

Action

entrepreneurship
GROWING YOUNG ENTERPRISE
FAIRE GRANDIR LA JEUNE ENTREPRISE



Action Entrepreneurship: Growing Young Enterprise

Roundtable Backgrounder 2015

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INTRODUCTION

Futurpreneur Canada launched Action Entrepreneurship in 2014 to bring attention to the key challenges inhibiting youth entrepreneurship. We engaged over 1,000 of Canada's best and brightest young entrepreneursⁱ, and stakeholders that support them, in interviews, roundtable discussions, a national survey and a national summit. The initiative culminated in September with "*Unlocking the Power of Youth Entrepreneurship: An Action Plan for Canada*". The Action Plan identified over 80 actions that key stakeholders, including Futurpreneur Canada and young entrepreneurs, can take to help expand youth entrepreneurship. One of the highest priority recommendations for Futurpreneur Canada was to continue Action Entrepreneurship.

Action Entrepreneurship 2015 will focus on growth, which was a hot topic last year because it is challenging yet critical to Canada's future. Much has been written about challenges **all entrepreneurs** face in attempting to grow, as well as the numerous actions proposed to help them. Our focus will be on the growth challenges and opportunities that are particularly important for **young entrepreneurs**.

Action Entrepreneurship 2015 will begin in late January with twelve roundtables across Canada followed by a national summit in May. This backgrounder is intended to be a discussion starter for the roundtables. We ask you to read it in advance, think about the questions posed, and come prepared to participate actively in the conversation.

BUSINESS GROWTH IS IMPORTANT

Domestic growth creates jobs that are essential to sustain healthy local and provincial economies. Export growth is even more critical. Canada is a trade-dependent economy in an increasingly global world. Growth in exports is essential to improving Canada's economic performance and sustaining our standard of living. Exporting is also important to the health of businesses. Businesses that export grow faster, are more productive and profitable, and stay in business longer.¹

Small and Medium-sized Enterprises (SMEs)ⁱⁱ contribute significantly to Canada's economy accounting for almost 90% of employment, 39% of private-sector GDP, and 34% of exports.² High-growth entrepreneurship contributes more than all other businesses to innovation and job creation but very

'Business growth' is a complex concept. It refers to growth in sales, profits, assets or numbers of employees. It occurs in local markets or through expansion within a province, into other provinces or into other countries. Expansion takes different forms such as introducing new products or services, franchising, exporting, and foreign direct investment. Different types of businesses have inherently different growth potential and paths to achieving it.

ⁱ Youth or young entrepreneurship refers to the 18-39 year old age group.

ⁱⁱ Industry Canada defines SMEs according to number of employees, with small businesses having less than 100 employees and medium-size businesses having 100-499 employees.

few SMEs would be classified as high growth firms.^{iii,3} Reducing the barriers that inhibit entrepreneurs from growing their businesses is critical for Canada to realize the economic and social benefits of business growth.

TOO FEW ENTREPRENEURS GROW SIGNIFICANTLY OR TRADE

Canadian entrepreneurship is relatively healthy. The birth rate of new enterprises is high, and about half survive their first five years. But Canada generates a lower proportion of fast-growing companies than other developed countries, and relatively few small businesses sell outside their local markets or export internationally.^{4,5} The few SMEs that do export have been critical to Canada's export performance. They have grown their exports over the past decade while large businesses' exports declined and Canada's overall exports remained flat.⁶ Appendix I contains a compilation of data on SME growth and trading activity from Industry Canada research.⁷ Some highlights include:

- Between 2009 and 2011, 62% of SMEs grew their sales revenues but only 8% were high-growth entrepreneurs.
- 76% aspired to grow over the next three years (2012-2014) with the majority aspiring to moderate growth. Only 8% aspired to high growth.
- In 2011, 44% of SMEs sold outside their local market but within the same province. Only 18% were 'domestic traders' that sold goods or services in other provinces and 10% were exporters.
- SMEs that traded domestically were larger, more innovative and more export-oriented - with 41% selling abroad compared with 3.5% that only sold in their home province. They were also higher growth and had higher future growth aspirations.
- Finally, domestic traders and exporters tended to be older and more highly educated with more management experience than SME owners that focused on their local markets.

The data indicates that SMEs that grow do so in stages, beginning in their local markets. With time and experience some expand domestically and internationally. There are exceptions to starting locally, particularly in high-tech sectors where some say that being 'born global' is essential given the small size of the Canadian market and the global nature of competition. But, regardless of sector, accelerating growth is critical for our economy and a supportive domestic environment is essential to help more SMEs develop and grow domestically and internationally.

"SMEs are key to improving Canada's trade performance because they have been more successful at growing exports in emerging markets, and because a majority of them do not currently export meaning that even small increases in trade activity can have a significant economic impact."

J.M. Laurin, Octane Strategies

ⁱⁱⁱ Statistics Canada defines 'high-growth' firms as growing in excess of 20% per year for at least three years. Growth between 11% and 20% per year is classified as 'significant' and growth between 1% and 10% per year is 'moderate'.

CHALLENGES TO GROWING BUSINESSES

Challenges to growth vary by stage of business development. TD Economics recently analyzed the challenges using a five-stage growth framework from Harvard Business Review: existence, survival, success, take-off, and resource maturity.^{8,9} Briefly, the challenges for the first four growth stages follow:

1. **Existence** – The business has to prove its economic value to attract the resources it needs to grow. Obstacles at this stage for young entrepreneurs who participated in our national survey last year were: fear of the unknown; lack of knowledge, skills and experience; lack of government support; and difficulty finding funding.¹⁰ Members of the Canadian Federation of Independent Business (CFIB) also view government taxes, regulation and paper burden as major challenges. These challenges exist at all growth stages but are particularly onerous for start-ups. Almost one-third of CFIB members wouldn't have started their businesses had they known the extent of the burden of regulation.¹¹
2. **Survival** – Financing and cash flow management become the biggest challenges as the business strives to achieve sufficient size and profitability to survive. This critical stage is often called the 'Valley of Death' because 70% of start-ups survive more than two years and only 51% survive for more than five years.¹²
3. **Success** – The business is now profitable and cash flow-positive. Challenges shift to leadership and human resources as the owner must attract good quality, talented employees, retain them, and learn to delegate responsibility. This stage could go on indefinitely in a stable market and competitive environment. Most Canadian SMEs remain at this stage while only a very small percent of firms sustain high growth after five years.¹³
4. **Take-off** – The biggest challenge at this stage is financing rapid growth. This is particularly challenging in Canada, where early-stage growth funding is hard to obtain. Traditional financial institutions perceive younger businesses as higher risk. The venture capital industry is underdeveloped and has been retrenching to focus on high-tech companies that are later-stage and lower risk. The angel investor pool is small, also tends to focus on high-tech, and can be difficult access.¹⁴

In summary, the key growth challenges are: fear of the unknown; accessing financing and financial management; government taxes, regulation and paper burden; lack of knowledge skills and experience; and human resource attraction, retention and management. These challenges become amplified and new challenges arise for businesses that strive to be high-growth **and** export to new markets, as evidenced in Exhibit I, a Conference Board compilation of third party surveys done by CFIB and others. Interestingly, many sources report that inter-provincial trade barriers make it even harder to do business in other provinces than to export.

Exhibit 1: The Most Critical Challenges Facing Canadian SMEs in Exporting Internationally

1. Identifying good market opportunities
2. Finding reliable business partners
3. Managing supply-chain relationships and demands of complying with quality control and systems requirements
4. Getting access to financing
5. Handling authentication and security
6. Protecting intellectual assets and business information
7. Overcoming trade and regulatory barriers

Source: Conference board of Canada's summary and analysis of SME surveys done by CFIB, UPS, and others (2008) drawn from CGA's *Issue Brief on Canada's Global Trade Agenda: Opportunities for SME's* by J.M. Laurin (2013)

An additional challenge, Canadians' high aversion to risk, doesn't show up frequently in quantitative surveys on growth challenges but does get raised in reports on entrepreneurialism from qualitative initiatives such as the Canadian Chamber of Commerce's recent roundtables.¹⁵ One possible explanation is that risk aversion is more of an obstacle to starting businesses than growing them. In surveys on entrepreneurial intent by BDC, CFIB, and others, fear of debt and fear of failure are often cited as reasons for not starting businesses. Both factors relate to risk aversion. Happily, young entrepreneurs reported relatively high entrepreneurial intent in Global Entrepreneurship Monitor's (GEM) recent research which may indicate lower risk aversion.¹⁶ We look forward to exploring this challenge in our roundtable discussions.

ROUNDTABLE DISCUSSIONS WITH YOUNG ENTREPRENEURS

Much of the research on obstacles to business growth deals with all entrepreneurs and not **young entrepreneurs** specifically. While young entrepreneurs tend to have newer and smaller firms than older entrepreneurs, there are some encouraging signs with respect to their growth prospects. For instance, the 2013 Global Entrepreneurship Monitor (GEM) reported positive attitudes and aspirations towards entrepreneurship in Canada, with peak entrepreneurial activity among 25-34 year olds. Recent work by TD Economics indicated that young entrepreneurs typically record higher growth rates and higher concentration in knowledge-based industries.

The purpose of the roundtable discussions is to explore the challenges that **young entrepreneurs** face after the start-up stage in growing their businesses and to identify opportunities to help them overcome those challenges. The following questions will be considered at the roundtables:

- Why is it important for **young entrepreneurs** to aspire to grow their businesses?
- What are the biggest challenges that **young entrepreneurs** face in pursuing business growth opportunities in their local markets, other provinces and internationally?
- What needs to change to make it easier for **young entrepreneurs** to grow their businesses successfully in their local markets, other provinces and internationally?

APPENDIX I: COMPILATION OF GROWTH-RELATED DATA

SOURCE: Industry Canada (2011 unless otherwise specified)

I-A: Per Cent of All SMEs Growth Rates per Year: Actual (2009-11) and Future Expectations (2012-14)

Growth Rates	% SMEs Actual	% SMEs Future Expectations
Declining sales	16%	18%
No growth	22%	7%
Between 1% and 10% (Moderate)	44%	56%
Between 11% and 20% (Significant)	11%	12%
Over 20% (High)	8%	8%
Total	100%	100%

I-B: Where SMEs Sell (% of total SMEs) and % of Sales Revenue by Destination

Data	Local Market	Non-local but in Home Province	Other Province(s)	Export
% of Total SMEs	94%	44%	18%	10%
% of SME Sales	79%	14%	4%	4%

I-C: Past 3 Years Sales Growth (Expected Growth Next 3 Years) by Domestic Trader^{iv} Status

DATA	In Home Province	Domestic Trader	Domestic Trader; Non-Exporter	Domestic Trader; Exporter
Declining sales	15% (7%)	18% (6%)	18% (6%)	19% (5%)
No growth	23% (18%)	18% (15%)	19% (15%)	16% (14%)
Between 1% and 10%	44% (56%)	45% (58%)	45% (60%)	44% (54%)
Between 11% and 20%	10% (12%)	11% (12%)	10% (11%)	11% (14%)
Over 20%	8% (7%)	8% (10%)	8% (8%)	10% (13%)

I-D: Growth Attitudes of New (SMEs) vs. Established Businesses for Exporters vs. Non-Exporters (2007)

% With Growth Intentions	New Businesses	Established Businesses	All Businesses
% Non-Exporters	55%	33%	38%
% Exporters	73%	65%	67%

^{iv} Domestic Traders sell to other provinces and possibly export. Columns add to 100%. Bold values indicate significant differences versus In Home Province

I-E: International Business Activity by the 10% of SMEs That Export

Export Location	% of SME Exporters
US	89%
Europe	32%
Latin America	12%
China	10%
Other Asia	12%

Type of Exports	% of SME Exporters
Goods only	49%
Services only	40%
Both	12%

I-F: Owner Characteristics by Domestic Trader Status

DATA	In Home Province	Domestic Trader	Domestic Trader; Non-Exporter	Domestic Trader; Exporter
Less than 40 years of age	13%	9%	9%	10%
More than high school	65%	75%	71%	78%
10 years+ in management	76%	83%	82%	85%

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