

# Foreign Investment Initiatives in the GTA

By: Dan Kershaw and Paul Parker

Foreign Direct Investment (FDI) is a critical element in the economic health of our communities, our province and ultimately, our nation. Many Canadians are unaware of the importance that FDI plays in our economy. With four out of every ten manufacturing jobs and over half of all manufacturing production coming from foreign firms it is no surprise that Canada has been referred to as "the largest branch plant economy in the world" (Dickens 1992). Look at the industrial directory of any community, and the ownership linkages of these firms demonstrate that global contacts are not far away. As other countries become acutely aware of the forces of globalization for the first time, Canada has a history of high levels of interaction (investment, trade and migration) with other countries. The relationship between foreign capital and local communities continues to be of great importance. The uncertainties of the 1990s create the need to review and learn from our previous experience to better prepare for the future.

The attraction of direct investment is a traditional part of the role of Economic Development Professionals (EDPs) in the community. Whether this investment is from elsewhere in Canada, or FDI from a new Korean firm, the attraction of new investment is considered to be one of the more satisfying accomplishments of EDPs. However, the process of attracting this new investment is an uncertain and sometimes frustrating undertaking. The question is raised: Can EDPs influence investment decisions, or are final site selection factors beyond the control of the community? In the past, most researchers concluded that location decisions of new FDI were beyond the influence of the community. This paper questions that conclusion.

## Investment models

There has been extensive research into

the operation of TNCs, but no single theory or model has been able to consistently identify the set of characteristics that explain final investment locations. Academics such as Vernon (1966); Dunning (1977); and Rugman (1990) have each proposed TNC investment theories that provide reasons for investing beyond the home country. In essence, these theories present sound arguments for why a firm will invest in another country, but they have been unable to identify how an investor makes the final location decision.

These traditional TNC investment theories were extended by Edgington (1988) who argued that the location behaviour of TNCs tends to be reflected by the nature of each home country from which investment comes and the conditions found in the host country. The conditions of interest in the host country go beyond the factor costs normally associated with investment decisions. While factor costs will always be of central importance, the role of past experiences, and the local "investment culture" will also affect the final investment decision. The investment culture includes the attitudes of local business, local government and community groups. It reflects the level of confidence in future profitability and the strength of support networks, including local EDPs. In this way, the experience of an initial investor can affect the decisions of subsequent investors. A host country or community that is able to show a consistently favourable investment climate will likely be selected over other areas with similar costs, but greater uncertainty or risk.

When investors contact a local community, they typically have already narrowed the location site down to a market region, (Gerking and Morgan 1991; Woodward and Glickman 1991). It is here that studies in the US have shown EDPs to be able to influence final investment decisions through their individual efforts, (Fox and Murray 1991; Doeringer and Terkla 1992). Al-



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though EDPs in Ontario are unable to offer the substantial financial incentives that US Economic Development Corporations are able to, this does not preclude EDPs in Ontario from being effective in influencing final location decisions.

This paper presents some of the findings from a Local Economic Development research project underway at the University of Waterloo. The project is investigating the policies and program initiatives adopted by EDPs in the Greater Toronto Area (GTA) to promote foreign investment in their community. A combination of questionnaires and interviews with EDPs were used. The 13 largest GTA communities were selected for the study and 12 of them completed and returned the survey. In addition, 10 of the EDPs agreed to participate in interviews for additional information. The initial results are presented below.

## Investment in the GTA

The Greater Toronto Area is the single most important market in Canada containing the most populous urban area in Canada with an estimated 3.65 million residents; and a total 1990 income of \$79 billion (17% of Canada's total income). In terms of employment, the GTA's share of national employment approaches one in four jobs overall and one in five jobs in manufacturing (Gertler 1991). The concentration of FDI was even greater. For example, Japanese foreign investment was concentrated in Ontario with the province receiving 56% of all investments in Canada (Rugman 1990). Within Ontario, the concentration was even higher with 80% of Japanese investment projects in Ontario being located within the GTA. This list of investments was compiled from several data sets and is thus more inclusive than those frequently used (JETRO 1993; Ontario House 1992; Investment Canada 1993).

While the recession of the early 1990s has reduced employment in the Ontario economy, the GTA will nonetheless remain the location of a large share of any new foreign investment, by nature of its relative market size and prerequisite characteristics for economic growth (TREB 1993). It possesses a large and diversified collection of economic activities, a strong base of private and public services, highly-developed infrastructure, an excellent educational system, and a large, high-quality labour pool.

During the 1980s foreign investment into Canada, and in particular into the GTA, exceeded all earlier decades (Gertler 1991). The suburbs of Toronto grew rapidly in the 1980s as their share of GTA industrial space rose from 29 percent in 1980 to 75 percent in 1990 (TREB 1990). However, this rapid expansion was not uniform. Some areas attracted far more investment than others. One factor contributing to uneven investment could be the "investment culture" of communities and the associated activities of EDPs.

## Foreign Investment and Community Priorities

Twelve of the largest Toronto municipalities participated in the study (Brampton, East York, Etobicoke, Markham, Mississauga, North York, Oakville, Pickering, Scarborough, Toronto, Vaughan and York). These communities were divided into groups, based on their rating of

the importance placed on attracting foreign investment. Group 1 comprised the three municipalities which placed only low importance on attracting foreign investment. They tended to be reactive in undertaking this task, and simply provided local information when requested and directed enquiries to related provincial and federal programs. Group 2 municipalities placed average importance on attracting new foreign investment, and the three municipalities were considered to be passive in the promotion of foreign investment, overall. In contrast, Group 3 consisted of six members who were proactive in the attraction of new foreign investment to their respective communities. Note that these groupings were not based on the actual incidence of FDI in each community, but rather on the importance that each community placed on this activity.

Group 1 municipalities place a low priority on recruiting foreign investment. In part, they also reflect a general shift in emphasis among many EDPs from the attraction of investment from outside of the community to the retention, support and development of local business. In response to a question which asked the importance of selected economic development activities as measured on a 5 point scale (1 = low importance, 5 = high importance), they placed their greatest importance on business retention and other local activities (Figure 1). National and regional marketing, along with small business and entrepreneurship development, were given a secondary importance. The least important activities were international in nature - trade, marketing and investment. In the interviews and survey responses it was clear that while they would not neglect international opportunities, the limited resources of the office were focused on local activities which were considered more profitable for their individual communities in the long run.

These communities, have received foreign investment in the last decade, but have not directed their offices to focus on this aspect of economic development. Specific policies aimed at foreign investors were limited. New investors are generally directed to federal and provincial agencies for details regarding support programs. However, some effort is made to suggest appropriate potential sites and streamline necessary municipal approvals. Efforts to tailor policies to the needs of individual

investors come only after they have located in the community, in which case seminars regarding export and trade opportunities are provided on occasion.

Group 2 municipalities placed more emphasis on international activities than Group 1 municipalities, but considered the process of attracting foreign investment to be of average importance (Figure 1). Instead, these communities emphasised trade expansion and worked with both foreign and domestic firms to improve their business through trade initiatives and the provision of information services. Business retention was a high priority, as among Group 1 municipalities, while small business and entrepreneurship development were also considered to be very important.

Average importance was placed on foreign investment by Group 2 municipalities, but there were few defined investment policies for dealing with foreign investors. The only specific effort reported by this group which was aimed at international investors was the joint GTA marketing committee formed in 1993 to promote a collective GTA presence at national and international trade shows. With regard to tailoring investment policies to individual investors, some translation of marketing materials, and periodic contact with investors was reported. While specific programs were not identified, there was a general awareness that different investors have different needs and in many cases are treated individually. *note: (1 = low importance, 5 = high importance.)*

The six municipalities which formed Group 3 placed a very high importance on attracting foreign investment, and their efforts and knowledge were actively directed toward achieving this goal. Other economic development tasks were also assigned above average importance, but the highest overall ranking was given to foreign investment (Figure 1). These proactive municipalities have adopted some innovative approaches to promote foreign investment. Information was more readily available and more widely distributed to potential investors. Marketing tools were often translated into major languages, and provided to local realtors who often have the first contact with investors. Many of these communities have focused their marketing efforts on particular nationalities or types of investor, (e.g., Mississauga-Japan, Vaughan-Japan & Italy, Oakville-USA). For example, one municipality explained the success they had in attracting Japanese firms

over the years, and in maintaining excellent relations with existing investors through focused brochures, marketing campaigns, annual dinners, opportunities for

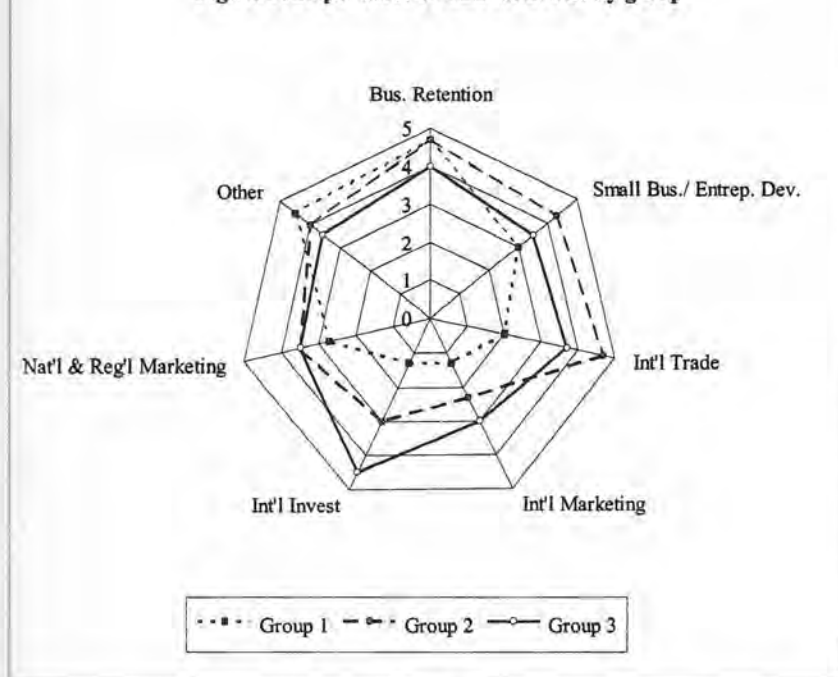
lack of political support and uncertain returns on this type of expenditure have forced their communities to reduce the marketing budget. In the surveys and

from expanding their efforts, the high cost of international marketing also prevents penetration into all markets of interest. It was generally considered better to specialise in particular target sectors or countries than to attempt general coverage. There was a positive attitude in the interviews, that expressed the EDPs' general belief that with sufficient budgets, international marketing could be effective. In the case of Group 3, many communities were satisfied with their budgets, and felt their success rate with this expenditure was acceptable. Most of these international marketing efforts were focused on specific countries like the US, Japan, Hong Kong or Italy. The result is the active promotion of a local "investment culture" which builds on the distinctive features of the community. The presence of a distinctive cultural group (residential or industrial) is often used as a valuable community resource to demonstrate a comparative advantage in constructing an "investment culture" which supports further investment by new members of that group. Important social networks and infrastructure are often in place and can be used as positive features to further strengthen the local economy.

One example of foreign investment which grew rapidly in the 1980s was Japanese FDI. Although total investments in Canada were small compared to Japanese investments in the US, East Asia, Europe or Australia, the investment of an estimated \$4 billion created many new industrial spaces in Canada. Investments in automotive transplants are probably the most publicised, but nearly 200 other investments were made in Ontario by Japanese firms during that period. How does the distribution of this Japanese investment compare to the initiatives identified by EDPs?

Within the GTA, three communities identified special efforts to attract Japanese investment while another three communities expressed their desire to eventually focus on Japan as a marketing target. A comparison can be made between the actual Japanese investment pattern and the communities which were most strongly pursuing foreign investment in general and those which specifically targeted Japan as a source of investment funds.

Figure 1: Importance of LED activities by group



direct business contact with the mayor and an emphasis on an open door policy to deal promptly with issues as they arose. Efforts were made to streamline the investment process at the community level in order to minimize difficulties for the investor.

### Marketing Budgets

The stated importance of international investment can be measured indirectly by the foreign marketing budgets allocated by each office, as a percentage of the total marketing budget. A clear and consistent difference is found among the three groups of municipalities. The heavy emphasis on international marketing by Group 3 is contrasted with small allocations in Group 2 municipalities and no international marketing reported by Group 1 municipalities (Table 1). Overall, marketing efforts are predominately aimed at domestic media, but the percentage of budget directed to international markets varies widely. In Group 2 the average international marketing budget was six percent of the total marketing budget. When questioned as to whether or not the budget was sufficient, EDPs responded that

interviews they highlighted their involvement in the GTA marketing initiative, as a means to market themselves better.

Table 1: Foreign marketing budgets market/group reactive passive proactive

	(% of total marketing budget)		
	reactive	passive	proactive
US	0	1	11
Europe	0	1	3
Japan	0	1	8
Other Asia	0	4	6
Other	0	0	4
Total	0	6	32

note: addition error due to rounding

Group 3 communities devoted much larger shares of their marketing budget to the international marketplace. In one case, the entire marketing budget was directed internationally. The other five communities in this group allocated 32 percent of their marketing budget to international marketing, on average. When asked how sufficient this budget was, most communities responded that while political constraints have frequently prevented them

### Constraints to Future Investment

The final topic of the questionnaires and interviews was the impact that a



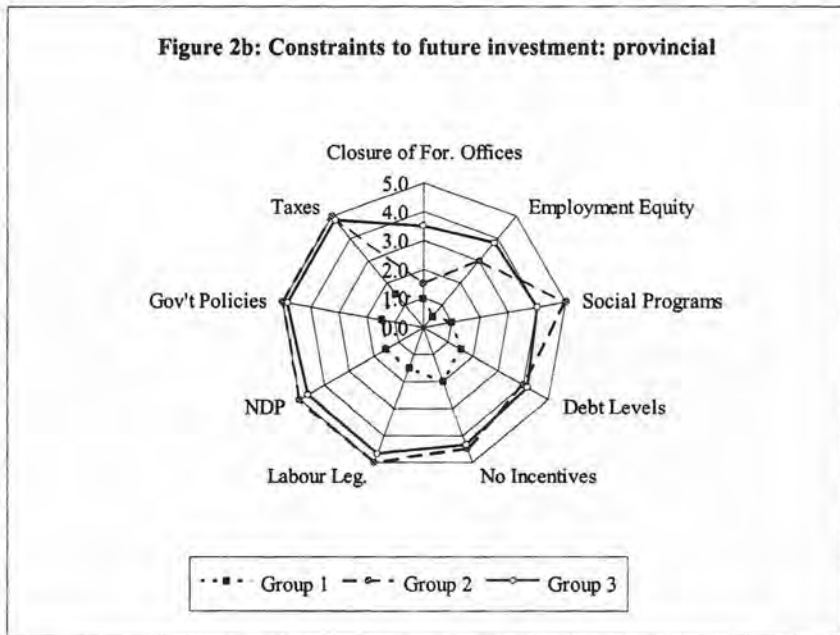
number of national, provincial and local factors have on their attractiveness as an investment location. EDPs were requested to list national, provincial and local factors which either promote or impede investment from abroad. The list was generated in the first survey, and then evaluated in terms of importance during the interviews. EDPs rated the promotions or impediments in terms of their impact on promoting or preventing further investment from abroad.

EDPs identified a series of constraints at the national, provincial and local levels to future investment. At the federal level, taxes and government policies were considered the biggest impediments with other factors like the debt, trade barriers and GST being of average importance (Figure 2a). The concern about these national impediments was greatest among the proactive municipalities and lowest among the reactive municipalities. This pattern matches the importance they place on attracting foreign investment. In other words, EDPs who are less concerned about foreign investment, are also less concerned about national impediments to that investment. The reactive group was also less concerned about provincial impediments to investment than the other two groups. Both passive and proactive groups reported a high level of concern about provincial taxes, policies, labour legislation, social programs, debt levels and the lack of incentives for investment

### Factors Promoting Investments

The impediments to investment are offset, at least in part, by factors which promote investment. At the national level, factors like export opportunities, the Canada-US Free Trade Agreement and research and development incentives were considered to be very important by both the proactive and passive groups of EDPs. The reactive group again placed less importance on these factors and remained consistent with their earlier views on investment impediments. Natural resources were identified as a promotional factor, but were considered to be less important than other factors (Figure 3a).

At the provincial level, the proactive municipalities considered the quality of labour, quality of life, health care and business technology to be very important promotional factors. The passive group con-



sidered the same factors to be important, but not to the same extent. Predictably, the reactive group placed little importance on these factors, with the exception of quality of life. Provincial investment services were identified as a positive factor, but not valued as highly as other factors (Figure 3b).

At the local level, there was greater agreement on promotional factors. All three groups agreed that public infrastructure and location were important factors. The proactive and passive groups placed similar high importance on the availability of

industrial and commercial land, the local labour force, retail space and FDI awareness. The passive group also valued the municipal ombudsman highly, while the proactive group placed higher importance on educational excellence than the other two groups. Overall, EDPs in all communities identified local factors which strongly promoted investment while opinions were more clearly divided on provincial and federal factors (Figure 3c).

Figure 3a: Factors promoting investment: national

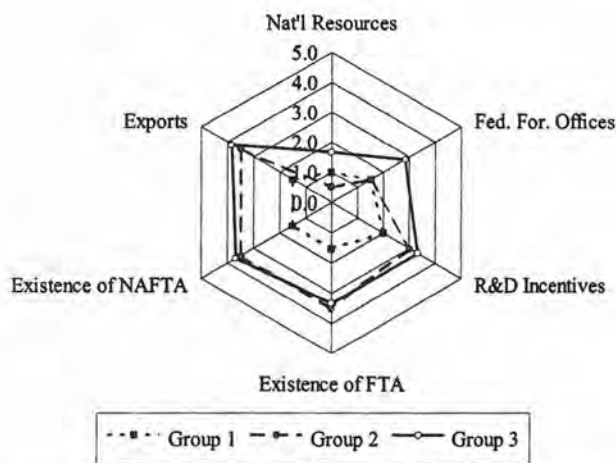
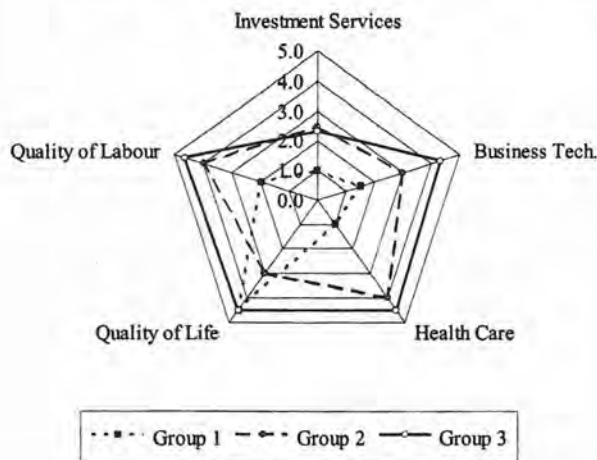


Figure 3b: Factors promoting investment: provincial



## Distribution of Japanese Investment

Having identified the differences in policy priorities and initiatives, it is necessary to compare this pattern to the distribution of actual investment. Japanese investment is shown in Figure 4. The three groups of municipalities are shown along with the average number of Japanese investments per municipality. The data are presented on a sectoral basis and in each case, the proactive group of municipalities (group 3) gained more investments than the passive municipalities (group 2) which in turn received more investments than the

reactive municipalities (group 1). This pattern supports the proposition that initiatives and policies designed to attract investment are effective.

However, many of the initiatives described above were introduced in the late 1980s or early 1990s after many investments had already been made. Figure 5 presents the pattern of investment in the three groups of municipalities over time. Once again, the investment pattern is consistent with more investment being located in group 3 municipalities. This pattern was consistent for all time periods. The implication is that Japanese investment continued to locate where previous investors had concentrated. The policy initiatives of the

late 1980s or early 1990s do not appear to have caused a change in aggregate behaviour, but they may have been important to maintain the reputational value or "investment culture" of the community.

## Discussion

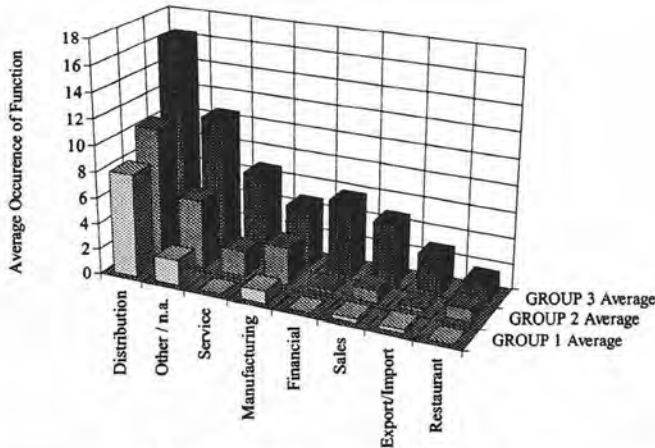
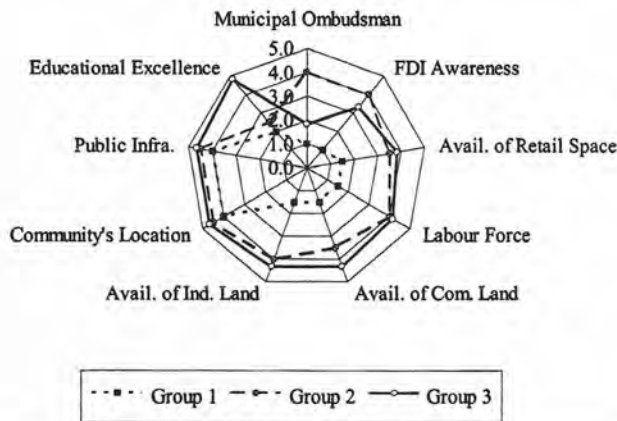
Many EDPs are preparing for the 1990s by identifying a niche for their community. The cost of maintaining a comprehensive marketing campaign is too high for most municipalities, so efforts are targeted to maximise the benefits from a known specialisation and supportive "investment culture". Many municipalities have decided to specialise by focusing on particular national groups (US, Japan or Hong Kong) while others concentrate on target sectors (e.g., information technology or automotive parts). The general strategy is to identify and then support local strengths. In this way, EDPs are able to position their communities to attract the new investors of the 1990s.

Part of the explanation for the low priority attached to foreign investment by some EDPs is the recession of the early 1990s with disinvestment being more common than investment in most communities. Firms restructure to remain competitive in the global economy and most restructuring occurs on-site, so there are fewer new investment location decisions than during the boom of the 1980s. Reduced municipal budgets also create pressure to reduce expenditure and marketing budgets are often trimmed.

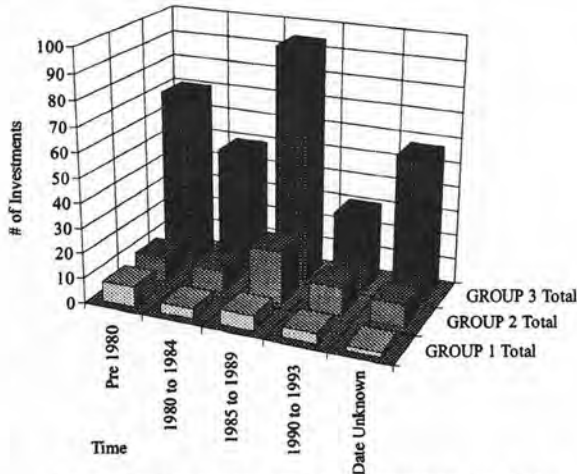
The challenge is to find the balance appropriate for each community. There is no benefit from spending scarce municipal funds to chase firms which are unlikely to choose your community. Equally, the community will suffer opportunity costs if potential investors choose to locate elsewhere simply because information was not provided to make them aware of the advantages of the community.

While the future is uncertain, and specific investment trends are hard to identify in advance, it is certain that opportunities will arise for those who are ready. For example, the devaluation of the Canadian dollar in 1992 and the appreciation of the yen in 1993 has shifted factors like labour unit costs in Canada's favour. More manufacturing by Japanese firms is likely to be transferred overseas in the 1990s. Once again, the distribution of this investment will be uneven. Some communities will benefit by having a supportive "investment culture" in place, while others watch.

**Figure 3c: Factors promoting investment: local**



**Figure 4: Investment per municipality**



**Figure 5: Japanese direct investment in the GTA**

## Conclusion

This paper contributes to the debate over the effectiveness of EDPs in attracting foreign investment by reporting on the experience of EDPs in Canada's largest market, the GTA. Foreign investment accelerated in the 1980s, but was unevenly distributed throughout the GTA. One factor which could influence this distribution is the local "investment culture" generated in each municipality. Virtually all EDPs agreed that business retention is very important. However, the importance placed on foreign investment varied widely and three groups of respondents were identified: reactive, passive and proactive. The reactive group placed a low priority on foreign investment and allocated no funds to marketing in this area. The passive group considered foreign investment to be of average importance. Although they allocated some funds to this activity, they placed greater emphasis on business retention and entrepreneurship development. In contrast, the proactive group rated foreign investment as being very important and typically allocated one-third of their marketing budget to international media. The proactive group also had the greatest range of policy and program activities designed to support foreign investment.

## Acknowledgement

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