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Maple Leaf Foods fighting to become a global player

By Roger Martin

As Canada transitions to the globalizing world, we are going to face delicate and thorny issues such as the one now being played out at Maple Leaf Foods. In August, Ontario Teachers' Pension Plan (OTPP), dissatisfied with the performance of its big investment in Maple Leaf, sold off a portion to aggressive private equity firm West Face Capital. On Wednesday, Maple Leaf management responded by announcing a plan to make the company internationally competitive with strong brands and a competitive cost structure.

Management concludes that this is the best way to provide attractive returns to shareholders. There is, as always, an alternative: auction the company to the highest bidder, most likely a large foreign food company. That is something that a private equity player with a very short term horizon like West Face might find highly attractive. This raises the question of whether Canadians and large Canadian capital investors like OTPP should care about facilitating the sale of Canadian assets to foreigners.

Foreign direct investment in Canada is by no means a bad thing for Canada. On average, international firms pay higher wages, do more R&D, and are more innovative. They also spur better performance from Canadian competitors and suppliers.

The challenge for us in Canada is to grow a sufficient number of Canadian global leaders to more than compensate for the great Canadian companies we lose. So while it's sad that we lost Canadian ownership of Falconbridge, Inco and Cognos, we've created Research in Motion, Barrick, Manulife and many others.

We need Canada to be a place where global leaders are built, not just a place where foreign global leaders set up shop. A healthy roster of Canadian global leaders means higher wealth creation here in Canada and more opportunities for creative careers for us and our children. It's also a good indicator of the quality of environment we have created for business success and innovation.

To develop these global leaders, we need bold leaders with smart strategies. We also need investors with a long-term perspective. While investors thinking independently of management are important counterweights to poor management and contribute mightily to our economic system, they also make mistakes.

Many of our global leaders succeed in spite of the lack of encouragement they received from the capital markets. Analysts and investors were highly critical of some of the bold and daring moves made by the management teams at companies who ultimately became Canada's global leaders. There were howls of protest when Thomson acquired West Publishing. And when Couche-Tard made its major foray into the U.S. by acquiring Circle K, or when Manulife purchased John Hancock.

And foreign investors have made some huge mistakes. British-Australian mining giant RTZ paid US\$38 billion for Canadian global leader Alcan in 2007 – a \$15-billion premium over its market value. Only one year later RTZ had to write down its investment by about \$8 billion, a massive destruction of its shareholders' value.

And Canada lost a great global leader that we won't get back – a global leader that we might not have lost if RTZ had bid only the post-write-off value, a mere 30 per cent premium over pre-offer market value, rather than the value-destroying 65 per cent premium that won the day.

Michael McCain and his management team at Maple Leaf Foods are attempting to transform an iconic Canadian company into an internationally competitive player. They realize that the status quo is the riskiest option and that their business needs capital investment to achieve scale economies and make the research and marketing investments necessary to have a high-margin branded product line. Look at the list of Canadian icons who didn't seek to become internationally competitive and succumbed to foreign takeovers – E.D. Smith, La Senza, Sleeman Breweries, and Stelco, to name a few. It is exceedingly unhelpful to Canadian firms for the capital markets to fixate on the risks of achieving global competitiveness while largely ignoring the risks of the status quo. In doing so they avoid the consequences of failed efforts to achieve international competitiveness, while at the same time eliminating much of the upside they could also enjoy through the successful globalization of Canadian firms. In discouraging such strategic investments, they are inadvertently threatening Canada's long-term prosperity in our increasingly interconnected world.

I, for one, hope that OTPP recognizes that to have a market to invest in, we have to have globally competitive Canadian companies. Within a couple of decades, there will be no significant public companies with Canada-only franchises. There will be foreign subsidiaries and global Canadian companies – that's it.

Sadly, there aren't nearly enough Canadian CEOs attempting to overcome the disadvantages of our small market through investments in scale and branding to achieve global relevance. Michael McCain is one and we need to help and encourage CEOs like him – not put albatrosses around their necks while they work.

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