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CANADIAN DIRECT INVESTMENT IN WESTERN NEW YORK:
AN EMPIRICAL ANALYSIS OF THE STRATEGIC CHARACTERISTICS OF CANADIAN PARENT CORPORATIONS AND THEIR U.S. SUBSIDIARIES

Alan D. MacPherson and James E. McConnell

Canada-United States Trade Center
Department of Geography
State University of New York at Buffalo
Buffalo, NY 14261

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Abstract. This paper examines the organizational and strategic characteristics of Canadian Corporations that control subsidiary establishments in the Western New York region of the United States. Survey data from two interlinked inquiries are presented. The first survey describes the nature, scale, and bilateral economic impact of recent Canadian direct investment in Western New York. The second survey describes the investment motivations, expectations, and strategic intentions of Canadian parent corporations that have recently established business operations in the study region. A major finding is that Canadian direct investment has generated reciprocal benefit streams between Canadian parent corporations and their subsidiaries in Western New York. A further finding is that the close geographical proximity of the study area to central Canada is a major factor in the decision-making priorities of Canadian investors. The paper concludes with a brief research agenda for future work on the academic and policy implications behind Canada-United States direct investment in the post free-trade era.

INTRODUCTION

As the Canada-United States Free Trade Agreement (FTA) approaches its fourth year of operation, many Canadians are concerned that new rounds of industrial rationalization will soon take place, leaving Canada with diminished manufacturing employment, reduced output, and a truncated production base [Drache, 1990; O'Grady, 1990]. Fears of this ilk have been compounded by the prospect of further US disinvestment in Canadian manufacturing [MacLachlan, 1990], prompting some critics to advocate an immediate cancellation of the accord [Drache, 1990]. One issue of particular importance to Canadians concerns the extent to which smoother bilateral investment relations have stimulated new streams of southbound capital migration, notably from Ontario and Quebec. Outflows of foreign direct investment (FDI) imply a potential loss of domestic employment, exports, and tax dollars, especially in goods-producing sectors. Southbound investments also imply industrial job-creation outside Canada, much to the irritation of the New Democratic Party, the Canadian Labour Congress, and other domestic interest groups. On the civic front, moreover, public emotions have recently been fired by a number of contentious business decisions, not the least of which includes Varity Corporation's proposal to relocate its global headquarter facilities from Toronto (Ontario) to Buffalo (Western New York). Not surprisingly, then, many Canadians have legitimate reason to question the political and economic merits of North American market integration, notably from an employment perspective.

Having said this, however, scant empirical work has been carried out on the cost-benefit distribution of Canadian FDI for specific target regions, source locations, or companies. At the same time, rather little is known about the precise mix of corporate motives that have propelled particular types of Canadian firms toward specific parts of the United States. This is unfortunate for both countries, if only because private and public decision-makers are left with a lack of current information to support the design of optimal strategy. While it is evident that growing numbers of Canadian companies have been establishing a direct presence in the United States over the past few years [Investment Canada, 1990a, 1990b], the underlying rationale behind recent FDI is unlikely to be the same across all sectors, industries, and corporate size-classes.

Keeping these observations in mind, this paper offers a region-specific perspective on the nature of recent Canadian direct investment in the United States. The study area is Western New York (WNY) -- a declining manufacturing region with a distinctly Rustbelt location. The source region for incoming FDI is central Canada, consisting primarily of southern Quebec and the Toronto urban agglomeration. Data for the inquiry come from two principal sources. The first source (1989/1990) consists of survey evidence from a self-administered questionnaire that was recently mailed to the entire population of Canadian-owned business establishments in the WNY area. The second source (1991) comprises follow-up survey data that were collected from a representative subsample of parent corporations in Canada. Using these data sources, three general sets of questions are addressed in the empirical analysis. First, what are the main sectoral and performance features of WNY's current population of Canadian-owned subsidiaries? Second, what are the principal strategic characteristics of the Canadian parent companies that have recently spawned subsidiary operations in the study region? And, third, what types of academic and policy implications can be drawn from the empirical results?

While the survey data are restricted to a single border region (leaving the analysis rather limited in terms of geographical scope), some of the results suggest partial correctives to a number of popular perspectives on the nature of Canadian investment in the United States. At the same time, the data suggest potentially useful directions for additional empirical work at an expanded geographical scale. Prior to an examination of the results, however, it is appropriate to outline a brief regional context. Why is Western New York worth investigating? And, why is Canadian FDI such a popular topic for local policy discussion?

RECENT CANADIAN DIRECT INVESTMENT IN THE STUDY REGION

Structural unemployment and industrial decline represent conspicuous themes in the recent economic history of WNY. The collapse of Buffalo's steel industry in the early 1980s continues to restrain the regional economy, affecting diverse networks of producers in metal-related sectors and ancillary services. Since 1981, the study area has lost almost 40 percent of its manufacturing jobs [U.S. Bureau of the Census, 1982,1991], and few analysts expect this trend to reverse itself over the short-run [Kraushaar and Feldman, 1988]. When the FTA came into effect on January 1, 1989, however, local optimism concerning the region's long-run economic future increased dramatically. Part of this optimism can be traced to WNY's internationally competitive factor costs, its close geographical proximity to central Canada, and its longstanding role as an entrepot centre for cross-border trade [McConnell, Chandra, and Steinitz, 1989]. In addition to these factors, WNY also contains an abundance of inexpensive industrial land, skilled labor, and cheap energy [MacPherson and McConnell, 1990]. Clearly, then, the advent of more liberal trade and investment relations between Canada and the United States has given the WNY area a new set of growth possibilities [McConnell, Chandra, and Steinitz, 1989]. Specifically, the study region exhibits a favorable set of geographical and cost-related attributes that are likely to be of interest to Canadian investors that wish to serve the American domestic market. At the same time, the study region is well positioned to expand its exports to Canada, especially as the new tariff schedules of the FTA come into effect over the 10-year phase-in period (1989-1998).

One issue of growing interest to local policy agencies concerns the extent to which WNY can attract new Canadian direct investment over the 1990s. Ironically, however, very little is known about the industrial and organizational characteristics of those Canadian firms that are already well-established in the study area, and even less is known about the attributes and entry motives of Canadian businesses that have moved into the region since the bilateral trade deal was ratified. Furthermore, virtually nothing is known about the organizational and strategic features of the Canadian parent corporations that have recently spawned new business operations in the study region. In this regard, it should be noted that policy agencies on both sides of the border have neglected to compile, process, and/or distribute basic information regarding the recent cross-border flow of direct investment -- leaving business organizations and public decision-makers in both countries with inadequate data to assist strategic planning, policy design, or impact analysis of the FTA.

Set against this context, the Canada-United States Trade Center (CUSTAC) at the University at Buffalo launched a series of inquiries in 1989 to ascertain the scale, nature, and bilateral economic impact of recent Canadian FDI in the WNY border region. These inquiries were partially motivated by speculative media reports on both sides of the Niagara River -- reports that alluded to a post-FTA surge of Canadian FDI in the study region. The authors were also motivated by a desire to construct detailed profiles of Canadian corporate development across a representative range of industry sectors and company size-classes. The salient findings of the CUSTAC inquiry are summarized below [MacPherson and McConnell, 1990].

- 133 Canadian establishments with a direct (active) WNY business presence were identified; 58 of the latter participated in the CUSTAC survey, giving a response rate of 43.6 percent.
- 86 percent (n=50) of the Canadian establishments were formed via greenfield development (rather than by acquisition or merger).
- 46 percent (n=27) were primarily engaged in manufacturing (the remaining 54 percent were distributed across a broad mix of service activities).
- almost 50 percent of the Canadian establishments had arrived in the study region during the 1980s; over 30 percent were post-1985 arrivals.
- establishments in the manufacturing sector had significantly outperformed

their service sector counterparts in terms of start-up (entry) versus current (1989) employment levels.

- spatial proximity to parent corporations in Central Canada was a major factor in the WNY locational decision.
- most of the recent Canadian arrivals (post-1985) cited low factor costs as a significant impetus behind the FDI decision.
- a majority of the WNY subsidiary establishments actively transfer strategic information, knowledge, technology, or merchandise back to their parent corporations in Canada.
- for most of the Canadian establishments, a central motive behind locating in WNY was to gain geographically convenient access to regional markets in the United States.

While it is not possible to describe the full range of our 1989/1990 survey results in this paper, at least three sets of findings merit emphasis. First, 77 percent (n = 45) of the Canadian subsidiaries indicated that geographical proximity to their parent corporations north of the border was a major factor in the decision to locate business operations in WNY. A majority of the establishments also stated that WNY provides a convenient distribution point for serving regional markets in the United States. Second, 86 percent (n = 50) of the Canadian subsidiaries were formed as a result of new business development (greenfield) rather than by acquisition or merger. Clearly, Canadian investors see the study region as a target for "new business formation" rather than "old business acquisition." Third, 46 percent (n = 27) of the region's Canadian-owned firms regularly send strategic information back to their corporate parents in Canada. Notable examples of "information exports" to Canada include research and development findings, market data, sales leads, and product specifications/designs.

Overall, the results of the first stage of the authors' research revealed that both Canada and WNY enjoy reciprocal benefit streams as a direct result of Canadian FDI in the study region. On the Canadian side, for example, parent companies receive strategic information and/or data inputs that support corporate development and sales expansion inside the United States. For

Western New York, moreover, the benefits can be measured in terms of job-creation (or retention), economic diversification, and a series of multiplier effects that ultimately imply positive gains for the study region [MacPherson and McConnell, 1990]. Having said this, however, a more important goal of the present paper is to assess the strategic motivations, expectations, and organizational features of the Canadian parent corporations themselves.

CHARACTERISTICS OF PARENT CORPORATIONS' STRATEGIES

Initial Objectives

As noted above, the second and primary purpose of this paper is to examine variations in the investment strategies of the parent corporations that have located subsidiaries in the WNY area. Five major questions are addressed in the sections that follow. First, what are the overall industry and firm-level characteristics of the Canadian parent corporations that have recently made direct investments (FDIs) in the WNY region? Second, what are the primary competitive advantages held by these headquarter operations, and to what extent are their assets similar to Canadian multinational corporations (MNCs) in general? Third, why have these parent corporations made direct investments in the U.S. marketplace in general, and in WNY in particular? Fourth, what types of benefits have the parent corporations recently derived from their WNY subsidiaries? And fifth, what factors are likely to influence the strategic decisions of these parent companies over the next few years? In several instances, the same questions were posed to the presidents of the parent corporations as were asked in the earlier survey of the managers of the subsidiaries. This procedure was followed to corroborate the responses of the two groups of decision-makers. As Ghertman has noted in his work on strategic investment decisions, the parent company's perception of the decisionmaking process and its outcome is frequently different from that of the subsidiary [Ghertman, 1988, p. 50].

At the outset, it should be noted that the authors employ the term "strategy" to refer to the balance that a business organization strikes between its internal resources and skills (on the one hand) and the opportunities and risks created by its external environment (on the other). From an organizational perspective, Hofer and Schendel [1978, p. 25] define strategy as "the fundamental pattern of present and planned resource deployments and environmental interactions that indicates how the organization will achieve its objective." On this basis, "strategic management" provides a framework into which each operating plan of the corporation can be integrated so that it functions as efficiently as possible in whatever market it chooses. It follows, then, that a major component of a corporation's strategy is its competitive advantage. This refers to the unique position the organization develops vis-a-vis its competitors through its pattern of resource deployment and environmental interaction.

As Porter [1985] notes, competitive advantage is based upon the value that a firm is able to create for its buyers minus the private costs associated with product and/or service creation. In short, "value" is what buyers are willing to pay. In formulating a competitive strategy, firms must choose a position within their respective industries. Following Porter [1990, pp. 37-8], positioning embodies the firm's overall approach to competing and involves two important variables: competitive advantage and competitive scope. The two main types of competitive advantage a firm can possess are cost leadership and product differentiation. Competitive advantage of either type translates into higher productivity than that of competitors. Equally important in positioning is what Porter refers to as "competitive scope, or the breadth of the firm's target within its industry" [Porter, 1990, p. 38]. If a firm is to attain competitive advantage, therefore, it must make a choice about the type of competitive advantage it seeks to exploit and the scope within which it will attain it. Two questions thus arise: what are the main sources of competitive advantage for Canadian firms that have recently located business operations in WNY, and, what types of organizational strategies have these firms been pursuing?

Expectations

When firms adopt an international strategy (for example, the decision to make a direct investment in another country), they seem to enjoy economic and strategic advantages over locally oriented firms [Wortzel and Wortzel, p. 48]. In his articulation of the internalization theory, Dunning argues that the competitiveness of the international operations of a company depends upon three main factors: a) firm-specific (ownership) advantages (FSAs), including both proprietary know-how and transactional advantages; b) country-specific advantages (CSAs) that are associated with locating certain activities in particular nations; and c) internalization advantages that make it beneficial for the firm to maintain control over the sale and distribution of its product, service, or technology [Dunning, 1988]. A firm possesses a competitive advantage outside its domestic marketplace when it owns (or has access to) tangible or intangible assets that are denied to its competitors in the host country, when it can sell or manufacture a product or service in the host country in a competitive manner, and when it is efficient for the company to maintain control over the sale or distribution of its product or service [Dunning, 1988; Porter, 1985].

In an oft-cited investigation of the primary characteristics of Canadian MNCs, Rugman claims that the "advantages of Canadian multinationals tend to be in marketing and distribution, rather than in innovation and new product development" [Rugman, 1987, p. 30]. He further states that: "Most Canadian multinational giants are operating in mature or resource-based product lines, yet their excellent managerial skills and marketing advantages make them able to perform as well as other multinational enterprises" [Rugman, 1987, p. 30]. Although Rugman's findings are based upon a sample of Canada's largest MNCs, it is not unreasonable to propose that smaller transnational corporations from Canada, and specifically those with subsidiaries located in WNY, are likely to exhibit a similar basis for their competitive advantage. The logic here is that both the tangible and intangible assets of MNCs typically reflect unique sets of competitive strengths gained from domestic experience [Rugman, 1987, p. 31]. As affirmed by Porter, a firm's home nation is an important determinant of the firm's strengths and weaknesses relative to foreign rivals and hence shapes where and how the firm is likely to succeed in global competition [Porter, 1990, pp. 598-9].

In addition to these expectations, the authors also anticipated (based upon their earlier findings) that the locational decisions of the Canadian parent corporations would reflect a desire to have a direct market presence within the United States while simultaneously retaining close geographical proximity to their external investment. Moreover, they were expected to indicate that they benefit significantly from having subsidiary plants in the WNY region. In particular, it was expected that the linkages that would be perceived by headquarter management executives to be the most important would also be those that supplement the parent's marketing and distribution assets (in line with Rugman's findings).

Finally, regarding the economic outlook of the parent corporations over the next few years, it was expected that headquarter executives would be especially concerned about the possible negative impact of current economic conditions in Canada upon their domestic and international competitive posture; that they would look with considerable optimism upon their business opportunities in the American marketplace; and that they would strongly endorse the positive benefits of the FTA between Canada and the United States.

The Survey

Given the objectives and expectations noted above, a survey instrument was constructed with a view to collecting proprietary data along four major dimensions. The first section of the instrument was designed to obtain information on the parent corporations' size (as measured by employment, annual sales, and number of countries in which they have subsidiaries), product lines, and orientation toward technology-intensive operations. In Section II, the objective was to determine the nature and perceived benefits of the ownership and technological linkages between the Canadian parents and their WNY subsidiaries. Section III focused upon various dimensions of the parent corporations' competitive posture, and upon the economic outlook of management executives over the next few years. The final part of the instrument was designed to examine the various factors that influenced the parent corporations' locational choices within the United States.

Fifty of the WNY companies that were part of the first phase of the investigation were deemed eligible for the follow-up research. During the second week of January, 1990, the survey was mailed to the presidents of the 50 Canadian parents. The executives were asked to return their responses in self-addressed, stamped envelopes. By early February, only 15 completed surveys had been received. Consequently, a follow-up letter and a second copy of the original survey instrument were sent to the 25 non-respondents. Of the 50 parent corporations that received the survey, 4 were subsequently eliminated because 3 were no longer in business, and another one had been acquired by a European corporation.

Of the 46 parent companies considered eligible for the analysis, valid responses were finally received from 25, giving a response rate of 54.4 percent. This figure is somewhat higher than the participation rate of 43.6 percent that was received in the first phase of the authors' study of Canadian subsidiaries in the WNY region; moreover, it is considerably higher than the response level that is frequently received locally in similar surveys by government agencies and business groups. Nevertheless, and unfortunately, it must be noted that the nature of the non-response bias is impossible to estimate.[1]

Survey Findings

Overall industry and firm-level characteristics

Several features of the respondents and their parent corporations are noteworthy. First, 60 percent of the respondents were the presidents of their corporations. Of the remainder, 24 percent were either Executive Vice Presidents or Vice Presidents, and 16 percent were corporation controllers or directors of operations. Second, most of the parent companies have been in business for a considerable length of time. For example, the start-up dates for the parent corporations range from 1867 to 1986, and more than two-thirds of the companies have been in business prior to 1970. In fact, only 2 of the parents have been incorporated in Canada since 1980. Third, the 25 parents vary considerably in terms of worldwide employment and annual sales (Table 1). On the employment front, for example, the companies range from a low of 3 to a high of just over 25,000 employees. Five of them have over 90 percent of their worldwide employment based in Canada, while another 13 have between 70 and 90 percent of their employment located in the home country; only 8 have employment in countries other than Canada and the United States. In terms of worldwide sales for 1990, the companies range from a low of US$340,000 to a high of US$2.85 billion. In this regard, it should be noted that one of the respondents ranks among Canada's 25 largest MNCs. For comparison purposes, it is

TABLE 1

General Characteristics of the Canadian Parent Corporations

(n=25)	Average	Median	High	Low
Worldwide sales (US$)	$331M	$30M	$2.85B	$340K
Worldwide employment	2,642	350	25,000	3
Age of corporation	43	59	124	5
% of sales on R & D	1-4%	1-4%	5-20%	0%

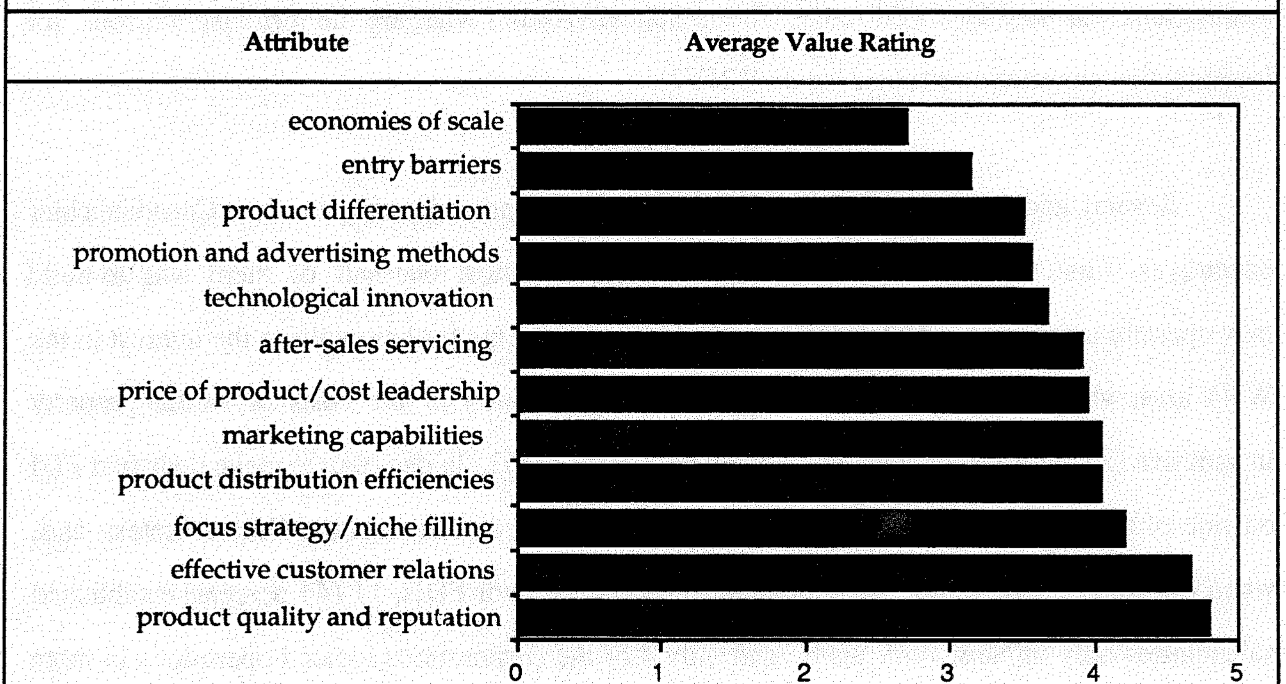
interesting to note that Rugman's analysis of the largest Canadian industrial MNCs quotes an average annual sales figure (1979-83) of C$2,279M, and a median sales estimate of C$1,875M [Rugman, 1987, pp. 28-9]. Using a currency conversion rate of US$0.85 = C$1.00, the mean and median figures for the large Canadian MNCs were approximately US$1,937M and US$1,593M, respectively. Even accounting for the difference in years between Rugman's study and the present one, it is clear that the Canadian parent corporations of the WNY subsidiaries are quite small by Canadian standards for transnational corporations.

A fourth feature of the parent corporations is the rather wide range of industrial products and service activities represented. For example, the major product lines and services represented by these corporations include clothing, industrial textiles, scientific instruments, educational videotapes, steel bars, construction equipment, newspaper publishing and printing, engineering consulting, lumber, brass and steel fittings, electrical transformers and wiring devices, management consulting services, cement products, transportation equipment, fabricated steel products, electronic components, molds, robotics, real estate and residential development, computer supplies, business communication services, and electrical winches. It is also evident from the responses that over 50 percent of the corporations are somewhat technology-intensive, as measured by investment in research and development activities. More specifically, 2 of the parent corporations spend between 5 and 20 percent of their annual sales on R&D, while another 11 invest between 1 and 5 percent. At the same time, however, 9 of the remaining corporations invest none of their annual revenues in R&D.

Primary Competitive Advantages of the Parent Corporations

One of the major questions underlying this research was to determine the nature of the competitive advantages of the Canadian parents. The expectation was that these ownership assets would reflect the primary characteristics of large Canadian MNCs, in that their competitive advantages would be in marketing and distribution, rather than in process innovation and/or new product development. To investigate this issue, the executives of the Canadian headquarter operations were asked to consider how important or unimportant several factors were in accounting for the competitive advantages their firms possessed over other companies in similar industry groups. On an attitude scale ranging from 1.0 (unimportant) to 5.0 (very important), several factors were identified by the executives as being "important" or "very important" (Figure 1). Interestingly, the top-ranked advantages imply that the Canadian executives perceive their primary competitive edge in the North American marketplace in terms of marketing and distribution advantages. This finding corresponds closely with the conclusions reached by Rugman [1987]. What is also clear is that very few of the Canadian corporations have been basing their primary competitive posture upon such assets as technological innovation, economies of scale, or new product development.

Figure 1. **Sources of Competitive Advantage Among Parent Companies**



Reasons for Making FDI in the United States and WNY

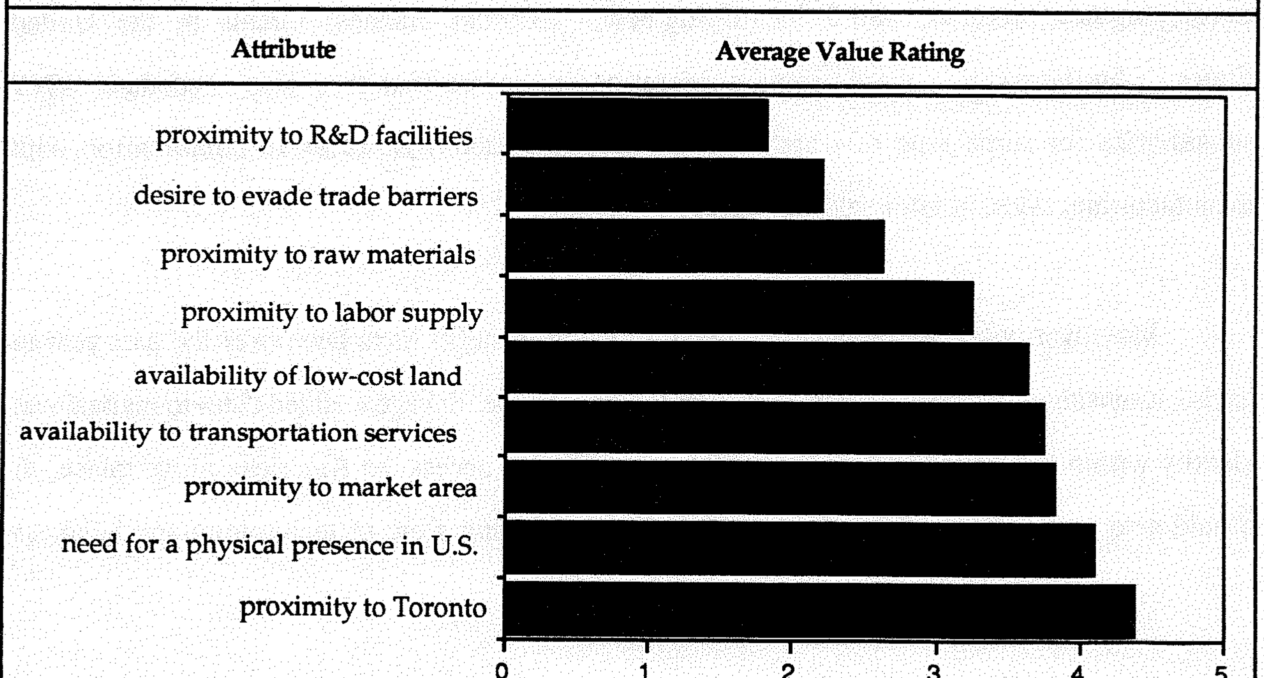
The third focus of this phase of the research was to determine why the Canadian parent corporations located their subsidiaries in the United States in general, and in the WNY region in particular. From the previous analysis of the Canadian-owned subsidiaries in WNY, it was established that the primary reasons for locating Canadian direct investments in WNY were: 1) the close proximity of the region to metropolitan Toronto, which was the headquarters for most of the WNY operations; 2) the desire of the parent company to expand operations outside the Canadian domestic market; and 3) the importance to the parent of having a physical presence inside the U.S. [MacPherson and McConnell, 1990, p. 7]. The responses of the presidents of the Canadian parent corporations confirm and reinforce the findings from the previous study. More specifically, proximity to the home base in Canada and the desire to have a presence in the American market were the top two answers given by the chief decision-makers of these companies in response to each of the following questions: a) Why was the United States selected over other locations for the company's first FDI? b) Why was New York State selected over other states and regions for their first FDI in the United States? And c) what are the primary reasons for locating the corporation's subsidiary in WNY?

Several additional insights are evident about the locational strategies of the Canadian chief executives. First, the direct investment preference of almost one-half of them was to build new operations rather than to acquire existing businesses. This further explains the interest in the WNY area, where the costs of industrial land are but a fraction of the costs of similar property in southern Ontario [MacPherson and McConnell, 1990, p. 7]. In deciding to make their first FDI outside of Canada, moreover, only 6 considered a country other than the United States; and, when deciding where within the United States to locate their FDIs, 11 (44 percent) established subsidiaries only in New York State, and only 4 of the corporations located operations in more than 2 states.

The very limited number of locational alternatives considered by these companies is explained by their underlying direct investment strategy. The executives were asked why they selected the United States over other global locational choices; they were then asked why they selected New York State over other locations within the United States. For each question, the predominant strategies identified were: 1) the goal of having the subsidiary in close geographical proximity to the headquarters' location; and 2) the desire to capitalize upon the relatively large size of the American marketplace and upon the parent's general familiarity with the business environment of the United States.

Finally, these same rather conservative locational tendencies are further revealed by inspecting the reasons the Canadian executives gave for selecting WNY as the site of their FDI (Figure 2). By far, the principal factor identified was "proximity to Toronto (driving time)." On the 1.0 to 5.0 rating scale, this had an average rating value of 4.38. Next in strategic importance were: the desire to have a physical presence in the United States; proximity to market area; proximity to transportation services; availability of low-cost land; and proximity to labor supply.

Figure 2. **Factors Affecting the WNY Locational Decision**



In general, the locational strategies of the parent corporations reflect their relatively small size; the fact that for many of them this is their first FDI venture outside Canada; and the perception on the part of the executives that there is a need to maintain close control over the FDI -- an objective that can best be achieved by locating the operation as close to the headquarters as possible. Of considerably less importance were such factors as proximity to R & D; the desire to avoid American tariffs and other trade barriers; and proximity to raw material sourcing. These responses suggest a strong correlation between the marketing and distribution assets that form the basis of the corporations' competitive strategies and the geographical forces that influence the parents' locational preferences.

Benefits Derived by the Parents from the WNY Subsidiary

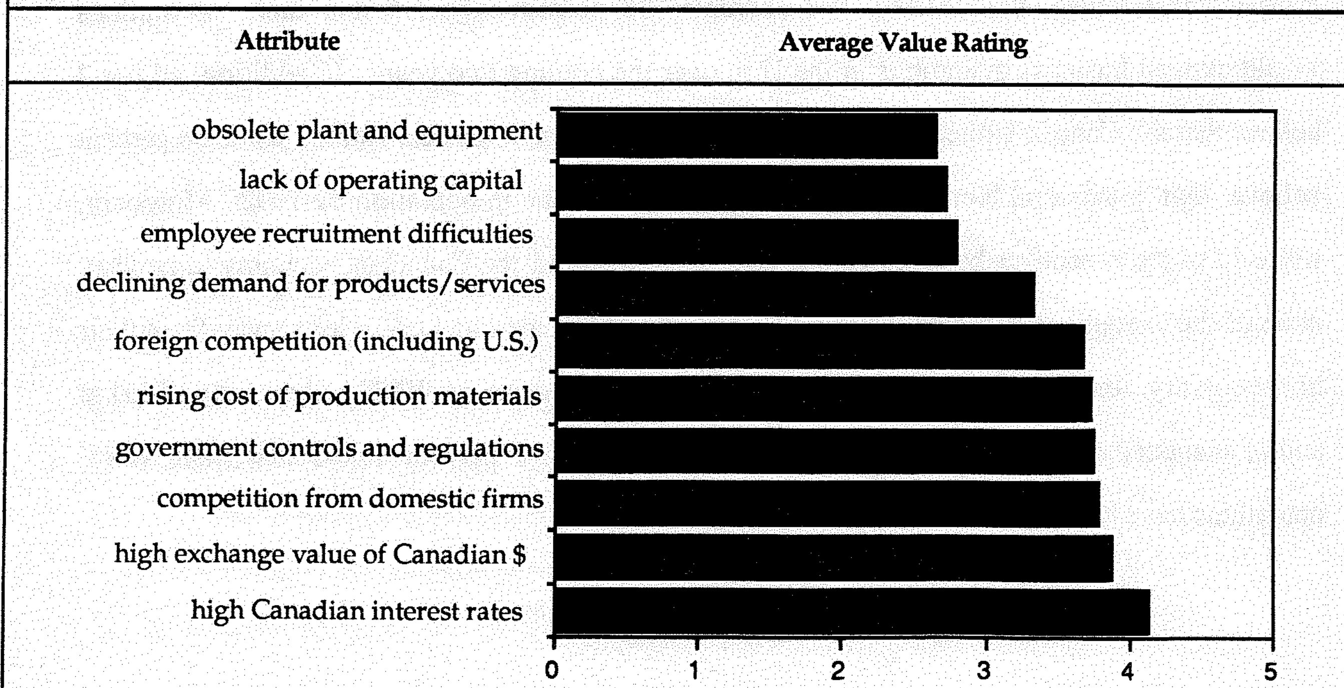
The relative importance of marketing and distribution strategies are also evident when the Canadian parent corporations were asked to assess the benefits they have recently derived from having a subsidiary in the WNY region. The survey asked the executives to identify strategic areas of intracorporate/crossborder linkage in which the parent assumed 50 percent or more of the responsibility in 1990 for servicing its subsidiary. Fifty-two percent of the respondents indicated that they assumed primary responsibility for: 1) designing, testing, and developing new products; and 2) identifying new, potential business clients in the United States. Furthermore, these same corporations indicated that they also used their WNY subsidiaries for some type of warehousing/distribution activity, often in combination with manufacturing, sales, or after-sales servicing.

Moreover, when asked what the most important benefits have been over the past year in having a subsidiary located in WNY, 72 percent said that the linkage enabled them to maintain an identity within the United States and, at the same time, to access the American marketplace. It should also be noted that 56 percent indicated that a greater flow of technology and business know-how was moving from Canada to the WNY subsidiaries than in the opposite direction, although some 32 percent indicated that such flow was fairly balanced. It seems clear, therefore, that the parent companies have been benefiting from their WNY linkages, but that the two-way flow may not be as asymmetrical as some critics of Canadian FDI in the United States have claimed [Drache, 1990]. Certainly, from a strategic perspective, the WNY location has been providing the Canadian parent companies with the means whereby they can better exploit their competitive advantage in the American market.

Factors Likely to Influence Strategic Decisions in Near Term

Another important objective of the survey was to discover the outlook Canadian executives had for their business operations over the near future. Significantly, most of the respondents identified high interest rates as the most limiting factor for their corporations over the near future (Figure 3). This factor has an obvious impact upon the organization's ability to expand business operations in Canada. The second most important factor was the relatively

Figure 3. **Factors and Constraints Likely to Influence Strategic Decisions in the Near-Term**



high value of the Canadian dollar vis-a-vis other currencies. One might suspect that the foreign direct investment strategies of Canadian corporations would be better served by a relatively strong domestic currency; however, for most of the businesses in the sample, exporting to the U.S. is at least as important as FDI activity, if not more so. For these companies, therefore, a relatively strong Canadian dollar weakens their marketing capabilities outside the country. The other factors that were seen as likely business constraints over the near future included competition from domestic firms, government controls and regulations, the rising costs of production materials, competition from foreign producers, and declining demand for products. All of these factors reflect the executives' perceptions of deteriorating domestic business conditions over the near term. In contrast, factors internal to the corporations were perceived by the executives to be relatively unimportant in restricting economic performance over the immediate future. These internal factors included poor labor-management relations, out-dated plant and equipment, lack of sufficient operating capital, and employee recruitment difficulties.

Notwithstanding some concerns for the economic health of their own domestic environment, the executives in the sample expressed considerable optimism about their business prospects inside the United States. For example, 88 percent expected that their corporations would expand business operations in the U.S. over the coming two years. In addition, all but 2 believe that the Canada-United States FTA will remain in tact in the near future, while 68 percent believe that a trilateral North American trade accord will be in operation by 1992. Moreover, while 12 of the executives believe that the FTA has damaged the Canadian economy somewhat, none of the executives believed that their FDIs in the WNY area had taken jobs away from their home country. Indeed, 48 percent indicated that their presence in WNY had recently added to and/or sustained employment in Canada. The remaining 52 percent stated that their WNY operations have had no impact upon jobs in Canada.

CONCLUSION

This research provides a region-specific perspective on the nature and impact of recent Canadian direct investment in the United States. Using survey data from Canadian-owned business establishments located in the WNY area and from their parent corporations in Canada, several important findings emerge. First, recent Canadian FDI in the study area has not been driven primarily by the trade and investment provisions of the Canada-United States FTA. Rather, Canadian companies have been attracted by a combination of competitive factor costs, locational advantages (i.e., proximity to American regional markets), and accessibility to parent corporations in central Canada. In addition, Canadian direct investment has been accompanied by cross-border flows of technology, information, merchandise, and management expertise. These flows are distinctly two-way in focus, providing both southern Ontario and the study region with significant commercial benefits, and suggesting the existence of strong synergy within the cross-border area.

Moreover, Canadian investment has brought an element of structural diversification to the WNY economy, as well as new jobs, exports, tax dollars, and spending on research and development activities. At the same time, the investment thrust has created a heightened awareness of the continuing importance of manufacturing as a source of regional employment. Contrary to popular belief, scant evidence exists that manufacturing is in imminent danger of sectoral extinction--at least not in the WNY region.

Another important finding is that the typical Canadian parent corporations that are making direct investments in WNY have employment and sales levels that, by North American standards, are relatively small to medium-size; their industry affiliations represent a wide diversity of manufacturing and service activities; and they tend to invest between one and five percent of their annual sales revenues in R & D activities. Also noteworthy is the fact that most of these Canadian parents have not had much experience in making direct investments outside of Canada. Hence, their decision to locate subsidiaries in the nearby WNY area reflects their desire to develop a physical (i.e., marketing) presence in the United States, while maintaining close supervision and control over their cross-border operations.

Finally, in their attempts to position themselves strategically within the United States marketplace, most of the Canadian parent corporations examined are basing their competitive edge upon perceived marketing and distribution advantages, rather than upon such assets as economies of scale or technological innovations. Thus these relatively small companies are utilizing some of the same firm-specific advantages of marketing and distribution developed within the home environment of Canada that are characteristic of Canada's largest multinationals [Rugman, 1987]. Moreover, their direct investments in the United States confirm Rugman's suggestion that successful strategic management of Canadian international business does not have to follow the American and European formula of developing firm-specific assets based upon proprietary knowledge and the embodiment of high technology; instead, it can be based upon an efficient marketing system and an extensive distribution network [Rugman, 1987, p 12]. Thus, by venturing into the WNY region as investors, these companies, many of which were formerly exporters-only to the United States, are internalizing their firm-specific advantages in an effort to extend their control over the marketing and distribution functions of their operations across the border in the United States.[2]

These basic conclusions lead quite naturally to several theoretical and policy issues that require further investigation. First, although this study has revealed some of the assets that underlie the competitive advantage of particular types of Canadian firms, a more detailed assessment is necessary to test Dunning's [1988] "Ownership-Location-Internalization" model. Moreover, once these firms have located in WNY, how does their economic performance over time compare to that of their American counterparts? What are the long-term prospects for the successful business performance of these Canadian subsidiaries? These and related questions suggest a comparison of a sample of Canadian subsidiaries and American competitors in the same industry categories over a specific time horizon.

Second, the authors are interested in monitoring closely the operations of the Canadian subsidiaries and their parent corporations after the initial FDI in the United States has been made. The research already completed provides a benchmark from which such a longitudinal profile of economic performance and business strategy can be developed. Such an undertaking should provide new theoretical insights into the parent companies' learning curves as they seek to grow and expand operations in the United States. Of particular interest is how subsequent locational strategy evolves for the corporations, and how the firms' marketing-information system develops as it expands business operations in the United States.

For Canadians, of course, an important policy issue is the extent to which southbound FDI has affected domestic employment in export-oriented sectors. Current viewpoints on this issue are mixed, at best. What is needed is an in-depth, corporate-level assessment of the precise impact Canadian FDI in the United States has upon jobs and possible disinvestments in Canada. Using the sample of firms from the present study, it is possible to begin to expand this research to obtain a more comprehensive perspective on the job issue. Such insights would have important repercussions upon public opinion and policymaking in Canada, and they would have obvious overtones for the ongoing North American trade negotiations where fears abound that a continent-wide trade accord will erode job levels in both Canada and the United States.

A fourth concern generated by this research is the likely impact of a North American Free Trade Agreement upon the regional border economy of southern Ontario and WNY. Interest has already been expressed by local policymaking groups on both sides of the border about the potential impact such a trade accord might have on existing subsidiaries in the region, and upon employment in such labor-intensive industries as automobiles and textiles. Within a broader, North American context, the authors' research on the FTA and cross-border trade and FDI leads quite naturally to considering the likely impacts of a North American FTA upon the three countries. Of particular note are the impacts such a trilateral trade accord might have upon the regional border economies of the three countries. For example, to what extent will these regions of the continent be any more or less impacted than other areas? Will the existing border regions, such as the Toronto-to-Buffalo-Commerce-Corridor and the maquiladora industrial zone, assume an even greater economic role after a tri-national trade pact occurs than they are now, or will forces be set in motion by such an FTA that greatly weaken the comparative advantages currently enjoyed by these border areas? Moreover, what are the complementarities of the three countries, and how might these be capitalized upon to intensify the economies of the cross-border regions? These questions, among others, are already being raised by policymaking groups in each of the three countries, and their answers have important ramifications for the current trade negotiations, as well as for policymakers in the cross-border regions.

ENDNOTES

[1] The non-response error is impossible to estimate because the precise number of all Canadian-owned establishments located in the study area is unknown. At the outset, a Canadian-owned establishment was defined as a manufacturing or service operation that maintained a physical presence within the area (i.e., the parent company had to own or lease space in the region; it could not simply rent out a mail box at a local commercial bank) and employed locally at least one person. In an effort to verify the population of Canadian operations in the region, the authors acquired or purchased five different data bases from local, state, and federal (Canadian and American) government and private-sector agencies. Unfortunately, no two data bases were the same. Consequently, the authors developed their own data base by merging all of the available lists and confirming through telephone calls whether or not the Canadian-owned establishment had a physical presence in the region and employed at least one person locally. However, it was not possible to determine unmistakably that all of the Canadian-owned subsidiaries had been identified.

[2] One may wonder why these Canadian parent companies do not remain in Canada and utilize their marketing and distribution advantages as exporters to the United States After all, the Canada-United States FTA is designed to lower the barriers to cross-border trade over a ten-year period, and entering the United States as direct investors would appear to add to the transactional costs of reaching the United States marketplace. For many of these companies, however, the decision to enter WNY as an investor has two principal advantages over remaining in Canada and exporting to the United States : first, the FDI provides them with a physical presence within the United States , which is perceived to be advantageous from a marketing and distribution perspective; and second, because of the significantly lower cost of doing business in WNY vis-a-vis southern Ontario, the transactional costs associated with an FDI are considerably reduced. In fact, for certain distribution functions, it is cheaper to ship merchandise from Canada to a warehouse in WNY and distribute it from there to other places in the United States than it is to distribute products to the United States from a location within the southern Ontario region.

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