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The Case for Developing Canadian Private Equity Capacity

The Canadian business community would feel more comfortable about the increasing role of private equity, and would be less worried about the “hollowing out” of corporate Canada, if Canadian private equity had the capacity to lead the way. This is according to this quarter’s survey of C Suite executives.

These are issues of great interest to Canadian business leaders. News coverage of Canadian interests falling into foreign hands and of the sale of BCE were among the most closely followed news stories among executives.

In addition to being interested, they are concerned. A majority of executives now say that, rather than being completely open to foreign investment and ownership, Canada has some industries of such strategic importance that they require some Canadian ownership. And they worry that policy is driving the dynamic the wrong way. There is no Canadian company that is too big to be taken private now. Most already think it is easier for Americans to buy Canadian companies than it is for Canadians to buy American companies. Add to that the belief that the decision to tax income trusts is going to lead to sales of Canadian companies to foreign interests.

On balance, most see the increasing role being played by private equity as a positive development. However, underneath the surface it is clear that many are conflicted. Private equity is seen to be good for business and investors – offering better returns for individual investors, more effective management of companies, more emphasis on growth, and a sharper strategic focus. However, executives see private equity as bad for the country – fewer Canadian owned companies, weaker contributions to the Canadian economy and to communities, and worsening labour relations.

One third of executives say that they have a more favourable opinion of Canadian private equity than they do of foreign private equity. The rest say that they are ambivalent. But if one looks at their views of the impact of private equity, most of the concerns the C Suite has would relate to a foreign private equity investment – the loss of Canadian ownership, of Canadian control, and of Canadian based head offices. Over 40% of executives who think it is important to retain Canadian ownership in strategic industries favour Canadian private equity over foreign private equity. Over half of executives who have a negative view of the increasing role played by private equity say that they favour Canadian private equity. A majority of all C Suite executives think that private equity firms are contributing to the hollowing out of corporate Canada.

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Clearly, the role of private equity is becoming linked with the debate over foreign ownership and hollowing out. The C Suite clearly thinks it is in the interests of business to consider private equity arrangements, and it is in the interests of Canada that those sources of private equity be Canadian. The policy solutions will no doubt be difficult to find. Executives reject the idea of tax disincentives to limit the influence of foreign private equity in Canada. The other option is to encourage the development of Canadian private equity options – whether corporate or institutional such as pension funds. Despite the strong performance of the economy and optimism for the coming year, executives are looking for policies from government that boost the competitiveness of the Canadian economy. The government is losing the confidence of the business community, in part because it is not seen to be addressing the major challenges facing the economy. Executives have repeatedly told us that issues of human resources, currency adjustment and corporate taxes are fundamental to their success. Helping the economy adjust to the changes brought by both the increasing role of private equity and the aggressiveness of foreign buyers is another of those challenges, and a clear government agenda regarding both Canadian ownership and Canadian equity options – based on developing Canadian capacity rather than a punitive approach to foreign investment - would be welcomed.

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