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AN ICE CEILING:

OVERCOMING THE GROWTH CHALLENGES FACED BY CANADA'S MID-SIZED COMPANIES

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IDENTIFYING THE KEY BARRIERS TO CANADIAN BUSINESS GROWTH

Mid-sized companies have proven themselves to be crucial drivers of the Canadian economy by applying their energy, perseverance and creativity to spur economic growth, employment and innovation. However, when asked about the state of entrepreneurship in Canada, top business leaders often assert that their company's economic impact is hindered by a number of increasingly evident constraints.

These hurdles to growth, which could be dubbed Canada's very own "ice ceiling," include access to talent and financing, government regulation and an underlying Canadian psyche that may diminish entrepreneurial ambition beyond a certain size. This paper discusses these challenges from the perspective of the leaders of Canada's elite mid-sized businesses.

These viewpoints are gathered from in-depth interviews and surveying completed as part of the annual QuantumShift Summit, a gathering of more than 400 Fellows of **QuantumShift**™, Canada's premier leadership development program. Founded in 2004 by KPMG Enterprise and the Ivey Business School, QuantumShift combines a prestigious annual program for top Canadian executives with an alumni network of the entrepreneurs driving the growth of Canada's most successful private companies.

Canada's mid-sized companies exert a major influence on the Canadian economy

Although some may question whether Canada's mid-sized companies are reaching their full potential, few would doubt their tangible impact on the Canadian economy. In a study of private enterprises with between 100 and 499 employees, the Business Development Bank of Canada (BDC) reported that, while these companies represent less than 1 percent of all Canadian firms, they account for 16 percent of national employment, generate 12 percent of national GDP and produce 17 percent of Canadian exports.[1] They also generate annual revenues of $34 million, on average.

At the same time, the BDC study identified some notable trends, including a 17 percent decline in the number of Canadian mid-sized firms from 2006 to 2010. Over the same period, an average of 14 percent of mid-sized firms either shrank into small firms or ceased operations each year, whereas just 1.4 percent grew into large companies with more than 500 employees. While this observation reflects the broad mid-sized market, it is important to note that the number of QuantumShift firms remains stable, in light of their higher growth rates and history of increasing revenues.

The BDC study identified employee acquisition and retention, availability of financing and fierce competition among the top reasons mid-sized business owners cited for their inability to grow. These findings align with QuantumShift's own review of mid-sized business challenges. QuantumShift research also noted a continuously declining number of entrepreneurs who have started a company in the last 10, 20 or 30 years.[2] Paired with data that indicate nearly 50 percent of entrepreneurs plan to sell or transfer ownership of their companies within the next 10 years, these facts suggest a looming drop in the role mid-sized businesses may play in the Canadian economy.

These data are cause for concern if one believes that mid-sized companies form an essential pillar for Canadian growth and innovation. Entrepreneurism is also often described as a critical source of future employment, both to offset parallel declines in large manufacturing, natural resource and government jobs, and to help correct regional economic imbalances.

[1] Business Development Bank of Canada, "What's Happened to Canada's Mid-Sized Firms," 2013.

[2] QuantumShift Anatomy of Canada's Most Successful Entrepreneurs Survey, December 2013.

THE ICE CEILING CHALLENGE: ACCESS TO TALENT

In each of the past 12 years, QuantumShift participants have highlighted the ability to attract and retain talent as their top concern. In fact, a survey of these business leaders found that, although 71 percent planned to grow their workforce in the near term, 28 percent stated that talent attraction and retention was their number-one challenge. This concern even surpassed worries about competition, which preoccupied 20 percent of respondents.[3]

This sentiment was also captured in BDC's 2013 survey of mid-sized businesses, in which 45 percent of participants said that employee acquisition/retention and talent/expertise development was a top internal challenge they contended with.[4] More specifically, 14 percent highlighted "lack of skilled/capable management" as a key factor that impeded their business growth, and 12 percent noted "lack of qualified staff."

While Canadian business leaders credit recent government job creation and training measures with helping to improve access to unskilled or semi-skilled workers, they state that few meaningful programs support the development and availability of more skilled workers, ranging from welders and engineers to specialized IT and science professionals.

Indeed, scarcity of skilled, semi-skilled and unskilled labour in Canada has prompted many mid-size employers to seek talent outside the country; approximately 25 percent of QuantumShift Fellows stated they have done so. Unfortunately, even this option is studded with hurdles. Business owners describe the considerable red tape and expenses involved, including costs that may reach $15,000 per permanent foreign worker and a potential two-year wait to on-board foreign candidates.

In addition, the recent public backlash against misuse of federal unskilled foreign worker programs has prompted program changes that have made the process more onerous for all employers. In fact, QuantumShift participants have observed that some mid-sized employers are now hesitant to leverage federal or provincial immigrant recruitment programs for fear of harming their reputation as responsible Canadian employers.

On the other side of the talent management coin, mid-sized firms also describe the challenges of retaining their current talent in a highly competitive job market. Particularly among coveted skilled and professional workers, mid-sized firms often find themselves unable to match the compensation that large corporations or foreign-based employers offer to lure away their best talent.

Enabling growth by driving company and government ingenuity

Potential solutions to the talent challenge range from increased government programs to build domestic skills and ease immigrant worker entry, to developing more creative human resources strategies on the part of individual companies or industry groups.

In terms of potential government action to address immediate recruitment issues, federal and provincial governments should consult with mid-sized employers to better understand their needs and adapt foreign worker hiring programs. Public sector consultations could also help simplify and streamline processes for employers to bring in skilled and professional talent. In addition, government reforms of existing unskilled foreign worker programs should focus on penalizing companies that abuse the system rather than punishing legitimate program users with increased red tape.

Government measures to remedy longer-term talent challenges could also encompass collaboration with the private sector to ensure their effectiveness and relevance to labour demand. Measures could include the expansion of job and skills retraining initiatives for displaced workers, increased post-

[3] Ibid.

[4] Business Development Bank of Canada, "What's Happened to Canada's Mid-Sized Firms," 2013.

secondary trades and professional training, and scholarships and tuition aid for education in targeted occupations.

Innovation is also called for among private sector employers. For example, employers could better partner with colleges, universities and government agencies to create "hiring pipelines" of new talent in specific professions. They could multiply their influence with these parties by cooperating with their industry peers to create hiring and training networks.

Savvy mid-sized employers could also borrow from the recruitment playbooks of major corporations, who carefully define their "employee value proposition" so they can clearly communicate to job candidates why their firm is a great place to work. For today's discerning job-seeker, points of differentiation such as a family-like work culture or a specialized niche firm can help mid-sized firms stand out from large, higher-paying corporations.

Such tactics have been well executed by business leaders like Paul Antony, Chairman of CarProof, a proudly Canadian provider of vehicle history reports for buyers and sellers of used vehicles. "It was hard at certain points along the journey to find the right people, but recruiting is much easier for us today," says the QuantumShift Fellow. "We got to this point by building a culture, and word really spread. We invest heavily in our people, so they want to give back to the company and they don't want to leave. We've put in place training and coaching programs that are as good as large companies and built our brand as a top employer with a clear vision. Those are powerful things, and they're worth the effort because, with the best people, you're destined for greatness."

This type of creativity and innovation shows that the challenges of hiring and retaining talent are not insurmountable for enterprising mid-sized companies.

THE ICE CEILING CHALLENGE: ACCESS TO CAPITAL

Business financing is an eternal challenge for entrepreneurs, particularly at the start-up stage. However, discussions with QuantumShift Fellows, whose organizational revenues on average range from $50 to $100 million, indicate that access to capital continues to represent a barrier to growth even for well-established, successful organizations.

A survey of QuantumShift executives highlighted their interest in improved access to funding in Canada, ranging from business loans to growth and venture capital. They noted that, while they are largely able to access sufficient operating capital, they face challenges obtaining funds for expansion or acquisition, particularly within the $10–$100 million range. This sentiment was mirrored in the 2013 BDC survey in which 40 percent of mid-sized business leaders cited availability of financing as a key external barrier to growth.[5]

In the words of **QuantumShift Fellow Hanif Patni**, President and CEO of Coventry Connections: "Many Canadian companies have grown impressively, but the jump from small to mid-sized, and from mid-sized to a big company, is a very tough one. We have all the elements to make those companies successful, but we are in the strange situation that capital funding is not available in Canada." Noting that banks are very conservative lenders, Patni adds, "With a greater level of government support to encourage increased levels of bank lending, Canada could gain a competitive edge compared to other developed countries."

So where do most mid-sized firms find funding currently? Among QuantumShift Fellows, 29 percent rely on bank loans, 22 percent leverage their cash flow and 15 percent draw upon their savings.[6] Another 11 percent of these firms borrow primarily from family and friends, exceeding the combined impact of angel investors, venture capital and private equity financing, which represent only 10 percent of funding. Government funding lags even farther behind at 1.7 percent. The remainder of respondents indicated that they chose not to pursue growth through leverage.

These data contrast sharply with the US mid-sized business market, where growing companies are much more likely to seek and access venture capital, private equity or other alternative financing sources. A number of QuantumShift Fellows also reported that they have turned to US-based sources of financing for previous expansion activities.

Limited funding sources are a result of market supply and demand

The lack of "made in Canada" funding options can be attributed in part to the nation's small size compared to the United States, which results in fewer lenders and an absence of innovative alternatives, such as mezzanine financing, which could be a helpful mid-tier funding option for smaller companies. In addition, while some business leaders praise the funding support they received from government sources, such as Export Development Canada, the BDC or provincial programs, these initiatives are often highly targeted, short-term in nature or limited in scope and scale.

In regards to why more Canadian entrepreneurs do not look south for capital, there is no single answer. While some observers claim Canadian firms lack the knowledge, experience or confidence to pursue foreign lenders or partners, others believe Canadians' hesitancy is more intentional and strategic. For example, sophisticated Canadian business leaders may reject the complexities of alternative financing, recognizing the considerable reporting and regulatory demands, as well as currency exchange factors, entailed in taking a privately held company to the US public markets. Others refuse to surrender control of their business to private equity or venture capital partners, or to accept stringent conditions or restrictive terms.

[5] Ibid.

[6] QuantumShift Anatomy of Canada's Most Successful Entrepreneurs Survey, December 2013.

In addition, some analysts opine that lack of growth financing is not due to lack of funding options but rather limited demand from Canadian entrepreneurs. They attribute this to a unique, low-key and risk-averse "Canadian psyche." This perspective is based on the observation that, while entrepreneurs in the United States are aggressively growth-oriented, Canadian businesses are more inclined to target measured growth.

This viewpoint suggests that some Canadian business owners define success differently from their US counterparts, and that "being my own boss" and "doing what I love" are at the core of Canadian business culture. For these individuals, achieving growth at all costs is not a driving motivation. This point of view arose among a third of QuantumShift executives, with 33 percent stating that their strongest motivator for starting their business was to satisfy a personal goal. Only 16 percent reported that creating wealth was their strongest motivator. If this point of view is widespread in Canadian business culture, it could help explain why growth financing options are limited in the Canadian market.

Enhancing access to capital by pursuing unique public and private funding solutions

Potential solutions to the funding challenge—for those companies that are growth-oriented—are diverse and complex. While some analysts urge governments to expand direct financing programs to support business growth—or increase government indirect financing through insurance to banks—others advocate for minimal government involvement. Some observers point out that Canada's carefully designed and intentionally conservative banking system should be maintained to ensure national economic stability and strength.

With no obvious sign of new funding sources on the near horizon, mid-sized companies might be well advised to work together to expand self-funding opportunities or introduce innovative approaches. For example, peer-to-peer lending schemes could bring together parties to fund and mentor other growth-oriented mid-sized firms. A number of QuantumShift participants have also chosen to invest in start-ups, which represent the next generation of mid-sized businesses, rather than growing their original companies beyond a certain size.

> "Many Canadian companies have grown impressively, but the jump from small to mid-sized, and from mid-sized to a big company, is a very tough one. We have all the elements to make those companies successful, but we are in the strange situation that capital funding is not available in Canada. With a greater level of government support to encourage increased levels of bank lending, Canada could gain a competitive edge compared to other developed countries."

~ QuantumShift Fellow Hanif Patni, President and CEO of Coventry Connections

THE ICE CEILING CHALLENGE: ACCESS TO GOVERNMENT SUPPORT

While successful entrepreneurs attribute their success to the strength of their product, business model and people, and to an intangible mix of risk-taking and determination, they agree that government plays a role, either as a business catalyst or an obstacle.

In support of greater government involvement, many QuantumShift leaders acknowledge that government can create a competitive economic environment. Among survey participants, 27 percent stated that government should improve the competitiveness of the local economic environment through measures such as interest rate and foreign trade policies, while 25 percent advocated for lower corporate and personal tax rates, or tax incentives that benefit business.[7]

Observes **Rudi Kroeker**, President & CEO of Whiting Heavy Industries Inc., "There are a few government services that we use all the time, including the Trade Commissioner Service, which is perhaps Canada's best-kept secret. They are an invaluable source regarding conditions in foreign markets and available programs." The QuantumShift Fellow adds, "In Canada, these agencies give us a unique advantage and they are very accessible to small and medium-sized companies. For example, federal and provincial government trade delegations often provide invaluable introductions between Canadian companies and prospective overseas customers."

Advocating for less government involvement

Although there is enthusiasm for this variety of government involvement in business promotion, many QuantumShift executives hold a strong belief that the best role for government in support of company growth would be to simply step out of the way. This perspective is revealed by the relatively small number of survey participants who sought increased investment by government in R&D and infrastructure (8 percent) or the creation of more government incentives and support for business (7 percent).[8] Among QuantumShift leaders, 19 percent stated that government should reduce regulation, including labour rules, reporting requirements and other business policies.

This perspective is often fueled by a negative perception of government bureaucracy as impeding business agility and flexibility. A number of mid-size business leaders have described how compliance with outdated or irrational government regulations creates costly delays for business and, particularly in smaller organizations, can divert limited resources from other tasks. They also note that mid-sized companies are unable to win lucrative public contracts because government procurement procedures are so cumbersome that they give an advantage to large corporate bidders.

Wendy Taylor, President of Yukon-based Alkan Air Ltd., notes, "In recent years, government departments like Transport Canada have expanded their service delivery roles, from pilot licensing to aircraft approvals. Unfortunately, they don't have the resources to dedicate to those duties. Since my company serves the exploration and mining industry, I can't wait a year for government approvals when I need to make decisions now based on the stock market and metals prices today." Taylor suggests, "I think that the government is currently involved in a number of services that could either be outsourced to the private sector or else improved in order to increase efficiency. That would really help mid-sized companies to grow our businesses."

Other business leaders echoed this perspective, adding that business productivity is impeded by duplication of regulation and lack of alignment between levels of government. Sometimes the approach taken by government departments is not designed

[7] Ibid.

[8] Ibid.

to reflect or accommodate the realities of small or mid-sized organizations. A frequent example cited by QuantumShift leaders is the Canada Revenue Agency (CRA) review and audit process, which creates considerable complexity and cost for companies, both to achieve tax compliance and to challenge or appeal agency decisions.

Empowering business growth by collaborating to refine government service delivery

In terms of solutions, a number of QuantumShift leaders point out recent success stories in which government bodies have effectively reduced red tape, streamlined processes or evolved their delivery models to benefit business. For example, business leaders are complimentary about the CRA's efforts to increase its online service delivery and support to improve convenience, efficiency and transparency for business owners.

To support this type of "business friendly" evolution of government services, mid-sized companies could collaborate with their government counterparts to influence the shape of future public programs and to urge reform of current regulations. To do so effectively, mid-sized companies could work collectively through their peer networks of industry associations to gather business viewpoints and undertake focused government relations and lobbying programs.

QuantumShift participant Connie Clerici speaks enthusiastically about this approach. The President and CEO of Closing the Gap Healthcare Group explains, "The government not only ensures that standards of quality care are met, but they are also an enabler of change and they introduce innovation and technology. We have a more collaborative environment in Canada, and the government has been a very strategic partner of ours. They seek our feedback when appropriate and they have an open-door policy for us to share our feedback in a constructive way."

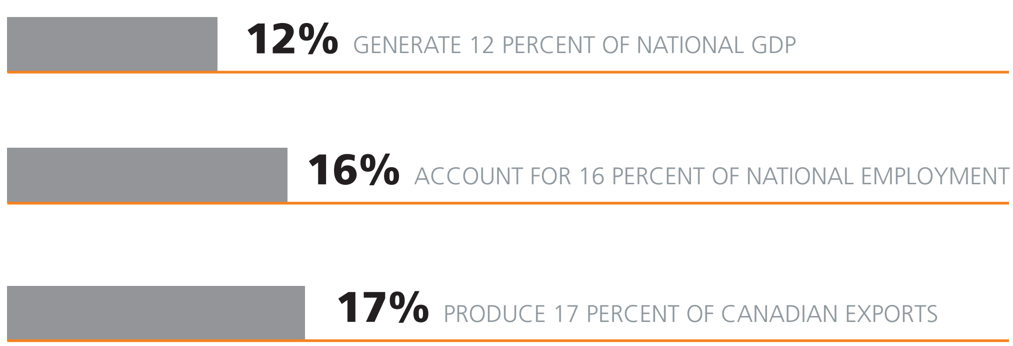
CREATIVE AND COOPERATIVE APPROACHES WILL DRIVE THE GROWTH OF MID-SIZED CANADIAN FIRMS

In a nation as vast and diverse as Canada, opinions naturally vary regarding the challenges faced by mid-sized companies and what solutions are required. Although there are consistent themes among successful mid-sized company leaders, including the community of QuantumShift Fellows, there are also divergent views on whether Canadian companies require more government support or less.

These thought leaders also raise intriguing questions as to whether seemingly muted growth rates among Canadian companies are the result of external barriers, such as lack of capital or excess government interference, or whether Canadians simply define success differently than their counterparts in other markets, resulting in a less growth-obsessed Canadian psyche.

Regardless of the philosophical considerations, the input from Canadian business leaders in this paper highlights a number of factors that could contribute to greater growth by mid-sized companies. Among the key considerations, mid-sized companies could continue to hone their own organizational capabilities and creative strategies, particularly in the pursuit of future talent. These organizations could also cooperate with their peers to create improved access to both human and financial capital and talent. Such joint efforts, within industry sectors or across business groups, could also be an effective means to encourage government reform and modernization. By applying these strategies, mid-sized companies with growth aspirations will be better positioned to overcome the obstacles they face, break through the ice ceiling and remain important contributors to Canada's long-term success.

Private Canadian companies with 100 to 499 employees:



SOURCE: Business Development Bank of Canada, "What's Happened to Canada's Mid-Sized Firms," 2013

ABOUT QUANTUMSHIFT

QuantumShift is Canada's premier leadership development program and network for the entrepreneurs and executives who drive the growth of Canada's most successful private companies. To be eligible for this annual week-long program, candidates must be CEOs (or the equivalent) of thriving privately owned Canadian companies. Developed and delivered by the prestigious Ivey Business School, hundreds of candidates from across the country compete for only 40 spots in this exclusive program. The case study–based curriculum is led by award-winning professors and leading speakers and serves as a catalyst for participants to think about their businesses differently and ultimately helps them achieve the next level of success. Program alumni form a powerful peer network of Fellows across the country who remain active in the program through annual events and conferences. Founded in 2004 by KPMG Enterprise and the Ivey Business School, QuantumShift is also sponsored by TD Commercial Banking and the Globe and Mail. For more information, please visit www.quantumshift.ca.

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Eric Morse, Ph.D. is a Professor of Entrepreneurship at the Ivey Business School. Eric served as Associate Dean Programs for a six-year term, which ended in 2014, and prior to his service as Associate Dean, Eric served as the Director of the Morrissette Institute for Entrepreneurship. Dr. Morse is the founder of and the Academic Director for, Ivey and KPMG Enterprise's QuantumShift Program for Exceptional Entrepreneurs. Over its twelve-year lifetime the QuantumShift Program has inspired over 500 of Canada's best and brightest entrepreneurs and companies onto even greater success.

Eric's research has been published in top journals around the world including: the Academy of Management Journal, Entrepreneurship Theory & Practice, the Journal of Business Venturing, the Journal of Management, The Strategic Management Journal and the Sloan Management Review. Eric's work with business leaders has been widely cited by CBC News, The Globe and Mail, Toronto Star, Financial Post Magazine, Vancouver Sun, The South China Morning Post, Chatelaine, and Cosmopolitan (HK).

Eric has served on the board, been an advisor to, founded, or been an investor in a variety of entrepreneurial start-ups. Dr. Morse actively consults with both private and public enterprises across Canada and around the world. He has worked with a diverse range of corporate clients on strategy, strategic planning, growth and innovation.

Paul Woolford
Tax Partner
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Paul Woolford leads the GTA KPMG Enterprise Tax Group with over 20 years of tax-related experience. His practice is focused in the firm's Enterprise practice, which is dedicated to assisting entrepreneurial clients and private companies with all facets of the financial issues surrounding their businesses.

Paul's practice ranges from privately owned multinationals to large owner-managed businesses. He advises on matters such as acquisitions and divestitures, corporate reorganizations, compensation strategies and integrated tax advice for privately owned corporations. He also assists many clients with various cross-border transactions including tax-efficient financing arrangements, in-bound investments and repatriation matters.

For several years, Paul has been a group leader of the group study and in-residence programs of the In-Depth Tax Course of the Canadian Institute of Chartered Accountants. He has also been a lecturer at the University of Waterloo Masters of Taxation program.

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