

# Intelligence MEMOS



From: Peter Hall  
To: International Trade Watchers  
Date: January 12, 2024  
Re: **NEAR-SHORING AND SMES: BENEFITS AND COSTS**

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Business investment is being rocked by a new movement. Proof is pouring in that near-shoring is taking the world by storm. That is, as far as we can tell at this point.

This wave is so new that it's going to take time for the data to catch up to the trend. And of all the economy's big numbers, investment data is notoriously hard to quickly pin down. We have to rely on anecdotes, and these – Honda's reported consideration of Canada for a \$13.8-billion electric vehicle project is just the latest – are yelling out pretty loudly that something big is afoot. So what does it imply for small and medium-sized enterprises (SMEs)?

One of the key reasons for this massive change of mindset is supply-chain security. We vowed we'd bring our supply chains closer after SARS, after tsunamis, after the global financial and economic crisis and never really followed through. These events sowed the seeds, however, and the COVID-19 pandemic pushed us over the edge. Supply chains became so compromised for so long – we are still absorbing the fallout – that we'd had enough. Now, near-shoring is really happening.

Proximity is obviously key. The long-run costs of far-flung supply chains are perceived to be greater than their so-called “short-term” efficiencies. If this is the case for large companies, then it is certainly so for SMEs. Compromised supply chains have immediate cost implications. Simply put, supplies are short, and there's a bidding war for what's available.

SMEs can't compete with cash-rich monoliths on price. If they try, it likely comes straight off the bottom line. Even if SMEs do meet price demands, they may still not get product. Typically, suppliers will favour large accounts, making sure they are serviced at the expense of the small folks. Then there are the demands of SMEs customers. Cost-containment is still their aim, so their sympathy for supply constraints, labour shortages, general inflation and the like only goes so far; they'd expect their SME suppliers to find efficiencies elsewhere. Finally, with access to cheap financing now just a memory, it is doubly hard for SMEs to manage cash flow.

Against these significant challenges, bringing supply chains closer is thought to make them more manageable and secure. In theory, production lead times are shorter. Output is not as easily stranded by weather and other natural phenomena. Political alignment is also a perceived objective: Shifts in politically unstable or politically misaligned nations are avoided by locating in zones that are closer politically as well as geographically. Legal proximity is increasingly seen as a must, as the need to protect intellectual property is critical to achieving and/or maintaining digital supremacy. And sadly, military proximity has emerged as a key factor, with the recent rise of actual and threatened conflict on multiple fronts.

Thus far, the benefits are really about risk mitigation. There are also more obvious opportunities created by near-shoring. Bringing activity back into a more local orbit creates more local jobs and spinoffs (not to mention political photo-ops). Local clustering of activities also creates research and development opportunities not as easily afforded by remote activities. This in turn gives rise to the application and commercialization of new technologies that are essential to maintaining a technological edge.

If the costs of compromised supply chains are disproportionately high for SMEs, it follows that the security, manageability and predictability of near-shoring yields a relatively greater return for SMEs. It also creates a more reliable investment environment. This is an opportunity to address more than a decade of under-investment, and to improve and enhance Canada's global competitiveness.

It remains to be seen whether near-shoring's benefits will outweigh the benefits that globalization brought for consumers and businesses. Higher prices and fewer export opportunities in far-flung markets may be the result of a general trend toward near shoring. In the meantime, it is happening, and SMEs will need to leverage opportunities closer to home in order to go head-to-head with competitors across the world.

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