

Does the speed of change blur or sharpen your focus?

How Canada's middle-market
businesses are building solid growth
on local foundations



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Introduction

Canada's middle market is targeting solid growth built on the domestic economy, as tensions in the trading relationship with the US begin to increase. Canadian business leaders are focused on the upside of disruptions caused by industry convergence fueled by new technologies. While sufficient working capital and finding talent with the right skills remain challenges, the middle market is looking to artificial intelligence (AI) to deliver an improved customer experience and process efficiency.

Survey methodology

EY commissioned Euromoney Institutional Investor Thought Leadership to undertake an online survey of 2,766 C-suite (60% CEOs, founders or managing directors) in companies from 21 countries and with annual revenues of US\$1m-US\$3b. The survey was conducted from 15 January-1 March 2018. EY further invited the network of EY Entrepreneur Of The Year™ alumni from across the globe to take the survey. The survey was available in English and six other languages. Further in-depth interviews were carried out during March-April 2018 to provide additional specific insights.

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Chapter 01

Strategies for growth

The Canadian C-suite is putting customer experience, talent and tech at the heart of its growth agenda, as the global economy continues to strengthen.

This three-pronged strategy underpins uniformly robust revenue forecasts from the country's executives. Two-thirds (67%) expect annual growth of 6%-10%, significantly above the International Monetary Fund's April 2018 projection of 2.1%.¹

Canadian business leaders are, however, more measured in their predictions than their international peers, according to the 2018 EY Growth Barometer global survey. Only 1 in 10 Canadian respondents anticipates growth of more than 10%, far below the rest of the world, while almost one-quarter are looking at less than 5%.

Expanding within national borders

The middle market's forecasts rely primarily on expansion within national borders, despite foreign trade currently making up 64% of Canada's GDP.² Almost one-quarter (24%) see entry into a new home market as the main strategic priority, with just 11% choosing entry into a new overseas market.

Likewise, a new overseas opportunity is the most important factor when evaluating a new business initiative for just 7% of middle-market respondents, compared with 21% in the rest of the world.

This domestic focus may reflect the July 2017 enactment of the Canadian Free Trade Agreement, which reduces barriers to trade, investment and worker mobility across the country's 10 provinces and three territories.

"Digitization is proving particularly disruptive in consumer-focused industries such as technology, retail, financial services and consumer products. They are facing immense disruption as they are closely linked to consumer behavior which is changing significantly."

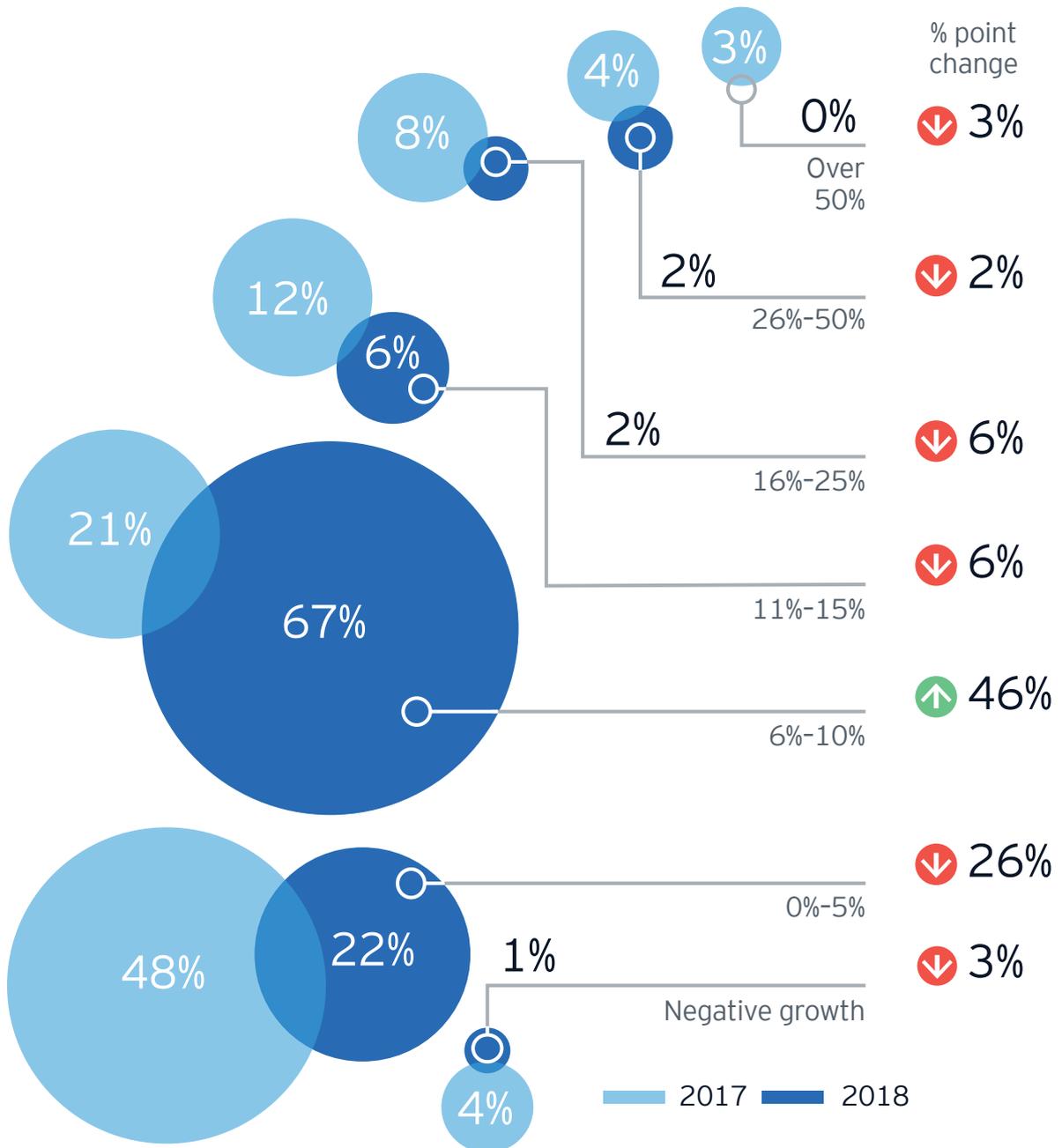
François Tellier
Canada Growth Markets Leader, EY

¹ "World economic outlook, real GDP growth," *International Monetary Fund*, http://www.imf.org/external/datamapper/NGDP_RPCH@WEO/OEMDC/ADVEC/WEOORLD/CAN, accessed 23 April 2018.

² "What's next for Canada's economy," *The Economist*, <https://www.economist.com/the-americas/2018/03/01/whats-next-for-canadas-economy>, accessed April 2018.

Revenue growth projections

This chart shows growth expectations for 2017 and 2018, ranging from negative growth to growth above 50%, including year-on-year percentage point changes.





Chapter 02

Challenges to growth

The middle-market's local ambitions could also result from recent strains in Canada's relationship with its largest trading partner, the US. Having withdrawn from the Trans-Pacific Partnership³ (TPP) trade deal, the US has threatened to "tear up" the North American Free Trade Agreement and imposed tariffs on Canadian lumber imports.⁴

Such tensions with its neighbor also help explain why 15% say geopolitical uncertainty is the second greatest external risk to growth, versus 9% elsewhere. Yet, despite protectionist headwinds from the US, only 8% want higher trade barriers to remove overseas competitors, versus 15% in the rest of the world.

The cash flow squeeze

The number one challenge to growth for Canadian respondents, however, is insufficient cash flow, at 21%. Francois Tellier, Canada Growth Markets Leader, EY says, "Cash flow is a real issue for many businesses. It reflects the disruption caused by changing sales cycles, as industry convergence, unpredictable online buying patterns, and the need to invest quickly in response to changing consumer demands are all increasing demand for ready money."

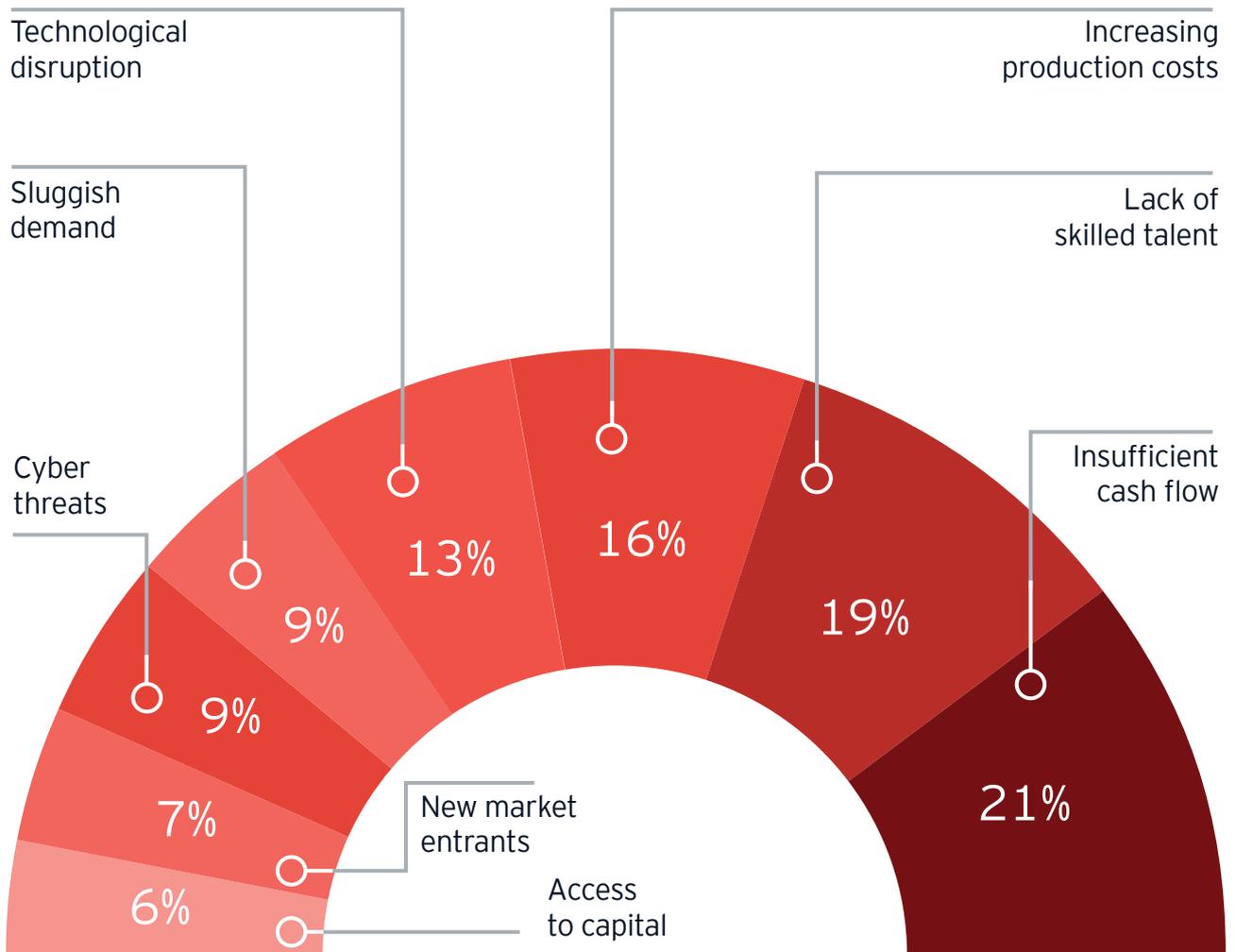
Such concerns may explain why, despite the solid growth forecasts, the Canadian middle market remains cautious about recruitment. Half are looking to keep current staffing levels compared with one-third in the rest of the world. However, 42% do intend to hire more full-time staff, with fewer contractors and no part-time hires.

³ "Comprehensive and progressive agreement for Trans-Pacific partnership (CPTPP)," *Government of Canada*, <https://international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/cptpp-ptppg/index.aspx?lang=eng>, accessed April 2018.

⁴ "Stung by U.S. Tariff Plan, Canada Takes a Deep Breath," *The New York Times*, [nytimes.com/2018/03/02/world/canada/canada-us-tariff.html](https://www.nytimes.com/2018/03/02/world/canada/canada-us-tariff.html), accessed March 2018.

Challenges to growth

This chart outlines the key operational challenges that are restraining growth in the middle market.





Chapter 03

Building stronger teams

Recruitment may be on hold for many but, as is the case throughout the developed world, the small pool of talented labor is a great concern. Skilled talent is considered the top accelerated growth enabler, while its lack is the second greatest challenge to growth.

However, the Canadian C-suite's top recruitment priority is more team players, at 31% (18% in the rest of the world), with people with specialist skills being the must-have for just 12%. This may reflect Canada's high availability of scientists and engineers, which the World Economic Forum rates as the fourth highest in the world.⁵ The country's middle-market businesses may feel they have enough specialist skills for now.

Reflecting the talent squeeze, the middle market sees demographic shifts as the second most disruptive megatrend, at 28%. To correct the skills imbalance, the country's C-suite rates higher investment in education as one of the top three ways for government to boost growth, and Canadians are twice as likely as their peers in the rest of the world to say that widening the skills of current staff is the best way to improve productivity.

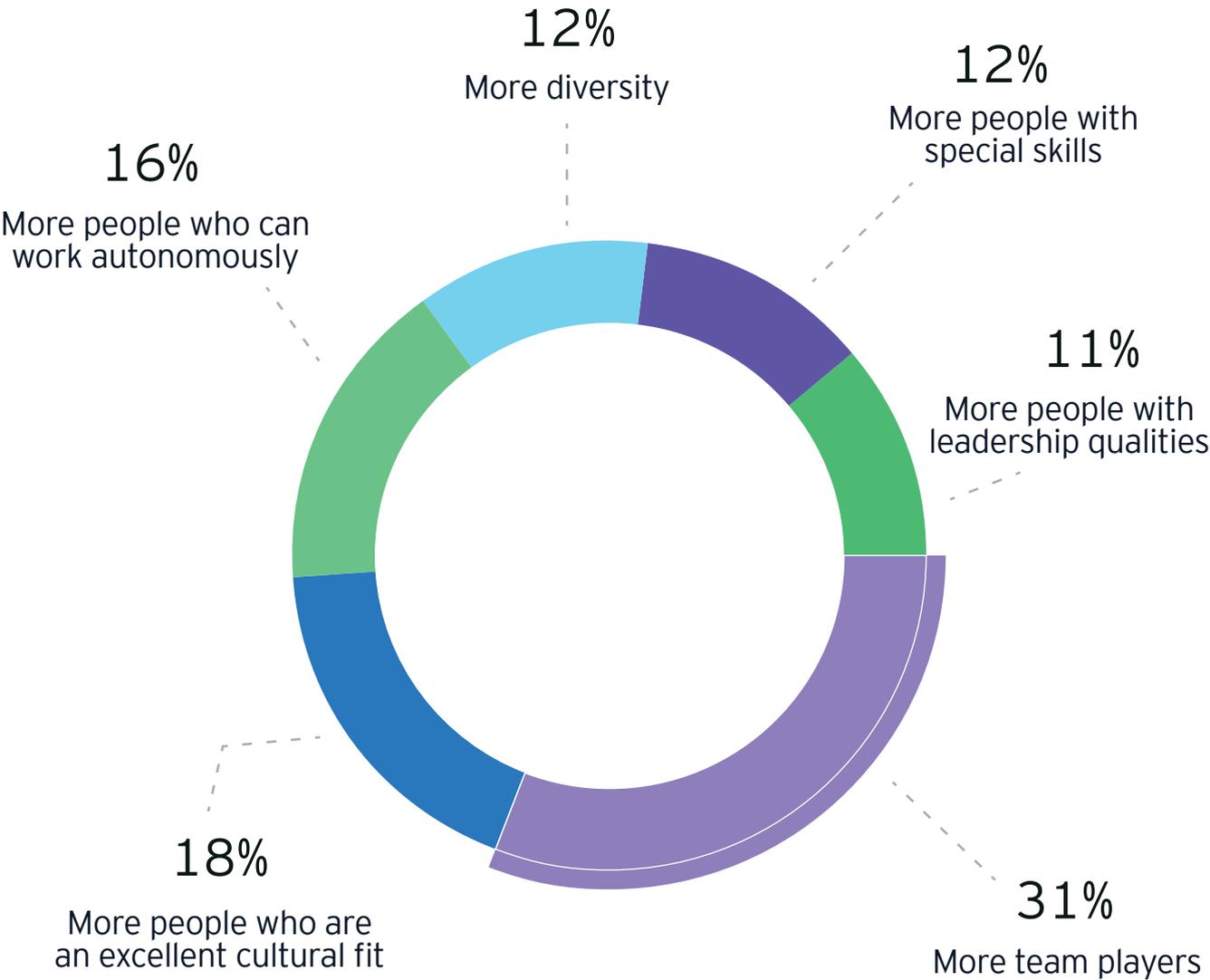
Despite Prime Minister Justin Trudeau's Government's current attempts to boost female participation in the workplace,⁶ the middle market isn't very interested in increasing diversity, in sharp contrast to the rest of the world. Just 12% of the Canadian C-suite considers "more diversity" a strategic priority versus 42% elsewhere.

⁵ "The Global Competitiveness Report 2016-2017," *World Economic Forum*, <https://www.weforum.org/reports/the-global-competitiveness-report-2016-2017-1>, accessed March 2018.

⁶ "What's next for Canada's economy," *The Economist*, <https://www.economist.com/the-americas/2018/03/01/whats-next-for-canadas-economy>, accessed April 2018.

Recruitment and talent needs

This chart illustrates companies' priorities when they are hiring new talent.



Chapter 04

Embracing business change

Canada's C-suite also diverges from their peers elsewhere in the strength of its intention to divest, at 36% versus 19% in the rest of the world. This emphasis comes after another 2018 EY survey found a 300% annual increase in the number of Canadian executives looking to sell, with 41% saying the need to fund new technology investments triggered a recent major divestment.⁷

As further evidence of how technology is calling the tune in business, industry convergence – which has tech as its launch pad – is the most disruptive megatrend for 33% of the Canadian middle market, higher than the rest of the world (23%), with digitization itself being the most impactful for a further 14%. EY's Tellier says: "Digitization is proving particularly disruptive in consumer-focused industries such as technology, retail, financial services and consumer products. They are facing immense disruption as they are closely linked to consumer behavior which is changing significantly," he points out.

Canadian fintech company Overbond is one of the companies causing – and benefiting from – such disruption. CEO Vuk Magdelinic says, "A lot of the disruptive forces that many might see as a threat, such as digitization, globalization, and the cost and availability of capital, are precisely the trends that give us our edge. We are a disruptor and we are leveraging those trends with our technology to show there is a better way of doing things."

The middle market recognizes that technology offers opportunities as well as threats. Technology is seen as the most important factor in improving productivity (27%) and, after skilled talent, as the next-best means to accelerate growth. No Canadian respondents see reducing staff costs as the primary objective of major tech investment.

Made-in-Canada Silicon Valleys

Artificial intelligence (AI) is under a particular spotlight, with 42% planning adoption in the next two years (68%, elsewhere) and 44% more in the coming five. This comes as the federal government is investing more than CAD\$750 million in five high tech "superclusters" of innovative businesses – what it calls "made-in-Canada Silicon Valleys" – including two focused on AI and digital technology.⁸

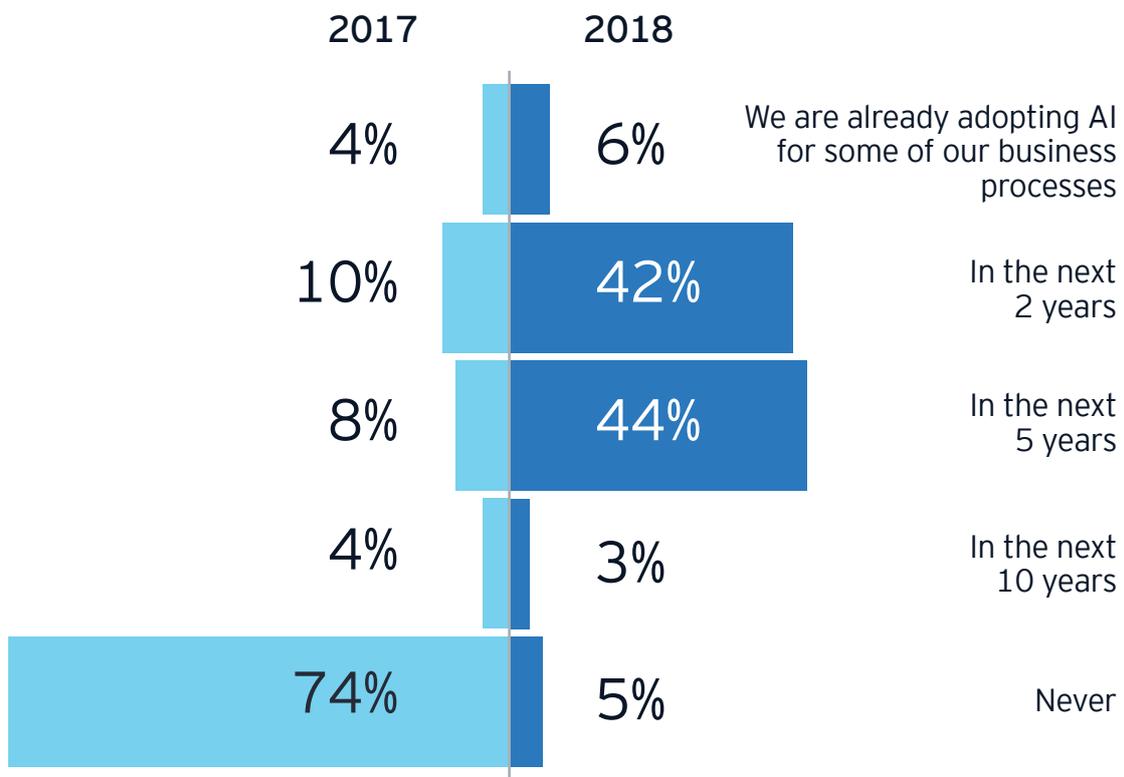
Surprisingly, despite this IT focus, digitization and investment in technology is the strategic priority for just 12% of the Canadian middle market, although even this low figure is double the rating in the rest of the world of 6%. Furthermore, only 9% see cyber threats as the primary challenge to growth.

⁷ "How can divesting fuel your future growth?" EY, Global corporate divestment study 2018, Canadian findings, <https://www.ey.com/ca/en/services/transactions/divestiture-advisory-services/ey-corporate-divestment-study-canada-findings>, accessed March 2018.

⁸ "Government reveals who is getting \$950M in 'supercluster' funding," *Global News*, <https://globalnews.ca/news/4027827/superclusters-initiative-getting-funding-navdeep-bains/>, accessed March 2018.

AI adoption

This chart shows the massive shift in the number of companies in 2017 and 2018 that intend to embrace artificial intelligence (AI) over the next 10 years.



World-leading customer focus

Canadian executives are investing in technology primarily to improve the customer experience (cited by 36% of respondents). This is just one indicator that Canada is outpacing its peers in its customer-centricity. Nearly one-third of Canadian respondents see better customer understanding as the key to agility (30%), far ahead of the rest of the world with 8%.

The second greatest way Canadians think they can boost innovation is by using customer data to drive innovation from the bottom up.

Customer demand is the top innovation driver for 40% of Canadian execs, whereas it is profitability for the rest of the world.

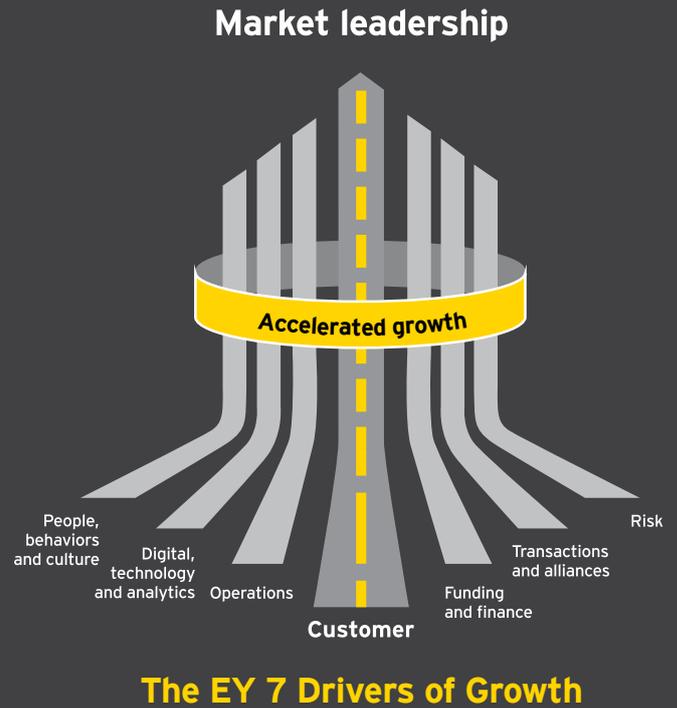
This commitment to innovating on the basis of demand chimes strongly with Overbond's Magdelinic. "Innovation starts with a view about how the industry is changing and what you can do to contribute to the change. You have a mission, a vision, of what you want your company to be, and then it is a question of creating a product that fits the vision and satisfies the need of the industry."

Accelerating growth with the EY 7 Drivers of Growth

EY Growth Barometer explores entrepreneurs' and middle-market leaders' growth strategies, and how they are bringing these strategies to life across a wide range of capabilities. These capabilities are linked to the EY 7 Drivers of Growth – EY's proprietary framework to help business leaders think differently about how to accelerate growth.

We developed this framework by listening to and working with hundreds of companies around the world, ranging from start-ups to leading businesses; conducting in-depth interviews with winners of EY Entrepreneur Of The Year™ program; and gathering insights from more than 500 partners serving middle-market companies.

The EY 7 Drivers of Growth helps leaders think differently about how they create growth and customer value beyond the traditional focus on people, systems and processes. By focusing on a broader set of capabilities, leaders can build a plan to realize their growth ambitions.



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