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CANADIAN-OWNED ESTABLISHMENTS IN WESTERN NEW YORK: KEY CHARACTERISTICS AND POLICY IMPLICATIONS FOR THE CROSS-BORDER REGIONAL ECONOMY

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Canadian-Owned Establishments in Western New York: Key Characteristics and Policy Implications for the Cross-Border Regional Economy

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ABSTRACT. This paper examines the scale, sectoral composition, and regional economic impact of Canadian direct investment in Western New York. Empirical perspectives on the role of the Canada-United States Free Trade Agreement (FTA) are presented, notably with regard to Western New York's growing absorption of Canadian industrial capital. Data from a postal survey of Canadian investors are used as the basis for the investigation.

Several important findings emerge from the research. First, recent Canadian foreign direct investment in Western New York has not been driven by the trade and investment provisions of the Canada-U.S. FTA. Rather, Canadian companies have been attracted by a combination of competitive factor costs, locational advantage (proximity to U.S. 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 economic synergy within the cross-border region.

Moreover, Canadian investment has brought an element of structural diversification to the Western New York 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 this region. The paper concludes with some suggestions for policymakers in the cross-border region.

INTRODUCTION

Across most regions of the United States, including the industrial northeast, foreign direct investment (FDI) has become an issue of growing public concern (Little, 1988). Civic emotions have recently been touched by foreign acquisitions of landmark public buildings in New York, Los Angeles, and Chicago, and by major commercial takeovers involving well known companies like Firestone, Federated Department Stores, and Columbia Pictures. From an emotional perspective, acquisitions of this ilk have mobilized a good deal of anti-FDI sentiment among public interest groups, not least because of the perceived erosion of US economic sovereignty in key sectors. At one end of the political spectrum, unrestricted FDI is viewed as a potentially major threat to US commercial autonomy. At the other end of the scale, inflows of foreign capital have been identified as a positive stimulus to domestic economic development (Little, 1988; McConnell, 1983, 1989). Those supporting the latter position argue that FDI is a powerful source of new employment growth, technology transfer, and economic diversification. Irrespective of which perspective one happens to adopt, however, the fact remains that the United States has become a major target for new external investment across a broad range of sectors, including real estate, manufacturing, retailing, distribution, and financial services.

This paper offers a local perspective on the recent impact of FDI upon one region of the United States that has enjoyed significant inflows of foreign capital for several decades -- Western New York. While this region has attracted investment funds from a wide variety of sources, including Britain, the Netherlands, and Japan, FDI from Canada has long played a distinctive economic role. Moreover, as the governments of Canada and the United States continue to implement the Free Trade Agreement (FTA), which came into effect on January 1, 1989, local expectations concerning future Canadian investment are remarkably optimistic. Part of this optimism can be traced to Western New York's competitive factor costs, its close proximity to

southern Ontario, and its strategic location along the Canada-United States border. Now that the FTA is in place, moreover, the long-term economic prospects of the region look reasonably good (Harrington, 1989; McConnell, 1989), especially with regard to cross-border trade, investment, and corporate joint-ventures (Investment Canada, 1990). Unlike any other region of the United States, Western New York enjoys a central location with respect to Canada's largest concentration of industry, people, and capital -- metropolitan Toronto. Over the past few years, moreover, the Western New York area has absorbed substantial investment from Ontario, such that, by now, local policy agencies are reshaping their development priorities to stimulate additional inflows from Canada (McConnell and MacPherson, 1990). A popular hope among local politicians is that Canadian FDI will further diversify the region's economic base, bringing new industrial vitality to an otherwise depressed manufacturing region. A less optimistic hope is that new inflows from Canada will decelerate the region's industrial decline, providing valuable breathing space for local economic restructuring (MacPherson, 1990).

Set against this backdrop, three principal questions are addressed in this paper. First, what are the primary factors attracting Canadian-owned establishments to the Western New York border region? Second, what are some of the key industrial and organizational characteristics of these subsidiaries? And, third, what are the policy implications of these direct investments for the economic growth prospects of the region in the near future? Before exploring these questions, it is appropriate to consider the economic and locational characteristics that make Western New York a viable target for Canadian capital flows, and to review the procedures that were used to identify and survey the Canadian subsidiaries.

THE STUDY REGION

Western New York is strategically located within a 500-mile radius of more than half of

the 270 million people that reside in Canada and the United States (Figure 1). From a North American marketing perspective, the study region enjoys quick access to almost half of the consumer purchasing power of both countries, 55 percent of U.S. manufacturing activity, 77 percent of Canadian manufacturing activity, and over half of the professional, scientific, and technically skilled manpower of the two nations (McConnell et al, 1989). In addition to geographical advantages, average factor costs in Western New York are significantly lower than those that prevail in central Canada, and this has been true for some time. By now, in fact, the average price gradient between metropolitan Toronto and Western New York slopes distinctly downward, leaving business locations in southern Ontario at a comparative disadvantage in terms of labor costs, land prices, and corporate taxes (among other things). For instance, manufacturers that want to operate in metropolitan Toronto will find industrial land costing anywhere between $200,000 and $400,000 per acre, compared to an average of $25,000 per acre in Erie and Niagara Counties (McConnell et al, 1989). Furthermore, central area office space in Toronto begins at around $25 per square foot, compared to only $9 per square foot in Buffalo (Erie County United States-Canada Commerce Task Force, 1989). Since southern Ontario and Western New York are close geographical neighbors, cost differentials of this magnitude are far from trivial.

From the standpoint of Canadian investors that want expanded access to the U.S. regional markets, Western New York provides a convenient entry point for new capital investment. Not only is the region locationally and culturally proximate to central Canada, it is also very familiar to Canadian shoppers, tourists, and other visitors -- droves of whom regularly cross the Niagara River in search of bargain retail prices. For Canadian companies, moreover, the Western New York area may also function as a low-cost export platform for serving both foreign and Canadian markets.

Western New York in Geographic Context

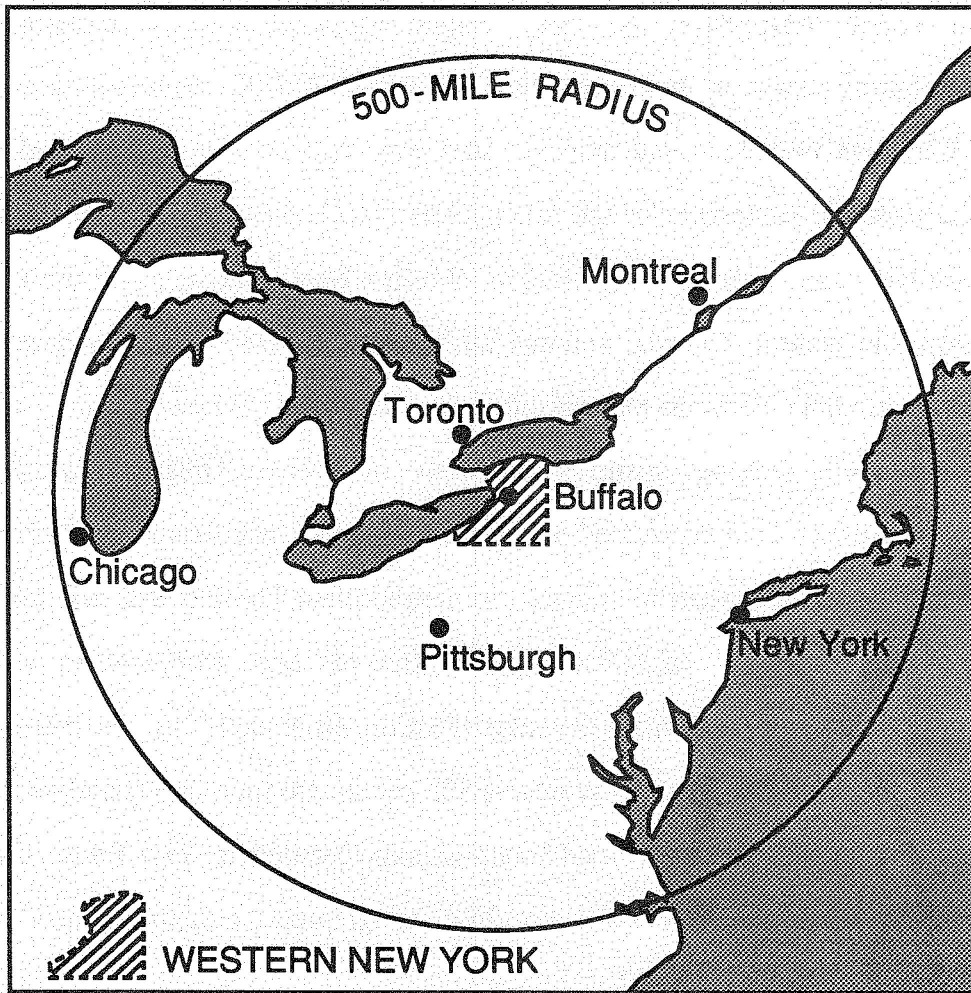

Figure 1

To date, however, very little empirical work has been carried out on the scale, structure, or economic significance of Canadian direct investment in this region. In addition, rather little is known about the precise mix of entry motives for different types of Canadian investors. Indeed, as far as Western New York is concerned, a curious situation that confronts local policy agencies is that the exact number, sector mix, and employment contribution of recent Canadian entries remains unknown. For example, contemporary population estimates range from an optimistic high of 500 establishments to a low of about 150. Within this range, moreover, the distribution of Canadian arrival dates is also unknown. In this regard, it should be noted that neither the New York State Department of Economic Development nor Investment Canada has access to a reliable data-set, and the same holds true for a wide range of public policy agencies in both countries. Appropriate monitoring systems are clearly not in place on either side of the border. This is unfortunate for both nations, if only because policy units, firms, and other business organizations are left with a paucity of solid information to support strategic decision-making. While regional and national newspapers in both countries have followed the investment story with lustre, journalistic anecdotes are a poor substitute for systematically assembled data. Furthermore, as catholic newspaper readers will attest, conflicting impact statements in both countries raise disturbing questions concerning the quality of information that flows toward the public domain.

SURVEY METHODOLOGY

As a first step toward addressing the questions noted above, the authors estimated the likely regional population of Canadian establishments by crosstabulating multiple company listings from Dun and Bradstreet credit files, the area Chamber of Commerce, the Canadian Government, the New York State Department of Economic Development, and the Canada-United

States Trade Center (CUSTAC) at the University at Buffalo. The objective was to identify Canadian-owned establishments that had a physical presence in the Western New York area, which was defined as a business that owned or rented an office or production facility in the area and that employed one or more people locally. Suffice it to say that over 200 allegedly Canadian companies were quickly eliminated from our listings, leaving a total population estimate of 182 establishments. Of the latter, 49 were subsequently removed from the sampling frame because they were either no longer in business or were improperly identified as Canadian-owned.

The questionnaire was designed and pretested with a view to collecting proprietary information across the following dimensions: corporate strategy, business performance, organizational structure, and regional economic impact. Prior to the mailing of the survey in Autumn, 1989, the Chief Executive Officer (CEO) of each establishment received an information packet containing two letters of introduction: one from the president of the Can-Am Business Council of the Niagara Frontier endorsing the inquiry, and one from the two investigators describing the purpose of the survey. Several days later, the survey instrument was distributed to the 182 establishments in the five-county region of Western New York. As noted earlier, 49 establishments were subsequently eliminated from the inquiry, bringing the total population estimate down to 133. A total of 58 valid questionnaires were returned, giving a final response rate of 43.6 percent. While this is a respectable response rate, especially in view of the length, complexity, and breadth of the survey instrument, the extent of non-response bias is impossible to estimate. Virtually nothing is known about the strategic business characteristics of the 75 non-respondents. The "true" population size of Canadian companies also remains unknown. Keeping these reservations in mind, then, the survey results should be treated as exploratory rather than conclusive.

OVERALL PROFILE OF THE CANADIAN SUBSIDIARIES

Several general characteristics of the 58 Canadian-controlled companies in the sample are worth mentioning. First, all but two have their headquarters in southern Ontario. Not surprisingly, a substantial majority (n = 50) of the parent companies resides in the Toronto urban region. Second, the average age of the survey establishments is approximately 12 years (the range is from a few months to 79 years). Third, the average employment level of the establishments at the time when they first moved into the region (start-up) is 21, compared to approximately 75 at the time of the survey. Fourth, all but eight of the subsidiaries were created as new businesses in the area, rather than as acquisitions of existing operations. Sixth, average annual sales over the most recent operating year are a little over US$9 million, compared to approximately US$1 million at start-up. Fifth, and contrary to local popular belief, most of the Canadian companies in the sample did not move across the border to escape US tariff protection, government taxes, or other regulations of commerce. Indeed, almost 80 percent of the CEOs indicated that such concerns were of little significance in the decision to locate in the study area.

For the sample as a whole, the decision to invest in Western New York can be traced to a relatively small range of factors. For instance, over 50 percent of the managers ranked the following criteria as either "important" or "very important" in the decision to locate in the study area:

- the close proximity of the study area to metropolitan Toronto;
- the desire of the parent corporation to expand outside the Canadian domestic market;
- the importance to the parent of having a physical presence inside the United States;
- the proximity to existing transportation facilities and services in the United States;
- the need to be centrally located with respect to the establishment's principal market area;
- the availability in the area of important labor supply.

Interestingly, a significant percentage of the "newer arrivals" (establishments that moved to the study area over the past 5 years) also ranked highly the availability of low-cost industrial land and the ease of establishing business operations in Western New York. In short, it is apparent that Canadian investors view the border region as an attractive platform for gaining physical access to the U.S. domestic market. Because Toronto is less than 2 hours driving distance from the region's principal transportation hub (metropolitan Buffalo), a business location in Western New York enables Canadian parent companies to exercise considerable control over their subsidiaries in the United States. At the same time, of course, Canadian investors can also take advantage of the region's competitive factor costs; its proximity to the U.S. economic heartland; and its expanding infrastructure of business services, transportation facilities, and inexpensive housing (among other things).

It is interesting to note that the importance of having a physical presence within the United States while remaining in relatively close physical proximity to corporate headquarters correlates well with the results of Gandhi's (1989) study of 29 Canadian direct investments in northern New York State. [Gandhi surveyed 81 Canadian-owned establishments in the Plattsburgh, New York area, and received a response rate of 36 percent.] Gandhi attributes the need of these establishments to be in close proximity to their parent corporations to the fact that most of them are small, family-owned operations, where commuting time to and management control over the subsidiary are critical considerations in the location-investment decision (Gandhi, 1989).

INDUSTRIAL CHARACTERISTICS OF THE CANADIAN DIRECT INVESTORS

Twenty four (41 percent) of the survey establishments belong to the manufacturing sector. The principal two-digit manufacturing categories represented in the sample are food,

furniture, printing and publishing, rubber and plastics, metal fabricating, electrical equipment, leather, primary metals, industrial machinery, and apparel (that is, ten of the twenty possible two-digit SIC manufacturing categories). The number of respondents per two-digit industry sector is fairly evenly dispersed across the ten categories, with the largest concentration -- some five establishments -- belonging to the electrical equipment subsector. While the 34 service-sector establishments (59 percent of the sample) are also dispersed over a wide range of activities, the level of dispersal is much lower than is the case for manufacturing. For example, approximately 24 percent (n = 8) of the service-sector cases are in transportation-related activities, an additional 38 percent (n = 13) are in wholesale trade (both durable and non-durable), 3 establishments offer engineering services, and the remaining 10 companies provide hotel (n=1), business (n=5), equipment rental (n=2), and health services (n=2).

A comparison of current versus start-up employment for the two sectors is presented in Figure 2. Interestingly, establishments in the manufacturing sector were found to be more likely to significantly expand their employment base than companies in the service sector. For example, 39 percent of the manufacturing establishments currently employ 50 workers or more, compared to less than 5 percent at start-up. For the service sector, the relative proportions are 24 percent and 6 percent, respectively. While Figure 2 captures only three size-classes, it should be noted that the underlying picture remains constant no matter how the data are carved. An implication here, and one which warrants policy consideration at the local scale, is that efforts to attract further inward investment ought not to overlook the manufacturing sector as a future source of new employment, tax dollars, and output. Although Western New York has been experiencing absolute employment decline in manufacturing since the late 1970s, Figure 3 suggests that the relative share of Canadian-related employment in

PERCENTAGE DISTRIBUTION OF CANADIAN-OWNED ESTABLISHMENT IN EACH SECTOR, DISAGGREGATED BY START-UP AND CURRENT EMPLOYMENT CLASS

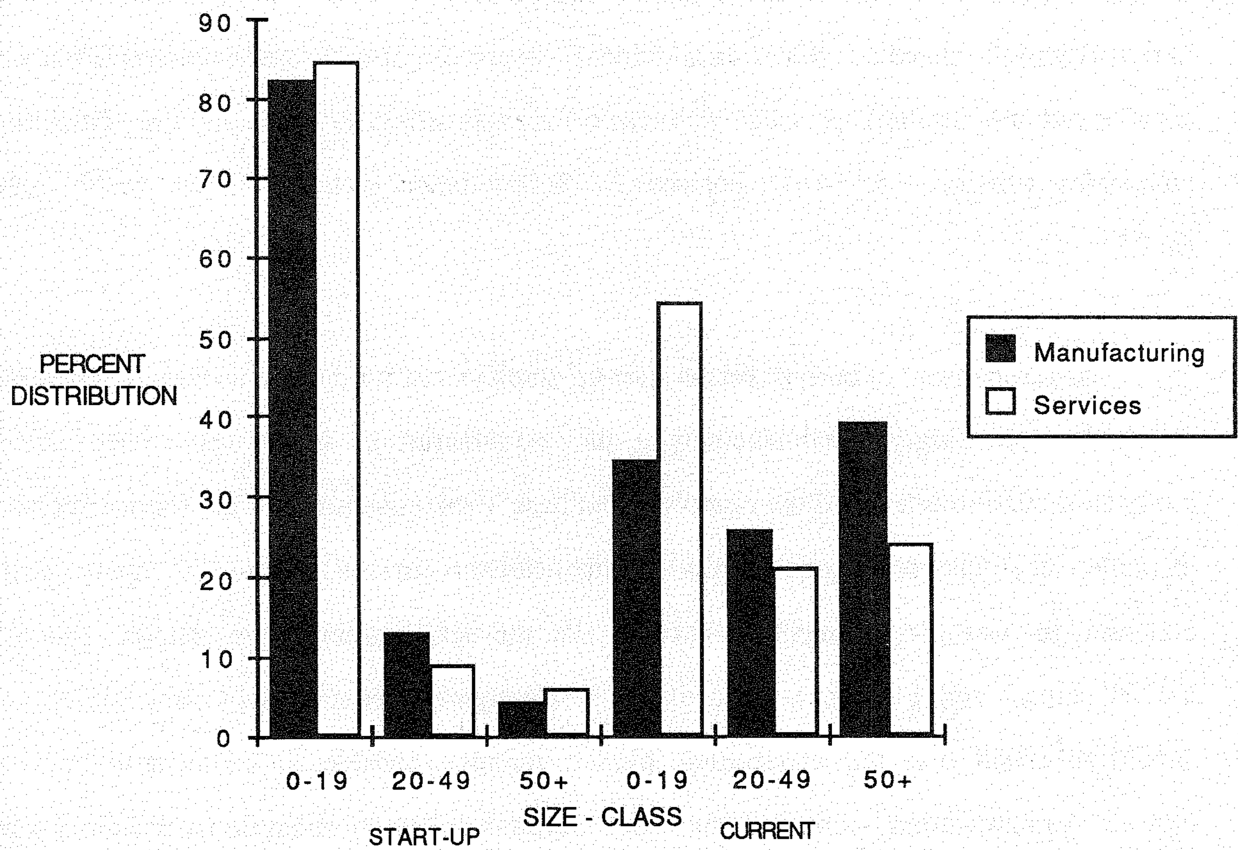

Figure 2

SECTORAL SHARE BY TOTAL CANADIAN EMPLOYMENT, DISAGGREGATED BY START-UP VERSUS CURRENT EMPLOYMENT SHARES

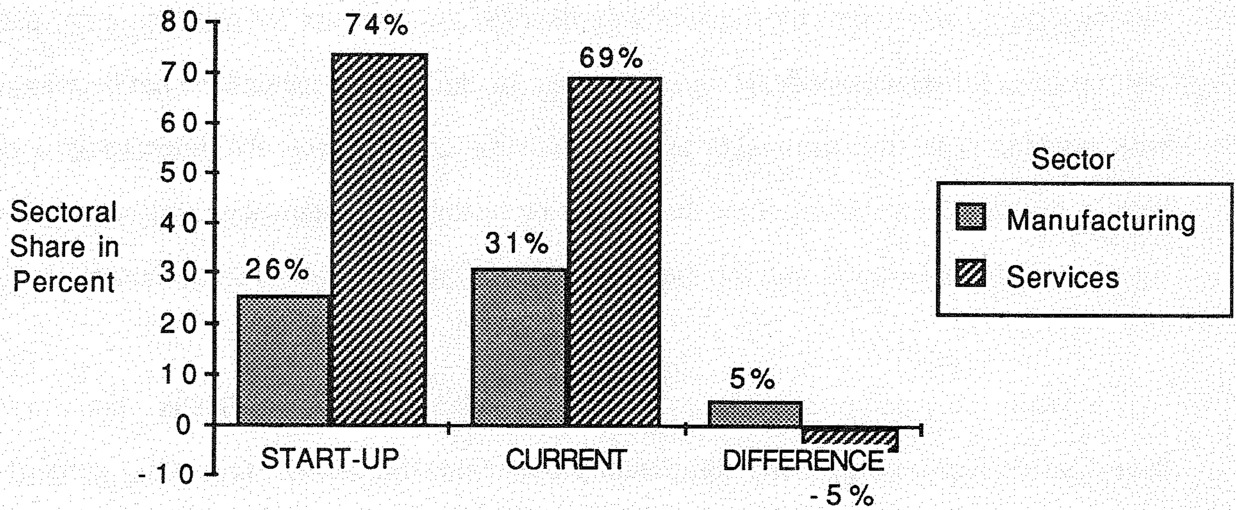

Figure 3

manufacturing has been increasing. In aggregate, Canadian manufacturing establishments achieved an average rate of employment growth of almost 400 percent between start-up and 1988, compared to an average rate of approximately 270 percent for their counterparts in the service sector. Moreover, by standardizing the data to account for different entry dates and start-up sizes, it becomes evident that companies in the service sector have not been expanding with anything near the same vigor as their industrial counterparts. An interesting conjecture here is that the recent decline of the manufacturing sector in Western New York would have been significantly faster were it not for the entry of new industrial firms from Canada.

While more will be said about this later, a further pattern in the data is that inward FDI from Canada has been growing significantly over time (Figure 4). Over fifty percent of the Canadian-owned establishments arrived in the 1980s, and this holds true for both manufacturing (n = 12) and services (n = 18). Interestingly, a good deal of the recent Canadian-related employment growth in both sectors has occurred since 1985. Fully 40 percent (n = 23) of the region's Canadian-owned companies arrived in western New York over the past 5 years (1985-1989/90). Arrivals in this group account for almost over 50 percent of the jobs created by the survey establishments. This suggests that Canadian interest in the Western New York area has been growing steadily since the late 1960s. While Canadian FDI in this region is hardly a new phenomenon, a moderate acceleration of the investment thrust would certainly appear likely over the next few years.

An additional point worth noting is that average levels of start-up versus current employment are significantly different for the sample as a whole. Average start-up employment is approximately 20 employees, compared to over 70 employees today. Accumulated over the entire population of Canadian-owned companies that are known to operate in the region (n = 133), estimates of this magnitude translate into a total Canadian employment contribution of

PERCENTAGE DISTRIBUTION OF ESTABLISHMENTS IN EACH SECTOR, DISAGGREGATED BY DATE OF ARRIVAL IN WESTERN NEW YORK

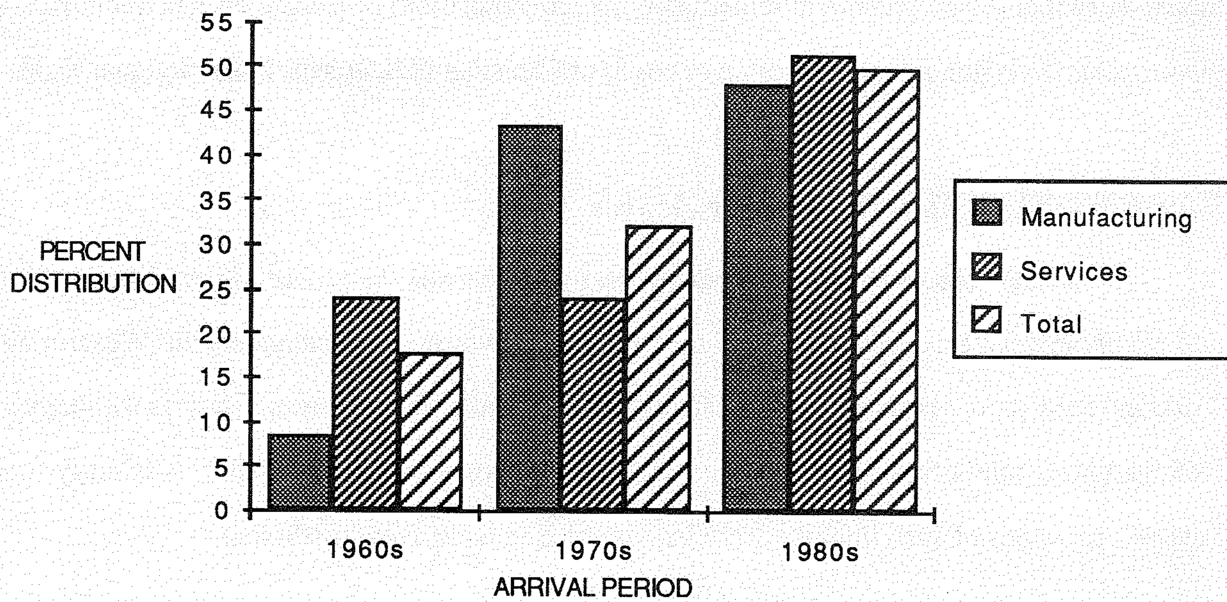

Figure 4

over 10,000 jobs. While this estimate must be treated with caution, especially in view of the small size of the sample, an employment impact of around 10,000 jobs is not too far removed from other recent estimates produced by academics and government agencies in the Western New York area. According to the New York State Department of Economic Development (Lewington, 1990), for example, Canadian direct investment in New York State has created over 7,000 jobs since 1985 alone -- representing a post-1985 investment total of over $1 billion (Figure 5). Clearly, then, it is reasonable to propose that Canadian-owned companies have had a significant impact on the region's employment performance, particularly over the past 10 years. Moreover, because new-start operations are typically viewed more favorably than acquisitions from the perspective of job creation (and expansion of the local tax base), the preferred modal entry mode (i.e., greenfield rather than merger/acquisition) of Canadians has minimized the employment diversion effects (opportunity costs) of Canadian FDI, at least at the regional scale.

PARENT-SUBSIDIARY LINKAGES

A further objective of the inquiry was to determine the nature of the organizational and technological linkages between the Canadian-owned establishments in Western New York and their parent corporations in Canada. Specifically, the goal was to assess the degree of technological, marketing, and decision-making autonomy enjoyed by the subsidiary firms. Several measures of such linkages were incorporated in the survey instrument.

First, intra-corporate trade linkages were assessed. It is generally accepted in international business that between one-third and one-half of world commerce is conducted on an intra-corporate basis (Root, 1990). In this survey, 22 (38 percent) of the 58 subsidiaries export some of their output to Canadian customers. Of the latter, 8 send 100 percent of their Canada-bound exports to parent establishments, and a further 2 send 15 and 50 percent,

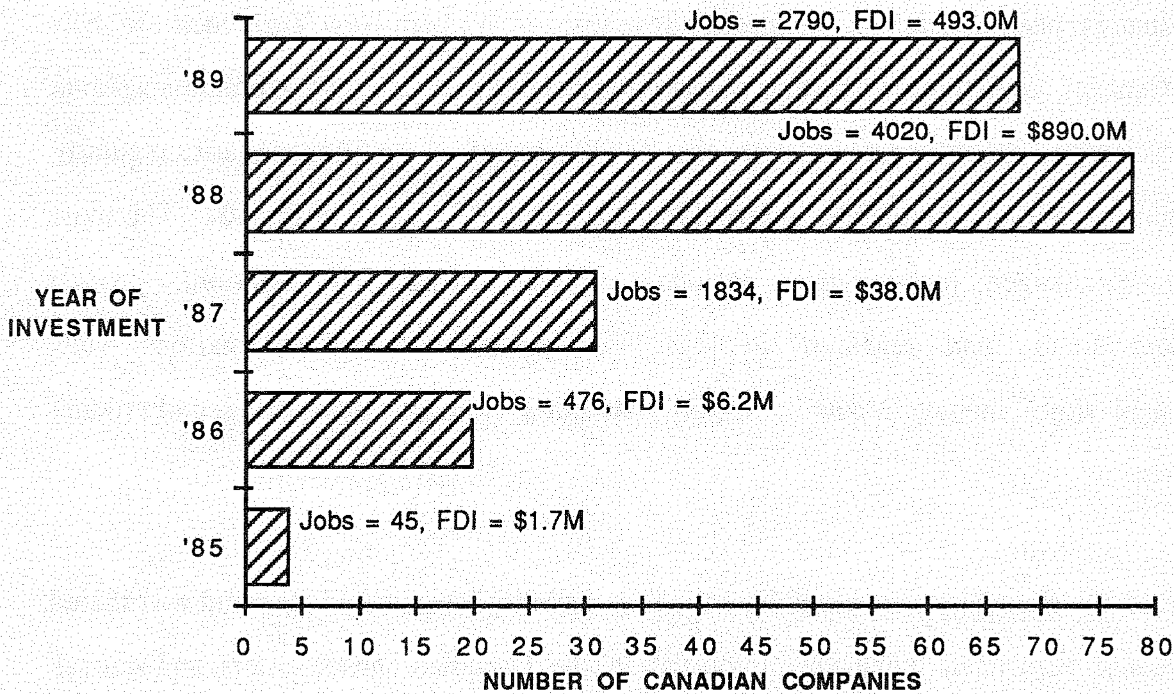

Figure 5

Data for Canadian Direct investment (US$) in New York State in 1988 are extraordinarily high as a result of Robert Campeau's (Campeau Corporation) purchase of US-owned Federated Department Stores (valued at US $6.5 billion in 1988). Subtracting the Campeau purchase from Figure 5 provides a steady inward investment curve that shifts smoothly upward from 1985 to 1989.

respectively. In short, almost 50 percent of the 22 subsidiaries with Canadian export markets have direct intra-corporate trade linkages with their parents in Ontario. Many of these subsidiaries also import components and supplies from their parent companies, giving the intra-corporate relationship a distinctly two-way dimension in terms of merchandise trade.

Another component of intra-corporate interaction is reflected in the cross-border flow of technology, market information, and management expertise. In this regard, three principal questions were posed in the analysis. First, to what extent are the subsidiaries dependent upon their parents for various corporate planning and development responsibilities? Second, have the subsidiaries been transferring technology developed in Western New York back to their parents in Canada? And third, what kinds of technological linkages exist at the intra-corporate level? Interestingly, the responses indicate that 23 (40 percent) of the 58 subsidiaries regularly send technology and/or marketing information back to their parents in Canada. The most frequently exchanged technologies include product design information, process development ideas, and research findings. On the management information side, Canada-bound flows include inputs to export marketing strategy, advertising, and product modification.

When the managers were asked how the responsibility for strategic planning was shared among in-house personnel, management located in the Canadian headquarters, and sources external to the Canadian corporation, a majority of the subsidiary plants was found to rely greatly upon parent inputs. For example, the parent corporations of over one-half of the subsidiaries assume over 50 percent of the responsibility for the following support services: research and development, product design, accounting, marketing strategy, quality control, and product testing. A slightly smaller number of establishments also depends heavily upon parent

enterprises for their engineering drawings, equipment specifications, and export planning. Having said this, however, it would be incorrect to view the region's Canadian-owned establishments as truncated units that lack in-house expertise in spheres like R&D, marketing, and management. For example, 17 of the survey establishments (30 percent of the sample) generate at least some of their research requirements through in-house R&D. Thirty seven percent of the latter (n = 6) are fully self-contained in terms of R&D, and all of these establishments periodically send R&D outputs back to Canada. In short, most of the Canadian-owned subsidiaries located in the border region maintain strong ties with their corporate parents. Moreover, these cross-border linkages are economic, technological, and organizational in nature. It would also appear that these flows are distinctly bilateral in focus, so that both the Canadian parent corporation and the Western New York region are beneficiaries of the intra-corporate transactions.

POLICY IMPLICATIONS FOR WESTERN NEW YORK

While it is not possible to generate policy prescriptions from a survey of this size, the empirical results of this research suggest several factors that are likely to be important considerations for private- and public sector decision-making groups in the local area. In the first place, Canadian direct investment in Western New York is by no means a recent phenomenon. Although the study area has attracted a growing number of Canadian investors over the last few years, many of the region's largest Canadian-owned firms have been active in Western New York since the late 1960s. Second, the structure of Canadian direct investment in the study area closely resembles the aggregate sectoral profile of the region as a whole. When the Canadian subsidiaries are viewed over time, however, it would appear that Western New York is attracting an investment mix in which manufacturing firms are becoming increasingly prominent. Third, Canadian-owned manufacturing firms have been outperforming their service sector

counterparts in terms of start-up versus current employment. Manufacturers appear more likely to move beyond the 0-49 employment class than service companies. Fourth, most of the Canadian-owned subsidiaries operate with intra-corporate linkages that involve cross-border flows of merchandise, technology, and information. At this juncture, then, it is pertinent to review the main implications behind the empirical results.

First, it is apparent that the Canadian investors in the sample view the Western New York area as a very desirable location for their U.S. operations. By locating facilities within the region, Canadian parent corporations can exercise considerable control over business operations, and, at the same time, take advantage of the region's wide range of business-support services, favorable costs of doing business, and accessibility to a major portion of the economic heartland of the U.S. It is also clear that when locating businesses within Western New York, most of these investors prefer to establish new facilities rather than to acquire existing operations. It seems important, therefore, for local policymaking groups to continue to emphasize policies and programs that:

- improve the transportation infrastructure of the cross-border area to minimize driving time between the two regions and to maximize the integration of the local region with the U.S. national transportation system.
- foster the creation and nurturing of business-support services in the area.
- increase the pool of skilled labor in the region so that businesses from Canada (and elsewhere) can obtain appropriately trained workers.
- promote the many business attributes of the cross-border region to other potential investors within and beyond the North American continent.
- provide potential investors with appropriate levels of legal, financial, and governmental assistance that minimize the difficulties of establishing a new business within the region.

Another implication of this research for local policymakers relates to the overall economic benefits of Canadian FDI to the local region. Although regional economic impact is traditionally measured in terms of employment creation, input-output linkages, and various multiplier

effects, a major issue for Western New York must surely be the extent to which Canadian investment has broadened the region's economic base. Industrial diversification is widely perceived as an insurance policy for coping with cyclical downswings in the economy (Little, 1985, 1988), and this type of insurance is particularly appropriate for Western New York. Indeed, the region's continuing dependence on a narrow range of mature industries suggests an urgent need for structural diversification. In this regard, evidence presented earlier suggests that Canadian direct investment has indeed brought a diversification thrust to the region, particularly since the mid-1980s. It should also be noted that Canadian investors have not simply been transferring low-order business activities to Western New York -- far from it. Several of the region's Canadian-owned companies perform significant levels of research and development; several manufacture high value-added end-products; and several operate in important service areas like engineering consulting, transportation, software distribution, and finance. In short, it would be incorrect to view the investment trend as a cost-driven redistribution of low-order business operations from southern Ontario to Western New York. This is simply not the case.

Further evidence to support this proposition can be gleaned from the recent business performance of the Canadian subsidiaries, notably with regard to profits, market focus, and employment creation. For instance, 60 percent of the establishments exhibit above average profitability relative to their specific industry/sector class, and over 90 percent cater primarily to the high-price/high-quality end of the market. A majority expects to create new jobs over the next few years, and a majority expects to invest in new plant and equipment. Fully 64 percent (n = 36) of the survey establishments expect to expand significantly their business operations in Western New York over the next 5 years. While the data are not very robust with respect to any of the preceding variables, the results certainly suggest "good news" as far as local policy agencies are concerned. It is important, therefore, for these local groups to focus upon policies

and programs that:

- encourage the inflow of FDI in manufacturing industries.

- foster the creation and nurturing of small and medium-sized establishments in industries with potential for creating new jobs.

- portray with renewed vigor to the outside world that the Western New York region is capable of attracting and sustaining a rich diversity of foreign-owned and domestic manufacturing and service-sector activities.

In addition to the 133 Canadian companies that are known to operate in the study region, it should also be noted that significant numbers of new Canadian entries are expected over the early 1990s. While solid data on this topic cannot be presented here, partly because of confidentiality restrictions, the fact that several major legal firms in Buffalo have been processing growing numbers of Canadian business immigration applications implies that the recent investment trend is more than a temporary quirk. In this regard, the post-1985 proliferation of Canadian post-office box addresses in Buffalo and Niagara Falls may provide a partial indicator of the future potential for new firm entry. While the growth of Canadian PO Boxes may simply reflect a move toward more aggressive marketing among Canadian firms (many of which may wish to retain all of their operations inside Canada), there is good reason to suspect that early establishment of a local business address (albeit with no business presence) may represent a potential indicator of long-run intent. With this thought in mind, an interesting direction for future research might be to assess the extent to which PO Boxes convert into locally active business operations. One hypothesis that merits attention is that the PO Box may represent an early (and low-cost) market-appraisal device. Therefore, agencies in Western New York that are responsible for attracting new FDI to the region should not overlook these holders of P.O. Boxes because they may become future investors in the area.

A further issue for Western New York concerns the extent to which Canadian-owned

firms generate backward linkages to local suppliers of business services, industrial components, and other inputs. While our data are rather sketchy in this regard, it is worth noting that over 70 percent of the subsidiaries purchase at least half of their business services from local vendors. Of those companies that buy some or all of their services from within the study region, input categories of particular importance include (from most important to least): advertising, accounting, printing, banking, office and secretarial support, customs brokerage, legal advice, transportation and shipping services, office supplies, and marketing know-how. Clearly, input demand on the part of the Canadian-owned business population does not wholly bypass local suppliers. This is an encouraging finding, if only because intracorporate transactions at the international scale typically result in suppressed demand for local service offerings (Britton and Gilmour, 1978). It is important, therefore, for local policymakers:

- to encourage the development of export-marketing-assistance programs and the creation of trade-management companies (in the private sector) that can provide the support services needed by local companies to market globally.
- to assist in the formation of educational programs at various levels that are designed to train service personnel for local business-support operations.
- to promote regional and national trade and industry shows, as well as technology-exchange programs, within the area that call attention to the changing nature of the local industry base, and that promote the two-way flow of information and technology between southern Ontario and Western New York.

POLICY IMPLICATIONS FOR CANADA

Thus far, the discussion has presented a distinctly local (US) perspective, leaving the broader implications for Canada untouched. While the authors intend to remedy this situation in the near future, several general statements can be made that are pertinent to the broader interests of the Canadian economy. To begin with, growing outflows of direct investment imply a potential loss of domestic employment, output, and tax dollars, particularly in secondary manufacturing. At the same time, investment outflows that replace domestic exports may

ultimately worsen Canada's current account balance with the United States (O'Grady, 1990). Issues of this sort have become increasingly controversial in Canada, especially in light of the perceived investment implications behind the FTA (Lipsey, 1990). For example, the accord eliminates at least part of the rationale behind the continued operation of U.S. subsidiaries in Canada, and the same logic presumably applies to Canadian firms with branch plants in the United States. The accord also incorporates North-American-content rules that may force Canadian firms that depend on imported inputs to operate inside the United States -- rather than export from Canada.

Ironically, however, there is no solid empirical evidence to connect the FTA with Canada's recent employment losses in manufacturing (Rugman and Verbeke, 1990). Moreover, as several scholars have shown, powerful trends toward industrial rationalization at the continental scale were evident long before the FTA reached the negotiating table (Bluestone and Harrison, 1982; Lipsey, 1990; McConnell, 1983; Rugman and Verbeke, 1989). In this regard, it should be noted that recent Canadian investment in Western New York can be explained in terms of simple economic geography -- that is, the host region is close to the market that Canadian companies wish to serve. Western New York is also close to Toronto (a very expensive city to do business in). Having said this, however, the authors do not wish to minimize the potential long-term significance of the FTA, particularly with regard to cross-border investment. At least three factors warrant attention here. First, the FTA appears to be creating a heightened awareness of the disadvantages of operating inside Canada. The accord also allows for easier FDI in both directions -- giving cheaper business locations in the United States a distinct competitive edge. Second, the extent to which Canadian FDI in the United States has been accompanied by disinvestment in Canada is unknown. More work needs to be conducted here, and the work must be empirical rather than rhetoric-driven. Third, the extent to which US subsidiary firms have been disinvesting in Canada as a result of the

FTA is also unknown. While the Canadian Labour Congress purports to have an answer to this question, the present authors (and no doubt many others) would like to see some hard data on this topic.

On a more positive note, Canada's growing business presence in Western New York implies significant benefit streams for parent companies north of the border. Faced with limited growth opportunities at home, small and medium-sized firms that serve specialized customer segments are well advised to exploit US regional markets via direct investment. Corporate expansion based exclusively upon export marketing is a poor strategy for any firm that requires rapid and direct customer contact with its foreign client base. In this regard, data presented earlier underscore the strategic importance of spatial proximity to US regional markets, as well as a direct physical presence within the US itself. The corporate development path implied by this mode of market entry reflects a sober concern for sustained sales growth, especially among firms that serve well-defined market niches. The empirical findings also suggest an element of technological reciprocity between the Canadian parent companies and their subsidiaries in Western New York, and this must surely be a good thing for both countries. A further benefit for Canada is that Canadian products and services are given increased exposure inside the US domestic market. Northern Telecom and Dominion Textiles provide classic examples of the commercial benefits of this sort of visibility improvement, and there is no reason to believe that smaller Canadian companies will fail to capture similar benefits. Finally, the Canadian FDI thrust in Western New York (or, for that matter, anywhere else) implies a profit repatriation stream that may ultimately strengthen the competitive posture of parent companies in Canada, many of whom continue to act as the nerve centers of new product development, service innovation, and strategic corporate control. In short, it would be incorrect to condemn all Canadian FDI in Western New York as a loss to the Canadian economy. A more realistic view is that the investment relationship involves reciprocal flows between the two parties, rather like the international benefit streams envisaged by normative trade theory.

SUMMARY AND CONCLUSIONS

Recent Canadian FDI in Western New York has not been driven by the trade and investment provisions of the Canada-United States Free Trade Agreement. Rather, Canadian companies have been attracted by a combination of competitive factor costs, locational advantage (proximity to US regional markets), and accessibility to parent corporations in central Canada. 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. Canadian investment has also brought an element of structural diversification to the Western New York economy, as well as new jobs, exports, tax dollars, and R&D spending. 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, there is scant evidence that manufacturing is in imminent danger of sectoral extinction -- at least not in this region. On a more cautious note, the empirical results are significantly weakened by our inability to estimate the level of non-response bias that surrounds our conclusions. In addition, we are unable to document the true scale of Canadian FDI in this region, not least because public agencies in both countries have neglected to compile basic statistics.

Despite these caveats, the results suggest a number of useful directions for future empirical work, each of which offers a starting point for policy-oriented research. First, Canadian companies that have been attracted to Western New York are unlikely to exhibit the same strategic characteristics as those that have favored the Sunbelt, Mexico's maquiladoras, or other distant locations. Short-distance FDI, of the sort described in this paper, appears to represent a

foothold strategy in which small and medium-sized firms are particularly prominent. Does this hold true for other Canada-US border regions? Second, the structure of cross-border linkages between parent companies and their subsidiaries needs to be examined in detail. These linkages are likely to provide important insights into the nature of Canadian corporate thinking across different sectors, industries, and size-classes of firms. Finally, the long-run business performance of Canadian firms would be worth monitoring. Are these companies outperforming their US counterparts? What are the firm-specific advantages that allow Canadian FDI to take place successfully? While the present paper has merely scratched the surface of these issues, further scratching will undoubtedly require substantial empirical effort.

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