VII EXPANDING THE TRADING HOUSE OPTION

The preceding chapters of this report have identified and examined the important role and function of trading houses in Canada and have attempted to address the problems and opportunities faced by this sector. An investigation of the trading house issue would, however, not be complete without an examination of potential new participants in this arena and the application of the trading house concept to traditional international marketing structures and methods.

In this context, the final chapter will examine the potential for direct involvement in trading houses by Canadian banks, the participation in exporting by the distributive trades in Canada through the use and formation of trading houses, and the adoption of the trading house concept by diversified and multi-product Canadian companies as an organizational approach to international marketing.

CANADIAN BANK INVOLVEMENT IN TRADING HOUSES

The Task Force's examination of this subject was given impetus by several factors. In a letter dated March 29, 1984, the Task Force was directed by the Minister for International Trade to examine the issue of bank ownership and operation of trading houses. This request was based upon a recommendation adopted by the Export Trade Development Board to that effect.

As well, in our own review, we have noted the recent developments in the United States with the passage of the U.S. Export Trading Company Act of 1982 (examined in Chapter II), the longstanding bank involvement in trading houses in Europe and other countries, the rising frequency of countertrade, the capitalization needs of existing trading houses, and the need to involve more small and medium-sized companies in exporting. All of these points give weight to the need to consider how Canadian banks might become more involved in the Canadian trading processes.

Several points of interest can be raised with respect to the U.S. and European situations.

(1) Bank involvement in trading houses in some European countries, notably Great Britain, France, Germany, Holland, and Switzerland, exists through direct investment by the banks, and indirectly through non-banking subsidiaries and shareholding networks. This involvement stems from historical and economic developments, and recognizes that banks can be active partners with industry in their home country in the interest of expanding overseas sales.

(2) In the case of Japan, the relationship between banks and trading houses is well known and documented. Brazil and South Korea have followed similar examples in encouraging the establishment of their own general trading companies.

(3) In the United States, legislation was amended to allow banks to invest in trading companies in an effort to assist in the creation of new U.S. exports. This change was intended to respond to the problems of the existing U.S. trading house structure which, as in Canada, is characterized by mostly privately-owned firms restrained in their ability to raise capital, and which are among the lowest ranked firms in bank loan ratings. As stated in Chapter II, Congress recognized that if U.S. export trading companies were to be successful in promoting U.S. exports and in competing with foreign trading companies, they should be able to draw upon the international resources, expertise, and knowledge of the U.S. banking system.

(4) Given the close inter-relationship between the U.S. and Canadian economies, Canadian banks face a potential disadvantage, vis-à-vis their American competitors in Canada, in offering services to their clients, and in becoming more involved in trade facilitation.

Countertrade, examined in Chapter VI, is a growing trade dimension that can be expected to affect more Canadian exporters in the future. The Canadian banks offer some services in this area which could be expanded in a manner similar to those being offered by their U.S. and European competitors presently. If Canada is to compete effectively in an increasingly competitive global marketplace, it must develop the necessary expertise. Permitting Canadian banks to have greater involvement in trading companies that can provide countertrade services, is a step in the right direction.

Finally, the services of trading houses are essential for assisting small and medium-sized manufacturers to export. Bank participation in this area will provide another linkage to existing and new manufacturers in the delivery of their goods to international markets. In addition to creating new exports, this involvement has a potential for leading to greater understanding of, and support for, small manufacturers by the banking community as a whole.

The Task Force envisages several potential scenarios for increased bank involvement in trading houses. These might include:

(1) Joint participation in trading houses, export consortia or export marketing companies;
(2) Participation in overseas projects;
(3) Provision of full countertrade and financing services through bank-owned trading houses;
(4) Combination of working capital, financing and international marketing services for small and medium-sized manufacturers and producers;
(5) Expansion of sales and markets of Canadian raw materials and commodities through bank-owned trading houses; and
(6) Participation in joint export marketing companies in the high technology, telecommunications, resource, electronics, transportation, and engineering services fields.

As well as those kinds of direct involvement, Canadian banks can also be expected to make increasing contributions to the success of Canadian trading houses if they implement the kinds of recommendations made in Chapter IV of this report.

Currently, the general prohibition against Canadian banks dealing in goods and trading, contained in Section 174 of the Bank Act, precludes a bank from taking title to goods for commercial trading purposes. The Act states:

174 (2) Except as authorized by or under this Act and in accordance with such terms and conditions, if any, as are prescribed by the regulations, a bank shall not, directly or indirectly:

(a) deal in goods, wares and merchandise or engage in any trade or business;

The Act also contains provisions limiting the ownership in non-banking companies to 10 per cent.

As was seen in the U.S. example, bank participation in this field has led to numerous trading stragegies being followed on the part of the banks. However, given the early stages of the U.S. development, perhaps its most important effects have been a better understanding and accept-