengthen its economic policies to attract FDI investment. Attracting FDI into the rural communities will require integrating the use of new learning technologies, improving the skills of human capital, establishing policies to attract immigrants

into the rural communities, and capitalising and utilising the existing resources of the agricultural sector and using it for green energy.

Canada's policy needs to shift its attention in developing the rural communities by enhancing and modernising its infrastructure, improving the talent and providing education to create skilled human capital, improving the immigration skilled-workers credential process, and most of all finding a niche within the rural communities to promote them in the global market. There is tremendous hidden potential in the rural communities in Canada that remains untapped. Opportunities in rural Canada are waiting to be explored. Canada needs to communicate the potential of rural communities to the world to attract serious FDI attention.

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