

**ASSESSING THE KEYS AND BARRIERS TO SUCCESS IN THE  
VALUE-ADDED WOOD PRODUCT MANUFACTURING SECTOR:  
A MULTIPLE-CASE STUDY ANALYSIS OF SMALL AND  
MEDIUM-SIZED ENTERPRISES**

by

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## **Abstract**

Small and medium sized enterprises (SMEs) in the value-added forest products sector play an important role, both socially and economically, in forest dependent communities across Canada, yet the long-touted potential of the sector has not been attained. An assessment of the success factors as well as the barriers to success for SMEs operating in the value-added forest products sector is a key step in ensuring that firms operating in the sector, as well as policy makers at various levels of government are better informed. This will allow the firms in the sector to leverage their strengths and address their weaknesses in order to have a strong contingent of successful value-added forest product SMEs vital to sustaining community wealth. The study is conducted through an in-depth examination of four SMEs in the value-added wood products sector in British Columbia. The four cases represent different types of businesses with varying levels of performance. The results of the study indicate that management skills, access to skilled labour, access to fibre supply, and access to financial capital are fundamental success factors. The entrepreneurs and industry experts involved in the study suggest that for British Columbia's value-added forest products sector to prosper, the development of management skills and skilled labour requires greater attention. Consequently, increases in the level of investment in skilled labour training and management skill development options that are easily accessible to entrepreneurs in rural communities, in conjunction with the provision of timber at a scale and means that is more suited to small and medium-sized value-added firms were suggested as means to reduce barriers to success faced by SMEs in the value-added sector.

## **Preface**

Philip Grace identified the research problem and methodologies and developed the research design with the guidance of Dr. Harry Nelson, Dr. Robert Kozak, and Ken Day RPF. Dr. Kozak suggested the use of case studies to address the research problem and Ken Day provided valuable insight into the research topic and structure of the research. Philip Grace collected all the data, performed all the analysis and completed the write-up of the research. Dr. Nelson, Dr. Kozak, and Mr. Day gave valuable feedback and critiques of the research methods.

This research was approved by the UBC Behavioural Research Ethics Board (Certificate number: H10-00681).

## Table of Contents

Abstract .....	ii
Preface.....	iii
Table of Contents .....	iv
List of Tables .....	vii
List of Figures .....	viii
Acknowledgements.....	ix
1 Introduction.....	1
1.1 Competitive theory .....	2
1.2 Competitiveness: why size matters .....	4
1.2.1 Factors influencing SME competitiveness .....	6
Risk management .....	7
Regulatory environment.....	9
Financing.....	9
Collaborative strategy .....	10
Innovation .....	12
Skilled labour .....	13
Management .....	14
1.3 British Columbia's forest sector .....	16
1.3.1 The forest industry in British Columbia.....	16
International markets .....	17
Value-added forest products .....	18
1.3.2 Forest policy in British Columbia.....	20
The importance of forest tenure in British Columbia .....	21
Small Business Forest Enterprise Program .....	22
British Columbia Forestry Revitalization Plan .....	23
Mountain pine beetle epidemic .....	25

Canada-US softwood lumber dispute.....	26
1.4 Resource dependent communities .....	28
Forest-dependent community assessment .....	30
Forest-dependent community sustainability .....	33
1.5 Objectives .....	34
2 Methods.....	36
2.1 General approach.....	36
2.2 Case selection .....	37
2.3 Data collection.....	40
2.4 Data analysis.....	43
3 Results.....	47
3.1 Firm A .....	47
3.1.1 Firm description.....	47
3.1.2 Fibre supply .....	48
3.1.3 Financing .....	49
3.1.4 Skill.....	50
3.1.5 External environment .....	51
3.1.6 Strategy .....	52
3.2 Firm B.....	54
3.2.1 Firm description.....	54
3.2.2 Fibre supply .....	54
3.2.3 Financing .....	57
3.2.4 Skill.....	58
3.2.5 External environment .....	59
3.2.6 Strategy .....	62
3.3 Firm C.....	65
3.3.1 Firm description.....	65
3.3.2 Fibre supply .....	67
3.3.3 Financing .....	68

3.3.4 Skill.....	69
3.3.5 External environment .....	71
3.3.6 Strategy .....	72
3.4 Firm D .....	75
3.4.1 Firm description.....	75
3.4.2 Fibre supply .....	76
3.4.3 Financing .....	77
3.4.4 Skill.....	78
3.4.5 External environment .....	80
3.4.6 Strategy .....	81
3.5 Multiple case study overview .....	84
3.5.1 Fibre supply .....	84
3.5.2 Financing .....	85
3.5.3 Skill.....	87
3.5.4 External environment .....	89
3.5.5 Strategy .....	90
4 Discussion and conclusions .....	92
4.1 Implications .....	92
4.2 Limitations.....	95
4.3 Further research .....	96
Bibliography .....	99
Appendix I: Forest policy timeline .....	111
Appendix II: Invitation to take part in the study.....	117
Appendix III: Consent form.....	119

## List of Tables

Table 1 Criteria and weighting for evaluating bid proposals.....	23
Table 2 Forest sector expert backgrounds .....	38
Table 3 Characteristics of participating firms.....	40
Table 4 Themes and subthemes identified during the focused and in-depth interviews .....	44

## List of Figures

Figure 1 Data collection process .....	43
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*“It’s easy to start a business; the hard part is keeping it going”*

- Owner B (personal comment, 2011)

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*“Being born is the easy part, yes it is staying here that’s difficult”*

- Catherine Hunter, *“Moon Again”* in Lunar Wake (Turnstone Press, 1994)

# 1. Introduction

This thesis presents a study of the barriers and keys to success faced by small and medium-sized enterprises in the value-added forest products sector in the Interior region of British Columbia. There has been wide-spread support and long-term interest in developing and expanding the value-added sector, which is seen as offering multiple economic benefits compared to the primary sector- more employment per cubic meter, higher value for the fibre, and a more diversified forest sector. Yet while there have been a number of efforts, including policy developments and programs to support the sector, there have been relatively few studies of what factors influence the success of firms operating in the sector; and those studies have approached the issue from a sectorial point of view but have not investigated, in-depth, what factors are important at a firm-level.

The introductory chapter provides a review of relevant literature to the study. The first section examines the relevant literature from the fields of economics, organizational theory, and sociology dealing with business competitiveness, reviewing the principles of competitive theory, then adapting the concept of competitiveness for the case of smaller firms, with special attention paid to the unique role human resources play in establishing overall competitive position of a business. A review of the literature pertaining to British Columbia's forest sector is presented in the second section- first, an examination of the external factors affecting the environment for the value-added sector, including trends in the solid wood products industry and the reasons behind the strong support for the value-added sector; and second, the developments in the policy arena and programs both targeting and directly affecting the value-added sector. The literature review is followed by the principal objectives of the research.

The second chapter describes the methodology used: the overall approach using case-based methods; the selection of experts and cases; the description of cases; the data collection process; and the data analysis techniques. The results are presented in chapter three, followed by a discussion of the results in chapter four. The main conclusions drawn from the study are also presented in chapter four along with limitations of the research, and suggested areas for further research.

## **1.1 Competitiveness Theory**

There are a number of different disciplines spanning economics, organizational theory, even sociology that investigate firm behaviour, including decision-making, price setting, and human resource management. These, along with other aspects of how firms operate, influence firm outcomes. While these different disciplines offer valuable insight into specific areas of firm behaviour, the only one that systematically looks at outcomes and what determines which firms do well and which ones do not is competitiveness theory.

Michael Porter's (1980) work on the competitive forces affecting businesses has come to be, for many, the *de facto* model by which industry competitiveness is assessed. Porter's analysis is built on five forces that affect a firm's competitive position. Moving away from the model of perfect competition, which is fraught with unrealistic assumptions, Porter looks at (1) the threat of new entrants as well as (2) the jostling for position within an industry as two key forces that shape a business' competitive strategy. Recognizing that competitiveness is also heavily affected by (3) buyers and (4) suppliers, he incorporates bargaining theory into his examination. He completes his five-pronged analysis by looking at (5) the role substitute products (or services) can play in competitive dynamics.

What competitiveness ultimately boils down to, is advantage. If a firm can leverage a competitive advantage over its rivals, it is in a position to compete successfully in its industry. Day and Wensley (1988) propose the SPP framework (*sources, positions, and performance outcomes*) for measuring competitive advantage by asking the following questions: what are the sources of competitive advantage (skills, resources)? What are the firm's positional advantages (value, cost)? Are performance outcomes favourable (customer satisfaction, loyalty, etc.)? They argue that the SPP framework represents the components that make up competitive advantage, and that the components are sequential. That is, sources of advantage will only truly represent an advantage if the firm is positioned in such a way as to exploit the advantage. Along the same lines, the performance outcomes are a result of the carefully aligned source and positional advantages. They posit that although superior skills and resources may be essential for sustained competitive advantage, they are not enough to guarantee competitive advantage. An advantage can only be profitably exploited if it is positioned in such a way as to be valued by the customer.

In summary, competitiveness theory identifies what factors are relevant for explaining whether or not a firm will be competitive; the importance of strategy in how it aligns with those factors; and how competitiveness (performance outcomes) can be assessed. However, this general framework glosses over one critical issue-firm size. A review of the existing value added sector in BC, and Canada more generally, shows that the sector is overwhelmingly made up of small and medium-sized enterprises; there are few larger companies in Canada that operate in this area. While there are some aspects of the theory that touch on size - i.e. relationships between buyers and suppliers - this factor is generally overlooked. The size of these firms has important implications, not only for how it influences industry dynamics, but also the role size

plays in influencing the success of these firms and the key role business owners play in both the establishment and ongoing operation of the firm.

## **1.2 Competitiveness: why size matters**

Many of the characteristics of competitiveness mentioned can be applied regardless of firm size; however SMEs are often faced with further challenges to competitiveness because of their smaller size. Therefore, competitiveness frameworks must be adapted to take into account how the size of a firm influences its competitive position. Two important ways in which this can happen are through *economies of scale* (having to do with production technology) and *bargaining power* (having to do with industry structure and firm relationships).

While Porter (1980) argues that the achievement of economies of scale will deter potential new entrants to the industry or industry subsector as well as position a firm to have a cost advantage, other researchers have argued for a reduction in economies of scale in favour of a more diversified product line. Dixit and Stiglitz (1977) posit that while economies of scale may enable a firm to compete on costs, product diversification, often achieved at the expense of economies of scale, will be preferred by consumers and therefore increase customer loyalty. This, they argue, will reduce the threat of new entrants and ultimately improve a firm's competitive position in relation to its existing industry rivals. In the value-added sector, which includes a wide-range of product categories- some suited for commoditization and potentially economies of scale, and others being more in line with strategies incorporating economies of scope- both Porter's and Dixit and Stiglitz's theories may be applicable.

As mentioned earlier, the bargaining exercise can play a significant role in the competitiveness of a firm or industry. Moving away from Nash's (1950) assumptions of equal

discount rates, equal bargaining skills, and equal ability to consider and compare different alternatives, Porter (1980) notes that bargaining power at different stages of the supply chain can be a major determinant of the degree of competition in an industry.

Many competitive theorists will make strong underlying assumptions that may prove to be true in the case of large businesses, but fail when applied to smaller firms. A good example of such situation is John Nash's (1950) seminal work on the bargaining problem of game theory. A key assumption in Nash's model is that bargaining parties have equal discount rates<sup>1</sup>. When applied to a bargaining game with a large and a small or medium-sized firm, the assumption does not hold up. This is not meant to point out a weakness in Nash's work, but rather to emphasize that although there are a number of indicators available to the competitive analyst, in order to properly assess the competitive landscape, appropriate criteria selection is key. Finally, beyond the importance of SME firms in the value-added sector, they also play an important role in the Canadian economy. Despite the seemingly endless growth in market share of large corporations, the likes of which populate well publicized industry lists such as the Fortune 500<sup>2</sup>, SMEs are still holding their own when it comes to key economic indicators. Statistics Canada reports that in 2011, 48% of employed Canadians worked for firms with fewer than 100 employees, and a further 16% worked for medium-sized firms<sup>3</sup> (2012). Of greater importance in a time of economic uncertainty is the fact that despite employing over 65% of all Canadians, in the worst of the 2008-09 world-wide recession, SMEs were only responsible for 44% of Canadian job

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<sup>1</sup> This essentially means that both parties are willing to negotiate until an agreement is reached, regardless of how long that may take. When applied to the case of an SME negotiating with a much larger supplier, for example, the two parties have different discount rates. Where the larger firm can afford to be "less impatient" and hold out for as long as is required to meet certain negotiation goals, holding out beyond a certain amount of time could prove to be fatal for the smaller business (Wagner, 1988).

<sup>2</sup> To access full list of Fortune 500 companies, see:

[http://money.cnn.com/magazines/fortune/fortune500/2013/full\\_list/index.html?iid=F500\\_lp\\_toppr](http://money.cnn.com/magazines/fortune/fortune500/2013/full_list/index.html?iid=F500_lp_toppr)

<sup>3</sup> Businesses having between 100 and 499 employees are classified as medium-sized according to Statistics Canada (2012).

losses, significantly less than their larger counterparts (Statistics Canada, 2009). SMEs' positive macroeconomic contributions are not limited to employment figures; in Canada, SME exports accounted for over 40% of total exports in 2010 (Statistics Canada, 2012).

### 1.2.1 Factors influencing SME competitiveness

While there are a number of tools available for assessing competitiveness, not all can be directly applied to SMEs. Evaluating competitiveness at the SME level is different from evaluating the competitiveness of larger firms because on many levels that affect overall competitive position, small and large firms are inherently different (Burns, 2001). Perhaps the most important distinction lies in the firms' relationship with its external environment. Understanding the environment, or the context, under which a company operates will go a long way in understanding the competitive strategy adopted by a firm as well as offer insight into the competitive nature of an industry. A core concept that Porter (1979, 1980, 1991) stresses in a number of works is that certain strategies will be more effective in certain environments. That is, the environment will invariably shape successful competitive strategy.

Often times, small and large companies will have vastly different responses to their external environment, different competing tactics, diverse managerial styles, and varying access to resources (Chen and Hambrick, 1995; Rangone, 1999; Man et al., 2002; Bierly and Daly, 2007). SMEs have very limited influence on the business landscape, whereas larger firms will play a large part in shaping their operating environment. Large firms, on the other hand, by virtue of their size, can exploit their bargaining power, achieve economies of scale, or offer more diversified product lines. These opportunities will be more limited, if not absent, for SMEs. From

this pivotal difference stem other competitiveness issues such as the need for SMEs to carefully craft strategies around risk management, staying up-to-date with changes in the regulatory environment, ensuring that the firm is well financed, leveraging collaboration opportunities with other firms, and making sure that the firm is in a position to adapt and innovate to remain competitive. SMEs' management of human resources, including skilled labour and skilled management, also plays an essential role in firm success.

### ***Risk Management***

As SMEs tend to be more vulnerable to external influences than their larger counterparts, they must not only be very *aware* of the exogenous factors affecting their business, but also be prepared to *adapt* quickly as the environment changes (Man et al., 2002). Garg, et al. (2003) use the term 'environmental dynamism' to refer to the rate at which the business environment changes and the unpredictability with which the changes occur. The oft-unpredictable risk associated with the external environment is a risk that businesses must factor into their competitive strategy. In their exposition on the risks faced by entrepreneurs starting SMEs, Everett and Watson (1998) list economy based risk, industry based risk, and firm based risk<sup>4</sup> as the three main categories of risk that determine whether a SME will be competitive or not. Of the three categories of risk identified by Everett and Watson, two are exogenous (industry and economic), with economy based risk being associated with 30% to 50% of small business failures (p. 387). The authors also highlight the fact that while economic risks are somewhat systematic, industry based risks tend to be rogue in nature. This stresses the importance of

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<sup>4</sup> Economy based risk is assessed based on the macro-economic variables affecting the economy in which the firm operates; industry based risk is beyond the realm of control of the firm, but is specific to the sector, or industry in which the firm operates; firm based risk is endogenous to the firm, and presumably within the firm's control (Fredland and Morris, 1976; Everett and Watson, 1998).



accounting for the external environment when formulating strategy as well as recognizing that business and economic environments are not static or necessarily predictable.

While domestic economic risks and uncertainties leave a number of SMEs exposed, those who choose to operate in foreign markets by incorporating exports into their business strategy often open themselves up to further risks. Posner (1997) characterizes export related risk as commercial, political and economic. Common risks include buyer default on loans or insolvency (commercial), changes in policies affecting import/export regulations (political), as well as overall changes in country's economic position vis-à-vis its trading partner due to exchange rate fluctuations or market uncertainties (economic) (Rienstra-Munnicha and Turvey, 2002).

Despite the increased exposure to risk, for many firms, the realities of competing in a globalized world make it nearly impossible to focus solely on domestic markets and as a result an increasing number of small businesses are developing their export capacity (Pett and Wolff, 2003). Not surprisingly, Golovko and Valentini (2011) found that successful participation in export markets leads to improved growth for SMEs<sup>5</sup>. However, the implementation of a successful export strategy can be challenging; export development, particularly in the case of SMEs, is rife with barriers that are both internal and external to the firm. Leonidou (2004) posits that problems within the firm such as lack of information on foreign markets, lack of managerial time devoted to exports, high transportation and insurance costs, as well as meeting foreign markets' standards of quality, labelling and packaging can prove to be major obstacles in SMEs' export ventures. According to Leonidou, these internal barriers are compounded by hurdles in the external environment such as aforementioned fluctuations in foreign exchange rate and various regulatory frameworks involving tariff and nontariff barriers.

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<sup>5</sup> Golovko and Valentini (2011) found that while exports contribute positively to SME growth, the most significant positive impact of exports on a firm's rate of growth is felt when an export strategy is coupled with a strong innovation strategy.

### ***Regulatory Environment***

The numerous standards and regulations by which firms must abide undoubtedly influence a firm's operating environment, regardless of whether the firm is focused on foreign or domestic markets. Industry regulations and standards are usually the result of industrial policy designed to protect free markets from being hampered by market failures which would limit their proper functioning; however, despite industry standards being in place, gaining access to information about standards is often relatively more time and resource intensive for SMEs than for larger companies (ESCWA, 2007). Such intensive allocation of resources towards staying current with industry standards can hamper SMEs' competitive position by limiting resources available to other aspects of the business.

### ***Financing***

One such area of business that firms must devote considerable amounts of time to is securing financing for ongoing activities and business expansion. While it is true that a firm's performance and credit record are important factors in a financing institution's decision provide a SME with access to capital or not, when the macro economy suffers and credit markets tighten, SMEs are often left with limited financing options, regardless of their financial track record (ACCA, 2008). Berger and Udell (2006) argue that the elements that affect the credit available to SMEs are: *the information environment* – presence of credit bureaus and the reliability of credit information; *the legal, judicial, and bankruptcy environment* – the laws around property rights as they relate to the provision of financing, as well as the level to which those laws are enforced; *the social environment* – the level of social capital in the economy (regional or national); *the tax*

*and regulatory environment* – the policies and regulations in place that affect lending institutions' supply of credit of SMEs' ability to secure financing. They posit that more reliable credit information, strong, transparent property rights, and strong mutual trust between lenders and borrowers will increase the availability of financing to SMEs whereas certain types of value-added tax regimes and tougher bank supervision regulations are likely to have negative impacts on overall credit availability.

### ***Collaborative Strategy***

One way to overcome limitation of size is to take advantage of agglomeration benefits where possible. The literature on the benefits of industry clusters, defined by Bell (2005) as “groups of geographically proximate firms in the same industry” (p.287), dates back to Alfred Marshall's seminal work, *Principles of Economics* (1890). Marshallian externalities, or the non-price benefits that accrue to firms belonging to an industry cluster, have been linked to benefits in the factors markets, improved networking potential, as well as upgraded public infrastructure (Arthur, 1989; Porter, 1990; Krugman, 1991,1995; Fujita and Thisse, 2002). The benefits of clusters are particularly apparent in the case of SMEs.

Networking and clusters have become one of the most successful means of improving SME competitiveness through improvements in productivity and innovativeness (Karaev, et al., 2007). As customer expectations rise and competition within industries intensifies, Karaev, et al. (2007) note that members of industry or geographical clusters may cooperate as partners or compete fiercely against one another depending on the market environment, all of which they argue lead to a healthier competitive landscape. The benefits of networking and informal clusters are so well perceived that significant investment by various levels of government in the

establishment and support of SME clusters have been documented throughout the world (Pyke, 1994). Governments recognize that as global competition becomes the norm, smaller firms by themselves are unable to keep atop the various international standards and trends that will keep them competitive in the future (Westerlund, et al., 2008). However, Hooley and Greenley (2005) warn that the presence of a network is not enough to improve competitive positioning. They posit that improvements in competitive position attributable to industry networks depend on the additional resources, or additional access to resources, that a network can provide. Westerlund, et al. (2008) point out that when venturing into international markets, SMEs often fail due to a lack of organisational resources<sup>6</sup>; a lack of resources that could potentially be remedied by the establishment of a network, formal or not (Kingsley and Malecki, 2004).

Interestingly, Kingsley and Malecki (2004) found that cluster effectiveness varied depending on whether the cluster was primarily composed of rural firms or urban firms. They found that groups of firms in urban centres were much more active in developing strategies for accessing external information to benefit the competitiveness of the sector, whereas rural clusters were much less aggressive and as a result, the effectiveness of the cluster in enhancing competitiveness was limited.

In addition to clusters based solely on geographic positioning, Bennett (1998) points out that professional associations are good sources of information on various industry, provincial, and federal standards. He also argues that industry associations serve to cooperatively improve the standards of their respective industries which in turn lead to greater sharing of information among companies and between companies and governments, which ultimately leads to increased competitiveness. Doner and Ross Schneider (2000) warn, however, that only those associations

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<sup>6</sup> Interestingly, in their study of various SME clusters, Westerlund, et al. (2008) found that firms who focused on local markets were significantly more profitable than those with emphasis on international business.

that actively seek to improve standards of quality, communication, and labour force skillset will have a significant positive impact on their business environment.

Highly active business associations can play a vital role in bettering SMEs' competitive position. In their study of the Canadian secondary wood manufacturing sector, Delong, et al. (2007) identify that firms belonging to an industry association were significantly more likely to be profitable. While they stress that no causality was identified, attention is drawn to industry associations' role in SME competitiveness. The authors posit that the finding may indicate that members of industry associations show interest in staying up to date with current trends, or alternatively, that profitable firms may be more likely to join industry associations (pp. 2223-2224).

### ***Innovation***

Innovative capacity is an important determinant of SME competitiveness (Cakar and Erturk, 2010) and ultimately of SME survival (Joyce and Woods, 2003). While large firms have often relied on economies of scale to gain a competitive edge (Stigler, 1958; Simon and Bonini, 1958; Krugman, 1991), many smaller firms have adopted the "economies of specialization" strategy by focusing innovation as a means for competing successfully (Preissl and Solimene, 2003, p. 6). As the realities of competing in a global marketplace become engrained in the business psyche, SMEs have to make concerted efforts to innovate, specialize and focus on their core competencies in order to compete (Deavers, 1997). In order to innovate effectively, firms must have a strong knowledge base, which Bierly and Daly (2007, p. 493) describe as the combination of experience, skills and tangible and intangible knowledge that is present within an organisation. The authors point out that SMEs tend to face stricter resource constraints than

larger firms, which limits their opportunities to develop a sound knowledge base. Should a knowledge base be established, a firm, regardless of size, must then translate the knowledge base into a knowledge strategy (Zack, 1999). Bierly and Daly (2007) argue that a successful knowledge strategy, with appropriate allocation of resources to the generation of new knowledge or the enhancement of the established knowledge base, is a fundamental factor in overall SME competitiveness.

SMEs must be ready and able to use their knowledge base to foster innovation within their companies in order to be in a position to respond to customer demands quickly; this, Clark and Guy (1998) argue, should be incorporated into a firm's competitive strategy. While large firms will often have a market research department in charge of keeping up with customers' needs and wants, SMEs usually lack the resources to conduct quality market research which is instrumental in reducing reaction time to market developments. By cooperating with other SMEs through industry clusters or associations, they can often pool resources in order to improve their competitive position in the marketplace. Participating in these types of networks can also lead to greater lobbying power and greater familiarity with relevant government policies and industry standards.

### ***Skilled Labour***

Regardless of a business' stage of expansion, skilled labour is an essential element of business development and, ultimately, survival. SMEs consistently have greater difficulty attracting skilled employees than their larger counterparts (Fitzsimmons and Fitzsimmons, 2003; Peters, 2005). Fitzsimmons and Fitzsimmons (2003) argue that this is due to SMEs lacking economies of scale and consequently having lower marketing, advertising, and human resource

training budgets to draw skilled labourers. Highlighting the important and influential role small business owners play in overcoming the negative scale effects, Ware and Grantham (2009) argue that SME owner/managers are strongly involved in the daily operations of the business to compensate for the lack of skilled employees; this takes valuable resources, notably time and energy, away from the SME's strategy development. This lack of skilled employees may also be the result of smaller businesses offering fewer employee benefits as well as less desirable employment opportunities (Addis, 2003).

The end result of smaller firms being unable to attract skilled labour is an SME workforce with very low standards of basic skills<sup>7</sup>, not to mention the lack of specialized skills (Addis, 2003). Subsequently, the overall economic performance of SMEs is seriously threatened by low levels of basic skills (Moser, 1999). Despite the potential risk of under-skilled workers, employers are still reluctant to embrace skills training as a means of improving their competitive position (Addis, 2003). SME reluctance to invest in employee skills training has been attributed to the lack of funds required to set-up training programs (Moser, 1999) as well as the fear that employees will be trained at the expense of the firm only to be "poached" by other firms who do not have workplace skill development programs (Greenhalgh, 1999).

### ***Management***

Given that SME owners are often also the founders of the business, the hands-on approach many owners take in the day-to-day affairs of their business, their management skills and management style greatly influence the growth and development of their enterprise (Gagnon

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<sup>7</sup> Addis (2003) describes basic skills as literacy and numeracy skills as well as the ability to communicate effectively in a workplace environment.

et al, 2000; Peters, 2005). The entrepreneurs' creativity, ability to innovate, ability to communicate with employees, drive to seek out new market opportunities, and attitude towards risk are all important factors in determining the overall competitive position of SMEs (Peters, 2005; Wickham, 2006). Therefore, management skill development, an area which is often seen as one of secondary importance for SMEs (Fitzsimmons and Fitzsimmons, 2003; Coetzer, et al., 2011)), is an essential component of a successful SME's business strategy (Libutti, 2000). Yet despite the well-documented link between the learning process of entrepreneurs and the development of their firms (Deakins and Freel, 1998; Watts, et al., 1998; Cope and Watts, 2000), management development still lacks in many SMEs (Thomson and Gray, 1999; Patton and Marlow, 2002). This becomes especially problematic when firms experience significant growth and management skill development lags; like other core areas of a business, the array of skills SME managers require to ensure that the business is successful must evolve to reflect the growth stage of the business (Churchill and Lewis, 1983; Jayawarma, et al., 2006).

### ***Summary***

As the review of competitive theory literature has demonstrated, a number of factors go into determining a business' competitive position. Whether a firm is small, medium-sized, or large, it must be able to identify, exploit, and maintain a competitive advantage over its rivals in order to be successful. SMEs are often in a category of their own when it comes to factors that affect their competitiveness, and as a result, assessing their ability and readiness to compete requires an evaluation of factors that may not necessarily be vital to big business competitiveness.



For SMEs, the characteristics of the external environment will be important in shaping how firms position themselves within it; in particular, how they address issues of risk management, stay up-to-date with developments in the regulatory environment, secure adequate financing, take advantage of industry clusters, and address matters relating to human resources both in terms of skilled labour and management skills development. All these factors must be incorporated into a firm's strategy if it to achieve success.

In the next section, a key part of the external environment for SMEs operating in Interior British Columbia's value-added sector – the forest sector as a whole – is examined.

## **1.3 British Columbia's forest sector**

### **1.3.1 The forest industry in British Columbia**

For over a half-century, forest policy in Canadian provinces has emphasized some form of sustained yield timber planning mechanism as a means for supporting communities by ensuring that there is an even flow of timber (Haley and Luckert, 1995). The central goal of the development of the forest resource has been the provision of economic benefits, with particular attention paid to jobs (Niquidet, et al., 2007). Throughout the history of British Columbia's forestry industry, the focus has been on the volume of timber extracted rather than the value of the final good produced from the forest resource.

Major primary manufacturers in British Columbia have seen most of their growth over the last 30 years come as a result of mergers and acquisitions (Roberts, et al., 2004). The consolidation of the industry, according to Roberts, et al. (2004), has come as a result of larger companies looking for synergies in order to minimize costs and maximize efficiency. As Cathro,

et al. (2007) point out, consolidation of the lumber industry has led to a reduction in the number of small mills as a result of major, vertically integrated forest products companies opting for “super mills” closer to markets (p. 63) to take advantage of scale economies and bargaining power; but this too has also employed a volume-based approach rather than value (Nelson, et al., 2009).

### ***International Markets***

In 2006, Statistics Canada reported that approximately 80% of lumber production in Canada was exported with 80% of total lumber exports being shipped to the United States (Dufour, 2007). While exports have allowed Canadian manufacturers to explore new markets, the risk associated with being so reliant upon the United States manifested itself in the wake of the 2008 recession. The collapse of the American housing market has been particularly hard on forest product manufacturers, with its effects continuing to be felt throughout the industry<sup>8</sup>. So strong is the influence of American housing starts on Canadian lumber exports, it is of greater importance to bilateral trade than the exchange rate (Baek, 2011). Partially as a response to frail economic conditions in the United States and strong demand from China, Canadian log and lumber exports, particularly British Columbia’s, have been increasingly geared towards Asian markets in recent years (BCMofLNRO, 2011).

While expansion into Asian markets has countered, to an extent, lackluster American demand, the fact remains that the main product basket offered by the British Columbian forest sector is a highly commodified one. As international competition in the commodity lumber

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<sup>8</sup> New single-family home sales fell to a new record low in February 2011 (Buehlmann, et al., 2011).

market intensifies, prices for commodities like dimensional lumber continue their downward trend, and access to economic timber supply becomes increasingly restricted (Roberts, et al., 2004). In response, a wide range of experts (academics, analysts, government) have called for a move away from a commodity, volume-based focus towards a focus on deriving greater value from forest resources have been tabled (e.g. Roberts, et al., 2004; Schultz and Gorley, 2006; Working Roundtable on Forestry, 2009).

### ***Value-added forest products***

The value-added sector of the forest products industry is broadly defined by Schultz and Gorley (2006) as wood products manufactured beyond boards and dimension lumber, spanning from sorting for grade to making high end goods like furniture or cabinetry. In a survey of the sector in 2006, Stennes and Wilson (2008) found that approximately 20% of firms in the sector were primarily remanufacturers, 18% were log home and timber frame builders, 14% focused on millwork, and nearly 12% on engineered wood products; the rest of the population was distributed among firms producing cabinets, furniture, pallets and containers, and shakes and shingles. The 2006 survey also found that nearly 95% of firms had 75 employees or less (Stennes and Wilson, 2008).

According to Schultz and Gorley (2006), the large number of small value-added manufacturers in the province has the potential to create more competition for raw materials which they posit will lead to a more market-based mechanism for pricing timber. Another perceived benefit of the value-added wood manufacturing sector is its ability to do more with less; that is, as economic timber supply becomes increasingly hard to come by (especially in the

Interior), the sector has the potential to offset some of the setbacks expected to be experienced in the primary processing sector (Schultz and Gorley, 2006). This notion is seconded by Stennes and Wilson (2008) who state that the level of economic activity associated with harvested timber under value-added is superior to that of commodity product manufacturing (p.1). Some of the other benefits associated with a strong value-added sector are a better investment climate due to the higher margins, more customer brand loyalty with non-commodity products, and resilience to commodity market cycles (Shultz and Gorley, 2006).

Some industry players are skeptical about the promise of the value-added sector as the way forward. Russ Taylor, president of Wood Markets International Group, argues that the British Columbian forest industry is a commodity business and will remain as such; that value-added forest products are not suited for British Columbia's softwood industry (Nielsen, 2011). However, the most widely embraced view has been a call for a larger, more active value-added forest products sector in British Columbia in order to generate more value from the forest resource (Kozak et al., 2003; Parfitt, 2005, 2011; Shultz and Gorley, 2006).

Many value-added firms struggle to meet their growth prospects (Kozak and Maness, 2005). Numerous value-added firms report inability to find skilled workers as the biggest impediment to growth along with taxation policies and increased competition (Price Waterhouse, 1992; Delong, et al., 2007; Stennes and Wilson, 2008). Kozak, et al. (2003), highlight that the value-added sector is very heterogeneous and different factions have different characteristics, yet all sub-sectors seem to have lumber procurement problems of one form or another. Studies by Nelson, et al., in 2006, and Parfitt, in 2005, looking at the impacts of the termination of the Small Business Forest Enterprise Program's bid proposal program in 2003, indicate that the elimination of the bid proposal program has resulted in declines in labour and capital employed, and

subsequent reductions in value-added product exports (Niquidet, et al., 2007). Stennes and Wilson (2008) also note that although there have been improvements in adoption of the internet as a tool for doing business since Kozak (2002) reported that wide-scale adoption of e-business was lagging, they find that only 24% of surveyed firms used their websites for sales; a factor which could also be limiting their growth, particularly in foreign markets.

### 1.2.1 Forest policy in British Columbia<sup>9</sup>

For SMEs operating in British Columbia's forest products sector, staying up to date with developments in government policies, acts and regulations as well as keeping track of all applicable policies can be challenging. By the early 1990s, British Columbia's provincial government estimated that six federal acts, twenty provincial acts, over 700 provincial or federal regulations and 3,000 guidelines governed activities related to forest and range management in the province (Association of BC Forest Professionals, 2009).

In British Columbia, where 95% of the land base is publicly owned (Haley and Nelson, 2007), the foundations of forest policy lie in the tenure system and the various forms of tenure available to businesses in the forest industry. Due to its ability to create incentives and disincentives for investment and innovation, Vertinsky and Luckert (2010) see forest tenure as one of the most important instruments available to policy makers. Historically, a number of tenure arrangements have been devised to meet a range of socio-economic goals like increasing local and regional employment, increasing the value of the forest resource, and providing incentives for small operators (Niquidet, et al., 2007).

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<sup>9</sup> For a detailed timeline of relevant policy developments in British Columbia since the Pearse Royal Commission in 1976, see Appendix I.

### ***The importance of forest tenure in British Columbia***

When looking at how the tenure system is so deeply rooted in British Columbia's forest policy and why forest tenure is seen as a central factor, an "evergreen matter" of public debate throughout Canada according to Kant (2009, p.6), and a steadfast topic at conferences throughout the world, one is naturally driven to ask "*why?*". A number of studies have looked into this question, with findings ranging from timber supply security (Kuuluvainen, et al., 2006) to facilitating access to credit (Demsetz, 1967); however, these realities may be undergoing changes. Block and Sample (2001) as well as Kant (2009) note that there have been changes in the long held perception that tenure title was an essential part of the procurement of relatively low cost timber. In their studies of various countries in the sub-Saharan, both Besley (1995) and Sjaastad and Bromley (1997) found that firms tended to invest and seek out credit in order to enhance their level of tenure security. While Canada's tenure system differs from many other jurisdictions because its tenure arrangements are primarily leases as opposed to outright ownership, the economic theory behind the entitlement of tenure should still hold true. As Vertinsky and Luckert (2010) allude to, secure and transferable tenure plays an important role in the activities of forestry firms in Canada. They point out that inefficient producers are often willing to sell their tenure rights to more efficient producers thereby using the tenure rights as a form of leverage in negotiations. . Ultimately, the issue of forest tenure is likely an important one for the value-added sector, but the verdict is unclear as to how it plays out and influences firm decision; while it is clear firms need fibre to produce their products, it is unclear whether they need tenure.

Historically, the policy most tied to delivering fibre specifically to the value added sector was the Small Business Forest Enterprise Program (SBFEP) launched by the British Columbia

government in 1980 as part of the new Forest Act (1978). Integral to the policy was the view that raw material was the critical factor for value-added success, so the program's ultimate goal was to address issues relating to access to the forest resource.

### ***Small Business Forest Enterprise Program***

Drawn up to facilitate entry to new small logging outfits and manufacturers, the SBFEP was particularly aimed at small forest enterprises geared towards job creation and value-added products (Niquidet, et al., 2007). The SBFEP, commonly referred to as the *small business program*, awarded short-term timber sales licenses through competitive sealed bid auctions that were open to three types of registrants: *category 1* – market loggers, who were in the business of timber harvesting, but not processing; *category 2* – sawmill owners without replaceable tenure, value added primary processors and lumber remanufactures; and *category 3* – registrants with no mill or processing facility, but who intended on building one (Forest Act, 1999).

Registrants could bid on two major types of sales- section 20 sales, which were awarded solely on the basis of the highest bid; and section 21 sales which were geared towards value-added firms, where the criteria for the evaluation of proposals included revenue and non-revenue considerations. Section 21 sales, or bid proposals, had the potential to provide enough leverage to value-added manufacturers for them to capitalize their operations with transferable timber sale licenses which could be used as a business asset and serve as a source of collateral (M'Gonigle and Parfitt, 1994). See Table 1 below for a breakdown of the criteria used in awarding bid proposals.

**Table 1      Criteria and weighting for evaluating bid proposals**

Criterion	Weight
Employment	30%
Revenue	20%
Change in value-added	15%
Existing plant	10%
New capital investment	10%
Proximity	10%
Labour value-added	5%

Source: Niquidet, et al., 2007

While many firms in the value-added sector saw the SBFEP as vital to their success and survival, the program as whole did not result in significant growth for the sector; in fact, in the final years of the program's existence, value-added production in the province stagnated (Parfitt, 2005). In 2000, Peter Woodbridge and Associates reported that the value-added sector in British Columbia had less than a one percent share of the North American market for its products despite, according to the report, having a realistic potential of capturing at least 5% of the market.

### ***British Columbia Forestry Revitalization Plan***

The Provincial government introduced British Columbia's Forestry Revitalization Plan (FRP) in 2003, which aimed to bring a market-based approach to various forest policies. As part of the FRP, major licensees had 20% of their allowable annual cut (AAC) taken away – subject to compensation – with 10% reallocated to smaller-scale tenures (BCMof, 2003). The goal of this was to create a competitive market for fibre that would also contribute to a competitive



pricing system for timber. These small tenures were targeted to particular groups like community forests or First Nations, but not firms.

At the same time the government of British Columbia axed the SBFEP and its non-revenue bid proposals and introduced the British Columbia Timber Sales program (BCTS) which awards timber solely on the basis of price (Niquidet, 2008). BCTS was the beneficiary of the other half of newly available timber volume that came as a result of the province-wide tenure reallocation from major licensees<sup>10</sup>. It is important to note that under BCTS, restrictions on who could bid for timber (i.e. - only value-added firms) that were central to the SBFEP were eliminated.

Investigations of the impacts of the FRP-related tenure reforms have been undertaken and demonstrate that despite it still being too early to definitively evaluate the reforms, they did appear to leverage the processes already in place (Nelson, et al., 2006) and although a number of forest sector-dependent regions are likely to experience net income losses, the overall reform exercise is emerging as a more efficient means of allocating timber (Niquidet, et al., 2007). The goal was to develop a competitive market for fibre allowing it to flow to the highest bidder and the best use; however, consolidation reduced the competitiveness of the market. When assessing the overall impact of the FRP on publicly traded forest companies, Niquidet (2008) found that the announcement of the FRP, coupled with the loss of forest tenure, led to significant negative returns for a number of firms. Niquidet's study did not explore the effects of the tenure reform on smaller, private forestry enterprises.<sup>11</sup>

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<sup>10</sup> Major licensees were characterized as those with more than 200,000m<sup>3</sup> of replaceable AAC (BCMoF, 2003).

<sup>11</sup> While a number of other forms of tenure have undergone changes in recent years, they are not discussed here as they tend to have limited direct significance on small, value-added firms. Numerous other sources are available for further breakdown of the different tenure types (Luckert and Haley, 1990; Cashore, et al., 2001; van Kooten and Folmer, 2004; BCMoFR, 2005). For a breakdown of the distribution of different tenure arrangements in British Columbia, see: <http://www.for.gov.bc.ca/hth/timber-tenures/apportionment/index.htm>.

At the same time, offsetting some of the effects of significant reallocation due to the FRP, most of the economically accessible timber in British Columbia is still controlled by the major licensees who have continued the trend of consolidation, closing smaller mills and concentrating on larger mills in their pursuit of efficiency through economies of scale (Cathro, et al., 2007). With increased consolidation comes a drop in competition for the resource and the end result is that a larger portion of the provincial AAC is controlled by a smaller number of firms (McNaughton, 2010).

### ***Mountain pine beetle epidemic***

The mountain pine beetle (MPB) epidemic devastated forests throughout the British Columbia Interior and is expected to lead to reductions in harvest levels and have significant negative economic and employment impacts for many communities in the medium-term (Central 1, 2010). This wide-spread forest disturbance is of particular importance in the Central Interior where, despite the epidemic being officially declared over by the Minister of Forests, the impacts on timber supply are currently being felt and are likely to continue into the mid-term. As Watson (2006) points out, the killed or damaged stands are quickly deteriorating and there is much pressure to recover as much economic value from the stands as possible. As a result, the Chief Forester for the province has temporarily increased allowable annual cut (AAC) in order to allow for greater salvage harvesting. While the uplift in AAC has resulted in increased employment in the short-term, the expected reduction in AAC when the epidemic has passed and salvage logging is no longer an economically viable option will likely lead to another round of significant job loss in the sector (Central 1, 2010). While some studies have looked at the expected extent of the changes to timber supply and employment to come as a result of the MPB

epidemic (Patriquin, et al., 2007; Patriquin, et al., 2008), Schwab, et al., (2009) highlight the fact that these do not look at the transitional processes local economies will face as they adjust to the new timber supply realities.

While the MPB epidemic has devastated Interior forests, in recent years, due to the uplift in AAC, there has been an abundance of wood at relatively low cost. This highlights the fact that while the timber profile may not have been ideal for some SMEs in the value-added sector (i.e.- those looking for cedar or fir, for example), the lack of wood in and of itself has not been the limiting factor to firm success; although fibre supply shortages may become a reality firms will have to deal with in the future.

### ***Canada-US softwood lumber dispute***

Being one of the world's leading exporters of wood products and softwood lumber (Cohen, et al., 2003) and a close neighbour to the United States (US), the world's leading importer of goods (World Trade Organization, 2010), Canada's forest sector has very important trade relations with the US. However, given the differences in institutions that govern timberlands (primarily public in Canada, versus primarily private in the US) and further divide in the manner in which timber prices and logging rights are determined, a long-standing trade dispute over the export of Canadian softwood lumber to the US has become an established issue in Canadian forest policy, particularly in British Columbia. For a long time, Canada's stumpage system, which administered stumpage fees rather than letting market forces determine prices, was at the heart of the dispute (Begley, et al., 1998). The policy changes introduced in British Columbia's Forestry Revitalization Plan came partly, or wholly, as an attempt by the provincial government to increase market access to the US (Niquidet, 2008). That being said, Niquidet

points out that the move to a more market-based approach to timber allocation and stumpage determination failed to grant British Columbian exporters unrestricted access to US markets as the 2006 Softwood Lumber Agreement (SLA) between Canada and the US still limits Canadian access to American markets (2008). The latest agreement, signed in 2006, which extends to 2013 with an option to prolong the agreement to 2015 (the agreement has been extended to 2015), has failed to put an end to the frequent calls for countervailing duties and claims of dumping by Canadian exporters (Random Lengths, 2010). A number of complaints alleging that certain provinces had violated their quota and taxation agreements and that some provincial forest industry aid packages conveyed subsidies to producers led to arbitration cases argued through the London Court of International Arbitration (Foreign Affairs and International Trade Canada, 2009). Recent quarrels between the two nations should not come as a surprise. van Kooten noted in 2002 that due to the issues at the core of the dispute, which have remained more or less the same for the better part of the last century (Random Lengths, 2010), US efforts to restrict Canadian imports of softwood lumber should be expected to continue well into the future.

Value-added firms exporting to the US have been directly impacted by the softwood lumber dispute. In the softwood lumber agreement signed in 1996, (SLA I) which lasted until 2001, where producers were entitled to quota exemptions if they produced high value-added products, Stennes, et al. report that value-added producers shifted to higher value-added products in order to qualify for exemptions (2005). They argue that, overall, the first softwood lumber agreement was generally favourable for Canadian value-added manufacturers exporting to the US.

Following a five year period of frequent disputes between Canada and the US, the two nations signed the second softwood lumber agreement (SLA II) in 2006. When compared to SLA

I, SLA II is not as favourable for the Canadian value-added sector. While value-added producers still qualify for certain exemptions, they must pay taxes on their exports. With exemptions tied to issues of forest tenure and remanufacturing of primary wood products, a number of value-added producers in British Columbia have restructured their operations in order to remain competitive under SLA II (PricewaterhouseCoopers, 2007). Restructuring efforts included increasing production of exempt products, expanding domestic markets, and delaying expenditures to mitigate the impact of shrinking margins (p.25). Firms taking these steps were located mainly in the Southern Interior and Coast Forest regions of British Columbia.

#### **1.4 Resource-dependent communities**

Much as the policy environment is important in influencing the availability of timber, the setting within which value-added firms operate, the communities in which they are located or which are near-by, also have an important influence on factors such as labour supply or the availability of financial institutions. Regional and community-level strategies will have tremendous impact on SMEs, especially in resource-dependent communities where SMEs often rely on community networks in the day-to-day operations (i.e.- relationships with primary manufacturers for fibre supply).

Throughout Canada, many local and regional economies rely on natural resource exploitation as their sole economic engine. In British Columbia, and particularly in the province's Interior region, many communities are extremely dependent on the forest. The strong socio-economic ties to the forest in British Columbia, and in the rest of Canada, are not new developments- Statistics Canada reported that in 2011, nearly 600,000 Canadians' employment

was dependent upon the forest industry<sup>12</sup> (2012). It should be noted however, that in 2001, employment figures for the forest industry were much higher with an estimated 873,000 workers. Given that so many people's livelihoods are so closely linked to forest resources, a number of researchers have examined the relationship between natural resources and the socio-economic realities faced by communities and regions that depend heavily on the natural resources.

Perhaps as important an external factor as the forest sector policies discussed above, the community in which an SME in the value-added sector operates plays an important role in the determination of strategy and, subsequently, competitive position. For example, while smaller communities tend to have relatively limited pools of skilled workers, community or regional investments in infrastructure, can be beneficial in attracting and retaining skilled workers thus mitigating a potential barrier to success (Fox and Porca, 2001). Communities may also wish to take measures to attract firms of a certain industry subsector which has the potential to not only expand the economic base, but also create the right environment for the development of industry clusters. A good example of this in the value-added sector is the community of 100 Mile House, in the British Columbia Interior, marketing itself as the “*Handcrafted Log Home Capital of Canada*”<sup>13</sup>.

To ensure that forest-based economic development is pursued in a sustainable manner, it is important to consider the impacts on the community and on the forest resources, as well as to get a good sense of whether or not community members' perceive the proposed development strategy is a good one (Brennan, et al., 2005). A number of studies highlight the fragile equilibrium in which forest resource-based operators must operate, citing the oft delicate nature

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<sup>12</sup> Includes direct, indirect, and induced employment.

<sup>13</sup> See: <http://www.100milehouse.com/>

of balancing the pursuit of economic well-being with sustainable resource use (Egan and Luloff, 2000; Gamborg and Flemming, 2004). Brennan, et al., (2005) see these factors as potentially benefiting small, locally owned entrepreneurial forest ventures as they are likely to be more attuned to their communities' concerns. Yet despite what may be a favourable operating environment for SMEs, the road to success for small firms remains a challenging one.

While economic development is often associated with business start-ups and job creation, Fritsch (2008) draws attention to the fact that while new businesses may create supplementary positions needing additional personnel, the net effect on the number of jobs in the economy is not necessarily positive. The combination of competition and market selection make it very difficult for SME start-ups to prosper (Boeri and Cramer, 1992; Fritsch and Weyh, 2006), and those who do may actually crowd-out incumbents. Alluding to Schumpeter's (1911) idea of *creative destruction*, Fritsch (2008) argues that in many cases, one of the keys to a successful business start-up is actually the demise of well-established firms potentially leading to no net creation of jobs, perhaps even to an overall reduction in the number of jobs in the economy.

### ***Forest-dependent community assessment***

Though the term "community well-being" is often used in assessing levels of community development, particularly in the case of resource-dependent communities, a number of studies define well-being differently and the indicators used in trying to assess community well-being differ depending on the definition used. In his overview of the different methods of assessing community well-being, Kusel (1996) argues that community well-being cannot be assessed using country-level analysis. He argues that emphasis should be on individuals, communities, and the

capacity available in those communities. The key, he posits, is the examination of capacity which looks at how individuals within forest-dependent communities create opportunities for themselves that improve overall well-being and leverage the achievements of community members. Halseth (1999) looks at community well-being from the point of view of a population geographer and examines employment migration in small, resource-based, communities in British Columbia's Cariboo region. The study identifies worker and family migration as important factors in community dynamics and ultimately in the presence of a sense community (or lack thereof). In assessing what motivates household migration to and from rural resource-dependent communities, the author finds that economic and employment opportunities are often catalysts for migration.

Numerous studies have reported that forest dependence and community well-being are negatively correlated (Fisher, 2001; Rural Sociological Task Force on Rural Poverty, 1993; Stedman, et al., 2005). A study conducted by the Rural Sociological Society's Rural Task Force (1993) suggests that such a correlation is likely a result of a combination of underinvestment in human capital, peripheral industries<sup>14</sup> providing employment, bureaucracy, and pressure from outside parties lobbying against the extraction of resources. While recognizing that increased forest dependence tends to indeed be associated with lower levels of education, higher unemployment and family poverty in Canada, Stedman, et al. (2005) demonstrate that there are significant variations among different forest regions as well as among different forest sectors<sup>15</sup>. For example, the study results show that forest dependence, taking into account all forestry-related activities, is actually associated with lower levels of poverty in British Columbia and

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<sup>14</sup> The study describes "peripheral industries" as those that offer low wages, limited benefits, and part-time work only (Rural Sociological Task Force on Rural Poverty, 1993).

<sup>15</sup> The authors break "forest dependence" into reliance on: 1) all forestry, 2) logging, 3) services, 4) lumber, and 5) pulp.



Atlantic Canada. Within these regions however, there is variation amongst forest sectors: British Columbia's services and lumber sectors appear to be linked to decreased community well-being, whereas the logging and pulp sectors have positive relationship with overall community well-being (Stedman, et al., 2005, p. 218). These results support the argument posited by Averitt (1968), Overdevest and Green (1995), and Stedman, et al. (2004) that certain facets of forest reliance behave like "core" industries. That is, that they tend to be associated with increased income and well-being (Stedman, et al., 2004).

British Columbia's deviation from national forest dependence trends was explored in detail by Parkins, et al. (2003) who, like Overdevest and Green (1995) and Stedman, et al. (2004), consider forestry firms to be at the centre, or core, rather than on the periphery. To explain logging's positive correlation with poverty reduction, the authors point to the skill level required to log in British Columbia. Loggers in British Columbia are often faced with timber extraction methods (rough terrain, steep slopes) that require a higher level of skill than conventional logging in other parts of the country, and subsequently command higher wages (Parkins, et al. 2003). The study also notes that the large number of unionized forest workers, along with the distribution of high wages due to vertical integration of many companies in the province, may explain why forest dependence in British Columbia is associated with greater economic well-being.

Given their reliance on one economic engine, single industry resource-based communities are often seen to be more vulnerable to risks and disasters (Humphrey, et al. 1993; Flint and Luloff, 2005). Should the forest industry experience hardships, communities closest to the raw material, which are often, as Flint and Luloff (2005) put it, "little more than timber extraction corporate satellites" (p. 400), tend to be the ones who suffer the most (Marchak,

1983). Local empowerment as a strategy for mitigating such risks is presented by a number of studies (Flint and Luloff, 2003; Freudenburg, 1992; Gray, et al., 2001; Luloff and Swanson, 1995).

### ***Forest-dependent community sustainability***

The stability of forest-dependent communities has long been an issue of importance in policy-making arenas. As Beckley, et al. (2002) point out, for decades forest policy makers saw employment- often used as a proxy for community stability- as a function of timber supply (p. 627). The main downfall of this notion, the authors argue, is that it failed to consider the effects of input substitution. As technological advances in the industry led firms to favour machine power over man power (labour), the end result was a decrease in jobs despite an increase in timber availability. With certain subsectors of the value-added wood products offering higher jobs per cubic metre ratios than the primary manufacturing sector (Stennes and Wilson, 2008), it can be argued that the value-added sector provides some relief from the structural changes occurring in the forest products industry.

As the focus shifted from *stability* to *sustainability*, more concerted research efforts were put towards understanding the concerns of forest-dependent communities and their relationship with resource extraction moving forward (Lucas, 1971; Marchak, 1983; Beckley, 1995; CCFM, 1997). Kusel (1996) looks to community capacity as one avenue through which to assess the level of, and move towards, community sustainability. Kusel (1996) evaluates community capacity based on the availability of physical capital, human capital, and social capital. This puts an emphasis on the community as a whole rather than simply on the firms operating in the community. Echoing themes discussed above, while firms are indelibly integral parts of a

community, they can also be very dependent on a community's strategy towards attracting and maintaining different types of capital. Brennan, et al. (2005) posit that community leaders and organizations would be well-advised to focus their efforts on promoting and fostering relationships amongst local stakeholders to ensure that local concerns are taken into consideration when forest-related economic growth strategies are developed; this notion was further reinforced by Kozak, et al. (2008). This, they argue, will lead to greater buy-in on the part of community members and lead to more sustainable communities in the long-run. In the British Columbian forest products sector, small, locally-owned and operated firms would seem to be ideal vehicles through which to engage local community members, employers, employees, and government officials in the sustainable development dialogue encouraged by Brennan, et al. (2005).

## **1.5 Objectives**

As the review of relevant literature has demonstrated, the development and competitive position of firms in the value-added forest products sector remains an important piece of British Columbia's forest policy goals. Yet at the same time, careful analysis of what factors influence their success has been lacking. The success of SMEs in the value-added sector is dependent on factors ranging from managerial skills development and skilled labour availability to timber supply security and the ability to secure financing. While the focus of various government policies has been on timber supply, the skills and capacity development side of the equation, or the intangibles, have been lagging. Long touted as the new direction of British Columbia's forest products sector, the value-added sector has the potential to thrive in Interior British Columbia

forest-dependent communities as its ability to generate a greater level of economic activity per cubic metre will no doubt help mitigate the effects of a looming reduction in timber supply on local and regional economies. In order to capitalize on the sector's potential however, coordinated efforts bringing together the needs of the SMEs, effective forest policies, and community strategies are essential.

The goal of this research is to address the first of these conditions by assessing the factors leading to the success of SMEs in the secondary wood products sector, as well as identifying the barriers to competitiveness.

The main objectives of the research are to:

1. Develop a framework appropriate to analyze SMEs in the value-added sector.
2. Use the framework to determine which factors are key to SMEs' success.
3. Identify implications for businesses, policy, and further research.

## **2. Methods**

### **2.1 General approach**

The objective of this study was to explore the drivers and barriers to success in the secondary wood products manufacturing sector of British Columbia. As this was an exploratory qualitative study, whose focus was to examine what sets successful small and medium-sized firms apart from their struggling counterparts, the multiple case study method was deemed the most appropriate research strategy. The purpose of the study was not to generalize to the entire small and medium-sized enterprise (SME) population operating in the secondary wood products manufacturing sector, but rather to gain a strong understanding of the complexities of the cases and search for common or re-occurring themes, which could then be used in further research.

The decision to employ a multiple case study analysis was based on the research investigating a “contemporary phenomenon in-depth and within its real-life context” (Yin, 2009, p. 18) and drawing its data from multiple sources in order to develop comprehensive descriptions and analyses of the cases (Creswell, 2007). As Creswell (2003, 2007) and Yin (2009) point out, constructing a research strategy that incorporates representative cases as research subjects provides different perspectives on the issue or issues being studied. The characteristics of the secondary wood products manufacturing sector, which is composed of a large number of small, diverse firms, would have made drawing conclusions from the study near impossible had the research been conducted on a single case. Whereas a survey may have carried a lesser financial burden and reached a wider number of firms than individual case studies, the case study approach and its predominantly open-ended interview questions allow for the case study

participants to offer additional information and bring up areas of interest that may not have been previously identified in the literature review and included in a survey.

Despite the heterogeneous composition of the cases and their different perspectives, the multiple case study method sought to achieve external validity by “defining the domain to which the study’s findings can be generalized” (Kidder & Judd, 1986). As previously mentioned, this research did not seek to generalize to the population of SMEs in the industry sub-sector, but rather to find emerging themes among the selected cases (the domain). In order to generalize to the domain, replication logic was used where each individual case was treated as a stand-alone study with an individual case report followed by an analysis of cross-case conclusions and a cross-case report.

## **2.2 Case selection**

The study aimed to provide in-depth information and analysis on the key factors that separate successful SMEs in the secondary wood products sector from those firms who struggle. In order to best achieve the stated objective of the study, firms operating in the Central Interior region of British Columbia in or near a highly forest dependent community<sup>16</sup> were selected. The location was selected based on its forest dependent characteristics as well as due to the researcher’s familiarity with the area and the presence of a previously established local contact with vast knowledge of the community and the industry.

Using the latest Directory of Secondary Manufacturing of Wood Products in British Columbia prepared by the Canadian Forest Service’s Pacific Forestry, a list of all reported secondary manufacturers in the regional district was drafted to ensure that as many possible case

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<sup>16</sup> To preserve the confidentiality of the firms involved, the name of the community is withheld from the thesis.

study candidates were identified to ensure that no firm was overlooked in the selection process<sup>17</sup>.

To narrow the list of candidate cases, the local contact provided the researcher with a list of 9 local industry experts who were interviewed and asked to review the list of identified firms as potential cases and provide input as to which ones, on or off the list, they believe would offer the most insight. In total, eight cases were suggested as potentially interesting and willing research subjects.

The industry experts had a wealth of experience in the forest sector and collectively covered the spectrum of the forest sector in the region; Table 1 below provides an overview of the experts' background in the sector.

**Table 2 Forest sector expert backgrounds**

	<b>Government</b>	<b>Primary Industry</b>	<b>Secondary Industry</b>	<b>Forestry Consultant</b>
<b>Expert 1</b>		x		x
<b>Expert 2</b>		x	x	x
<b>Expert 3</b>		x		
<b>Expert 4</b>		x		x
<b>Expert 5</b>	x			
<b>Expert 6</b>	x			
<b>Expert 7</b>		x		
<b>Expert 8</b>		x	x	x
<b>Expert 9</b>	x			

<sup>17</sup> Not all secondary wood product manufacturers in British Columbia were included in the directory. Some firms elected not to respond to requests for company information and as such are not listed in the directory.

The selection criteria were based on the firms' competitive position at the time the research commenced. The eight suggested cases were divided into two categories: "successful" and "struggling". For the purpose of the selection process, success was defined as the achievement or active pursuit of management's goals (Beaver, 2003) and "struggling" firms were defined as those firms who were either lacking guiding objectives or had failed to achieve them. A careful review of each potential case's website (if available), relevant newspaper articles, other grey literature, as well as careful consideration of the forest sector experts' input, narrowed the potential cases further to the ultimate selection of four individual firms; two successful firms and two struggling firms. The narrowing down to four cases was due largely to the limited resources available for the research project. The diverse characteristics of the selected cases (summarized in Table 2) allowed for the study to incorporate different perspectives on the drivers and barriers to success in the secondary wood products manufacturing sector.

Firms were initially contacted by telephone to gauge interest in participating in the study, and were then provided with a formal invitation to take part in the research (see Appendix II). Prior to proceeding with any data collection, all participating individuals signed a consent form detailing the purpose and procedures of the study as well as the potential risks or benefits associated with participation in the study (see Appendix III). The signed consent forms were stored in a locked file folder in the researcher's office that was also locked.



**Table 3**                      **Characteristics of participating firms<sup>18</sup>**

	<b>Product</b>	<b>Number of employees</b>	<b>Years active</b>	<b>Current status</b>
<b>Firm A</b>	Custom remanufacturing	10 to 15	More than 20	Intermittent operations
<b>Firm B</b>	Timber frame houses, cabinetry, millwork	10 to 15	15 - 20	Operating full-time
<b>Firm C</b>	Engineered wood products, remanufacturing	More than 20	More than 20	Shut down
<b>Firm D</b>	Millwork, custom remanufacturing, engineered wood products	Less than 10	Less than 10	Operating full-time

## **2.3 Data collection**

Data was collected in a number of iterations where various types of data including academic literature, grey literature, focused interviews and in-depth interviews were collected. The initial step in the data collection process was a thorough review of relevant academic and grey literature. Using various electronic databases and archived printed material housed at the University of British Columbia and University of Victoria libraries, literature on subjects of relevance like firm competitiveness, entrepreneurial orientation, the secondary manufacturing sector, forest policy in British Columbia, and small business management were reviewed and are included in the literature review in Chapter 1 of the thesis.

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<sup>18</sup> To preserve confidentiality of the firms involved, their names, exact years in operation, and exact number of employees are withheld from the thesis. Firms were assigned generic names which will be used for the remainder of the thesis.

The second step in the data collection process consisted of a series of focused interviews with local forest sector experts. Focused interviews are open-ended and conversational, but generally follow predetermined questions from the themes and concepts identified in the literature review (Merton, Fiske, & Kendall, 1990; Yin, 2009). The purpose of these interviews was threefold: 1) to validate and add to the findings of the literature review, as they relate to the forest sector in the region; 2) gain a further understanding of the dynamics of the forest sector in the region; and 3) garner a list of potential candidates for the case studies. To facilitate the discussion, a timeline of relevant forest policy events was created and provided to the industry experts as an *aide-mémoire* (see Appendix I).

The length of the focused interviews ranged from 25 minutes to 56 minutes, with the average duration being just over 37 minutes. With the interviewees' prior consent, each interview was recorded using a digital recorder, and transcribed following the interview. All audio files and transcription documents were stored on the researcher's password protected computer at the University of British Columbia and backed up on an external hard drive.

After careful review of the focused interview transcripts, a further review of academic and grey literature was conducted to obtain further information on topics brought to light by the focused interviews, particularly with regards to matters pertinent to the local or regional context. This literature review was performed primarily using archived material at the University of British Columbia library and the community's local museum.

Following the literature review and focused interviews, in-depth, one-on-one interviews with the participating cases' owner-operators were conducted; these represented the main source of data collection for the study. In the in-depth interviews, participants were asked to give an

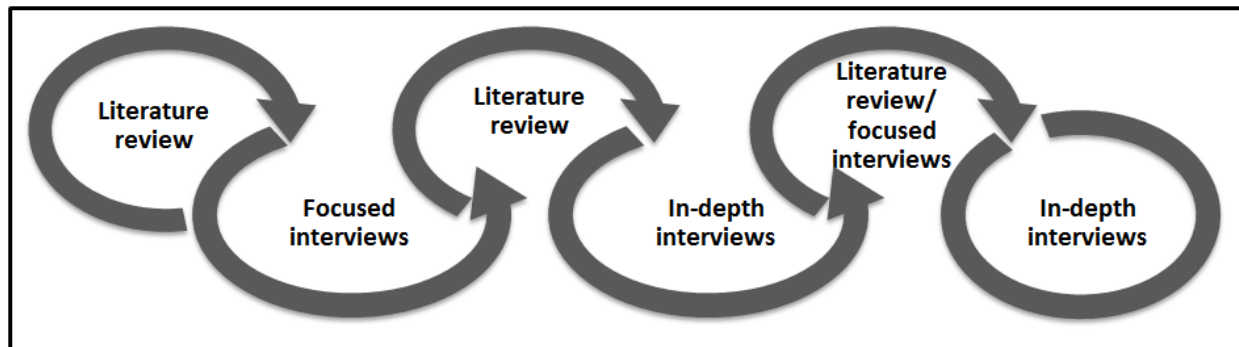
overview of the history, current situation and future direction of their enterprise. Rather than conducting the interview in a structured, question-and-answer manner, the in-depth interviews sought to cover a number of pre-identified themes and topics in a conversational manner.

Interviewees were encouraged to provide insights and opinions on the topics covered as well as delve into themes they deemed important to their firm, whether the themes had previously been identified or not.

Each owner-operator was interviewed twice, with approximately five months between interviews. The length of the in-depth interviews ranged from 58 minutes to 94 minutes, with the average duration being just over 73 minutes. As with the focused interviews, with the interviewees' prior consent, each in-depth interview was recorded using a digital recorder, and transcribed following the interview. All audio files and transcription documents were stored on the researcher's password protected computer at the University of British Columbia and backed up on an external hard drive.

In the time between interviews, interview transcripts and notes were comprehensively reviewed and a further literature review was conducted to gain a better understanding of new themes brought to light in the first round of in-depth interviews. The follow-up interviews reviewed points that needed clarification, explored certain themes from the initial interview in further detail, and provided the owner-operators with another opportunity to voice their opinions as to what they deemed the most important drivers and barriers to success for SMEs in their sector. The data collection process is summarized in Figure 1 below.

**Figure 1**      **Data collection process**



## 2.4 Data analysis

The data collection and analysis portions of the research were iterative processes. Each round of data collection, be it the literature review, the focused interviews or the first round of in-depth interviews, was carefully analysed to ensure that the data gathered was used effectively to collect information in the next step. After each interview, relevant literature was consulted to provide a deeper understanding of the emerging themes.

The data analysis was a four step process adapted from that suggested by Rubin and Rubin (1995). The four steps of the analysis procedure are described below.

**Step 1:** Once the data was collected, the interviews were transcribed from the digital recorder to Microsoft Word, a word processor. The interview material was carefully reviewed to identify themes and recurring topics and coded according to these themes and topics. Text summaries were created for each theme and irrelevant<sup>19</sup> themes identified in the interview protocol were dropped from the analysis. This resulted in the identification of six main themes to be used in coding (presented in Table 4).

<sup>19</sup> Themes were deemed irrelevant if interviewees did not discuss the themes sufficiently or explicitly stated that the issue was not of importance to their success or lack thereof.

Some of these themes and subthemes were deliberately discussed by the interviewer during the in-depth interviews as a result of the focused interviews and the literature review. Other subthemes were the result of the interviewees talking at length about certain topics that they viewed as important to their firm. While all the primary themes were touched on in each of the four cases, not all subthemes were addressed in each in case.

**Table 4** Themes and subthemes identified during the focused and in-depth interviews

Primary Themes	Subthemes
<b>Fibre Supply</b>	<ul style="list-style-type: none"> <li>• Tenure arrangements</li> <li>• Supply chain relationships</li> <li>• Interaction with major licensees</li> <li>• International competition</li> </ul>
<b>Financing</b>	<ul style="list-style-type: none"> <li>• Lending institutions</li> <li>• Cash flow</li> <li>• Provincial/National/Global economy</li> </ul>
<b>Skill</b>	<ul style="list-style-type: none"> <li>• Skilled employees</li> <li>• Management skill</li> <li>• Bookkeeping</li> <li>• Marketing and sales expertise</li> <li>• Competition from mining sector</li> </ul>
<b>External environment</b>	<ul style="list-style-type: none"> <li>• Land availability</li> <li>• Industry associations</li> <li>• Business development resources</li> <li>• Mining sector</li> </ul>
<b>Business Strategy</b>	<ul style="list-style-type: none"> <li>• Business plan</li> <li>• Mid-term vision</li> <li>• Risk management</li> </ul>
<b>Online presence (identified in focused interviews)</b>	Theme dropped
<b>Business culture (identified in focused interviews)</b>	Theme dropped

Throughout the data collection process, different themes of relevance to the SMEs in the value-added sector were identified. As Figure 1 demonstrates, the collection process was closely linked to the data analysis component of the research. The themes and sub-themes presented in Table 4 are the themes that were discussed at length in the in-depth interviews. Themes identified in the literature review were incorporated into the discussion, but they were dropped from the analysis if none of the four cases addressed them in any significant way (notably innovation). Two themes identified in the focused interviews, online presence and business culture, were explicitly tabled as discussion topics during the in-depth interviews, but were dropped from the analysis as all cases dismissed the topics as inconsequential to their firm's success or lack thereof.

**Step 2:** The interview material was then inputted into NVivo 8 qualitative analysis software. Using NVivo 8, transcripts were re-read and coded further based on previously categorized themes. Again, if themes were deemed irrelevant, they were dropped from the analysis. Additional analysis of the 6 primary themes and their text summaries revealed a number of subthemes (see Table 3).

**Step 3:** To ensure complete coverage and a thorough analysis of the interview material, a complete recoding of the original transcripts using the primary themes and subthemes was conducted. After this second round of coding, a new set of text summaries was drafted. These latest summaries are the source of quotations used in the results section of the thesis in Chapter 3.

**Step 4:** The final step in the analysis process was a verification of the accuracy of the interview summaries. To ensure that the interview summaries prepared in step 3 of the analysis reflected

the original content of the interview transcripts, each case study participant was sent a copy of the text summary drafted from the transcripts of their interviews. This gave participants an opportunity to provide feedback as well as to check the content for accuracy. All participants agreed that the summaries accurately reflected their statements in the interviews and no participant provided additional feedback.

### **3. Results**

This chapter examines each case study individually and provides an overview of the key findings in each. The individual case study findings are followed by a cross-case analysis exploring the common themes that emerge from the cases as well as the generalizable findings that can be applied to all four case studies.

#### **3.1 Firm A**

##### **3.1.1 Firm description**

Firm A is a family-run operation located within the city limits of the community of interest for the research. The firm has had the same owner-operator since its inception (Owner A). While the firm is operational, it operates well below capacity and struggles to find a consistent customer base. Its main product offerings are custom remanufactured timber products sold primarily to California fruit producers to be assembled into crates and furniture components again sold in the Western United States.

The current incarnation of the firm has been in operation since 2007 when it re-opened after a two year hiatus under bankruptcy protection and operates two or three days per week employing between 6 and 9 people. The original business was in operation from 1989 to 2005, but had to file for bankruptcy after a series poor investments starting in 2003. Although the focus of this case study is on the firm that has been operating since 2007, there are a number of lessons and themes that emerge from Firm A that existed from 1989-2005; as such, the results presented below focus mainly on Firm A post-2007, but valuable insights from the 1989-2005 Firm A are incorporated as well.



### 3.1.2 Fibre supply

Firm A is largely reliant upon the primary manufacturers for its supply of fibre. When asked about the impact of the trend of consolidation in the primary industry, Firm A's owner stated that his firm's buying power had greatly diminished as a result, "*we used to be able to shop around for wood. You know, go see a few people and get the best price. Now we have two options; and both are too expensive.*" (Owner A, 2010). This indicates that while fibre supply is an issue for Firm A, the issue is not so much the availability of fibre itself, but rather the availability of affordable fibre.

To partially meet its fibre supply requirements, the firm acquired a non-renewable volume-based forest license in 2009, but failed to act on the harvesting rights. As the owner pointed out, the costs associated with harvesting, transportation and primary processing proved to be too great for the firm to be able to turn a profit. As a suggested means of addressing his fibre supply issues, Firm A's owner, speaking in 2010, said, "*I'll apply for Section 21 sales next month, I think*". It must be noted here that Section 21 sales<sup>20</sup>, which were part of the Small Business Forest Enterprise Program (SBFEP), were eliminated as part of the Forestry Revitalization Plan in 2003. The notion that Firm A's owner was unaware that Section 21 sales had been eliminated for nearly a decade points to the fact that the Firm's inability to secure consistent fibre supply may be linked to the owner's lack of adequate understanding of the policy environment around fibre supply.

Although the owner argues that fibre supply is an impediment to the firm's success, he failed to articulate how things would be different for his firm if fibre supply woes were addressed. The fact remains that while fibre supply is an issue, a recent trend of inconsistent

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<sup>20</sup> Referring to section 21 of the Forest Act (1996).

orders and the threat of substitute products in the fruit crate market, like cardboard, are more important barriers to success than fibre supply shortcomings. In other words, the problems on the demand side of the equation appear to be more significant than those on the supply side.

### 3.1.3 Financing

The firm's financial situation is precarious. After growing steadily and establishing itself as a strong player in the market through the 1990's and early 2000's, the firm made investments of upwards of \$10 million beginning in 2003, essentially doubling capacity by making sawmill upgrades and adding a planer mill and making room for a potential of 150 full-time employees. The purpose of the 2003 investments was to create economies of scale to drive down production costs and allow the firm to become a price competitor in Asian markets. The plan was also to expand into commodity lumber, but as lumber prices began their downward trend soon after the investments were made, the venture never materialized. The potential for success was also thwarted by inadequate planning and strategy. No relationships were built with potential customers in Asian markets and a demand for the product was never clearly demonstrated. As a result, after a period of missed debt payments and accumulating interest, the firm had to file for bankruptcy in 2005.

During the period of bankruptcy protection, many of the firm's assets were sold off and by 2007, the firm was left with approximately half of its 2005 land and asset base. With the help of private investors and using personal property as collateral, Firm A re-opened its doors in 2007 under a new legal name, although most of the firm's advertising centred around the previous firm name. The firm's owner said he would like to get some loans to get some of his idling machinery running but admits that "*the banks will not lend [him] money*" (Owner A, 2011). The owner has

dealt with the Development Bank of Canada, Community Futures, as well as the Bank of Montreal for financing, but given that it was these institutions that financed the 2003 investments that resulted in the firm's bankruptcy, their reluctance to provide financial support is understandable.

When asked what the banks were looking for in terms of an application for a loan, the owner's response was, "*they want a plan for the next 5 years, or something. But this business does not work like that; you never know what will happen next year, so you can't have a plan.*" (Owner A, 2011). Much like the issue of fibre supply, whereas the financing issue may appear to be the lack of available financing options at first glance, a deeper analysis reveals that a lack of strategy for the future and a failure to demonstrate the ability to make loan and interest payments on time is truly at the heart of the inability to secure financing.

#### 3.1.4 Skill

Firm A's owner reported lacking skilled workers as well as noting his own skill limitations, "*I'm not the best at selling and dealing with money, you know, but I do my best. I'm a guy who makes things, not sells things*" (Owner A, 2011). That said, Owner A expressed an openness to attend small business training sessions should they be made available in the community. Highlighting financial and time limitations, he said he would consider registering for evening classes once a week if the classes were offered for free or at very low cost. Given that all of Firm A's marketing and sales is completed over the phone or in person, having some training in those core business areas would definitely be an asset for the firm.

The firm is also unable to attract skilled workers like millwrights and electricians despite always running an ad in the paper. The owner attributes the lack of skilled workers to “*people not being qualified and not really wanting to work*” (Owner A, 2010). When asked about the wages he offers potential employees, he stated, “*I pay minimum wage, sometimes a little more for really qualified people*” (Owner A, 2011). Failure to pay competitive wages may be a contributing factor to the hardships in attracting skilled workers.

The owner also mentioned that the state of his equipment and overall perceived safety of working in his business had been provided as reasons for workers to refuse work he offered them. When asked to elaborate on this, he replied, “*to me that is just an excuse that people give when they don’t want to work*” (Owner A, 2010). The current employment capacity is 20 full-time employees, although the average day sees between 6 and 9 workers.

### 3.1.5 External environment

The firm’s owner remarked that while he once supplied different markets in Canada, from Vancouver to Calgary, the American market will “*pay more for the product*” (Firm A, owner), so he sells only to the United States. He argues that there are too few people in Canada and too many mills already serving the market and, as such, there is no room for Firm A to carve itself a piece of the market.

Owner A views the arrival of China as a player in the demand for lumber as a major competitive hurdle for his firm. “*China will pay about \$80 more per thousand board feet than I can afford, so the [primary manufacturers] will sell to China rather than to Firm A*” (Owner A, 2010). Changes on both the demand and supply sides of the firm’s value chain have squeezed

the firm's profit margins, *"I used to be able to buy wood for \$2 and a sell it for \$10. Now I have to buy for \$5 because of China, and I sell for \$6 because of the markets"* (Owner A, 2010).

Reflecting on the hardships his firm is facing, Owner A believes that elected officials are not doing enough to help the situation in the community, *"everybody is in trouble: restaurants, big stores, little stores. It's not just forestry. The MLAs (Members of the Legislative Assembly) are not doing enough to help people"* (Owner A, 2011). When asked to expand on what he thought elected officials could be doing more, Owner A responded, *"Government can't give us money; they don't have enough money. But they do have logs. If forestry does well, then the whole community does well. So the MLAs should give forestry logs"* (2011).

### 3.1.6 Strategy

Firm A's strategy or lack thereof is the biggest barrier to its potential success. Goals are either absent or ill-defined. For example, when recounting the thinking behind the massive investments of 2003, Firm A's owner cited *"expanding to Asian markets"* (2010) as the primary motivation for the expansion. When asked about the market research that accompanied the desire to explore new markets, his answer was *"you know, everybody was talking about China, Japan, and India so I said – let's do it"* (Owner A, 2010). After the investments were made, the Firm refused to deal with brokers who were familiar with Asian distribution channels and opted to forge their way into the market themselves despite not having an online presence or people on the ground in Asia. However, the owner now recognizes the potential benefit of dealing with brokers and expressed openness to working with brokers to help address some of the firm's supply chain issues.

Looking to the future, things do not appear to be veering in a much different direction. The owner was adamant that “*in [forestry], you cannot make a plan for the future*” (Owner A, 2011). When asked about whether he had a plan in place when he first began the firm in 1989, the owner said that it was relatively easy to run a business when markets were good and he essentially “*rode the wave*” (Owner A, 2011) of high demand while times were good. There was never a real strategy in place, nor does there appear to be one now. Summarizing his plan for the short-term, he said “*I’ll give it a shot for one more year, and see how it goes*” (Owner A, 2011).

### ***Going forward***

Moving forward, Owner A points to two areas that are critical to the success of his firm: fibre supply and money. On the fibre supply side, Owner A expects to deal with some log brokers to help address his woes, though admittedly, somewhat reluctantly, “*ideally, I would do it all myself. I like to know what’s going and be in control.*” (2011). On the financial end, he recognizes that financing is not likely to come from the public sector, so he plans on sticking to his approach of seeking support from private investors and trying to obtain loans from the same three institutions he has dealt with in the past.

The development of a business strategy or business plan is not a primary concern for the owner who insists the exercise is pointless in the forest products sector. However, in order to determine fibre supply requirements and to secure a loan with financial institutions, Owner A will most certainly be asked to provide a business plan.

## **3.2 Firm B**

### **3.2.1 Firm description**

Firm B is a timber-framing company that has operated approximately an hour's drive from the community of interest since 1994. The firm began as a two-man operation that only operated in the summer months and slowly grew to a full-time enterprise that employs 12 people. The timber frame houses produced by Firm B are sold only in Canada and all timber frames are custom-designed for each client. The firm sells its product from Calgary to the east to the Gulf Islands in the west, and from Whitehorse to the north to the Kootenays to the south; though approximately half of all sales are completed within a two hundred kilometer radius from the community.

In recent years, the firm has seen its revenues grow by about 60% per year; a figure that is all the more impressive considering that this growth rate was achieved during the worst of the latest recession. Firm B is co-owned by two business partners; one who oversees the day to day operations of the firm and the other (Owner B) who splits his time between Firm B and another job in the community.

### **3.2.2 Fibre supply**

As a timber framing outfit, Firm B's fibre supply is comprised primarily of logs rather than lumber. Despite its heavy reliance on unprocessed logs, the firm does not have forest tenure to ensure a steady flow of logs. Rather, the firm relies on strong relationships along its supply chain, notably with small mills and log sorts.

“[The small sawmills and log sorts] *keep an eye out for us. They’ll let us know if they’ve got high quality wood,*” Owner B says. He adds that although the firm does not have any contracts in place with suppliers to ensure a steady flow of timber, Firm B does get preferential treatment from suppliers, “*guys would rather see the high quality stuff go to [Firm B] rather than have it go to a major mill who’s going to turn it into plywood*” (2011). This is due, in part, to the fact that Firm B pays a premium for logs. Owner B refers to the premium paid for the wood as the firm’s “*quality control department*” (2011). Paying premiums on logs and having strong relationships with suppliers has enabled Firm B to move to the top of suppliers’ list of potential buyers. As a result, the firm often receives notices from suppliers alerting them of material that may be of interest. In fact, Firm B has been in a position where they’ve had to decline wood that was perfectly suited to their needs because they had too much inventory, “*we don’t buy the whole, ‘we can’t get wood’ argument. It doesn’t come easy, but there are ways to get wood if you’re willing to pay for it; and being able to pay for it should be part of your business strategy*” (Owner B, 2011).

Owner B stresses the point that although the firm has good supply chain relationships, it embraces flexibility in its approach to secure wood. While Firm B would like to purchase all their roofing materials from a certain firm, it simply cannot be committed to that one particular firm; it must have other alternatives. If a supplying firm finds itself with inventory problems, it can prove to be a kink in the entire supply chain, so this is where some flexibility and diversity proves beneficial. “*If our regular supplier can’t produce for one reason or another, we can go to the log sorts. It’s more hit or miss with the log sorts, but you do what you can to make sure you keep your fibre supply steady*” (Owner B, 2011).



Although Owner B argues that, in his opinion, “*we can’t get wood*” is a poor excuse for struggling firms, he does believe the current make-up of the tenure system impedes the competitive process in the sector. He argues that the tenure system fails to cater to small firms that require limited volumes to keep their operations going, “*After all our growth, we still only need about 1000m3/year. So forget about BC Timber Sales or forest licenses, they’re just way too big*” (Owner B, 2011). Owner B believes that the Small Business Forest Enterprise Program (SBFEP) was the tenure arrangement that worked most favorably for small value-added manufacturers. “*When the section 21 sales were around, a few of the outfits in town really capitalized their operations with that. With all that timber to sell and trade after you bought it for a low price, some guys really made a good buck*” (Owner B, 2011).

When asked about whether Firm B could bid on a bigger sale and then sell or trade the logs, the owner argues that although it would be nice to be in complete control of the firm’s wood supply, the added burden of logging operations at a relatively large scale is not in the firm’s plans; the addition of logging operations on a scale large enough to deal with a BCTS licence would be akin to launching a whole new business, according to Owner B. “*The nice thing about the section 21 sales is that they were a manageable size for a small outfit,*” (2011) Owner B points out. In his opinion, the elimination of the SBFEP has left a void in the log market that has yet to be filled. He believes an expanded woodlot market and more private timberlands would greatly improve the competitiveness of the market for logs. According to him, the elimination of the SBFEP has most affected his firm’s growth potential.

### 3.2.3 Financing

While Firm B is doing well financially compared to many of its industry counterparts, Owner B does warn that financing “*could easily become an issue*” (2011). The nature of the business is such that the firm obtains only a few house building contracts per year; as a result, Owner B points out that one sale has the potential to either dramatically increase revenues, or dramatically decrease revenues. In the event of a sale not coming to fruition and the firm needing to seek external financing, Owner B believes that the firm would likely be able to obtain financing from the local Community Futures branch, a branch with which Firm B has dealt before.

While the notion that institutions like Community Futures are available to help firms in need is a comforting one, it is not Owner B’s ideal path. “*Community Futures is fine if you’ve got a solid business plan, but it’s extremely expensive financing. They serve the role they need to serve, but they don’t do it cheaply*” (Owner B, 2011). Despite voicing his concerns about the cost of financing with local institutions geared towards helping SMEs, Owner B did concede that it provides peace of mind to know that if the firm needed a loan to expand operations, local institutions would be there to help. Although the firm assumes that the local institutions would provide financing in the event of a need – they have successfully dealt with Community Futures before – Owner B recognizes that before any institution, local or not, agrees to assist with a firm’s financing, they will need to see a solid business plan. “[Community Futures] *have helped us out a lot before, but there aren’t too many friends in business- if a proposal doesn’t hold up on its own, regardless of the relationship behind it, it’s not going to fly. So we recognize the importance of getting our ducks in a row before approaching someone for a loan*” (Owner B, 2011).

For Owner B, the “ducks in a row” approach begins with bookkeeping; all quotes and invoices are prepared in-house, and year-end accounting matters are outsourced to an accountant. The decision to have an accountant deal with the year-end books stemmed from a realization that “[Firm B] *just didn’t have the time or, more importantly, the expertise to do that*” (Owner B, 2011).

### 3.2.4 Skill

As with many other firms in the region, Firm B has some challenges attracting and retaining skilled employees. Part of the challenge lies in the wages Firm B can offer relative to the wages offered in other industries – notably mining. “*We’re always looking for people, but we understand that if a mine is also looking for people, they’re likely to get the best workers. We just can’t match their rates.*” (Owner B, 2011). In order to compensate for their relatively lower wages, the firm is attempting to make the prospect of working for Firm B a career option as opposed to simply a job (Owner B, 2011). To achieve this goal, the firm is looking at different ways to make employment opportunities more attractive; among these are investments in employee training and a plan to match retirement savings plan (RSP) contributions. “*This,*” says Owner B, “*is really at the core of our strategy. We are always reflecting on and updating our strategy to make sure that we’re in a position to not only be a successful company, but also an attractive one to work for*” (2011). Owner B also strongly believes that the skillset of his employees and what they are able to accomplish with limited forest resources is where the true added value lies, “*We only need about 15 – 20 truckloads per year and our employment ratio is about 1 truckload per person year employed; now that’s value added*” (2011).

While Firm B does receive employment candidate résumés regularly, Owner B admits that “*only 1 in every 50 or so is actually what we’re looking for*” (2011). The firm relies on its website as a strong recruitment tool, both in terms of potential customers and potential employees. This ties in with the owners’ overarching view that attracting good employees and keeping those employees is closely linked to the firm’s overall marketing strategy and ultimate success of the firm. “*We need to be successful to be able to match [retirement savings plan] contributions and invest in our employees. That said, we need a good marketing strategy in order to be successful and we need a good crew to be successful, so it’s all interlinked*” (Owner B, 2011).

Owner B admits that while experienced skilled workers are great, managing their financial demands can be a difficult task. “*We’ve got a 60 year old timber framer right now. He’s great but he wants \$80,000 – can we afford that?*” (Owner B, 2011). The firm faces some important financial resource allocation questions. Whereas Owner B strongly believes in retaining skilled employees, he is also focused on the future of the firm and as a result must decide whether to maintain his current staff and their escalating financial demands, or go with less expensive labour that will need significant training to perform at a high level. “*For the price of our 60 year old timber framer, we can bring in three younger guys. But then who will train them? Will they learn fast enough or will it all fall apart? It’s a question of trade-offs and risk.*” (Owner B, 2011).

### 3.2.5 External environment

As mentioned earlier, Firm B’s success in attracting workers and customers is highly dependent on the external environment, Owner B believes that the community as a whole needs

to be involved in attracting new workers. *“There are a lot of skilled workers in Vancouver or on [Vancouver] Island, but they don’t want to come live in the area; there are a lot of misnomers about the area”* (2011). He believes the community’s recruitment and retention strategy can be improved by drawing attention to the vibrant arts and culture scene as well as making improvements to the local college; this, he says, would help draw more people to the area which would help all areas of the business. Owner B thinks an improved recruitment and retention strategy at the community level may attract enough workers to sustain services geared to the value-added sector. *“If we, as a community, can get a good-sized skilled labour force and demonstrate that this is a viable and attractive career path, then maybe we can get wood enterprise centre or something like that happening”* (Owner B, 2011).

Facilitating organizations, like Community Futures and the Development Bank of Canada (BDC) are also an important part of the external environment; Firm B has dealt with both organizations. Of the BDC, Owner B says, *“they helped us recognize that we really need to invest in marketing and making a name for ourselves. First we made sure we had a quality product and, naturally, the second step was to make sure potential clients knew about our product”* (2011). While Owner B agrees that they were helpful, he believes there are ways to improve the process, *“They will find consultants for you, but the mark-up is crazy. If they could just be paid to find the consultant and hook him up with the SME who needs him, that would be way better”* (2011). In addition to his complaint about the costs associated with Community Futures and the BDC, Owner B says the amount of paper work required in dealings with these organizations, particularly the BDC, is a big deterrent for SMEs with limited resources.

Touching on the operating environment within the forestry sector, Owner B believes the sector is not fostering innovation as well as it could, *“As far as innovation in the industry, I*

*really think that selling raw logs to China stunts innovation. Sure, you make a quick buck right there, but in the long run I don't think it's the solution. It's an easy alternative to having to innovate to stay ahead of the game"* (2011). That said, Owner B is optimistic that with increased global competition for commodity wood products produced by the primary sector, the value-added sector will gain greater attention and *"hopefully more resources as well"* (2011).

### **Land**

The most pressing issue for Firm B going forward is industrial land. *"Land is the biggest impediment to growth for us right now"* (Owner B, 2011). Located approximately one hour away from town, Owner B admits that there are a number of disadvantages with not being within the city limits, *"Our workforce is between 25 and 40, so most have children, or at least plan on having children so being that far away from town is not very attractive. They want their children to have neighbours to play with and all that stuff"*(2011). Additionally, from a business-to-client relationship point of view, the lack of proximity to town makes it difficult for customers to drop by.

Owner B says the issue is both a cost-issue and an availability issue. While there is some land available on the community's main industrial road, Owner B says that option is not optimal for Firm B, *"I would hate to take a customer through the dust bowl to get to the office. Everything is rusty and in really rough shape, so from a marketing perspective, that's not the direction we want to go"* (2011). As for land that is not in the community, but much closer than their current location, Owner B says that land is simply too expensive for a small business.

Working towards a solution to their land problem, the Firm intends to team up with some other firms and approach the regional district to encourage an expansion of light industrial

zoning regulations. Owner B cautions that he is not advocating for massive industrial encroachment into the surrounding natural environment, *“There is some land available but it’s beautiful grassland. We’ve got quite a bit of agricultural land around here and it would be a shame to put something industrial on there”* (2011).

### 3.2.6 Strategy

When assessing his firm’s attitude towards risk, Owner B believes that Firm B is more conservative than most, *“if we shut down, it’s not ideal, but it’s not the end of the world; we’re not over-invested to the point where we could lose everything”* (2011). Owner B argues that despite being successful, Firm B remains at the mercy of the economic environment and as a result needs to be cautious when making major decisions, *“If one mine comes in, it offers a bit of a buffer because we can capture some the extra spending that comes as a result of the mine; but then, on the other hand, if a major mill or a mine goes down, we’re stuck with all that overhead that added to cater to that inflated market. It makes for some interesting strategic planning.”*(2011). Consequently, he concedes that the Firm B does not capitalize as much as it could from a strong market, but when markets tighten, Firm B is not overly strained.

Despite recognizing that the external environment plays a major role in the firm’s success, Owner B stresses the importance of a well-devised, adaptable strategy. *“We are always planning on adapting. We’re always looking at the different things we can do. We don’t want to be just a timber frame company- that’s a huge buffer right there. Our strategy is when we’re shorter on timber frame work, we do more finishing work; we’ve made sure we have the skills to be able to do that.”* (Owner B, 2011) Owner B states that the firm’s strategy must address all areas of the business. *“Being able to meet clients’ demands at different stages of the supply chain*

*helps us attract new clients. It also helps us be a more attractive business to work for because guys know we don't lay people off as much as others might. It also helps to be able to show a bank that you've spread your risk and that you pretty much always have revenue-generating activities happening"* (2011).

Owner B says the firm's strategy ultimately comes down to capitalizing on every sale the firm gets, *"You've already sold the frame, sell the roof. Do the panels to lock it."* (2011). From his point of view, when the overhead resources required to complete a sale with a customer have been committed, the incentive is to provide more than just the timber frame in order to be as efficient as possible. By providing additional services like roofing and panelling to a timber frame sale, *"revenues shoot way up and the additional management and marketing costs are negligible."* (Owner B, 2011)

To ensure that customer satisfaction remains high, Owner B understands the importance of staying up-to-date with consumer demands and the technology developments that help in meeting those demands. *"More and more people are looking at green buildings, and, naturally, so are we. We are in a market that strives for innovation, so we have to be right there with the market. Essentially, we have the mindset that we need to be better at everything we do: be more knowledgeable builder, learn more about green buildings and design and implementation"* (Owner B, 2011). In order to do this, Firm B relies partly on industry associations like the British Columbia Log and Timber Building Industry Association and the Timber Frame Building Council; industry associations can *"do so much more than one small firm alone can because they are in-tune with higher level stuff that we wouldn't otherwise be aware of"*(Owner B, 2011) . Owner B uses the development of a safety manual as one example of how industry associations can be extremely beneficial, *"they developed a safety manual template for timber frame builders.*



*We never would have the time to write up a safety manual from scratch, but a template makes things so much easier” (2011).*

When asked to reflect on the importance of strategy, Owner B responds, *“It’s simply a necessary part of staying in business. That’s why so many start-ups fail: it’s easy to start a business; the hard part is keeping it going. You need a good book keeper, a good accountant, good employees, good marketing, good wood supply, good relationships along the supply chain.”*(2011). He argues that for firms in the value-added sector, who are often dependent on developments in the primary wood products sector and the mining sector, a good strategy must take into account a firm’s strength and weakness, while trying to mitigate potentially negative impacts of the external environment.

### ***Going forward***

Moving the business closer to town is at the top of Firm B’s list for their five year outlook, but they also intend to add 5 employees, which Owner B believes will be made much easier once the Firm relocates. The firm would like one of those employees to be an in-house designer, although Owner B recognizes that hiring an in-house designer is easier said than done, *“It’s really hard to find designers that are not only good designers, but who also understand timber frame houses. In order for us to be able to hire a designer though, we need to have work for him all year round; and that’s not the case right now”* (2011).

In order to achieve Firm B’s target of doubling gross revenue in the next five years, Owner B believes the firm needs to address possible synergies, *“I don’t really think a business needs to be stand-alone and run completely independently. It would be great if we could set up with, say, and electrician next door who could do all the wiring during the mock-up and it could*

*all be shipped together; or a plumber or something” (2011). While this doubling revenues is the current target, the firm is always reassessing its goals and strategies, “That’s our plan now, but we’ll see. We may refine and say, ‘You know what? We’re not doing that, we’re doing this instead”” (2011).*

Being in the wood products sector, fibre access and availability obviously plays an important role in the firm’s overall strategy going forward. Owner B would like to see SMEs in the sector have greater access to smaller sales like those offered in the SBFEP. While he accepts that the small business program is not likely to return, he does have suggestions on how to improve the tenure system in the future, *“increasing the woodlot program and having larger woodlots would help a lot. Having BCTS target some smaller sales would be helpful as well, but they’re too inefficient. They just don’t have the manpower to be able to manage smaller sales. It’s hard to imagine why they couldn’t expand the [woodlot] program though” (2011).* Owner B argues that improved fibre access channels would be very helpful in the strategic planning of firms like Firm B.

### **3.3 Firm C**

#### **3.3.1 Firm description**

Firm C began as a small operation in 1987 focused primarily on custom remanufactured wood products. Through the 1990s and early 2000s, the firm diversified and grew to a point where it was a major player on the North American engineered and machine stress rated (MSR) wood products markets, selling its products in the U.S and, to a lesser extent, in Canadian and Asian markets. Owner C, who had experience working in the primary wood products sector prior

to starting Firm C, says the introduction of Section 21 sales is what enticed him to explore possibilities in the value-added sector.

Having been trained overseas in management and finance, Owner C believes he was well equipped to start his own firm. After working for a major manufacturer for ten years and quickly working his way up from unskilled labourer to supervisor and ultimately to purchasing manager, Owner C purchased a small sawmill and launched his own business. Shortly after starting the business, which was initially competing in the primary sector and having difficulty secure fibre, Owner C opted to go into the value-added sector to take advantage of the newly available Section 21 sales. His vision for Firm C was to leverage his management skills so that Firm C would gain competitive advantage by being better planned and better managed than its competitors.

After two decades of growth and generally very successful expansion into different markets, the firm was forced into bankruptcy in 2009 due to their primary market, the US housing market, having crashed and their lending institutions, US banks, suffering largely the same fate. While Owner C has plans to re-open the firm in the future, Firm C's installations currently sit idle and the Firm remains out of operation. For the purpose of the thesis, the discussions around Firm C were centred around the growth and expansion of the firm during the 1990s and 2000s as well as the lead-up to its bankruptcy in 2009; the current state of affairs was not discussed at length.

### 3.3.2 Fibre supply

As Firm C established itself in the region, the Section 21 sales gave the firm some much needed fibre access and subsequently negotiating power. “ *Without [Section 21 sales], there’s no way we would have gotten started. It gave us an edge for negotiating that we wouldn’t otherwise have had*” (2011). Given that the value-added sector was not as well financially established as the primary sector at the time, small tenures which could be used by value-added firms as trading bait in dealing with primary manufacturers were key. For Firm C, and in particular Owner C, this relationship with the primary sector was a well-established one due to the decade he spent working and building relationships in the primary sector, “*I had a great personal relationship with the managers and owners at the primary manufacturer I used to work for, so that turned into a very good business relationship. We had some small tenures and we made a deal with the major: we sell you our logs and buy your lumber. That relationship was huge for us*” (2011). The relationship between Firm C and the primary manufacturer in question allowed Firm C to lock-in between 30% and 40% of their fibre supply.

By the time the SBFEP was terminated as part of the Forestry Revitalization Plan in 2003, Firm C had grown its capacity to a point where it could bid on 5-year forest licenses. While on the surface it may appear that the switch in fibre procurement had the same outcome – timber - Owner C recalls that the switch to forest license had its share of problems, “*First of all, with the category 2 sales you had no real obligations – you came in, harvested, paid your stumpage and walked away. Now with forest licenses, you have obligation to replant and you have to put down cash deposits*” (2011). Owner C says that at some points during the operation of Firm C, the firm had in excess of one million dollars in cash deposits sitting with the government as a guarantee that tenure obligations would be met. According to Owner C, this was

especially hard on Firm C and others in the value-added sector because deposits took money out of often already limited cash flow.

### 3.3.3 Financing

As Firm C grew throughout the 1990s and 2000s, some significant investments were made. Given his financial background, Owner C recognized the importance of carefully evaluating investment opportunities as well as the importance of crafting good proposals to present to potential financiers. If a potential investment was deemed favourable, the company would first raise much of the required money themselves, and then approach lending institutions. *“We didn’t apply for grants, because given the size we had achieved by the time we wanted to make new investments, we wouldn’t have qualified anyway. So our strategy was to put in our own equity and then have a good proposal for the banks to come on board; most of the time the ratio was one-to-one”* (2011).

Occasionally, if Firm C was experiencing lower than expected cash flow, Owner C’s previous employer in the primary sector would provide advances of up to one million dollars. *“This,”* Owner C says, *“was an unusual relationship, but they knew we had a good business plan and we would be able to cover the advance, no problem”* (2011). Even after the primary manufacturer was bought out and came under new management, many of the unusual perks of the business relationship with Firm C continued.

Owner C attributes the primary sector’s willingness to work with Firm C to its sound overall management strategy. *“Every cent we made over the years was put back into the company for growth. People knew that we weren’t doing this to line our pockets”* (Owner C,

2011). Owner C points out that perhaps the greatest benefits of the company's reinvesting its profits were the indirect effects, *"that money essentially went right into the community, so it helped everyone out. Not just [Firm C]"* (2011).

Despite the aforementioned occasional financial help of the primary sector, Firm C dealt mostly with American banks and some national Canadian banks for investment loans and shied away from dealing with any local banks. According to Owner C, *"Local banks are good for your home, but not your business"* (2011). However, whereas local banks and Canadian national banks escaped the US financial crisis largely unscathed, many American banks were heavily hit. *"We dealt mostly with American based lenders, so that's really where the big problem happened in 2008-09. It never would have happened under normal circumstances and I don't think anyone anticipated what happened. I don't take it personally either; it's a business and that's how you deal with it."* (Owner C, 2011).

As demand for the firm's product line declined and its sources of financing dried up, Firm C was forced to shut down in 2009. The financial institutions approached Owner C and informed him that they could no longer provide financing for the firm. *"I decided that I already had enough personally invested in it, so we mutually agreed to shut down."* (Owner C, 2011).

### 3.3.4 Skill

Owner C says that the skill level of his employees was where the true value-added was. From skilled labour to skilled management, Owner C says skills were at the core of Firm C's strategy, *"People started as unskilled labourers and then worked their way up to certified millwrights, electricians and tradespeople. So skill was acquired, but also developed. We would*

*acquire primary sawmilling skills, and then add on the value-added skills ourselves.”* (2011). He argues that the main reason Firm C developed the value-added skills themselves is because the province did not have a facility where training was offered to labourers.

Owner C says some people have the right idea with a few training facilities in the Lower Mainland, but he argues that a training centre would be much more beneficial in the Interior, *“With the Lower mainland, put in one machine and you’re in. The population is so big that you don’t necessarily have to be very good at what you do- somebody’s probably going to buy it regardless. Us on the other hand, if we’re going to ship it from the Interior to the market, wherever that may be, we need to make sure the value is actually there. So we need skilled people to get the job done right”* (2011).

As far as the skill level in upper management, Owner C says the firm’s mindset was management, *“My mindset was management. The fellow I had as VP of operations was a professional engineer who worked in the primary sector for 15 years being a general manager. My superintendents were all professional people too. We gave people chances for training within the organization too. They didn’t necessarily come to us with all these management skills, but our emphasis was on training”* (2011). Initially, the firm brought in experienced professionals in management roles, and part of their job was to train the next generation of managers within Firm C so that there was a strong succession strategy in place.

By the time of the firm’s closure, every aspect of the business was done in-house: the firm had its own engineers and accountants to go along with their sales, marketing and production teams. Reflecting upon the lead-up to the firm’s bankruptcy, Owner C does not believe management is to blame, *“Management was not an issue for us. It was probably our*

*strongest asset. If it hadn't been for the market we would still be there"* (2011). Owner C does not see a relationship with the firm's collapse and managerial decisions. Asked to reflect on the notion that Firm C may have been over exposed in the US market, Owner C says that management did all it could to save the firm but ultimately, the markets did not cooperate. He takes solace in the fact that Firm C was one of many to fall victim to the financial crisis.

### 3.3.5 External environment

The external factor that most affected Firm C is undoubtedly the economic downturn of late 2008. Whereas the downturn was felt by numerous firms in the forest products sector due to the strong links between the Canadian forest products sector and the US housing market, for a firm like Firm C, exposed to the American economy in both its housing sector and financial sector, the economic collapse spelled the end of a successful run in the value-added sector that lasted over twenty years.

While some, in retrospect, will argue that there were signs of an impending downturn well before the actual collapse, Owner C and his financial partners did not slow down their plans for expansion, *"In mid-2008, we started thinking of another project where we were going to add-on another finger-joint stud line. We had everything designed and engineered."* (Owner C, 2011). The new line was going to produce in excess of 150,000 board feet per shift and Firm C's management team and their financiers were confident that the investment would pay-off. However, before the investment could be finalized, Owner C says the firm and the entire market was blind-sided by the developments in the US economy, *"All was approved internally by management and the board as well as some of our financial partners and then boom – the collapse of the housing market and the financial institutions."* (2011). Asked if he thought



management could have mitigated the risks in order to have a different outcome, Owner C is adamant that management or strategy are not to blame for the firm's closing, *"Ultimately, the market collapsed in 2008 and took us down with it. I guess had we been better financed we would have been in a better position, but it wasn't a management issue"* (2011).

Owner C summarizes his thoughts on Firm C's closure, *"I have no regrets, to be honest. My only regret is that we lost a lot of money and that people lost their jobs. Nobody was hurt and we looked after every single employee until the very last minute. In a business you win some and you lose some; we happened to be on the losing end in 2008 and it was out of our control"* (2011).

### 3.3.6 Strategy

When Owner C first entered the value-added sector, he says the sector was *"very entrepreneurial and owner driven; not professional management driven"* (2011). He approached the management of Firm C from a more *"professional"* basis, *"I wanted to develop more on a professional basis. So we had an emphasis on management training and a management team"* (2011). His main motivation for adopting this mindset for Firm C was his strong belief in the need for a strong succession plan, *"It couldn't be focused on me because I knew that sooner or later I would need a back-up plan; my children are professionals in their own right, and they weren't going to take this over. I was very happy with this strategy"* (Owner C, 2011).

A key component of the firm's overall strategy was market research. Owner C says that the firm identified consumer demands that competitors had overlooked and put a lot of energy into ensuring that there would be enough buyers for their product. *"It was really about doing our*

*homework. And we had buyers lined up before we made our first product so we really hit the ground running*” Owner C, 2011). Much of Firm C’s market research was done on the ground in conversations with customers during sales visits. Owner C believes that customers feel more comfortable with a business relationship and are more open to make their demands known if the owner of the selling firm visits with them in person; he says he made a point of travelling with his sales team to meet with clients once every three or four months.

Owner C recalls one instance in particular which lead Firm C’s successful venture into engineered wood products (EWP), *“I was in Atlanta on a marketing trip and they had some long-length finger-jointed rafter studs and it was really low quality. The customer said, ‘if you can produce higher quality product than this, I’ll give you the orders now’”* (2011). After some additional market research into the product, Firm C went ahead with a \$21 million investment into a new plant. Owner C and his management team were confident that the investment was a good one, *“people said we didn’t really know what we were doing, but we had done some careful market research, looked at our competitors and their pitfalls and ultimately made sure we had a higher quality product”* (Owner C, 2011). Ultimately, Owner C says Firm C ended up being one of the only producers manufacturing rafters longer than 32 feet, *“I’d say we had up to 45% of the total North American 32 feet plus rafter market”* (2011).

Some years later, Firm C expanded further to include MSR wood products to its product line. At the height of the firm’s expansion, Firm C was a player in the EWP, MSR, high-end doors and windows markets as well as producing some furniture panels and shelving units. According to Owner C, the firm, *“basically tried to get to every area of the market so that no one could say they wanted something and [Firm C] couldn’t supply it”* (2011).

Throughout the firm's growth, Firm C was an active member of various industry associations. Beginning with smaller associations focused on the value-added sector, the firm soon found that while it was contributing to the smaller associations, it was not benefitting nearly as much as Owner C felt it should. As a result, Firm C left many of the smaller associations it had been part of and joined the Council of Forest Industries (COFI), a group largely made up of primary manufacturers. Given its relatively large size in the value-added sector, Firm C was able to establish itself as an equal at COFI meetings, *"We got to give our input. We were in the loop and part of the discussion so we knew what was going on"* (Owner C, 2011). Being a part of the discussion at COFI contributed to the firm's market research goals, *"they always advised us of new opportunities, especially in markets where we didn't necessarily have the resources to suss out new opportunities"* (Owner C, 2011)

Despite its aforementioned "supply it all" strategy, Firm C had to make adjustments to its strategy in order to remain competitive. After carefully looking at where they stood versus the competition in the windows and doors market, Owner C says the decision was fairly clear, *"we were competing with mom and pop shops who were really small operations with very low overhead and we were on a completely different plane with 50 employees and 10 sales people, so our overhead was much higher"* (2011). After nearly a decade competing in the windows and doors market, primarily in the Lower Mainland region of British Columbia, Firm C opted to pull out of the segment and tackle the EWP market more aggressively, primarily in the US catering to the housing market. While this strategy proved successful for a time, the onset of the financial downturn and its impact on housing starts exposed Firm C to economic risks that they ultimately could not overcome.

## Going forward

As markets recover in the US, Firm C plans to re-start operations in the future. Owner C admits that while he's reached an age where he could easily retire, he would like to take the helm of a re-launched Firm C for a few years if a re-start actually does take place. His plans are influenced by Firm C's financial partners who have asked him to come back to head the firm as it comes out of bankruptcy. In keeping with the firm's strong belief in having solid succession plans, Owner C says he will come back only for "*enough time to develop new management*" (2011). Although recent years have been difficult for Firm C, Owner C says the future looks bright and that former customers are asking when Firm C will re-open because they are eager to do business with the firm.

## 3.4 Firm D

### 3.4.1 Firm description

Firm D is a small value-added firm that specializes in custom remanufacturing and millwork along with producing EWP and cabinetry selling its products within the region of interest that has been in operation since 2005. The firm, which has seen its revenues nearly double every year since its launch, is family owned and operated by Owner D who is the majority owner and a European-trained carpenter along with his wife, his brother and nephew. In addition to family members, the firm employs two other labourers.

Initially relocating to the Interior from Europe in the late 1990s, Owner D started a carpentry business in 1999. After some running his carpentry business in the region, Owner D noticed that there was demand for value-added products like tongue and groove panelling and custom remanufacturing, so he began looking for an appropriate location to set-up a new firm. In

2005, Owner D purchased a vacant building approximately one hour's drive from the community, which had previously housed offices but was classified under light industrial zoning regulations. He found this to be an optimal location because he had moved to the Interior to enjoy the rural lifestyle and had no intentions of moving to the city. Upon purchase of the building, using much of the equipment he had brought with him from Europe and using his personal savings to finance the venture, Owner D launched Firm D which focused primarily on custom orders. Owner D says the motivation for running Firm D is, *"to make a living. I'm not trying to get rich, I just want to live comfortably and make a good life for my family"* (2011).

#### 3.4.2 Fibre supply

Firm D's timber profile is composed of spruce, pine, Douglas fir and cedar logs. The firm has never held a forest license or woodlot and obtaining forest tenure is not in Owner D's plans, *"With the log prices we've grown used to seeing, it doesn't make sense for us. We only produce about 2000 cubic metres a year, so a licence doesn't really make sense for us"* (2011). Firm D buys its spruce, pine, and Douglas fir logs from local woodlots and salvage loggers and purchases its cedar from the major licensees in the region who are not equipped to process cedar at their mills. While the firm has no contracts in place with log suppliers, it has established itself as a firm willing to pay slightly more than market value in order to ensure high quality logs; this has led to loggers and woodlots approaching Firm D when they have timber they believe fits Firm D's demands. Owner D says even the major licensees will sometimes make the first move, *"It's nice actually, one of the majors will occasionally come to us when they have cedar"* (2011).

While the relationship with most woodlots and salvage loggers is mutually beneficial and price negotiations are fairly straightforward, Owner D points out that the relationship is not

always so with the major licensees, *“One of the licensees is okay to deal with, but we can tell we’re not that important to them so sometimes they really try to push us around with their price. As for [the other major licensee operating in the region], I don’t want to deal with them at all – they are terrible to negotiate with”* (2011). In order to reduce some of the friction that occasionally develops during negotiations for their cedar supply, Firm D is looking at the possibility of entering into a contract with the major licensee they currently deal with. However, Owner D recognizes that this may be difficult, *“it’s really hard for them because they don’t know how much cedar they’ll actually harvest”* (2011). Despite occasional negotiating difficulties, Owner D says that his firm hasn’t had much trouble securing their supply of logs, *“we tend to pay a little bit more than everyone else, so I can’t say we’ve had much competition for our logs”* (2011).

### 3.4.3 Financing

Whereas Firm D’s funds to get off the ground were provided by Owner D and his family themselves, the firm has sought external financing to expand the business. Firm D began by applying for government grants, but applications were rejected and Owner D soon abandoned the idea of obtaining government funds and focused instead on local banks. The outcome was similar with the banks, *“the banks, well they say ‘the lumber industry is not doing well, so we’re staying away from that’. They don’t differentiate between commodity products and some really high end, high value stuff like we’re doing”* (Owner D, 2011).

Before appealing to private investors, Firm D tried to obtain a loan from the BDC but the experience is not one that Owner D looks back upon fondly, *“The BDC is even worse than the banks. We had to go through an environmental review to get approved for a loan, but there was*

*an issue with something that the previous land owners hadn't taken care of. To make a long story short, the loan application process itself ended up costing me \$10,000"* (2011). Firm D abandoned the loan application process because Owner D believed that the costs associated with the environmental review, were likely to be more than the loan itself. Reluctantly, the firm opted for private investor, but Owner D says that was an expensive option, *"private investment is way more expensive than the banks or government loan. We even had to put our own personal stuff up as collateral – like my house"* (2011). In retrospect, Owner D believes that he should have tried harder to get bank financing, but that he let frustration with the process get the better of him, *"I was just getting fed up with them always say no that I just walked away. It was really an emotional decision and looking back on it, I'm not sure it was the right one to make at that time"* (2011).

#### 3.4.4 Skill

As with other value-added firms in the area, Firm D struggles with finding skilled employees. In addition to the six person staff currently working for Firm D, the firm would like to add two more skilled workers, but Owner D says that task is difficult, *"We live in a community with high unemployment, but we had to hire a guy from Vancouver Island because no one in town has the skills. And we're too small to be able to do any kind of real intensive training"* (Owner D, 2011). The fact that Firm D is importing labour from outside the region to fill its needs is putting a strain on the firm's relationship with the community at large, *"People in the community didn't like that he just showed up and had a job right away"* (Owner D, 2011). However, Owner D says that for him and for Firm D, it ultimately boils down to hiring the most

skilled labourer, regardless of whether he or she is a resident of the community, *“if they’re trained and willing to relocate, then I have to hire them; it’s just business”* (2011).

Owner D believes the skills shortage is not limited to the local community; rather, he argues the problem is province-wide, *“British Columbia needs a better system that encourages more tradesmen. We always encourage kids to go to university but it’s not for everybody. Maybe we should push for a trade or an apprenticeship after high school and before university if that’s what students want to do. Because right now, the state of skilled labour is pretty sad.”*(2011). He says developing skilled labour is especially important in areas of British Columbia where economic activity still relies largely on blue-collar workers.

While Owner D considers himself a very skilled worker, he admits that his management skills are not as well-rounded as they could be, *“I focus on the product – that’s what I’m good at. You can’t be the perfect skilled worker and the perfect guy in the office. That’s why my wife does most of the office stuff. You have to recognize when you are good at something and, more importantly, when you aren’t.”* (2011). While the management side of the business may not be his strong point, he is fairly well-versed in business management, *“I had management training overseas; I went to school a bit for business classes.”* (Owner D, 2011). He says the recognition of his limitations in the management realm is the result of his years of experience running a firm, *“I used to try really hard to sell my product, but I’m not a good salesman at all, so I stay away from that. My mentality is to make a good product and let that be the main selling point; not me blabbing on about how great I am and how great my company is”* (2011).

While marketing Firm D is not Owner D’s focus, he has attempted to hire outside help where the firm’s expertise is lacking. Tapping into the community’s close-knit social circles,



Firm D was able to hire a recent retiree to help out with the marketing side of things, “*We have a guy who helps us out a lot with administrative stuff and does a lot of the advertising; he set up our website. He’s a retired policeman, so it’s not really what he’s done all his life, but he’s really good at it*” (Owner D, 2011). For other tasks that fall in the firm’s overhead, Firm D is fairly self-sufficient with Owner D’s wife taking charge of all the book-keeping and invoicing leaving only year-end accounting to be outsourced.

### 3.4.5 External environment

When asked about Firm D’s relationship with key areas of the external environment, Owner D breaks it down into three categories, “*there’s the political environment, the economic environment, and the business-to-business environment for us*” (2011). He says the firm’s problems with the political environment only go so far as the land on which they operate, “*We bought this building, but actually, the only thing that attracted us was the land. It’s flat and it’s light industrial zone. Of course, we had problems with the BDC application because of the land, but that’s not really generalizable, it was just bad luck*” (Owner D, 2011).

As for the economic environment and its impacts on the firm, Owner D says that while there are seasonal variations in the level of activity and population influxes due to different mining projects increasing demand somewhat, Firm D is often operating at full capacity regardless of what happens in the regional economy. This, says Owner D, is highlighted by the firm’s performance during what have been very difficult times in the forest products sector.

“*Obviously, for us, the biggest thing external to [Firm D] is the business-to-business stuff, especially with the majors*” explains Owner D, “*We didn’t really feel the impact of consolidation*

*in the primary industry as much as some of the others because of when we started, but it is something we have to deal with” (2011). The biggest impact of the consolidation of major licensees, according to Owner D, is the resulting limited pool of potential suppliers, “I can tell you that it narrows our options as far as who we buy from. It’s pretty easy right now because we essentially have two majors to choose from and one of them is impossible to work with- so greedy- so our choice is clear” (2011).*

In its dealings with other small firms, in particular those operating in the value-added sector, Firm D would like to take greater advantage of the potential benefits of collaboration. *“We have some good relationships up and down the supply chain, but we aren’t using the relationships to their fullest potential. I think we would gain a lot by being part of associations or industry groups, but we haven’t gotten around to thinking about it seriously yet” (Owner D, 2011). Owner D says that given the potential benefits of developing strong collaborative relationships with other firms, joining industry associations and being an active participant in the associations will be an important part of Firm D’s strategy going forward.*

#### 3.4.6 Strategy

In order to remain profitable, Firm D only takes on orders that exceed the firm’s minimum profit margin. Owner D says the reasons for this strategy are simple, *“If an order is below that certain threshold, we don’t do it. It’s just not worth the effort and the possible opportunity missed if we commit to this low paying job and have to pass up a higher paying job tomorrow or next week” (2011). Owner D says his careful consideration of the opportunity costs of picking one project over another is a skill he developed over the many years he has operated his own firm, “I’ve been doing this since 2005, and the carpentry business for six years in*

*Canada before that and 11 years in Europe before that, so that was the best kind of training. I learned about taking on orders with tight profit margins the hard way, unfortunately” (2011).*

The strategy seems to be paying off for Firm D. Since 2005 when the business was launched, revenues have almost doubled every year; a fact all the more impressive according to Owner D because, *“it was in the heart of the downturn”* (2011). Despite this successful run, Owner D says of the firm, *“we’re not where we want to be”* (2011). From his point of view, Firm D should not be deemed successful or profitable until it has paid off all of its loans. Only then, he says, will the firm be *“actually making money”* (2011).

Although Owner D wants to pay off all of the firm’s debt as soon as possible, he clarifies that he does not necessarily want to do this through expansion, *“We want to grow still, but we don’t want to get ‘big’. This is still a family business and we want to remain flexible”* (2011). He says that while Firm D has the skills to expand into new markets like timber framing, that is not the direction he wants to go, *“I could go the timber frame direction, because we can do that stuff, but I moved to Canada with my family so that I could be at home. If I’m timber framing, I’d have to be gone for one or two weeks at a time. It’s not what I want for [Firm D]”* (Owner D, 2011).

However, Owner D is not shutting the door on expansion or product diversification entirely, *“I’m not saying we aren’t going to grow, but we just want to do it in a managed way- at our pace”* (2011). He provides an example of how the firm came to the decision of expanding into panelling: *“I built my house here and in doing that I realized that there was only one kind of panelling that I could use. There weren’t many people doing this kind of stuff. So I said ‘we have the skills to produce this, let’s have some around the shop and when customers come by, maybe they’ll want it’; that’s exactly what happened”* (2011). He says the firm’s focus on hiring only

skilled labour also helps in keeping product diversification options open, *“That’s where really skilled people come in handy; they’re not robots trained to do only one thing, they can adapt really quickly”* (2011).

Owner D says the consistently high quality of Firm D’s products has led to a number of inquiries from brokers outside the region trying to entice the firm to export its products. In-line with the firm’s relatively conservative strategies on other aspects of the business, Owner D explains, *“We get call from exporters looking to sell to China, but that’s not where we are right now. So long as we don’t need exports to pay the bills, we’re not going to go down that road”* (2011). He says that he is happy with the current direction of the firm and that Firm D’s decision to sell its products in-region has its benefits, *“We save some money on shipping because a lot of our end consumers are right here in the region and they come down to pick up their orders”* (Owner D, 2011). He also points out that some downtime during the year is not all bad, *“We don’t lay-off guys. When things slow down, we build up inventory and take care of some of the smaller stuff that we don’t usually have time to get to”* (Owner D, 2011).

### ***Going forward***

Beyond Firm D’s rather straightforward goals for the future, Owner D admits that his ambitions for Firm D are vague, *“It’s hard to say [what Firm D’s goal is]; I just want to make it. We’d like to be out of debt”* (2011). For Owner D, and by extension for Firm D, the future comes down to simply ‘making it’, *“I’ve been self-employed for almost 25 years and I just want to live. I don’t want to be rich; I just want to live well. So it’s hard to say what our goal is. We would like to grow a little bit more, but we don’t really have a plan”* (2011).

Despite conceding that the firm does not currently have a detailed plan for the future, Owner D recognizes that if the firm wishes to obtain any external funding in the future, potential financiers will likely want to see a short- to mid-term plan. *“The future is definitely something we will have to think about in a more structured way. Right now things are good and we’re busy, but I guess we eventually have to get over the ‘now’ and start looking ahead”* (2011).

### **3.5 Multiple case study overview**

As the results of each individual case study demonstrate, while each firm involved in the study has its own strengths and challenges, certain themes emerge that apply to all investigated cases. To differing extents, fibre supply channels, the availability and development of skilled employees, financial matters, the development and implementation of strategy, and interactions with the external environment all play important roles for the SMEs studied. As the firms try to either build on recent success, transition from poor performance to successful outcomes, or, in the case of Firm C, start anew, how each firm deals with the aforementioned issues will influence their path forward.

#### **3.5.1 Fibre Supply**

The procurement of timber for operations is an issue of importance for all cases involved in the study. The results of the study demonstrate that the issue is not so much one of availability, but rather one of affordability. Although the availability of timber is likely to have an impact in the future due to the mountain pine beetle epidemic in the area, the current provincial strategy of increasing salvage harvest levels to achieve various goals has led to an increase in the supply of pine in recent years.

While conventional economics of supply and demand dictate that the market price of timber should decrease with an increase in supply, the consolidation of the primary wood products manufacturing sector and, perhaps more importantly for the firms involved in the study, the consolidation of major forest tenure holders has led to a decrease in the bargaining power of smaller firms in the market for fibre. As highlighted by Owner D and Owner A's comments about only having the choice of two major licensees to negotiate with, a limited choice of suppliers restricts bargaining power and further amplifies the differences in negotiating power between small and large firms outlined by Wagner (1988).

The owners interviewed presented alternatives to address some of the issues related to fibre supply. Ranging from an expansion of the woodlot market to a reduction in the size of British Columbia Timber Sales sale offerings to a relaxation of deposit requirements, the owners offered suggestions that would bring the tenure system closer to the configuration that was seen during the days of the Small Business Forest Enterprise Program (SBFEP). The owners' discontent with the fibre supply situation is, for the most part, not an operational issue but rather a strategic one. While wood is obviously a vital input in the value-added sector, it is also an important asset for firms trying to secure financing or further fibre supply as it can be used either as collateral or in negotiations with other firms (as demonstrated by Firm C and Firm D).

### **3.5.2 Financing**

The availability, affordability, and efficient use of financial capital also have a significant impact on the success of firms in the study. Although organizations providing different financial assistance options are present in the community along with local banks, the owners report having trouble securing financing. While three of the firms studied report that they have dealt with the

Business Development Bank of Canada (BDC) or Community Futures in the past, they all voiced criticisms of the organizations and are not currently in a business relationship with either agency.

The criticisms tend to revolve around the affordability of the services provided. While the owners admit that the lending institutions provide a much-needed service for SMEs, the resources required to enter into an agreement with the organizations can be a big deterrent. Firms A,B, and D have all moved away from dealings with the BDC and Community Futures, albeit for different reasons: Firm A failed to provide an adequate business plan to be approved for a loan and opted for private financing; Firm B, does not currently require financial assistance, but Owner B admits that the two organizations would not be the firm's first choice due to the cost of financing, and; Owner D became exasperated in his bid to obtain a loan from the BDC due to the amount of financial and human resources involved in the process, so Firm D obtained private financing.

It is important to note that both Owner A and Owner D, who sought private financing for their firms offered their own personal family homes as collateral to obtain private loans. While this collateral may have been essential to the firms obtaining their respective loans, offering personal assets and equity opens a small business owner and his or her family to significant risk should the business venture go awry. This practice, according to Berger and Udell (1998), may also signal to other lenders in the future that the firms' business plan was deemed risky by the private lender and may hamper the firms' chances of obtaining collateral-free loans in the future. The two firms' lack of a business plan detailing their firm's future plans and strategy likely impacted their loan applications.

Firm C is the only firm in the study to have sought international financing. Being the only medium-sized enterprise in the study, the firm's size places the firm in somewhat of a different

category when it comes to its financial needs. With high cash flow requirements as outlined in Firm C's results, Owner C believes the firm had to seek financing outside the region. While US financing was less expensive than Canadian financing, Firm C learned during the financial crisis of 2008-09 that the cheaper financing south of the border was also riskier. Despite ultimately having to shut down operations, Firm C appears to have had sufficiently strong business plans that allowed it to secure various loans in its years in business, though the business plans' strength when it comes to risk management, with nearly all sales going to the US housing sector, is questionable.

### **3.5.3 Skill**

#### ***Skilled Labour***

All firms involved in the study mentioned skilled employees as a fundamental component of firm success. While firms A, B, and D look to the labour market to supply skilled labour, Firm C relied on its internal employee development to ensure that workers had the required skills. Again, Firm C's size plays a major role in its human resource strategy. By being significantly larger than the other firms in the study, Firm C had the resources necessary to train unskilled workers; the other three firms are limited by their size and resources and cannot afford to spend time and funds on long training periods with their employees. As such, Owners A, B, and D were much more vocal about the lack of skilled workers on the labour market than Firm C.

The owners believe different levels of government have a role to play in addressing the skilled labour shortage. At the provincial level, Owner D argues that a training facility for forest product manufacturing would help address the shortage and should be a key part of the province's overall jobs strategy. Owner A echoes the same sentiment, although he does not



provide any specific suggestions on how to tackle the lack skilled workers. Owner B, whose firm also struggles with finding qualified workers, believes the region's recruitment and retention strategy is at the root of the problem; that is, there are skilled workers in British Columbia, but they simply do not see the region of study as an attractive place to live and work. The owners also mentioned that the skilled workers that are in the region are often drawn to the growing mining sector and its often-times higher wages.

### ***Management Skills***

Another factor affecting firm success is management skills. All owners interviewed play an active role in the management of their firms and all have more than fifteen years' experience running their own business. Three of the four owners report having some business training or graduate education, and the one owner with limited education, Owner A, states that he would happily take part in business management classes if they were offered in the community outside of work hours for a low price.

As with the development and acquisition of skilled labour, management skill development varies from firm to firm. Owner C says that his firm hired some managers with the qualifications required to step in and perform their job effectively as well as hiring employees and grooming them into strong managers. Once more, Firm C's ability to focus on management development and training was influenced by its size.

Owner B and Owner D both have some business management training, but perhaps their most important managerial contribution to their firm is their recognition of personal skill limitations. Both Firm B and Firm D outsource key areas of the business, notably marketing and accounting, which the owners agree are beyond their abilities. This is in stark contrast with Firm A, whose owner is in charge of all management tasks. As illustrated in the results pertaining to

Firm A, Owner A's ability to stay up to date with the firm's fibre supply requirements, labour needs, and financial dealings is handicapped by the fact that he is the only person performing those tasks. Owner A's reluctance, or inability, to involve other employees in the management of the firm is likely a contributing factor to the firm's recent lack of success.

### **3.5.4 External Environment**

The external environment plays an important role for each firm involved in the study, though each owner focuses on different aspects of the external environment. The economy, be it regional, national, or international, is a component of the external environment that all firms must deal with. Regionally, the economic environment plays an important role for both Firm B and Firm D's revenue stream; when the regional economy is strong both firms see an increase in construction that translates into higher sales volumes. That said, in recent years, a strong regional economy has usually been supported by the primary forest products sector or the mining sector which, as mentioned earlier, has adverse effects on the firms' ability to recruit skills workers.

At the national and international level, the firms are susceptible to changes in the economic environment whether it be the indirect effects of economic policies affecting consumer behaviour or the direct effect of measures such as trade restrictions. For Firm C, the tremendous downturn in the US economy in 2008-09 proved to be too big a shock to the external environment for the firm to recover.

Firms are also affected by changes in the regulatory environment, particularly when changes concern fibre supply channels (like the introduction of the Forestry Revitalization Plan in 2003) or skilled labour availability and training. Although the regulatory environment is external to the firms, there are ways for the firms to influence the regulations that affect them. As

Owner C notes, by participating in industry associations like the Council of Forest Industries (COFI), owners can indirectly lobby against or for regulatory changes they see as detrimental or beneficial to their firm.

### **3.5.5 Strategy**

The issue of planning and strategy is interesting on multiple levels. While each firm has an overall strategy as to how they serve their clients' needs, not all firms have a plan as to how they will continue to serve those needs. Interestingly, Firm B and Firm C have a well laid out plan for the future, while Firm A and D do not. The fact that Firm B has a plan and Firm A does not should not be surprising, given their competitive position and recent performances, but Firm D's lack of a plan for the future is surprising. Despite Firm D's strong performance and Owner D's decades of experience running a business, the firm's five year plan is vague at best, and absent at worst. As echoed in section 3.5.3, the firm's lack of a solid business plan for the mid-term likely has had an impact on lending institutions' reluctance to provide financial assistance.

Another interesting aspect of each firm's strategy is the exposure to risk. The results of the in-depth interviews demonstrate that Owners B and D, whose firms are deemed successful, are much more risk averse in their investments than their counterparts, Owners A and C; Firms B and D have not made the kinds of large investments that Firms A and C have made. Whereas Firm A made a \$10 million investment in the mid-2000s in attempt to significantly grow the business – an investment that ultimately led to its bankruptcy in 2005– and Firm C made several large-scale investments throughout the 1990s and 2000s, Firm B stays away from large investments that could handcuff the firm in the event of a downturn (the only hint of a large investment on the horizon for Firm B is the possibility of investing in new property) and Firm D

has no intentions of making major investments to grow the business as Owner D states that he is content with Firm D remaining a small family operation.

The firms' geographical sales regions are also indicative of their respective owners' comfort with different levels of risk. The two struggling firms, Firm A and Firm C, sell their products primarily in the United States (US), exposing the firms to greater economic, commercial and political risk, whereas Firms B and D sell only in Canada, mostly within region. While this is not to imply that the fact that Firms A and C sell to the US is the definitive cause of their struggles, it does demonstrate that the increased risks of dealing in international markets should be considered in an SME's strategy.

Overall, the results of the study indicate that the firms involved faced many of same issues. While each firm addressed the key themes identified in their own way, many of the owners' comments and perspectives on the issues were in-line with what is found in the literature. Although far from being able to draw general conclusions about the population of SMEs in the value-added sector as a whole, the results of this multiple case study analysis do provide valuable findings to be incorporated in future research. A discussion of the implications and limitations of the research follows in the next chapter as well as some concluding remarks regarding further research.

## **4. Discussion and Conclusions**

The discussion of the research begins by examining the implications of the findings for businesses and policy makers and exploring where the research fits within the broader field of research on SMEs and the value-added sector. A description of the research limitations follows and the chapter concludes with a look at how future research might incorporate the findings of this study and add to the results generated in thesis.

### **4.1 Implications**

The keys to success for the firms studied, as identified by their owners, can be categorized into a basic production function composed of physical capital (timber), financial capital, and human capital (skill). While other themes emerged from the interviews, like strategic planning and the firms' relationship with the external environment, the topics that the owners first addressed when asked about success factor for their firm were fibre supply, financing, and skill (both labour and management). The subsequent themes were largely deemed important because of their impact on the production function. Upon analysis of the case results, it appears as though human capital, management skill in particular, plays a pivotal role in the ultimate success of each case, though that is not to say physical and financial capital are unimportant. In fact, all in-depth interview participants addressed the issues of fibre supply, financing, and skilled labourers before turning the focus on themselves and their management.

The fact that fibre supply was the first issue raised in all cases is not surprising. The issue has been at the forefront of forest policy discussion since the first Sloan Commission in 1945. As the primary input in value-added wood products, fibre supply obviously preoccupies firm

owners, but as the owner of the raw material, the government, and by extension policy makers, is also keenly interested in the issue. The results of the research demonstrate that while fibre supply channels are far from being perfect, according to the case study interviewees, some firms, notably Firm B, Firm D, and for a time, Firm C have been able to work well within the system. Through relationships along the supply chain, firms are able to meet their timber needs, but all owners involved make suggestions on how to improve the wood supply channels or restore aspects of the tenure system that worked in their favour in the past. For example, the dissolution of the Small Business Forest Enterprise Program, as part of the Forestry Revitalization Plan, has, according to the case study participants, significantly handicapped the small players in the value-added sector who used timber harvesting rights acquired through the program for leverage along the supply chain or to improve their financial position. While this study in and of itself is not enough to catalyze an overhaul of the tenure system, policy makers can take note of the issues raised and suggestions tabled by the owners in their review of current and future policies.

With a basic understanding of business fundamentals and the high fixed costs needed to prosper in the forest products sector, financing being an issue of importance for all firms is to be expected. While the firms sought financing through different channels and for different purposes, the issue was important for all cases. While it would seem fairly obvious that financial matters would be at the forefront of a struggling firm's owner-operator's mind, this study demonstrates that even for successfully established, thriving firms like Firm B, financial trouble is never completely off the radar and could easily become problematic. Perhaps the best buffer against financial troubles for the firms involved in the study is a strong business plan and strategy which are inextricably linked to the third component of the production function, human capital.

The issue of skilled labour and skilled managers is one that touches both business owners and policy makers. The owners highlighted their difficulty in finding skilled workers and believe some of the responsibility for addressing the lack of workers lies with provincial and regional authorities. The sentiment is echoed in a number of reports, including a recent report by the Research Universities Council of British Columbia released in October 2012, which calls on the Province to increase its support of post-secondary education to meet what they project to be an increasing skills shortage.

Investment in skills development would likely help managers fill their labour needs, but where it may have the biggest impact for SMEs is with owners and managers running the firms. Despite the owners not saying so explicitly, the two struggling firms have some management shortcomings. Whether lacking in the understanding of the operating environment or the mismanagement of commercial and economic risk, both Firm A and Firm C demonstrated that significant strategic miscalculations were made. Although investment in management training would not eliminate management mistakes, it would likely equip SME owners and managers with better skills with which to assess different business decisions.

Another likely outcome of improved management skills would be better performance in other core areas of the business like financing and strategy development. With two of the four firms studied lacking such fundamental things as a detailed business plan, the fact that Owners A and D report that they were refused loans from lending institutions is not surprising. Perhaps with better business management foundations, the owners will take different approaches to the running of their firms and see better results in their search for financing.

The mainly positive comments about industry associations should also be noted. Though the decision to join an association ultimately rests with the firms themselves, regional business development strategies might benefit by increasing their promotion of local associations. As noted by Owner B, local government officials can play an active role in helping SMEs address some of their firm's needs.

While the research did not seek to make definitive conclusions about the value-added sector as a whole, the findings do bring a fresh perspective to some widely-held perceptions about the reasons behind the value-added sector's lacklustre performance. The issue of fibre supply and the supposed inability to obtain timber as the reason for firm struggles was met with scepticism by three of the four case study participants. The provision of timber through the different forest tenure types and supply chain agreements does play a large role in addressing the raw material needs of SMEs in the sector but the fact is that fibre supply is only one factor in the production function of value-added SMEs. The interviews with case study participants also reveal that human capital plays as large, if not larger, a role in determining the competitive position of firms.

## **4.2 Limitations**

The study had a number of limitations. The research studied cases that were all located within the same geographical area, which resulted in a rather homogenous group of cases. Beyond their geographical proximity to one another, the firms also had similar characteristics in terms of ownership with all cases being owner-operated and still owned by the founder of the firm. While this led to firms studied having similar concerns and experiences to some extent, it is



probably not an accurate reflection of the broader value-added SME population in British Columbia.

As time and financial resources for the research were limited, the number of cases involved had to be limited four. Had more resources been available, in-depth interviews with a greater number of firms would have been conducted to provide a larger sample of the value-added SME population and a greater exploration of relationships up and down the supply chain would have been undertaken. As relationships along the supply chain have proven to be important for the cases studied, interviews with suppliers and clients would have increased the study's credibility by not only having to rely on the firm owners' perspective and opinion. Similarly, as all cases were private firms, access to financial information was not available and the owners' word had to be taken with regards to financial performance.

### **4.3 Further research**

Although there was an existing body of work examining different aspects of the value-added wood products sector in British Columbia at the time the research began, an in-depth, thorough look at what individual firms see as keys to their success and barriers to achieving their potential. As this study has shed some light on the day-to-day concerns of value-added sector SMEs, it has opened up a number of avenues worthy of exploration in future research.

Following the approach developed by Rubin and Rubin (1995) and adapted for this study, it would be very interesting to expand this research to include a greater number of firms in the Interior region to paint a more accurate picture of the situation for SMEs in the value-added sector operating in the region. While it can be expected that the idea of the production function

will, once again, be at the forefront of discussion with a new set of owners, a greater number of cases will allow the research community and policy-makers to have a clearer idea of what needs are most pressing and which issues are the most important to firms. For example, while the issue of land availability was discussed at length in one of the case studies, it was not brought up by some of the other firms; an understanding of whether or not land availability is a wide-spread issue or simply one that applies to a select few firms would allow policy makers to address the issue in a more informed manner.

As the operating environment for SMEs is different in other regions of the province, the subject of the research would be well-served by a similar study in the Coast region, which also sees a high number of value-added forest product manufacturers, as well as in the Lower Mainland where a study of the dynamics of the value-added sector in an urban environment might reveal interesting similarities and differences between rural and urban-based firms. With calls for the British Columbia forest products strategy to move from a high-volume, low-value focus towards a greater role for the value-added sector recurring since the last Royal Commission on Forest Resources in 1976, an understanding of the challenges faced by value-added firms and the keys to their success is an important first step in answering those calls. By having a reliable, representative sample of the value-added SME population, we can begin to construct strategies to improve the performance of the sector.

The findings of the study, the results of further case studies, along with the body of research already in the literature can be used to construct an effective survey to reinforce the findings and test various hypotheses with regards to the value-added sector. One such hypothesis, which comes as a result of this multiple case study, is that management skills are both the most significant factor in a firm's success and its most substantial barrier. From the

results gathered in this thesis, it appears that while access to fibre, financing, and skilled labour are tremendously important for the firms involved, these areas of the business are inseparably linked and dependent upon the manager's skill. Testing this hypothesis, among others, would greatly improve policy makers' ability to concentrate their investment efforts in ways that would be most beneficial to this important industry sub-sector. A greater degree of knowledge from both business owners and policy makers is perhaps the best way to develop the value-added sector in a sustainable way.

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# Appendix I

## Policy Timeline 1976-2009

### **1976:** Royal Commission report (Pearse)

- *The report presents a number of recommendations to ensure tenure security, improved timber products market structure, and more consideration for environmental impacts of forestry activities.*

### **1978:** Forest Act amendments (and Ministry of Forests Act).

- *Determination of AAC is clearly laid out.*
- *Environmental concerns and values are treated explicitly.*

### **1980:** Small Business Forest Enterprise Program (SBFEP)<sup>21</sup>

- *Program established to help small entrepreneurs get access to timber and reduce the barriers to entry to new entrants.*
- *Three eligibility categories are established based on a number of factors including AAC apportionment and shareholder status with major licensees.*
- *Overview of the three categories:*  
*Category 1 – market loggers;*  
*Category 2 – sawmill owners and value-added processors;*  
*Category 3 – applicant intends to own or lease timber processing facility.*

### **1982:** Lumber I

- *The International Trade Commission looks into competitive factors affecting U.S. and Canadian lumber producers.*
- *The Coalition for Fair Canadian Lumber Imports (CFCLI) files a petition seeking countervailing duties (CVD) on Canadian Lumber entering the US on the basis that Canadian lumber is subsidized.*
- *In March of 1983, the Department of Congress determines that Canadian Lumber is not subsidized.*<sup>22</sup>

### **1986:** Lumber II

- *The Coalition for Fair Lumber Imports (CFLI) files a CVD petition arguing that Canadian stumpage represents a subsidy.*
- *The issue is resolved in December 1986, with the signing of a Memorandum of Understanding (MOU).*

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<sup>21</sup> Ministry of Forests, 1999

<sup>22</sup> Random Lengths, 2010.



**1988:** Expansion of the SBFEP

- *5% of timber held in various other forms of tenure is taken back by the province and re-allocated to the SBFEP; approximately 9 million cubic metres.*
- *Timber rights are allocated one of two ways:*
  - *competitive sales: logging rights go to the highest bidder (section 20 sales) ; or*
  - *bid proposal: award of a bid proposal based on criteria focused around value-added wood products. Bid proposals are commonly referred to as “section 21 sales”.*

**1991:** Forest Resources Commission report (Peel)

- *Report proposed a series of changes such as a trade-off between the amount timber allocation and timber security.*
- *Advocated for the adoption of a system of forest practices that would bring together renewable resource management, land use planning, and harvesting techniques.*

**1991:** Canada opts out of the MOU with the U.S.

**1992:** Timber supply review initiated

- *Timber supply reviews (TSR) are meant to review short- and long-term effects of current forest management practices on the availability of timber for harvesting from timber supply areas (TSAs) and tree farm licenses (TFLs) throughout British Columbia.*
- *TSRs also incorporate socio-economic analyses of their respective TSAs.*
- *Each TSA will have a TSR every 5 years.*

**1992:** Lumber III

- *Having found that Canadian stumpage and log export controls conveyed subsidies, the U.S. Department of Commerce imposes CVDs on all Canadian lumber imports except lumber originating from the Maritime Provinces.*
- *Canada fights the Department of Commerce ruling. Between 1992 and 1994, a number of rulings in favour of Canada result in the CVDs being refunded.*

**1993:** Clayoquot Sound Land Use Decision

- *A number of high profile protests in response to the Clayoquot Sound land use decision bring international attention to forestry activities and forest management in British Columbia.*
- *As a result, future land use decisions will face heightened scrutiny.*

**1994:** BC Forest Renewal Act & Forest Land Reserve Act

- *The BC Forest Renewal Act aims to reinvest government forest revenue into the forest resource.*
- *The Forest Land Reserve Act authorizes the regulation of forest practices on private land.*

#### **1995: Forest Practices Code**

- *Brings together the many policies regulating forest practices that previously spanned a number of different documents.*
- *The Code imposes regulation regarding biodiversity, silviculture and clearcutting and formally includes ecosystem-based management (EBM) into policy dialogue.*

#### **1996: Softwood Lumber Agreement signed with the U.S. (SLA I)**

- *Trade agreement through to 2001.*
- *The agreement consists of a tariff rate quota system in which BC, Alberta, Ontario and Quebec are assigned quotas. Individual companies within the provinces are allocated portions of the provincial quota.*

#### **1997: Jobs and Timber Accord**

- *The Jobs and Timber Accord intended to create 22,400 new direct jobs in the forest sector through a series of incentives and compliance measures by 2001<sup>23</sup>.*
- *One of the initiatives laid out is the Innovative Forest Practices Agreements (IFPA) Initiative. IFPAs are agreements by which designated licensees are given opportunities to increase their allocated harvest levels and maintain and enhance employment while the Ministry of Forests uses IFPAs to conduct several pilots to test new and innovative forestry practices.*

#### **1998: Community Forest Agreements**

- *Developed by the Ministry of Forests and stakeholders interested in creating opportunities for greater participation by communities and First Nations in the management of local forests.*
- *Amendments to the Forest Act created this new form of tenure.*

#### **2001: Lumber IV**

- *Representatives from Canada and the U.S. fail to negotiate an extension to the existing SLA. CFLI files for CVDs and anti-dumping duties against Canadian lumber producers.*
- *The dispute continues with different stages of negotiations and groups like CFLI and Free Trade Lumber Council weigh-in on the dispute consistently.*

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<sup>23</sup> Cashore, et al. 2001

- *Despite earlier rulings by the U.S. International Trade Commission, in 2005, NAFTA's Extraordinary Challenge Committee rules that Canadian lumber imports do not pose a threat to the US lumber industry.*<sup>24</sup>

### **2003: British Columbia Timber Sales replaces SBFEP**

- *As a central part of British Columbia's Forestry Revitalization Plan<sup>25</sup>, BC Timber Sales (BCTS) has as its mandate to develop and sell publicly-owned timber to establish market price and optimize net revenue to the Crown<sup>26</sup> (section 21 sales no longer offered, only section 20).*
- *Approximately 20% of the provincial allowable annual cut (AAC) is reallocated away from major licensees (licensees with upwards of 200,000m<sup>3</sup> of replaceable AAC<sup>27</sup>) and to small-scale tenures and BCTS.*
- *A grandfather clause is in effect for existing Category 2 and 3 registered enterprises; no opportunity for new entrants in Category 2 or 3.*
- *New registrants may only register in Category 1.*

### **2004: Forest and Range Practices Act**

- *The Forest and Range Practices Act (FRPA) replaces the Forest Practices Code.*
- *FRPA covers various areas of forest and range management including timber and forest health.*
- *FRPA aims to strengthen BC's global competitiveness, enhance timber supply while maintaining a balance between environmental, social and economic interests, and reduce costs to industry and government as well as reduce the complexity of legislation surrounding forest and range management.*<sup>28</sup>

### **2006: New Interior Log Grades & market based pricing system**

- *New grades will be based on the log's size and quality at the time it is scaled, or assessed, regardless of whether the tree was alive or dead at the time of harvest (as per the previous grading system).*
- *Stumpage rates for Crown timber from major licenses are now determined based on bids for rights under other tenures, adjusted to reflect differences in tenure obligations.*

### **2006: Softwood Lumber Agreement signed with U.S.**

- *An agreement between Canada and the U.S. is finalized in October, 2006.*

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<sup>24</sup> Random Lengths, 2010.

<sup>25</sup> Niquidet, 2008.

<sup>26</sup> BCTS, 2003.

<sup>27</sup> Niquidet 2008.

<sup>28</sup> BCMoF, 2004.

- *The agreement, valid to 2013 with an option for two additional years, states that taxes ranging from 5-15% or quotas on Canadian exports to the U.S. will be in effect if the Random Lengths Framing Lumber Composite Price is \$355 or below.*
- *Canadian provinces have the option to choose between a regime that has them paying taxes only; or one that has lower taxes combined with a quota. British Columbia chooses Option A, which has higher taxes, but no quota.*

#### **2009: Canadian Federal budget**

- *In response to the world-wide recession which began in 2008 and the troubles experienced by the forest industry as a result, the federal government budget earmarks \$170million in direct assistance to the forest industry.*

#### **2009: Report of the Working Roundtable on Forestry**

- Among other recommendations, the report encourages investment in value-added wood products.

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## Appendix II



THE UNIVERSITY OF BRITISH COLUMBIA

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### **Philip Grace**

Masters Candidate, Forest Resources Management  
2227 – 2424 Main Mall

Vancouver, BC, Canada V6T 1Z4

Tel: 604.822.9048

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DATE

NAME and ADDRESS of Participant

Mr./Mrs./Ms \_\_\_\_\_,

I would like to take this opportunity to invite you to participate in a case study as part of a research study for my Masters thesis in the University of British Columbia's Faculty of Forestry in the Department of Forest Resources Management.

Under the supervision of Dr. Harry Nelson, I will assess the factors that contribute to success in small value-added forest product companies as well as the challenges these firms face when they are experiencing difficulties. I have opted to focus on the NAME OF TIMBER SUPPLY AREA for my research.

You are being invited to take part in this research study because of your involvement in the value-added forest products industry as an employee/owner of COMPANY NAME. LOCAL CONTACT's NAME, manager of the LOCAL CONTACT's COMPANY, suggested that I contact you.

Should you be interested in participating, you would be asked to commit approximately 1 hour of your time to answer a series of questions about the value-added forest products industry in the NAME OF REGION, as well as some questions relating to the value-added firm you are associated with. The initial interview process will take

place from June through to September, 2010; the exact date of your interview, should you choose to participate, will be determined at a later date.

Your participation in this study would be much appreciated and very helpful in my research. Please let me know if you would be willing to participate in this study by email at [phil.grace.stfx@gmail.com](mailto:phil.grace.stfx@gmail.com) or by telephone at 604-822-9048.

I look forward to hearing from you.

Regards,

Philip Grace

## Appendix III



THE UNIVERSITY OF BRITISH COLUMBIA

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### **Philip Grace**

Masters Candidate, Forest Resources Management  
2227 – 2424 Main Mall

Vancouver, BC, Canada V6T 1Z4

Tel: 604.822.9048

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## **CONSENT FORM**

***“Assessing factors contributing to successes and the barriers to success in small value-added forest product enterprises”***

### **Principal Investigator:**

Harry Nelson  
Assistant Professor  
Department of Forest Resources Management  
University of British Columbia  
Tel: (604) 827-3427

### **Co-Investigator:**

Philip Grace  
Graduate Student (Masters of Science Candidate)  
Department of Forest Resources Management  
University of British Columbia  
Tel: (604) 822-9048

The research is part of the student's thesis as part of the requirement for his graduate degree. The results of this study will be included in the thesis, which is a public document.

### **Purpose:**



The objective of the research is to gather information about the risks associated with small value-added forest enterprises and the potential to provide incentives that exist for investors to enter the value-added forest products industry.

You are being invited to take part in this research study because of your involvement in the value-added forest products industry as well as your knowledge of the geographical area of study, the NAME OF TIMBER SUPPLY AREA.

**Study Procedures:**

Should you choose to participate in the research, you will be asked a series of question relating to the forest products industry in the NAME OF REGION region of British Columbia as well as questions which are directly related with your value-added forest products company.

The interview process will require a commitment of approximately one hour for the initial interview, as well as one hour for a possible follow-up interview.

The researcher will use an audio-recorder to record the questions and answers provided in the interview.

**Potential risks:**

No potential risks associated with participating in this research study have been identified.

**Potential Benefits:**

No immediate benefits associated with participating in this research study have been identified.

**Confidentiality:**

All notes and audio recordings from the interview will be kept in the Co-investigator's office which will remain locked and only be accessible to the Principal Investigator and Co-Investigator.

**Remuneration/Compensation:**

No remuneration or compensation of any sort will be provided for participation in the research.

**Contact for information about the study:**

If you have any questions or desire further information with respect to this study, you may contact Harry Nelson by telephone at (604) 827-3427 or by email at [harry.nelson@ubc.ca](mailto:harry.nelson@ubc.ca); or Philip Grace by telephone at (604) 822-9048, or by email at [phil.grace.stfx@gmail.com](mailto:phil.grace.stfx@gmail.com).

**Contact for concerns about the rights of research subjects:**

If you have any concerns about your treatment or rights as a research subject, you may contact the Research Subject Information Line in the UBC Office of Research Services at 604-822-8598 or if long distance e-mail to [RSIL@ors.ubc.ca](mailto:RSIL@ors.ubc.ca) or toll free 1-877-822-8598.

**Consent:**

Your participation in this study is entirely voluntary and you may refuse to participate or withdraw from the study at any time.

Should you choose to withdraw from the study prior to its publication, your comments and/or feedback will be removed from the record and not be included in the final publication.

Your signature below indicates that you have received a copy of this consent form for your own records.

Your signature indicates that you consent to participate in this study.

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Participant Signature

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Date

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Printed Name of the Participant