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***Support for Canada's Hopeful Monsters***

***Or, Understanding SME Financing***

Good morning. It is an honour to have been invited to join you today, and a pleasure to be with people who share a dedication to the success of Canada's entrepreneurs.

My first task is to thank each and everyone of you. My colleagues and I at BDC regularly rely on the information and data that you diligently produce. As direct beneficiaries of the fruits of your labour, we are very grateful. On behalf of everyone at BDC, thank you all.

My main task this morning is to share my thoughts on the financing needs of SMEs, which I am happy to do. My view is simple: I believe that we, as a group, must be more creative and collaborative if we want to make the most relevant, helpful contribution that we can to the health of Canada's SME sector.

Finally, we hope to hear some of your thoughts on SME financing needs. Given the expertise and experience in this room, I am sure you will have a few.

## 1. Relevance

To begin, since some of you may be unfamiliar with the Business Development Bank of Canada (BDC) and its relationship with your work, I will say a few words about who we are, what we do and why we do it.

BDC is a Crown corporation created to support entrepreneurs and promote entrepreneurship. We fulfill this mandate by offering, on a complementary basis, financing, consulting and venture capital services to SMEs. *Only* SMEs. We are the only financial institution that does so on a pan-Canadian basis.

As a bank, we match financing to ideas in order to create new wealth. We have been doing this, in a variety of ways, for *sixty-two* years.

At present, over 26,000 Canadian entrepreneurs are BDC clients. To support them, we have invested over \$10 billion in committed financing and venture capital. We also provide more than 2,000 business consultations every year.

One of the things that makes us most proud is the *close, long-term* nature of our client relationships.

As you can imagine, our client records are a *goldmine* of data on Canadian SMEs and their development over time. Indeed, I believe we may be one of the most SME data-rich financial institutions in the country.

One could think of BDC as an elegant marriage of public policy mandate and commercial imperative. We effectively meet a societal need. And we do so with private sector efficiency.

Parliament does not give us an annual subsidy; it makes us earn our keep. We are obliged to earn a return on equity that is at least equal to the government's average long-term cost of capital. We do so, handily. Over the past years, we have paid over \$100 million in dividends to the government – powerful testimony to our commercial viability.

It is important to note, however, that our obligation to be commercially viable does much more than remove us from the line-up outside the government's door at budget time - *it dictates a mode of operation that makes us shadow and anticipate SME needs*. As SME needs evolve – and of course they do so constantly - so do our services.

If we do not evolve with them, we will not be able to attract them as clients. Because we stay relevant to their evolving needs, we succeed, even though we price our financing higher than other financial institutions, which we do to compensate for the higher risk that we take.

This hardwired, operational focus on the changing SMEs needs make us an instrument of public policy like no other in Canada. If we cease to evolve in tandem with SMEs, we will fail to deliver our public policy mandate.

This means that market relevance is of *critical* importance to us. Our quest for it permeates our decision-making.

Our success thus far in staying ahead of the market in ascertaining and meeting SME needs is explained, I believe, by the wisdom born of sixty-two years in the business, thousands of relationships with entrepreneurs and an operational DNA that obliges a constant quest for relevance.

You will not be surprised to hear that our obsession with market relevance also permeates our information-gathering. This is why I was quick to accept the invitation to come meet you today.

I believe that we share a reason for being. Indeed, one might even say that we are an example of a productive symbiosis. You are as critical to the relevance of our role as we are to yours.

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To conclude on roles, Parliament's rationale in assigning BDC's mandate was simple. When it identified gaps in the marketplace's provision of services to SMEs and told us to support entrepreneurs hindered by these gaps, it had one thing in mind: the essential contribution of SMEs to the health of the national economy.

SMEs make a very significant contribution to our national GDP. They also employ about 65% of our labour force. When they succeed, Canadian society benefits.

It is easy for us - and please note that by "us" I mean everyone in this room – to forget this essential point. As we go about our daily routines of collecting data, doing research, formulating policy, and, at BDC, meeting entrepreneur clients and polishing contracts – it is easy to forget that we, as a group, provide important support to a sector that creates opportunity and prosperity that are vitally important to the lives of millions of Canadians.

We should all be proud of what we do to help bring about this positive state of affairs. Not all research communities can claim the same immediate relevance to society. Or the same influence.

But along with influence, of course, comes responsibility. I believe that responsibility requires us to be as rigorous and as relevant as we can when we offer information, ideas and recommendations to institutions that exert direct influence on the lives of our fellow Canadians.

And this, of course, is why we are here today.

## 2. The need for creativity

I recently came across a metaphor that I think captures well the plight of SMEs. I think it might be a helpful one for us as we galvanize our thoughts and efforts for the task ahead. The idea is from Charles Darwin, the famed evolutionary biologist. So, if you permit me a one-minute biology lesson, I will share it with you.

Darwin observed that Nature, with every new generation, throws up variations on species. For example, if we look closely at a nest of young birds, we will often see one that differs in some way from the others. A variation on the theme, if you will. Perhaps it has a longer beak, wider-set eyes or longer feathers.

Depending on its health, wherewithal and ability to survive, plus – and this part is key – depending on the changing demands of the environment, the odd-looking offspring can survive, prosper and reproduce. It can even go on to become the dominant form of the species.

Darwin chose a poetic term for these evolutionary variations. He called them “hopeful monsters”; monsters because they look different from the rest, hopeful because it is not at all clear they will survive. Their survival depends on their abilities, their wherewithal and the dictates of the environment. And sometimes, luck. Such is evolution.

Some SMEs are like hopeful monsters. They are variations on the theme, competing to survive in a changing, demanding environment. To support them, we have to search for and learn to recognize them. We also have to understand their environment, their place in it, and work to reduce the influence of luck in determining their success.

Understanding today’s business environment in these globalized times is no easy feat. In an interesting speech last month, the Chairman of the U.S Federal Reserve, Ben Bernanke, talked about globalization and its effects. He dubbed it “the defining force of our time”.

One of Mr Bernanke’s observations is that continued mainstream support for free trade and international economic integration is not inevitable. He said that the potential social and political opposition to globalized free trade is such that *policymakers should work to ensure that its benefits are widely shared*. I agree.

While Mr Bernanke did not speak specifically about small business, I am sure you will agree that globalization gives little shelter to Canadian SMEs. I think you will also agree that one way to ensure that the benefits of globalization are more widely shared is by supporting a category of market players who are struggling to meet its competitive challenges and who are trying to harness its benefits by creating new kinds of value: SMEs.

I would suggest that we use this as a starting point for our discussion: *SME competitiveness is an essential part of Canada's response to the challenges and opportunities of globalization.*

Our job is to help Canada's SMEs – especially its hopeful monster SMEs - survive, grow and thrive. The question, of course, is how. The *how* keeps changing.

According to reports, many of the internationally renowned speakers at Mr Bernanke's gathering made a consistent set of observations about globalization. They said that we have an imperfect understanding of what it is, an imperfect understanding of its likely outcomes and – my favourite - an imperfect understanding of its demands on public policy.

It is reassuring to know that we Canadians are not alone!

If our understanding of globalization – the defining force of our time – is so imperfect, we must show humility and creativity when we try to capture its effects on our SMEs, as well as their evolutionary response to it.

Intellectual humility will enable us to remember that our ideas may be out of date, declining in usefulness or even obsolete. It will also permit us to constantly scrutinize the bases of our assumptions and discard those frameworks that have ceased to be of help. Our frameworks and indicators must be as sophisticated as the enterprises they are trying to measure.

Humility will also remind us that our individual perspectives and experience, however positive or successful, do not constitute the whole. This can be easy to forget when the experiences are positive.

Some of BDC's pioneering successes have been business decisions based on a mix of insight and experience - feedback from the front lines plus a pro's intuition, if you will. Because we are close to the entrepreneurs, we hear and see evolutionary changes *as they happen*. Quite often, we use insights, qualitative information and processes that are more intuitive than rigorous. We have to rely on trial and error because data, by definition, is history by the time you receive it.

But, however well this approach has worked for us in the past, it does not, on its own, constitute a sufficient or reliable basis for determining BDC's long-term roadmap. Let's call it insufficient but necessary: BDC's practical experience on the entrepreneurial front lines is an absolutely essential input into the higher level policy issues that we are all discussing here today.

Intellectual creativity will enable us to begin to ensure, or at least improve, the ongoing validity, completeness and usefulness of our conceptual models, definitions and data. *This creativity is absolutely crucial.*

With this in mind, I would now ask us all to set aside our particular organizational perspectives and *creatively* brainstorm. My colleagues and I at BDC have several questions and issues that we feel merit a closer look. It is by no means a definitive list, but we'd like your thoughts on them.

- To begin, how should we define today's SME? Do we have candidate definitions that capture today's multiplicity of business models? (Do we even see and understand all the new business models around us?) Will these definitions begin to capture *tomorrow's* SME?
- What are the key factors that determine successful start-ups? Successful growth? Survival? What are the critical life cycle factors that affect growth and long-term survival? Do traditional metrics such as number of employees or revenue tell us everything we need to know about whether or not an SME is succeeding? For example, if we limit ourselves to number of employees as a measure of growth, are we minimizing the impact of improved productivity or profitability?
- How do we capture the increasingly intangible nature of so much of the value created by SMEs? At BDC, we have had real success in evaluating intangibles and in providing unique financing arrangements, but broadly speaking, many financial institutions find it hard. As a result, many entrepreneurs have difficulty getting financing for intangibles. We must rectify this situation.

### 3. Collaboration

Before I turn to my fellow panellists and open up the floor to what I am sure will be an interesting flow of questions and ideas, permit me to underline the other determining factor in our group success: collaboration.

People often describe the MacKay Report of 1998 as a turning point in SME research data collection. While the three surveys since the MacKay Report have been helpful, I think this description is perhaps too cheerful by half. "Turning point" implies a pivot and clear movement in a new direction. We have seen steps. Given the importance of our role, I think we need to see strides.

We should all aim for data collection that has greater depth and breadth. Plus of course a greater total amount. Greater sharing of research plans – a more structured approach than we have at present - will also help us reduce the likelihood of duplication.

We should be better about sharing results as well. Data isn't much use to others if we are sitting on it. We have to increase the number and range of organizations and people with whom we share. And we have to do so with more speed.

We at BDC consider this to be a top priority, and are in the middle of finalizing a research agenda. We intend to work with several partners, and will be making announcements in this regard in the very near future. I encourage you all to consider ways in which we might

collaborate with your organizations, and invite you to come see us if you have any ideas. Several of my colleagues are here for the duration of the conference, so I encourage you to introduce yourselves to them.

So, to conclude:

On relevance: although we have it today, we have to discover it for tomorrow.

On creativity: Yesterday's success is no guarantee of tomorrow's. We need more creativity to capture tomorrow's models.

On collaboration: we need greater volume, greater coordination, greater depth and breadth. And faster-shared results.

Thank you.