

ADDRESS TO THE CANADIAN CLUB OF TORONTO

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by

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Gentlemen,

I was very pleased to receive an invitation from your President to address your distinguished Club. There was some hesitation on my part in accepting this invitation, firstly because making speeches is not my forte, and secondly because my plate, this year particularly, has a lot on it. However, this was the first time that you had extended a speaking invitation to the President of the Investment Dealers' Association and since we will attain our 50th Anniversary this year I felt I could not decline.

I have been reading most of the speeches made before you this year and, somewhat like La Bruyere, I feel that "Tout est dit et l'on vient trop tard" - "Everything has been said and we come too late". Also, realizing that while we can only invent with memories, naturally mine cannot go as far back as some of yours.

There is a tremendous amount of interest these days in the ownership of Canadian companies. This interest also bears on the availability of capital to both develop new enterprises, enlarge existing ones and perhaps buy interest in companies controlled by foreigners. This interest starts with politicians, through the businessman and right down to the man on the street. I thought it would be apropos for me to entitle my address "A Case for Investing in Canada" and review with you:

- 1 - Our investment community;
- 2 - Our merchandise; and
- 3 - The climate in which we operate.

Our Investment Community

I think it can be fairly said - and in fact a former Governor of Bank of Canada did say - that the financial machinery existing in Canada for the placing of new issues is as good as that of any other country in the world and, in proportion to our size, year in and year out probably raises more new capital than any other country in the world.

The ~~well-worn~~ cliché - "from humble beginnings" - does not quite describe the manner of our birth. At the time of the outbreak of war in 1914 Canada was borrowing, chiefly from Great Britain, about \$1 million a day for federal, provincial, municipal, railway, industrial and other purposes. The needs of a war economy in Britain soon put a stop to that. The United States market filled the gap for a few months, but it too closed to us by the end of 1915. From that date, Canada was on her own. In 1916, to facilitate the mobilization of domestic savings to carry our share of the cost of the war, the 32 Investment Dealers then functioning in this country formed what later became the Investment Dealers' Association. Thus, our Association came into being somewhat dramatically in response to a critical national need.

The first task was the organization of the First Victory Loan Campaign. In six loans between 1916 and 1919 over \$2.2 billions was raised in Canada from 2,800,000 subscribers, out of a total population of less than 8 million. This experience served to bind the various underwriting and distributing operations into a cohesive and workable whole. The period between the wars saw the financial industry flourish, only to suffer no less than the rest of the country from the economic collapse in 1929 and the depression that followed.

When World War II started, again it was to the Investment Dealers that the Government turned. Staffed at the national, provincial and regional levels by IDA personnel, the National War Finance Committee succeeded in raising a total of \$13 billion through 23 million individual bond subscriptions. In the 9th Victory Loan, a bond was sold to one in every three of the population.

Since the war we have experienced our greatest growth period. In the five years from 1961 to 1965 inclusive, new Canadian bond financing alone amounted to no less than \$62 billion. The original membership of 32 in our Association has now grown to 179, with representation right across the country.

The expression "Investment Community" embraces, not only the members of the IDA and the stock exchanges, but also investing organizations such as insurance companies and pension funds, and financial intermediaries such as the trust companies and the chartered banks, which act both for their own account and for their customers. All of these organizations, however, use the facilities provided by the investment dealers and the stock exchanges to implement their investment transactions. The dealers originate and distribute new issues, and maintain day-to-day trading markets in outstanding issues--on the exchanges for listed stocks and in the between-dealer market for bonds and unlisted stocks. Because of the need to provide investors with a full range of services, the functions of raising new money through new issues (that is, underwriting) and acting as agent for trading existing securities (that is, brokerage) are frequently available in the same organization. Of 179 members of our Association, 125 now own 1 or more seats on stock exchanges.

The Merchandise

The merchandise we deal in can be divided into two categories: fixed income securities and equities.

The market for fixed income securities is naturally related to the ease or tightness of money, the credit of the account borrowing, the length of term, the conditions of the loan, etc. Within our country, interest rates are related to the top credit - the Federal Government. Vis-a-vis the U. S. market, there is a difference of about half-a-point to a point in the interest rate for comparable credits. For the purpose of my talk I see no need to discuss further these securities.

I wish to speak chiefly on equities because they are the vehicle which really reflects the prospects of our future. I would divide equities into "Blue chip" shares and new venture shares. By "new venture" I am not referring to promotional securities but principally to industrial issues which are coming to the market for the first time usually as a result of an underwriting by an investment dealer. By "blue chip" I mean the shares of existing companies that have become well-established and are widely held as conservative investments. Both of these classes of securities represent investment in the future growth of the ownership interest in Canadian business.

What is the opportunity to be shared in by the purchase of these securities? Here are some of the facts that we so often hear but that I think can still bear repetition.

The population in this country continues to grow faster than in the U. S., and most markets for industry are a function of population, at least in the western hemisphere where living

standards are high. With a growing population and hence a growing market, a larger degree of mechanization becomes possible, and this means lower unit costs on present production, thus improving export competitiveness. It also means that production here of more things previously imported, becomes economically feasible.

The increase in real output in Canada has substantially exceeded the average of all those leading industrial countries in the world which constitute the members of the Organization for Economic Cooperation and Development, (except for Japan).

• Canada on a per capita basis, has more natural resources, both in variety and quantity, than any other nation in the world. Here are some interesting figures: for the last five years, the Gross National Product in Canada has risen 35% as compared to 30% in the United States; industrial production here has risen 29% as compared to 25% in the United States; and corporate profits have risen 28% in Canada as compared to 24% in the United States. Not all comparisons of this sort would be favourable to us, but these are given to show that we have a tendency to grow faster than the more mature economy to the south of us.

As to potential, I believe that no other country offers a greater attraction for investments than does Canada, at least for Canadians. In the 1950's, Canadian stocks were probably over-valued in comparison with United States stocks. This was doubtless due to the tremendous interest by European and American investors in Canada at that time. However, things have changed. A common measure of the level of equity prices is how many dollars must be paid for a dollar of earnings -- the price/earnings yardstick. Today for investment-quality equities in the U. S., the market is 18.8 times earnings as compared

to 17.1 times in the Canadian market. Fourteen years ago the figures were the other way round. The price-times-earnings ratio in both countries was then, of course, much lower, but it was higher in the Canadian market at 9.6 than it was in the United States market at 8.5. There has now developed a willingness to pay a considerably higher price for one dollar of earnings, but on the other hand, there has been considerable disenchantment among foreigners over investing here and, of course, the Americans have been discouraged by recent legislation in that country. Thus, in terms of what you can do with capital today, it costs you less to buy one dollar of Canadian common stock earnings than to buy one dollar of similar American earnings. In addition, of course, there is the dividend tax credit which gives an additional dividend yield advantage to Canadians investing in Canadian stocks.

In recent weeks ^I~~we~~ have been conducting a one-man poll of professional investors and most of them think that our economic growth in the next decade should be at a faster rate than in the United States. However, some professional investors are not investing as heavily in Canada as they might. In this connection I cite the recent statement of one of our bank presidents ~~who pointed~~
~~out~~ that, on a per capita basis, investment by Canadians in the U. S. is at least 50% higher than the investment of United States citizens in Canada. Now why is it that these professional investors, who themselves see Canada as a land of investment opportunity, in fact buy heavily in the American markets? There are a number of factors which bring this about and these factors influence importantly the climate that surrounds our business today. I would now like to discuss several
^{FACTORS}
of these with you.

The Climate in which we operate

The main causes that explain the preference of the professional investor for U. S. equities versus Canadian equities include:

- 1 - Broader U. S. market;
- 2 - Wider selection of stocks;
- 3 - Availability of research;
- 4 - Fuller and more frequent financial reporting by U. S. companies;
- 5 - Legislation;
- 6 - The political atmosphere.

1 - The Broader Markets

There are three principal stock exchanges in this country - Toronto, Montreal and Vancouver and as they are geographically widely separated, they tend to be regionally oriented. They are in three different provinces and each province has standards of its own. The IDA, a voluntary national organization, also has some regional orientation. The handicap of relatively small and scattered domestic markets makes it very difficult to compete with the giant market in the U. S. so we are striving for better liaison within our industry and are trying to bring about common standards across the country. For example, the IDA has made available to the exchanges one of its educational courses and, together with these exchanges, we have

created the Canadian Securities Course which must now be passed by all those who wish to sell securities for any of our Members. I sincerely hope that this is only a first step of liaison within the community and that, in time, we may be able to tackle measures that would not only raise the standard of our community across the country but would also broaden the market place (one exchange, three floors).

2 - The Wider Selection of U. S. Stocks

A wider selection of stocks is something which can only be cured with the further development of our economy and perhaps, in this respect there may be some merit in making available to the Canadian market, interest in American companies operating in our country.

3 & 4 - Available Research and Fuller and More Frequent Financial Reporting by U. S. Companies

These two topics should be handled together. We can only make available to our clients that information which the companies make available to us. It is understandable that in a younger country we would have less formal and detailed requirements. However, if it is going to be to the advantage of all, then our disclosure regulations should be revised.

5 - Legislation

As part of the climate, I would like to say a word on securities laws. This is a field the provinces are jealous of. We, theoretically, have to deal with ten securities acts in ten provinces. Although the Securities Commissions across the country have been getting together more often, we still feel - and I believe that the Commissions feel the same way - that there is not only a need for uniformity but

for a community of interests. Our Association does not advocate a Federal Securities Commission. We would not want to add the burden and expense of having to deal with an extra ^{body} body. The cost of raising money is sufficiently expensive as it is, but we feel the provinces could only gain by adopting uniform or, at least, similar legislation that would bear the Canadian stamp. All borrowers as well as lenders would benefit. The same thing can be said of corporate legislation. Work on a uniform ^{PROSECUTION} Companies Act started, believe it or not, in the late '30s. A succession of conferences resulted in many proposals but, so far, not one province has definitely adopted the product of all this effort.

Perhaps the best indication of the need for more co-ordinated government effort in the area of corporation and securities legislation is the recent excitement caused by the U. S. Securities & Exchange Commission demanding that any Canadian company with more than 300 American shareholders must file, in Washington, a great deal of corporate information that is not required here ~~at all~~. The significance of this American demand is simply that our standards are not acceptable to them.

6 - Political Atmosphere

Lastly, to describe our "climate", I would like to speak about the political atmosphere. For years Canada was considered ~~not~~ ^{ANY} only a safe haven for investment capital but ~~also~~ a country with excellent growth possibilities. However, harmony is something that seems to have disappeared from the Canadian political scene. The way our governments have conducted their affairs in the last six to ten years has produced an environment that is not altogether encouraging to investment capital.

The differences of opinion between the provinces and Ottawa certainly have raised doubts in the minds of investors as to what the future holds for business in the way of costs, including, of course, taxes. Unless we have a strong and able central government, we could very well have a continuing deterioration of our investment environment. I do not think that concern from this point of view, by itself, is affecting investment decisions of institutional investors but the latter are well aware that foreign investors are taking a much less optimistic view of investment opportunities in Canada.

Because money is really our merchandise, I feel strongly about the priorities for its use. I would be the first to agree that welfare and social capital are both necessary, but how much? I believe that we have embarked on welfare schemes out of proportion to our financial capabilities. At the present time government transfer payments in Canada are said to amount to 12% of the gross national income as compared to 7% in the United States. The U. S. is a mature, fully developed country, capable of bearing a good deal of taxation and still producing surplus savings besides. We are a young country which has to import each year from abroad additional capital funds. You would certainly not feel that a young company should saddle itself with a relatively heavy overhead of fixed charges. Can it be any wiser for a young country to do the same? Not only that, but who is going to

feel able or encouraged to start new business if the larger part of any profit must be earmarked in advance for meeting the cost of government.

In the face of this already heavy burden, we even hear some suggestion of introducing a capital gains tax in this country. This is a matter that I could discuss seriously. However, if you will permit me, I will try to cling to my sense of humour. I would like to approach this from an ^{A BUSINESS MAN'S} ~~investment~~ point of view. Let us consider that the government is a partner with a very special status in every corporation in Canada, and this without investing as much as a token. Then, let us consider that this very Special Partner is entitled to all sorts of special favours and fringe benefits. For instance, without any compensation whatsoever, he wishes to receive from us the list of all those we employ and the salaries we pay them: then, without even having contact with these people, he wishes us to hand him a kickback on every one of these salaries.

As far as his partners are concerned, he deals with them directly, to make sure that he gets an even bigger share. This Special Partner also has the privilege of looking into the expenses of his partners. He wants to know who you take out to lunch, where you take them, what you feed them, where you travel, with whom, what kind of car you drive, whether you use it only for business or whether you use it to go to the barbershop. He doesn't particularly care about the money his partners may decide to invest in new plant, equipment, and so on; but he could kick up quite a fuss about the fact that you may have spent an extra dollar for béarnaise sauce with your meal. Then, at the end of the year, he is anxious to find out whether you have a profit. He may send his spies to check that profit and then immediately he wants about 50% of it. Then he wants to know from you who your other partners are, and if you decide

to distribute to these people the balance of your profit, he will go and see them and try to get another cut. If you don't have any profits, he doesn't even send you a word of sympathy. This indeed is a very Special Partner!

Now, consider that this Partner is thinking that perhaps your shareholders may, in spite of all that I have mentioned before, be able to find a buyer who might want to pay a little more for these shares than they have paid themselves. If that were the case, he is now thinking he can take another bite. Gentlemen, if this Special Partner were my client, I would be tempted to say to him that he has got a pretty good deal going for him and, rather than try to squeeze the lemon further, if anything, he should lighten his terms and try to broaden his market and bring in more customers.

Let us now consider the case of a sole proprietor who draws \$100,000 salary from his company which has a profit before tax of \$1 million. His net after tax amounts to \$250,000. Now, one may think that this is a lot of money for this man, but this man is a busy man indeed, so much so that he needs someone to shave him in the morning, someone to fry his eggs, someone to mow his lawn, someone to drive him to the office, someone to paint his house, someone to fix up the plumbing, etc., By the end of the year, he doesn't have too much left in his pocket. Now, this man is under the illusion that perhaps the money he has invested in his company will increase in value, and perhaps this is the only reason left to him to keep working as he does and, more particularly, for this Special Partner. If he has saved some money, most likely he has it invested in other companies where his very Special Partner also has quite an interest! If we are to take away what seems the last incentive for this man, will he not begin to wonder if it is worthwhile working so hard?

I say to the Special Partner "Leave him his last illusion. When he dies you will be able to take most of what he has left anyway!"

Gentlemen, I say to you, this Special Partner is quite an extraordinary character. I have a feeling that he does not quite know how good a deal he has and he should be very careful about killing the goose that lays such golden eggs. The proper role for government surely is not to compete with its partners but to foster a climate favourable to saving, investment and enterprise . . . in other words favourable to economic growth, to the creation of new jobs, to a higher standard of living for all Canadians.

It would be hard to overstress the importance of our maintaining incentives for all our thousands of businessmen to address themselves to seeking out profitable business opportunities. In some circles, the word "profits" is in disrepute, but it is interesting to note that it is a word in high repute now at the centre of communism, namely, Russia. The well-known Professor Lieberman, of Moscow, has been quoted in "Paris-Match" as saying: "Profit is the indicator of efficiency in production". Some months ago a Russian diplomat was sitting at a dinner beside the President of a large U. S. corporation and, turning to the American executive, he said: "You know, we are

eventually going to surpass you, for the very simple reason that you are busy destroying incentives here with your over-taxation and other restrictive devices, while we in Russia have rediscovered incentives and are using them wherever we can."

Conclusion

The wealth, both human and natural, above and below the surface of this tremendous country of ours, is needed by the world and if we Canadians do not make it available, others may do it for us. I think, vis-a-vis the rest of a hungry and underdeveloped world, we may be the wealthy landowner who could see his property, first coveted and then overrun because he is not developing it for the benefit of the world community.

I am not overly disturbed by the awakening and aggressiveness displayed at provincial levels but I desire to see the central government strong and active in directing its energies for the benefit of the whole country.

Our political, fiscal and economic climate should be such that we should not only attract new capital but retain that which we have. We should not only attract new enterprising citizens but we should keep those whom we have.

Then I, a Canadian with a French accent, have no doubt that Laurier's promise as to Canada's future will be surpassed, and I am convinced that many of my compatriots share this feeling. I hope you do. The case for investing in Canada is good. Let's make it better!