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Prepared for the
Canadian Association of Income Funds
Income Trusts and the National Economy
Executive Summary

April 6, 2006

Canadian Association of Income Funds

INCOME TRUSTS AND THE NATIONAL ECONOMY

EXECUTIVE SUMMARY

HDR|HLB Decision Economics Inc.

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Purpose of Study

This study examines whether the trust sector is having a positive, neutral or negative effect on the Canadian economy. The study was commissioned to address the public policy concern raised by some in government, the media and elsewhere that the trust structure, by virtue of the need to make regular distributions to unit holders, might attract companies with little need to invest in productivity-enhancing capital projects.

This concern stems from two related facts -- first, that productivity growth (growth in output per hour) is by far the most important source of Canadian economic expansion and second, that “capital formation” (investment in innovative new plant, equipment and high-technology business processes) is where the lion’s share of productivity growth comes from.

If the trust structure is indeed being adopted principally by firms with little reliance on fixed plant and equipment (i.e., low capital intensity) and little propensity to capital formation, people putting their money in trusts would indeed be diverting resources away from companies where the economy’s true growth potential lies.

Key Findings

The evidence amassed in this study demonstrates that the public policy concern over trusts negatively effecting productivity is not only unwarranted, but that suppressing growth in the trust sector – by means of law, regulation or taxation policies - could be tantamount to suppressing growth in the Canadian economy.

This conclusion is grounded in the following evidentiary findings:

- **Whereas it is capital intensive industries in which the propensity for Canadian productivity growth is the greatest, firms in the business and energy trust sector are disproportionately more capital intensive than firms in the economy at-large;**
- **The annual rate at which firms continue to invest in productivity-enhancing plant, equipment and high technology business processes is unaffected by conversion to the trust structure;**
- **Almost 40% of all business and energy trusts in 2004 resided in industry sectors exhibiting above-average productivity growth over the period 1997 to 2003; and**

- **Firms are taking capital needs into account as a precondition for adopting the trust structure. Firms are not adopting the trust structure unless sufficient cash or other sources of funds will remain available to finance capital formation. Having adopted the trust structure, some firms change their capital structure (shifting from debt to equity-based financing of capital projects, for example); and some firms reduce their payout ratios in order to preserve funds for capital formation.**

Conclusion

Income trusts are investing in the kind of productivity-enhancing technologies and business processes needed to fuel economic expansion. Market capital drawn to income trusts does not represent a diversion of resources from high growth to low growth industries.



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