

NEWS & COMMENTARY - GENERAL

Income Trusts Dominate Canadian Equity Markets

[Jul19'05] A number of reports have been issued by brokerage firms, dealers and advisors to confirm that the issuance of income trusts is becoming the dominant activity in growth of financial markets.

As summarized by James Langton for InvestmentExecutive.com [\[July 13 article online\]](#), BMO Nesbitt Burns has done a research note to suggest that the issuance of Canadian common stock actually "turned negative" in the second quarter, a first in more than four decades. They say, in effect, that income trusts have "crowded out common stock".

This is new for Canada, but not in other markets. Specifically, common stock has been shrinking south of the U.S. border where "new issues are frequently overwhelmed by leveraged buyouts and share buybacks".

The investment industry here is pleased with the growth of income trusts. As the consulting firm PWC recently noted, new issues of income trusts was more than \$5 billion in the second quarter. And while some of that eliminates common equity through conversion of securities into trust units, it delivers commissions and fees to brokers and bankers, none-the-less.

Many still ascribe the Canadian trend to the tax treatment of trusts because trusts eliminate one level of tax otherwise paid on common equities. But there are other factors involved in the competition for investors' dollars.

It turns out that there are different histories and stages of development in Canadian versus other markets. It turns out there are differences in terms of markets here and there, but also between markets in the U.S. in terms of both the ability or willingness of companies to make distributions and the relative opportunity to attract capital from "income" markets.

We are completing a new study by the iTrustReport, for the end of July, looking at investment opportunities for income-seeking investors. We see that the traditional distributions from market-exchanged units of ownership -- common equity, preferred shares, income or other units -- vary by market as do the relative levels of corporate "maturity" by issuer.

Investment dealers can talk about the nuances of making their lunch money. But we surmise that much of the change in form of our financial markets results from growing need and desire by investors -- including those dealers -- to earn real returns on their investments rather than just save for the future.

We observe, even within ourselves, the sense that investors actually want to make gains on their investments as the depth and range of individual participation increases over time. Surprising that! Investors don't just want to save for tomorrow's lunch. They want to ensure the lunch tomorrow is better than today. And they're willing to take some risk to do so.

The other emerging feature of equity markets is that income trusts offer a new opportunity to deliver "high" relative returns at low risk relative to the rest of the market.

Unit stability studies that we have done indicate that this is the case. And so too, BMO Nesbitt Burns has published it's Income Trust Book that suggests that -- using measures such as the Sharpe Ratio -- the stability of returns on investments relative to price stability or risk is nearly twice as much for income trusts as it is for common equities.

They attribute this to the "cash-in-hand" feature of income trusts with their regular distributions. And this may be statistically true. But there is more to it than that.

And we'll write more on this than this, when we've got our study together. Near the end of July we'll publish: **"Where's Good Money?"**

In the meantime: It's little surprise to the TrustInvestor that the Income Trust is a dominant form of investment in Canadian markets.

INVITATION: If you would like a copy of this article or the study, please refer to our download and [Study notification sign-up](#) page at www.trustinvestor.com/study.php.