BN Biggest Profit in 3 Years Set to Spark Economy: Corporate Canada
Aug 14 2014 4:30:00

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By Eric Lam

Aug. 14 (Bloomberg) -- Canadian companies are posting their best profit in three years, fueling hopes business spending will soon give a jolt to lackluster economic growth.

Earnings among the 84 percent of companies in the Standard & Poor's/TSX Composite Index that reported as of 4 p.m. yesterday reached a total C$216.01 per share, the most since the second quarter of 2011, data compiled by Bloomberg show. About 78 percent of them have posted higher revenue than a year ago, as companies from Canadian Natural Resources Ltd. to Magna International Inc. benefit from stronger U.S. growth and a weaker Canadian dollar.

"We're seeing early signs businesses are ready to ramp up their investments," said Craig Fehr, Canadian market strategist at Edward Jones in St. Louis. His firm manages about $750 billion globally. "That's a function of stronger revenues. We're on the precipice of increased business investment, which would be a strong component for not only strong earnings growth but strong economic growth as well."

Increased capital investments from the country's largest corporations will be a tonic for Canada's middling economic recovery, which is forecast to grow 2.2 percent this year and lag global growth until at least 2016. Both the government and the Bank of Canada have called on businesses to re-invest their profits into the economy.

Federal Finance Minister Joe Oliver said at a news conference this week he wanted to learn why companies aren't investing cash on their balance sheets.

Cash Hoards

Bank of Canada Governor Stephen Poloz said last month the abrupt slowing of the global expansion early this year is delaying the pick-up in business investment the country needs to have a self-sustaining recovery, prompting him to cut the nation's forecasts for growth in 2014 and 2015.

"After a number of years, CEOs are getting better visibility on the longevity of the recovery," said Paul Taylor, chief investment officer, asset allocation, at BMO Asset Management Canada in Toronto. His firm manages C$65 billion ($59.6 billion). "They had been sitting on cash hoards and not reinvesting. This is a transition period as the market looks for that acceleration."

The difference between economic growth of 2 percent and 2.5 percent to 3 percent is staggering, Taylor said. In the former, the economy struggles to create jobs and is akin to a recession. In the latter, "people are earning more, companies are hiring and businesses are starting to spend," he said.

Oil Driven

Signs of this are already appearing in the U.S., Canada's largest trading partner, with companies adding more than 200,000 workers to their payrolls every month for six straight months, Taylor said. Canada's job market has posted the weakest six-month growth since 2001, excluding recessionary periods.

Canadian equities have rallied 12 percent to a record this year, the second-best among major developed markets, led by gains among commodities producers and manufacturing companies on a combination of greater global demand, higher prices and a weaker loonie. The loonie, named for the aquatic bird on the one-dollar coin, has dropped 5.3 percent against the U.S. dollar over the past year.

Many of Canada's oil producers and exporters operate in Canada while selling their products in U.S. dollars, benefiting from the weaker exchange rate. The 62 energy companies that have reported this quarter have generated $66.8 billion in sales, a 21 percent increase from a year ago, data compiled by Bloomberg show. Profit is up 41 percent to $6.34 billion in the period.

Supply, Demand

Corey Bieber, chief financial officer at Canadian Natural Resources, pointed to "stronger benchmark oil pricing and a weaker Canadian dollar" as factors driving the producer's second-quarter cash flow. The company reported a 41 percent increase in revenue to C$5.37 billion.

Oil prices have slipped in the past month with Brent crude sinking to a 13-month low of $103.02 a barrel this week after the International Energy Agency said a supply glut was shielding the market against threats in the Middle East. The IEA cut global projections for demand growth this year and next. West Texas Intermediate crude has closed below $100 a barrel since July 31.

John Stephenson, portfolio manager and chief executive officer at Stephenson & Co. in Toronto, said prices even at current levels remain positive for oil producers and demand for crude will continue to grow in the developing world.

"We still have to look to places like the oil sands for output, so prices will continue to hang in here at $90-plus a barrel," he said. "Certainly $97 is healthy for oil prices."

Revenue Outlook

Magna International, North America's largest maker of automotive parts, reported record sales of $9.46 billion in the second quarter and raised its revenue outlook for the year to as much as $37.3 billion, from a previous high projection of $36.6 billion. North American, European and Asian production sales increased.

"You want to buy companies that have that currency leverage," said Irwin Michael, fund manager at ABC Funds in Toronto. His firm manages about C$900 million. "You mustn't lose sight of that."

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Even with the rally in the S&P/TSX, investors haven't regained their full faith in equities since the shock of the 2008 financial crisis, Bob Decker, fund manager at Aurion Capital Management Inc. in Toronto, said.

"I don't know what it is that's going to restore confidence but I don't think it's earnings," he said by phone.

The S&P/TSX has more room to rally higher as economic data continues to improve, said Stephenson.

"We've had a few dings and dongs along the way for stock prices, but frankly the data looks very strong," he said. "I'm expecting a good second half of the year for stocks. I'm very, very encouraged."

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