

LABOUR FUNDS FALL FROM FAVOUR

UNIMPRESSIVE PERFORMANCE, VOLATILE MARKETS AND DEMISE OF ONTARIO TAX CREDIT COMBINE TO PUSH SALES DOWN 37 PERCENT IN QUARTER

By Shirley Won, Funds Reporter

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Labour-sponsored venture capital funds are losing their allure - especially in Ontario.

The money raised by the funds in the first quarter fell 37 per cent to \$107-million from \$171-million a year ago, according to figures from Thomson Reuters Canada.

John Varghese, president of the Canadian Retail Venture Capital Association, suggested the main culprit in declining fund sales stems from the reluctance of financial advisers in Ontario to promote an asset class whose incentive program is winding down.

"They can get the credit now [for their clients], but they are asking themselves why do they want to support a program that is dying," Mr. Varghese, also a managing partner at VentureLink Funds, said in an interview. "It is that mentality that has more of an effect than does getting the credit."

When funds cannot raise a lot of money, advisers also worry about whether there will be enough cash in future years to provide second- and third-round financing for emerging companies, he said.

Labour-sponsored funds require an eight-year holding period, and offer tax credits to investors to compensate for these higher-risk investments.

Ottawa provides a 15-per-cent tax credit. Participating provinces currently add at least another 15 per cent. Before cancelling its credit, Ontario plans to reduce it

to 10 per cent for the 2010 tax year and 5 per cent for 2011.

"While Ontario is staying rigid on its decision - in a time when venture capital is declining across the country - other provinces are actually increasing their incentive programs," Mr. Varghese said.

Provinces like Quebec, Saskatchewan, New Brunswick, and Newfoundland and Labrador have raised their tax credits to between 20 and 25 per cent and that will be effective for the next RRSP season, he noted.

"I fail to understand why the largest province, which has a stated research and innovation agenda, is the only one winding down the credits at a time when we face a severe lack of venture capital," he said.

"If you want to increase entrepreneurial spirit and innovation, you have to be able to fund them."

A 25-per-cent Ontario tax credit and raising the annual contribution limit to \$20,000 from \$7,500 would help the economy at a much lower cost than various bailouts being proposed, he added.

While some investors may hesitate stashing money in labour funds because of poor or lacklustre returns, Mr. Varghese argued that investors are not factoring in the 30-per-cent tax credit.

Unlike in the past, the Thomson Reuters figure for labour fund sales is now reported as a net rather than a gross number. Thomson is using a new methodology, which strips out a portion of the cash parked for redemptions or diversification purposes if it is beyond 20 per cent of the fund's assets. (This is an issue mainly to Quebec-based funds where the reserve requirements are 40 per cent.)

"It [the gross sales number] overstates market resources, especially if the market has been challenged with fundraising," said Kirk Falconer,

director of private equity research at Thomson Reuters Canada.

"The retail numbers are following the same trend as private funds, which is primarily the rest of the [venture capital] market. All the fundraising is going down, and it's the nature of the beast at the moment."

Retail venture capital funds with at least a five-year record

	Assets, \$millions	1 YR	3 YR	5YR	10YR
Axis Investment Funds Inc. Ser. I	\$3.40	-56.3%	-37.8%	-26.1%	
B.E.S.T. Discoveries I	26.9	-38.7%	-2.0%	-5.1%	-3.2%
Canadian Medical Discoveries Ser I	100.5	-25.6%	-21.9%	-17.7%	-9.2%
Return on Innovation I	79.7	-25.3%	-8.8%	-3.8%	
VentureLink Diversified Income I	5.9	-19.6%	-9.8%	-3.5%	
VentureLink Financial Serv Innov I	50.9	19.0%	-6.9%	-2.4%	
GrowthWorks Cdn Growth I	10.6	-18.3%	-5.1%	-0.4%	
Working Opportunity Growth Ser 1	49.1	-16.1%	-3.9%	-3.1%	
GrowthWorks Cdn Income I	3.1	-15.8%	-5.8%	0.1%	
GrowthWorks Cdn Diversified I	13.1	-15.5%	-5.2%	-0.5%	
Dynamic Venture Opport Series I	36.7	-13.8%	-8.0%	-3.0%	2.9%
GrowthWorks Cdn Financial I	1.8	-13.8%	-5.1%	-0.6%	
Golden Opportunities Fund Inc.	138.4	-9.9%	-1.8%	1.1%	3.0%
Working Opportunity Balanced Ser 1	100.1	-7.9%	-2.7%	-4.9%	0.7%
GrowthWorks Canadian	143.9	-6.4%	-2.5%	-0.1%	-4.3%
B.E.S.T. Total Return Fund Inc.	8.6	-0.7%	3.8%	2.0%	
SaskWorks Venture Fund Inc.	109.5	2.4%	7.0%	4.4%	
ENSIS Growth Fund Inc.	73.9	10.4%	1.8%	-0.6%	-1.0%
BMO Nesbitt Burns Cdn Small Cap Index	-36.8%	-14.9%	-0.9%	5.3%	
NASDAQ Composite (\$ Cdn)	-15.8%	-7.6%	-4.9%	-5.7%	
S&P/TSX Small Cap	-43.8%	-19.9%	-8.0%		

As of April 30, 2009

Note: The Quebec Solidarity Fund, which had \$6.2-billion in assets at the end of May 31, 2008, only reports its one-year return at the end of its fiscal year. The fund lost 1.2 per cent over one year. However, it posted an average annual return of 4 per cent over three years; 4.5 per cent over five years and 2 per cent over 10 years. Funds include only those which have filed asset figures to Globe Investor.

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