Gauging Value Creation in Canada

EDITORIAL

If you spent the summer of 2002 in Toronto, you suffered wretchedly through a garbage strike and record-breaking smog. If you were in the prairies, you saw the worst drought conditions in over a century decimate crops and family farms across Alberta and Saskatchewan. But if you were watching the Canadian economy, there were a few surprising signs of life as the country pulled ahead of the United States with positive signs of economic growth, strong job creation numbers and a booming real estate market.

As fall approaches, one might even start to think that Canada has escaped the kind of market jitters that have badly shaken the U.S. economy in the past year.

But while the storm clouds over the Canadian economy might seem to be dissipating slightly, there are still spots of gloom on the horizon.

Our annual value creation survey looks depressingly similar to last year's—for the second year in a row, Vijay Jog's research shows that in 2001 over half of the most prominent publicly traded firms in Canada destroyed value. In "Value Creation and the Credibility of Financial Reporting in Canada," Jog not only looks at shareholder value, but at the quality of corporate financial statements. The good news is that there don't appear to be any major deviations in the financial statements of Canada's top companies.

More worrying, however, is the ongoing inability of management at more than 50 per cent of Canada's top firms to generate returns on invested capital that exceed costs. And, as Jog points out, that doesn't bode well for the state of corporate governance. He says that, while there is less reason to worry about the quality of reported numbers in Canada, "Boards of directors need to focus on the inability of a large number of Canadian companies to create shareholder value."

That's why Standard & Poor's raised some alarm bells in a report issued in August stating that Canadian corporate credit quality tumbled in the second quarter of 2002 (see Exchange, p. 10). Sadly, 20 per cent of the 141 Canadian companies rated by Standard & Poor's had a negative outlook as of July 9th.

One sign of hope could be the formation of the Canadian Coalition for Good Governance, a group of Canada's most influential investors who have gathered together to promote and encourage good corporate governance. The group is comprised of top money managers and pension funds, including the Ontario Teachers' Pension Plan and the Ontario Municipal Employees Retirement System. The idea is that strength in numbers can help to influence company management when it comes to decision making. And that can only help to make things better.

Here's hoping Vijay Jog's report changes for the better after the summer of 2003. ∎

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