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# Public Venture Markets in Canada

## An overview.

Public venture markets (PVMs) are a relatively new phenomenon on the global stage, though they have a long and therefore unique history in Canada. With the recent development of over 30 new public venture markets worldwide, many countries are recognizing the importance of small businesses in driving economic growth. There have been two key benefits associated with the proliferation of PVMs: emerging companies have gained increased access to capital, and investors have more opportunities to invest in emerging companies, something previously restricted to a small niche of active venture market participants.

PVMs have been operating in Canada for almost 100 years. Over this time, a broad support network has been established to assist emerging businesses, including securities and exchange regulation designed to provide public protection and foster economic growth.

A PVM must be credible and reputable to be viable. Unlike senior markets, where companies have inherent credibility (i.e. IBM, General Motors), in junior markets the credibility begins with the exchange, due to the largely unknown nature of junior listed companies. Stock exchange controls address regulatory risk, not commercial risk. Commercial risk is inherent in emerging growth companies, although a strong regulatory framework does increase a listed company's credibility, its access to capital and, accordingly, its probability of success.

The primary measures of success for Canada's current PVM – the Canadian Venture Exchange (CDNX) – are the amount of financing raised by its listed companies, and the number of listed companies that graduate to a senior market. In 2001, CDNX-listed companies raised total financing of $1 billion. Though down from the $2.4 billion raised in 2000, this figure still represents a significant amount of capital raised by Canadian emerging companies in a down market.

CDNX graduates to The Toronto Stock Exchange (TSE) totaled 26 in 2001 and 45 in 2000. Remarkably, the average increase in share price and market capitalization for the 45 CDNX graduates in the year 2000 was 195 per cent and 302 per cent respectively, as measured over their final 12 months of trading on CDNX. In 2001, the 26 CDNX graduates to the TSE averaged 32 per cent and 107 per cent share price and market cap increases, respectively, over the equivalent period.

However, a number of obstacles to increased participation in venture investing by institutional funds exist.

- Time and cost associated with venture investing generally (it is easier to manage a few large investments than a large number of small investments).
- Lack of specialized investment advice and analyst coverage (only the larger funds can afford to have in-house specialists, although some consulting firms are providing this service in Canada).
- Limited partnership and fund-of-funds products are less prevalent in Canada than in the U.S.
- Pension funds have co-invested among themselves, but many have found this approach costly and difficult due to organizational and logistical challenges (i.e. loss of control for each participant).
- Liquidity is a challenge. However, market participants generally believe that venture investing (whether in the private or PVM realm) means sacrificing liquidity for above-average returns.

On the world stage, relatively new PVMs will continue to battle for market share and there will be market consolidation. Senior exchanges will probably strengthen their ties to their domestic PVMs, as in Canada with the acquisition of CDNX by the TSE. This will help to overcome some of the challenges, as the profiles of PVMs are raised, graduation to the senior markets becomes more seamless, and the cost-adjusted returns of this asset class improve. ∎