

## Coventree insiders sell to let others in

CAISSE DE DEPOT BIGGEST OFFERING AS FIRM GOES PUBLIC

By Barry Critchley

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Eight years back, Geoffrey Cornish and David Ellins, a couple of lawyers from Davies Ward & Beck, and Dean Tai, a former treasurer at IBM Canada, started Coventree Capital Group Inc., a company that would provide structuring and funding solutions for clients active in securitization.

Over time, the privately owned Toronto-based firm expanded and became a significant player in the securitization business: the business of operating companies selling off cash-flow-producing financial assets to investors. Assets as diverse as credit card receivables, leases, equipment loans, trade receivables and residential mortgages have all been securitized.

Now comes word that the company, which sponsors and administers a pool of \$12-billion of such assets, is set to go public. But the company, which many don't regard as a direct competitor to the banks, isn't planning to raise capital from its initial public offering. Instead, the plan is for a group of insiders to lighten up on their stakes.

In all, the plan is to sell 22.81% of Coventree's outstanding common shares – equal to 3.792 million shares – to the public. (Given that it is in registration, Coventree, which is also planning to incorporate a Schedule 1 bank, declined to comment for this column.)

The prospectus indicates that Coventree's largest shareholder, Quebec's Caisse de depot et placement du Quebec, will be the biggest seller in the IPO. The Caisse owns 4.817 million shares (or a 28.96% stake) and plans to sell 3.155 million shares. If things work out, the Caisse, which is selling 83.2% of the shares on offer, will end up with 1.661 million shares, or a 9.99% stake in the publicly listed Coventree.

The next-largest seller is The 1999 Cornish Family Trust. That entity, which represents the interests of 15 Coventree employees, is planning to unload 287,500 shares. The next largest seller is 1615411 Ontario Ltd., a private entity wholly owned by Mr. Cornish, which wants to sell 150,000 shares.

In all, six insiders are selling some of their interest in Coventree. Mr. Ellins has since moved on and owns 112,625 shares.

The six sellers don't include two labour-sponsored venture capital funds: the Venturelink Financial Services Innovation Fund Inc. and the Venturelink Diversified Income Fund Inc. Prior to the deal, those two funds owned 2.93% and 0.37% of Coventree, respectively. The two funds invested in December, 2004, and Venturelink's annual report shows the two funds paid \$3.65 per share.

In the village known as Bay Street, the two funds had talked to the principals at Coventree in 2002. At the time, Coventree was involved with the privately held Xceed Mortgage Corp. (Indeed, it was a founding

shareholder in the specialty mortgage lender.) As a result of those conversations, the labour-sponsored funds made an investment in Xceed, which was taken public in the summer of 2004.

Coventree's shareholders list contains some well-known names. For instance:

- David Ward, an industry veteran and currently chairman and managing director of mergers and acquisitions at Sprott Securities Inc., Ward's firm, is the lead underwriter.
- Brendan Calder, along with Ivan Wahl, the current chief executive of Xceed Mortgage, is one of the legends of the mortgage business in Canada. (The two were partners in FirstLine Trust and CIBC Mortgages. Calder is now an adjunct professor of strategic management at the Rotman School of Management in Toronto.)

The prospectus shows that Coventree's business has grown substantially.

In September, 2001, the book value per share was 25 cents; with 14.2 million shares outstanding the company had shareholder's equity of \$3.55-million. A year later, the number had risen to \$9.15-million; in 2003 it was \$14.93-million; in 2004 it jumped to \$26.14 million; last year it had soared to \$46.22-million.

The business is very profitable. In 2002, Coventree's return on equity was 59.2%; in 2003 it was 48.3%; in 2004, 57.0%, and it jumped to 67.3% in 2005. (Since 1999, the average return on equity was 38.1%.) Over the same period, the so-called fundings outstanding have risen from \$2.6-billion to \$10-billion.

Coventree has sponsored eight so-called conduits: a special-purpose entity set up to purchase certain assets from a variety of sellers and fund them with an offering of securities, either commercial paper or term notes. The conduits have celestial names: Rocket, Comet, Aurora, Gemini, Planet and Apollo.

By its measure – market share of the multi-seller, asset-backed commercial paper market in Canada – Coventree is the third-largest player after BMO Nesbitt Burns and CIBC World Markets. Its share is 12.7% (versus 22.8% for BMO and 13.9% for CIBC). It is a touch ahead of TD Securities.

While Coventree likes to compare itself with the banks, some banks report that they don't compete directly with Coventree. "In my view, I don't think they are competitors," says one bank securitizer. "They exist parallel to the banks, indeed they are complementary to the banks. But you don't see them competing head-to-head with the banks for Tier 1 business."

Instead, says this banker, Coventree plays in the Tier 2 market. "They take strategic risk to create clients," he said, pointing to Nereus Financial Inc., a Coventree spin-off, that operates "in the leveraged senior super space. It sells credit protection ... the super senior tranches of credit risk held by large financial institutions."

Another banker says Coventree has been good at identifying emerging opportunities and finding a way to make money both as a service provider and as an owner. "They are the best of another breed of player that makes money in structured credit," he said.

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