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The Rise and Fall of the Widely Held Firm in Canada

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Abstract

A long panel of corporate ownership data, stretching back to 1910, shows that the Canadian corporate sector began the century with a predominance of large pyramidal corporate groups controlled by wealthy families or individuals, and relatively few widely held firms. By the middle of the century, widely held firms had become predominant. However, from the 1970s on, there has been a marked resurgence of pyramidal groups controlled by wealthy families and individuals, corresponding to a large decline in the prevalence of widely held firms. Improvements in the general institutional environment and high taxes on inherited income accompany the rise of widely held firms. A sharp abatement in taxes on large estates and a rise in the likely returns to political rent seeking accompany the resurgence of pyramidal groups.

1. Introduction

A long panel of corporate ownership data, stretching back to 1910, shows that the Canadian corporate sector began the century with a predominance of large pyramidal corporate groups, controlled by wealthy families or individuals, and relatively few widely held firms. By the middle of the century, widely held firms had become predominant. However, from the 1970s on, there has been a marked resurgence of pyramidal groups controlled by wealthy families and individuals, and a corresponding decline in the prevalence of widely held firms.

Pyramidal corporate groups are thought to be a response to a weak institutional environment. If markets and other economic institutions are costly, internal transactions between related firms may be preferable. Canada's corporate sector grew out of long and deeply established mercantilist traditions with roots in the country's French and British colonial past. These mercantilist traditions include many centuries of state-subsidized industrial initiatives and a long tradition of using political office for personal gain. We argue that these traditions rendered Canada's economic institutions, especially those responsible for allocating capital, quite weak at the beginning of the twentieth century, and consequently produced a competitive advantages for pyramidal groups.

As the century progressed, institutions improved and widely held firms became the dominant organizational form of Canadian business. However, the two processes do not track each other well. Shareholder rights remained weak in Canada until reforms in the 1960s, yet the transition to a widely held corporate sector was essentially complete by then. The economy actually became more closed, rather than more opened during some of the decades when widely held firms grew in importance. The rise of the widely held firm does correspond to a general trend towards greater professionalism in the civil service. An expanding middle class, capable of investing in shares, may also figure in. A confiscatory inheritance tax is also clearly important in several individual cases where a family patriarch dies and his heirs sell out to pay the succession taxes. Alternately, the aging patriarch sells the corporations and bequeaths the money in tax preferred ways. In either event, family controlled firms become widely held.

Our most puzzling finding is a steady decline in the importance of widely held firms in the final decades of the century and a resurgence of pyramidal groups controlled by wealthy individuals or families.

One change that was clearly important in specific cases was the repeal of the inheritance tax in the 1970s. The tax was replaced with the requirement that capital gains be realized upon death, however loopholes were included regarding the basis for calculating these gains and allowing realization to be delayed for two generations using family trusts. These loopholes are sufficiently costly that they are unusable for small estates; however several multibillion-dollar family fortunes have escaped taxation using this route. These tax changes allowed great family fortunes to pass from generation to generation intact and preserved family control over corporate empires.

Another change in Canada in the 1970s was a dramatic realignment of the role of government. Canada changed from a liberal democracy to a social democracy at this time. The professionalized civil service took charge of vetting foreign investment, managing an expanding stable of state-owned enterprises, supervising the energy industry, subsidizing and promoting "cultural industries" and strategic areas of the economy, and running an increasingly complicated and opaque system of taxes and transfers. We speculate that these changes, by greatly expanding the economic importance of government, correspondingly increased returns to political rent seeking. We further speculate that large family controlled corporate groups might be more adept at interacting with politicians and civil servants, and so might attain an advantage over free standing widely held professionally run firms. Further research is clearly necessary to confirm this hypothesis.

2. Description of the Data

Before exploring the evolution of corporate ownership in industrialized Canada's history, we briefly describe key developments in its earlier economic history and institutional development. Continuous quantitative data are unavailable for early years, with the sole exception of the dividend yield of the Hudson's Bay Company, which is available annually from 1670 on. However qualitative descriptions of business ownership are possible. Moreover, such descriptions greatly aid our understanding of quantitative data in later years when it becomes available.

Our qualitative descriptions summarize relevant parts of the writings of several business historians. Bliss (1986) presents a thorough review of Canadian business history that is broadly sympathetic to the country's business elite, emphasizing their entrepreneurial ventures and risk taking. In passing, Bliss provides much detail about who controls which companies. Hedley (1894) is a set of brief biographies of Canadian business leaders. Unfortunately, many are at too low a level to be of interest to us. Myers (1914) is something of a muckraker, focusing on the rent-seeking activities, unsavory undertakings, and politically incorrect philosophies of the business elite.

Naylor (1975) is quite critical of the business elite, and often appears sympathetic to leftist views. Like Bliss, both Myers and Naylor provide valuable information about ownership and control as asides to their main arguments. Taylor and Baskerville (1994) provide a highly useful history of Canadian businesses, though their coverage after 1930 is rushed. Tulchinsky (1977) provides information about colonial Montreal businesses.

Much of the qualitative description below is from these sources – especially Bliss. To avoid repetitive citations, specific references are mainly to other sources. However, a general reference pervades to these authors, and a degree of plagiarism is gratefully acknowledged.

Data on the historical growth rates of the Canadian economy become available beginning in 1870. These data are from Urquhart (1993) for years prior to 1926, and from Statistics Canada for subsequent years.

We obtain data on merger and acquisition activity beginning in 1885. These data are concatenated from several sources. Marchildon (1990) provides a series from 1885 through 1918. Maule (1966) provides a series from 1900 to 1963. The Royal Commission of Corporate Concentration provides numbers for 1970 through 1986. For 1985 through 2000, data are available from *Merger & Acquisition in Canada*.

Data regarding the financial records of Canadian businesses begin in 1910. Unfortunately, records are not available from a uniform source over the full history of the country. We therefore use all available sources in each time period to produce the most accurate representation possible. In general, our data for later years are probably better. For 1965 through 1998 we take the largest 100 companies, as ranked by the *Financial Post*. These companies were initially ranked by assets, and then by revenue from 1967 on. For earlier years, *Financial Post* rankings are unavailable. We therefore use annual reports data to construct our own rankings. Annual reports for Canadian companies are summarized in the *Canadian Annual Financial Review* for 1910 through 1940, and in *Financial Post Corporate Securities* for 1950 and 1960. We do not consider financial companies because these are not included in the top 100 rankings of the *Financial Post*. Also, ownership regulations forced them to be widely held in later years.

Two caveats arise in connection with the selection of the top one hundred firms. One is that state-owned enterprises are included in the data for certain periods, are dropped, and then reappear. For Example, Ontario Hydro was established in early 1900s, but its records are not available until after 1975. The government assembled Canadian National Railways out of bankrupt transcontinental lines in 1919. Financial records for CN are available prior to 1950 and after 1970, but not in between. For CN, we can interpolate asset figures for the missing years. For Ontario Hydro, there is little we can do to remedy the problem. We therefore consider alternative average ownership structures - first including and then excluding state-owned enterprises. A second caveat is that our rankings of top one hundred companies for 1910 through 1965 are based on assets, while those for later years are based on revenues. This is because only assets are available for many companies in the earlier years. For later years, when both rankings are available, the use of sales and assets generates similar pictures. Consequently, we do regard this as a minor problem.

Our early ownership data are from several sources. The annual reports collected in the *Canadian Annual Financial Review* and *Financial Post Corporate Securities* list the identity of controlling shareholder, though not their equity stake. However, these records are incomplete. We find instances where these data are inconsistent with descriptions of corporate ownership in books on Canadian business history - especially Baskerville and Taylor (1994), Bliss (1986), Myers (1914), and Naylor (1975). Where there is an inconsistency, we rely on the history books. This is because the beneficial ownership was not always clear at the time due to obfuscatory holding company structures. We rely on the business historians to have sorted this out. One shortcoming inherent in using these descriptive sources, however, is that we cannot provide a clear cut definition of precisely what it means to be "controlled" by a family or a "member" of a corporate group. A company is controlled by a family or a member of a group if one of our historical sources says so, or if its annual report indicates so.

From 1965 on, Statistics Canada produces a *Directory of Inter-Corporate Ownership* (ICO), our primary source for these years. The *Financial Post* also provides the name and stake of the largest shareholder for top Canadian firms from 1970s on. We define a company as "controlled" if there is a combined direct and indirect voting stake of ten percent or more, or if the ICO lists it as controlled.

Finally, we classify each company into one of the following categories: free standing widely held firms, free standing family controlled firms, firms in family controlled pyramidal groups, firms in pyramidal groups controlled by widely held companies, firms controlled by a government or government agency, firms with a controlling foreign shareholder, and firms we cannot classify.

3. Initial Endowments

To appreciate the origin of Canada's current system of corporate ownership, it is necessary to understand how starkly Canada's pre-industrial history differs from that of other European settlements in North America. In particular, Canada was a colony of resource extraction, not a colony of settlement for most of its history. During brief periods when settlement became paramount, Canada was a theocratic society, not greatly different from modern Iran. And when development was pushed, Canada became a testing ground for overtly mercantilist development schemes reminiscent of third world programs in the 1960s.

The values and ideals of French Canada can still echo these centuries of theocratic and company rule, though in unexpected and sometimes odd ways. English Canadians, many of whom descend from refugees who fled revolutionary tribunals and armed debtors, valued "peace, order and good government" to an extent that foreigners and more recent immigrants often found difficult to fathom. The Anglo elite, who dominated Canadian business from the 1780s on, co-opted the mercantilist state they inherited from France to preserve and protect the existing economic hierarchy.

L'Ancien Régime au Canada

In 1534, Jacques Cartier sailed up the St. Lawrence River and claimed Canada for France. Seven years later, Francis I created Sieur de Roberval Viceroy of Canada. Roberval Quebec City in 1541 and abandoned it the following year.

Although France lacked a permanent settlement in Canada, merchants in Atlantic ports, such as La Rochelle, organized an increasingly lucrative Canadian fur trade. From

1562 until the Edict of Nantes in 1598, France succumbed to bloody Wars of Religion, as Huguenots and Catholics vied for dominance. The breakdown of central authority left the Atlantic ports *de facto* independent of Paris, so a competitive fur trade rapidly developed involving Catholic, Huguenot, and Jewish merchants.

The Edict of Nantes ended the religious civil wars by granting Protestants full rights, but France remained deeply divided. To prevent further discord, the power of the monarchy was greatly enhanced, and the state was reorganized as a highly centralized structure that persists through various reincarnations to the present.

The consolidation of Royal authority bade ill for the competitive fur trade, for Henry IV granted a monopoly to a group of merchants in 1600. But the monopoly was unenforceable, for La Rochelle remained *de facto* independent of Paris. Nonetheless, in 1604 Henry IV granted Sieur de Monts a ten-year fur monopoly. Samuel de Champlain, hired by De Monts to establish permanent settlements in Canada, founded Port Royal (Annapolis, NS) in 1605 and reestablished Quebec City in 1608. De Monts' monopoly was renewed once, and then replaced with a monopoly for the *Compagnie de Rouen et St. Malo*, owned by Champlain himself. This monopoly was rescinded in 1620 as the counterreformation swept France, and replaced by the *Compagnie de Caen*, organized by the Rouen merchant William De Caen and his nephew, which was charged with settling Canada as well. The feudal system was established in Canada, and the first fiefdom was granted in 1623 to Louis Hébert, whose Canadian title was Seigneur de Sault-au-Matelot.

With the fall of La Rochelle to the Royal army in 1629, Cardinal Richelieu seized Canada. Richelieu had become chief advisor to King in 1624, and with the La Rochelle competition removed and the *Compagnie de Caen* monopoly rescinded, he organized the

Compagnie des Cent Associes, run by himself, with a permanent monopoly on the fur trade and limited monopolies on other transatlantic trades. The only requirement of the *Compagnie* was to transport at least 300 *habitants* (feudal peasants) per year to Canada. As a Province of France, Canada had a Provincial Government created by the *Compagnie des Cent Associes* and a *Conseil Souverain* made up of the governor of Quebec City and senior Jesuits. The *Conseil* had lawmaking power over all of Canada. Under this arrangement, every aspect of the habitants' existence was subject to the feudal order. Habitants were bound to the land, could not marry without permission from their Seigneur, and had no property except at the pleasure of their Seigneurs. As the Holy Inquisition swept Catholic Europe, the Provincial Government added an unforgiving Roman Catholicism to this mixture.

After the death of Cardinal Richelieu in 1642, the power of the *Compagnie* quickly faded. The independent and competitive *coureurs de bois* seized the fur trade within Canada, and many grew rich. The same year, Sieur de Maisonneuve de la Société de Notre-Dame de Montréal founded Montréal as a missionary base. The Montréal clergy placed themselves above civil law and exercised their feudal powers and rights of tithe to accumulate great wealth.[1] The *Compagnie des Cent Associes* became subservient to the *Communauté des Habitants*, through which the Canadian clergy and seigneurs took charge of local affairs through a Local Council.

This situation persisted until Jean-Baptiste Colbert became Controller of Finance in 1661. Colbert immediately began using Canada as a testing ground for his economic theories.[2] In 1663, Colbert formally dissolved the *Compagnie des Cent Associes*, and

[1] Myers (1914) chapter 2.
[2] For a detailed account of state subsidized diversification programs in New France, see Fauteux (1927).

replaced the Local Council with a new *Conseil Souverain*. The latter had a mandate to implement *la Coutume de Paris*, the *ancien régime* Civil Code, in Canada.[3] Colbert appointed Jean Talon as Intendant of Canada in1665, and charged him with diversifying the economy. Usually with himself as the major shareholder, Talon directed subsidies into brick making, shoe making, beer making, wool production and mining operations; and subsidized exports of wood, eels, sea oil, and cod to France and the Caribbean. Under Talon, the *Conseil Souverain* also imposed import restrictions and wage and price controls. Talon also began shipping *filles du roi*, peasant women, to Canada to promote population growth. All of this was subsidized by the *Departement de Marine*, even though Canada was now a *fief et seigneurie* of the *Compagnie des Indes Occidentals*, controlled by Colbert. Ultimately, none of these initiatives (save perhaps the *filles du roi*) proved viable.

Colbert's mercantilist adventure in Canada did allow some local entrepreneurs to grow rich. The most important was probably Charles Aubert de la Chesnaye, an agent in Canada for Rouen merchants. Chesnaye became a *négociant marchands* – a wholesaler, importer, exporter, financier, and moneylender. He backed loans with negotiable perpetuities, probably the first (informally) traded securities in Canada. His most important dealings, however, were buying and selling seigniorial estates. In 1670, Chesnaye died deep in debt after a series of risky investments soured.

In 1672, a young aristocrat Louis de Buade de Frontenac et de Palluau, Comte de Frontenac, desperate to evade his increasingly violent creditors, accepted the Governorship of Canada. (His pay was escrowed to his wife at court who slowly

[3] The *Coutume de Paris* granted the Canadian nobility the full feudal rights of the nobility in France, including the power of *haute justice* over their habitants.

discharged his debts.) Frontenac continued Colbert's mercantilist plans, supervising the Royal Army Engineers as they built a scratchwork of canals.

With Colbert's death in 1683, France's economic focus shifted to the new colony at Louisbourg, in Acadia, which proved more prosperous than Québec because of its proximity to the Grand Banks. But Colbert's mercantilist development vision was never forgotten. For example, the Intendants Bégon and Hocquart used state funds to establish a rope making operation, which quickly failed. Hocquart also subsidized a shipyard and an ironworks in St. Maurice, claiming that a lack of investment capital among Canadian merchants was the primary reason for the colony's slow growth. Both ventures, like the rope works before them, soon failed due to high costs and clouseauesque quality control. The ironworks, an initiative of François Poulin de Francheville, Seigneur de St. Maurice, in 1729, was reestablished by the engineer Olivier de Vézin on a larger scale as *La Compagnie des Forges du Saint-Maurice* with further state-sponsorship in 1737. Lunn (1942) describes the ensuing developments:

> Indications of the disaster which was to overtake the enterprise were evident from the beginning … . By October 1737, when the establishment was announced to be complete, the total expenditure was 146,588 *livres* instead of the 100,000 estimated … . In 1737 Hocquart had made over to the company the remainder of the loan of 100,000 *livres* agreed upon, but the partners declared they must have an additional 82,642 *livres*. Their need was so pressing that Hocquart took it upon himself to advance them 25,233 *livres*, to be deducted from the 82,642 *livres* which he begged the Minister to lend … .
>
> The Minister replied in accents of horror and indignation. … It seemed clear to the Minister that there had been much waste and extravagance. Nevertheless, he did consent to the new loan … .
>
> Further shocks were in store for the minister. In 1738, the company foresaw that it would not be able to meet its first payment due in 1739 and the King had to agree to yet another year's delay. … De

> Vézin's estimate had proved completely unreliable, for expenses far exceeded and production fell far short of what had been anticipated … Constant breakdowns of the furnace interfered seriously with production … The Forges were operated by a staff of costly, dilatory, insubordinate and discontented workmen.[4]

La Compagnie des Forges du Saint-Maurice failed in 1741 under the gravity of engineering, managerial, and financial folly. The state took over the forges and shipyards, and the latter remained in operation long after French rule ended. Its operations were never profitable. Indeed, none of these ventures made Canada less expensive to the Royal Treasury. Only once in the entire history of French Canada, in 1741, did exports exceed imports. The most consistently profitable business was the *Société du Canada*, run by the Huguenot merchant Robert Dugard, which shipped staples to the colony.

The War of the Austrian Succession (1740 to 1748) and the Seven Years War (1755 to 1763) saw a series of battles between Britain and France for control of Canada. Louisbourg fell to the British in 1758, and Québec City in 1759. With the 1763 Treaty of Paris, France ceded Louisiana to Spain and all her other territories in North America to Britain. Much to their astonishment, *L'affaire du Canada* relegated the last Governor, de Vaudreuil, the last Indendant, Bigot, and other senior Canadian officials to the Bastille for "corruption."

British North America

In 1610, Henry Hudson claimed the territories surrounding Hudson's Bay for James I of Britain. This claim lay unexploited until 1670, when George I granted a fur trade monopoly to his cousin, Prince Rupert. Rupert organized a joint stock company, *The*

[4] Quoted in Bliss (1986), p. XX.

Company of Adventurers of England tradeing into Hudsons Bay (a.k.a. The Hudson's Bay Company, the HBC, or The Bay), to obtain capital, and rechristened the region Rupertsland.[5] From 1670 to the War of the Austrian Succession, British interests in Canada consisted of the Hudson's Bay Company's scattered trading posts in Rupertsland and little else.

The Hudson's Bay Company, now a chain of department stores, still trades on the Toronto Stock Exchange. It has been widely held since its inception. The forts, trading posts, and ships required - as well as the risks inherent in the fur trade - were beyond the resources of even the wealthiest individual families. Thus, the Hudson's Bay Company, like the British East India Company and the Dutch East Indies Company, was among the first joint stock companies formed. Figure 1, showing the company's annual dividend, is a barometer of the prosperity of the fur trade and, later, of the Canadian economy.

[Figure 1 about here]

After the Seven Years War, a deeply corrupt British colonial government took charge in Québec City.[6] Colonel Talbot, General Brock, and Bishop Mountain all seized vast tracts of Upper Canada (Ontario), while the Governor, Henry Hamilton, Judge Elmslie, Judge Powell, and Solicitor General Gray appropriated huge swaths of Lower Canada (Québec). All of Prince Edward Island was divided up by the Montgomery, Selkirk, Westmoreland, Cambridge, Macdonnell, and Seymour families.

[5] The Company was empowered to employ an armed force, appoint commanders, erect forts and take other necessary measures to protect its property. See Myers (1914) chapter 3.
[6] For details of specific corrupt dealings, see chapter 5 of Myers (1914).

Partially in response to such abuses, London suspended British Common Law in Canada in 1774, restored the French Civil Code of the *ancien régime* in property law and all matters except criminal cases, and extended the boundaries of civil law application to all of British North America north and west of its thirteen coastal colonies. This recognition of civil law both consolidated the French feudal land tenure system and limited new land claims in this greatly expanded civil law jurisdiction.

These restrictions on land claims, a tax rebellion, and an elite deeply indebted to British merchant houses combined to inspire rebellion in the thirteen coastal colonies in 1776.[7] This conflict was essentially a civil war, with a about a third of the colonial population remaining loyal to the Empire. French intervention allowed a secessionist victory, and revolutionary governments took power in the thirteen colonies. Revolutionary tribunals confiscated the property of those on the losing side and exiled them. In one of history's largest forced displacements, hundreds of thousands of impoverished United Empire Loyalist refugees straggled north. Almost overnight, Canada was transformed from a Francophone country into a half-English half-French country.

Loyalists settling in Canada disliked the French Civil Code and coveted land. In 1791, Canada was divided into Upper Canada (Ontario) and Lower Canada (Québec), and in 1793, Chief Justice Osgood succeeded in restoring Common Law in Upper Canada (Ontario). Upper Canada's Governor, Robert Prescott, and Lieutenant Governor, John Graves Simco, stalwartly upheld directives from London to hold land open for settlement. In 1794, Osgood forced both from office and installed Sir Robert Shore Milnes as

[7] For statistics on the deep indebtedness of key colonial families, such as the Jeffersons and Washingtons, in 1775 see XX.

Governor and Peter Russell as Lieutenant Governor. Milnes, Russel, and Osgood apportioned virtually all the remaining unclaimed land to tiny elite of leading Loyalist families that, in the 1820s, became known as the *Family Compact*.

The extent to which the Family Compact, and an equivalent group in Lower Canada called the *Chateau Clique*, dominated colonial life is hard to overstate, as is the extent to which these family elites retarded economic development.[8] As absentee landlords, they opposed settlement and the building of roads for fear of losing title to squatters. The Family Compact controlled the legislative and executive councils, the Church, and colonial courts. This let it safeguard its members' business interests and property rights, and let it control the issuing of remaining land grants.

The influence of the Chateau Clique in Lower Canada was narrower, and perhaps less effective at slowing growth. In 1779, British and Loyalist merchants in Montréal established the Northwest Company to compete with the Hudson's Bay Company for the fur trade, contesting the legitimacy of the latter's monopoly. Among the original founders of the Northwest Company were Simon McTavish, Todd and McGill, Charles Grant, Benjamin and Joseph Frobisher, the firm of McGill and Patterson and five other merchants and firms.[9] The resulting wealth gave the same names prominence in banking, shipping, and railroad promotion decades later.

Since the Hudson's Bay Company had its own militia, the Northwest Company needed one too. Their battle for market share is best described in military terms. The results are also evident in Figure 1 in the reduced dividend of the HBC.

[8] See Myers (1914) chapter 6.
[9] See Myers (1914) chapter 4.

During this period, the most entrepreneurial regions of British North America were the Maritime Colonies of Nova Scotia and New Brunswick. Abraham Cunard, a master carpenter, arrived in Halifax in 1783 and quickly expanded into all manner of businesses - including stores, mills, lumbering, sawmills, shipbuilding, and accounting. Despite strong competition from other "timber barons" such as Gilmour, Rankin, & Co., Philemon Wright & Sons, William Price, and John Egan, the firm of A. Cunard & Son prospered. Many timber barons, including Christopher Scott, John and Charles Wood, and the Cunards, expanded into shipbuilding and shipping. Bliss (1986, p. 135) remarks that all of these fortunes were technically founded on theft, for the timber was almost all harvested from Crown land. The Cunard Line prospered, especially after it obtained a monopoly on delivering the Royal Mail between Britain and the Americas.

In 1812, the Napoleonic War engulfed the Canadas as an American invasion force crossed the border, burning Toronto and despoiling farms and villages. Figure 1 illustrates the disruption of the fur trade in the elimination of HBC dividends. The French and their American allies defeated, an inflow of settlers resumed. Although a new British colony was established in Manitoba in 1811, its remoteness (and the Hudson's Bay Company's unwillingness to grant settlers formal property rights) deterred settlement.[10] The Hudson's Bay Company viewed farmers as disruptive of its trading relations with Indians, and effectively prevented further westward expansion of settlement. Thus, immigrants from Britain and elsewhere remained in the Canadas and the Maritimes.

[10] Myers (1914) describes an 1857 a petition signed by Red River settlers to London describing how they had "paid large sums of money to the Hudson's Bay Company for land … yet we cannot obtain deeds for the same. The Company's agents have made several attempts to force upon us deeds which would reduce ourselves and our posterity to the most abject slavery under that body... ."

The economy grew faster in Lower Canada, where the Chateau Clique exercised a looser dominance than did the Family Compact in Upper Canada. Montréal, closer to the Atlantic and the coastal colonies, emerged as the economic center of Canada. In 1821, the Hudson's Bay Company absorbed the Northwest Company. The costs of their militarized competition had grown, in both money and death toll, and Figure 1 illustrates the advantages of a fur trade monopoly. The former principals of the Northwest Company in Montréal, the McGills, MacTavishes, Frobishers, Grants, and others, now had considerable wealth to invest in other ventures.

The House of Phyn, Ellice & Co. established a branch in Montréal in the late 1770s to finance the staples trade, and so was the first bank in British North America. However, the Napoleonic Wars disrupted this business. After peace was restored, John Richardson and Horatio Gates, the Montréal principals of Phyn, Ellice and Co., established the Bank of Montréal as a partnership. The Bank of Montréal subscribed to the *real bills doctrine*, and issued dollar bank notes backed by the staples trade, thereby establishing the currency unit for Canada. Rival banks quickly formed in Lower Canada, but the Bank of Montréal, soon run by Peter McGill, remained dominant. The Bank of Nova Scotia was chartered in 1832 in Halifax as the first limited liability joint stock company in British North America.

John Molson, a young Englishman, arrived in Montréal in 1785 and invested his inheritance in a brewery. This highly profitable venture allowed him to finance the first steamship in 1809. Although Molson lobbied for a steamship monopoly, his requests were denied and the low barriers to entry allowed brisk competition. The Molsons' profits from their brewery eventually let them buy out much of the competition on the St.

Lawrence, though. Their main competition would ultimately be the Allen Line, run by Hugh Allen, a partner in the Scottish shipbuilding and merchant firm of Edmonstone, Allen & Co., founded by his father. Using family money, Allen launched the Montréal Ocean Steamship Co. in 1852, and immediately reaped great profits transporting troops to the Crimean War. Bliss (1986) reports that "Allen ships sank, ran aground, and broke up with astonishing frequency", but that he courted politicians generously, and was a recognized master of political influence. By the 1860s, the Allen Lines safety record was improving, and the family was growing rich bringing steerage immigrants to North America.[11] According to Myers (1914) Allen served as president of fifteen corporations and vice-president of six others at the zenith of his career, in industries spanning telegraphy, navigation, iron, tobacco, cotton manufacturing, railways, sewing machine, cattle, rolling mills, paper, car, elevator, and coal. His Montréal Warehouse Company undertook land speculation.[12]

In 1838, Joseph Howe, a Nova Scotia colonial leader, pressed the Royal Mail to adopt steam delivery, and the Admiralty called for tenders. Although none of the responses met the Admiralty's conditions, Samuel Cunard, Abraham's eldest son and now running the family business, won the contract – apparently through his influential friends in England, including Lady Caroline Norton, the mistress of Lord Melbourne, then the British prime minister. This guaranteed mail business gave the Cunard Line a critical edge over its competition, the Inman and Collins Lines. The latter two modernized rapidly, switching to screw-driven ironclads at great expense, and ultimately

[11] The Allan Line sued the *Montreal Witness*, a newspaper that ran stories about the filth and overcrowding in its steerage compartments, for libel. In 1883, shortly after Allan's death, the jury, after hearing all of the evidence during a trial of eight days, returned a verdict in favor of the *Montreal Witness* on all counts. For details, see *Monetary Times*, Nov. 2, 1883 p. 491.
[12] Myers (1914) chapter 12.

failed. Cunard modernized much more slowly, and remained profitable as it delivered the Royal Mail at London, Halifax, New York, and Boston in wooden steamships.

The Bank of Upper Canada, controlled by the Family Compact, exercised a near monopoly over financing the staples trade in that colony, and reinforced the suzerainty of that Loyalist elite. In 1825, John Galt, a novelist, organized the Canada Company to resell land to immigrants; but such entrepreneurial ventures were notable in their rarity.[13] Some outsiders, notably the Scottish immigrants Isaac and Peter Buchanan and their Ulsterman partner Robert Harris, did obtain Bank of Upper Canada backing and grew rich off the Upper Canadian staples trade. Isaac recalled that

> "The wonderful success of my operations in Canada may be to a great extent attributed to my solemn determination not to trust Yankees and my exercising the most vigorous scrutiny before doing business with a man Canadian born …"[14]

The main big business ventures in Upper Canada in the early 19th century were canals. The Imperial government built the Rideau Canal from the Ottawa River to Lake Ontario. William Hamilton Merritt organized the Welland Canal, linking Lake Erie and Lake Ontario, as a joint stock company controlled by the Family Compact. After providing repeated generous state subsidies and loans, the Upper Canada government finally bought out the owners of the failing venture in 1841. The newspaperman William Lyon Mackenzie charged that the whole project was a scam to enrich the Family Compact. Upper Canada's public finances never recovered.

[13] Browde (2002).
[14] Bliss (1986) p. 154.

In 1832, railroad stocks began trading in a café in Montréal that eventually became the Montréal Stock Exchange. The Champlain and St. Lawrence Rail Road was built in 1834 with backing from the Molsons, Horatio Gates, and Peter McGill, then the president of the Bank of Montréal; and financing for other railroads was undertaken.

But complaints about gross corruption and abuse of office by the elites of both Canadas grew louder. Denied political influence and economic opportunities, new immigrants formed an opposition movement that ultimately coalesced into the Reform Party. Francis Bond Head, Governor of Upper Canada from 1835 to 1837 cracked down with a policy of "order and discipline". His refusal to permit the suspension of specie payment during the Panic of 1837 caused the Bank of Upper Canada to call in debts ruthlessly throughout the colony, further infuriating the populace. Lower Canada fractured along linguistic lines.

Open rebellion broke out in 1837, as Louis-Joseph Papineau declared a Republic in Lower Canada and William Lyon Mackenzie did likewise in Upper Canada.[15] Demanding an end to feudalism, church estates, trade barriers, and development barriers, the rebels had strong popular support.[16] Although the army restored order, Upper Canada debentures collapsed. London dispatched a new governor, Lord Durham, who sent back a report in 1839 damning decades of fraud and theft by the Canadian elite and recommending Responsible Government – democratic home rule.[17]

[15] Although Nova Scotians increasingly resented the appointed Council of Twelve (Cunard and other merchants) that ran that colony, democratic reform came peacefully there.
[16] See Myers (1914).
[17] See Lambton (1838) Vol. X for a description of the abuses.

The end of the Imperial Preference in 1846 forced Canadian merchants to compete in a world of free trade. The economy collapsed, and Lord Elgin, the Governor General of Canada, reported in 1849 that

"Property in most Canadian towns, and most especially in the capital [Montréal], has fallen 50 percent in value within the last three years. Three fourths of the commercial men are bankrupt. [18]

Canada's standing in the London markets, which collapsed during the rebellions of the late 1830s, sank further.

In 1849, responding to Durham's report (and British bondholders), London merged bankrupt Upper Canada and fiscally sound Lower Canada into a single, and solvent, Province of Canada with Responsible Government along the lines Durham had proposed. In response, a Tory mob burned parliament. But Canada now had a Prime Minister responsible to an elected legislature. However, the necessity of an Imperial guarantee on Canadian debt convinced the Imperial Government to appoint the London investment houses of Barings and Glyns to oversee Canadian finances.

The Galt family was by now well established in Lower Canada. Alexander Galt had formed the British American Land Co. in 1831 to buy land from absentee Loyalist owners in Lower Canada and resell it to English settlers, just as John Galt, his father, had in Upper Canada.[19] In 1844, Alexander Galt, John Galt's son, established the Sherbrooke Cotton Mill, Canada's first industrial joint stock company, and further growth opportunities seemed abundant with the return of political stability. Perhaps the most

[18] Bliss (1986) p. 158.
[19] Dowde (2002).

important development policy of the new united province was the new 1849 Patent Act, which forbade Canadian patents on American technology, creating hoards of business openings for local entrepreneurs capable of using such know-how.

The new colonial leaders felt hamstrung by their lack of fiscal freedom to subsidize these new ventures with state money. Francis Hincks, an entrepreneur and Member of Parliament, partially solved this problem with a new Municipalities Act that let towns issue public debt. A more complete solution appeared in 1849, when Canada began guaranteeing railroad debt, but only if prominent politicians, such as Hincks and Galt, were on the board to guarantee good management. After a brief financial crisis in 1849, a boom and bust in railroad stocks ensued, and railroad construction then began on a large scale. Although railroads built honest fortunes, such as that of the consulting engineer Casimir Gzoski, much evidence points to corruption on a huge scale.[20] Sir Allan Napier MacNab, president of the Great Western Railway, served Canada as chairman of the Parliamentary Standing Committee of Railways and Telegraphs. The grandest project, the Grand Truck Railroad run by Prime Minister Hincks, was built in such a slipshod fashion that it was almost unusable.[21] A British lobbyist hired by Hincks to lobby members of parliament wrote:

> I do not think there is much to be said for Canadians over Turks when contracts, places, free tickets on railways, or even cash was in question.[22]

[20] See Myers (1914) chapters 10 and 11 for a detailed description of specific allegations and evidence., including the report of the 1876-1877 Select Parliamentary Investigating Committee. Mills (1872), a Member of Parliament, writes that "Corruption taints the majority of railway enterprises from their inception to completion" and provides details.
[21] Myers (1914) chapter 11.
[22] Bliss (1986) p. 187.

An investigation by Barings exposed endemic fraud, kickbacks, and deceit; and Barings blocked further Canadian listings in London until Canada accepted a Barings veto over additional debt financing and guarantees. The Canadian government accepted these terms in 1851.

The subsequent decade saw a broad modernization of the economy. The Toronto Stock Exchange was founded in 1854, primarily as a commodity exchange. The end of the Imperial Preference System (Corn Laws) in 1846 and the elevated wheat prices during the Crimean War led to a Reciprocity Treaty (free trade) between Canada and the United States in 1854. Also in 1854, Prime Minister Hincks bought out the seigneurs of Lower Canada, and the feudal system finally disappeared.[23] Although slave sales had been abolished in 1797, French Canadian *habitants* only emerged from feudal serfdom a few years before the US Civil War. In 1866, Lower Canada replaced *la Coutom de Paris* Civil Code with the Lower Canada Civil Code, based on the Napoleonic code, and adopted Common Law for certain commercial and maritime disputes.

Railway subsidies were a top government priority. In 1858, Alexander Galt, now Finance Minister, subordinated Canada's sovereign debt to railroad common stock and raised the tariff to obtain funds for larger railway subsidies. Virtually every important politician now moonlighted as a railway officer or director, and railway subsidies remained a huge drain on Canadian government finances. Current, past, and future Prime Ministers Francis Hincks, Alexander T. Galt, and John A. MacDonald, respectively, and most of their cabinet ministers all had railway ties.[24] According to Naylor (1975), railroad construction and financing in colonial Canada were "appalling even by the

[23] Myer (1914) makes much of the generous terms of the buyout in contrast to the conditions under which feudalism ended in France in 1789.
[24] Myers (1914), Bliss (1986).

standards of the day." By the 1860s, Canada had both a shoddily built, poorly run railroad system and a near bankrupt government. However, union with the solvent Maritime colonies of Nova Scotia and New Brunswick promised renewed fiscal balance. When the United States abrogated the Reciprocity Treaty in 1866, Galt lowered the tariff slightly on manufactured goods to match those of the Nova Scotia and New Brunswick colonies, in preparation for their union with Canada.

Canada on the Eve of Industrialization

One important lesson to draw from this brief overview is the venerability of state patronage of business and the profundity of what we would now characterize as corruption. Mercantilism in the form of state subsidized ventures owned or run by a tiny elite was commonplace. This same elite monopolized all business, politics, church, and the judiciary.

While a few publicly traded companies existed, the greatest part of the economy was family businesses and an occasional partnership. A handful of genuine entrepreneurs had grown rich despite this ossified elite, and the Liberal revolutions of the late 1830s opened business opportunities to a somewhat wider cross-section. However, the new Liberal elite proved just as mercantilist as the old. Canada's policy of explicitly forbidding the enforcement of the intellectual property rights of foreignerswas regarded as a legitimate development tool.

What is remarkable is that despite these weak institutions, Canada transformed itself from a feudal wilderness into a country with farms, cities, canals and railways. Land development schemes opened new areas to settlement and the foundations of great business dynasties were laid down. While there was clearly enormous waste and theft, this deeply corrupt political economy nonetheless advanced to the earliest stages of industrialization.

These observations raise questions about the current condemnation of "corruption" as inimical to development in the third world. Canada's colonial heritage renders the hypothesis that honest institutions are a consequence of growth, rather than its cause, at least worthy of serious thought.

3. Early Industrialization

In 1867, a complicated series of intercolonial negotiations resulted in the creation of the Dominion of Canada, a self-governing entity within the British Empire, as British investors blocked New Brunswick and Nova Scotia financing in London to force those colonies into the union. Canadian independence is usually dated to 1867, though Responsible Government came earlier and Canada remained within the British Empire long after this date. Since the Canadian parliament assumed almost all of the powers of the parliament in London in 1867, this date is probably more appropriate than any other.

Reliable economic data also begins around this time, and Figures 2 and 3 illustrate population and GDP growth figures. This data allow us to move beyond the Hudson's Bay Company corporate records for quantitative appraisal of the economy's performance.

[Figures 2 and 3 about here]

The Hudson's Bay Company was in the charge of George Simpson, the bastard son of a Presbyterian minister. Though occasionally restrained by the London directors' concern for the welfare of the natives, Simpson's deep suspicion of ethics let him ruthlessly exploit Rupertsland from the mid 1820s to 1869, and push American competitors out of the Oregon Territory. Nonetheless, the settlement of the west bade ill for the fur trade over the longer term. The London Committee saw this, and the declining dividends evident in Figure 1, and invested Hudson's Bay Company funds in lumbering, fishing, livestock, coal mining, buffalo wool, and even a colony in Oregon. All these ventures failed. Consequently, the dividend, shown in Figure 1, continued to slide. After two takeovers, a new management team concluded that forsaking the fur trade and selling land was in the best interests of the shareholders.

By this time, the company had a new Chief Factor, Donald Smith (who later purchased the title Lord Strathcona and Mount Royal). Smith believed in industrialization. For example, he used his position as a Member of Parliament to undertake steamship and railway investments in Manitoba.[25] Later, he ran both the Canadian Pacific Railway and its vast land grants.

In 1868, Smith sold Rupertsland, including the Manitoba colony, to the new Dominion. Their property rights annulled, the Manitoba métis and other settlers rose in rebellion in 1869, as President Louis Riel declared a Republic and proclaimed Manitoban independence.[26] The rebellion was put down in 1870 and Riel went into hiding. Manitoba rejoined Canada as a new province and the rest of Rupertsland became Canada's Northwest Territories. In 1871, the British colonies on North America's Pacific

[25] Myers (1914) chapter 13.
[26] See Myers (1914) chapter 9 for a detailed description of the conflicting interests behind the rebellion and its suppression.

coast joined Canada as the province of British Columbia in return for a transcontinental railroad - to be financed by Canada. That year, Hugh Allen founded the Canada Pacific Co. to build the rail link. The Grand Trunk, fearing competition, lobbied furiously to undermine Allen's company.

The Panic of 1873 and subsequent depression – Figure 3 shows a drop in per capita GNP of almost 8% in 1876 - put these plans on hold, and the revelation of a huge kickback from Hugh Allen to Prime Minister MacDonald brought down the Tory government. The new Liberal government of Alexander Mackenzie raised the tariff and tried to rehabilitate Canadian debt in London. A series of bank panics and failures continued through the 1870s.

Still lacking a transcontinental railroad, British Columbia elected a separatist government in 1878. MacDonald recaptured power in 1879 on the platform of immediately beginning the railroad (as well as further raising the tariff and supporting the Roman Catholic clergy). The Canadian Pacific Railway (CPR) was formed in 1881 as a generously subsidized joint stock company run by George Stephen, who controlled several railways, which the CPR purchased. The subsidy included millions of acres of land in the west, which were transferred to a company controlled by Donald Smith and Edmund Osler, the latter also the owner of small railways bought by the CPR.

A period of rapid industrialization began in Ontario and Québec to supply railroad construction. Manitoba experienced a land boom, and ranching was established in the part of the Northwest Territories that would become Alberta, where large natural gas deposits were found in 1883. In 1883, the Hudson's Bay Company Chief Factor, Donald Smith, joined the board of the CPR and quickly came to dominate its management.

In 1884, as settlers moved west into the new District of Saskatchewan, Louis Riel reappeared – again declaring a Republic and leading the still predominantly métis Saskatchewan out of Canada. Construction of the CPR took on a new urgency, for MacDonald needed it to move troops to Saskatchewan. Riel was hanged and no province has seceded from Canada since (so far).

The CPR completed its transcontinental line in 1886, and then diversified into steamships and luxury hotels, quickly replacing the Hudson's Bay Company as the dominant business of the land. Presidents of the CPR and Prime Ministers of Canada renegotiated subsidies (upwards, eventually to over 200 million dollars plus land grants) as equals.[27] Meanwhile, the Canadian Pacific created the greatest fortunes of the era. In the 1890s, the richest Canadians were reputed to be Richard B. Angus, Joseph Hickson, George Cox, Duncan MacIntyre, Lord Strathcona and Mount Royal (formerly Donald A. Smith, Chief Factor of the Hudson's Bay Company), Lord Mount Stephen (formerly George Stephen), and William Van Horne. Of these, all but Cox and Hickson were major players in the construction or operation of the CPR.

Hickson grew rich revitalizing the old Grand Trunk Railroad, and Cox by reselling the bankrupt Midland Railway to the Grand Trunk at a huge profit.[28] Numerous politicians made lesser fortunes.[29] Cox, the six-term mayor of Peterborough, Ontario, ran British America Insurance, Canada Life, the Canadian Bank of Commerce (now CIBC), Central Canada Savings and Loan, Canada Landed & National Investment Co., Imperial Life, Manitoba Northwest, National Trust, Toronto Savings and Loan, and Western Insurance. Cox also founded the major investment firm, Dominion Securities. His other

[27] Myers (1914) chapter 14.
[28] Myers (1914) chapter 14.
[29] For a detailed list, see Myers (1914) chapter 15.

major venture outside finance and politics was Dominion Coal. Cox married his daughter to a talented manager, Alfred Earnest Ames, who took over the family empire and founded the large brokerage firm A.E. Ames & Co.

Another fortune in place at the beginning of industrialization was that of the barely literate Irish immigrant Timothy Eaton, who had built a nationwide catalogue department store business that bypassed wholesalers and used the railway system to deliver goods either to branch stores or directly to retail customers. Replacing the declining staples wholesale businesses of the Buchanans, MacDonalds, and others, Eaton's and its imitators - Robert Simpson and Charles Woodward, and the Hudson's Bay Company - would dominate Canadian retailing.

The Montréal merchant, W.W. Ogilvie built a grain elevator business along the transcontinental railways. His monopoly tracked that of the CPR across much of the country.

By this time, Canada's securities markets and financial system had developed to the point that growth through mergers and acquisitions was possible. Thus, George Cox and his partner, Prime Minister MacKenzie Bowell, were able to build National Investment Co. through an M&A program. In fact, the early 1890s constituted Canada's first M&A wave. Figure 4 shows M&A activity from the first Canadian records to the present, and reveals a distinct surge in this period. Since virtually all of the new companies that had grown to prominence were narrowly held, a takeover or merger required buying a private family company or buying a control block of a traded company from an existing dominant shareholder.

[Figure 4 about here]

The MacDonald Tories sought rapid industrialization through foreign direct investment (FDI). To promote FDI, MacDonald had revised the Patent Act in 1872 to allow the enforcement of US patents only if the U.S. patent holder had a subsidiary in Canada. In 1879, MacDonald enacted the sweeping National Policy - tariffs ultimately averaging 35% across the board designed to force foreign firms to substitute FDI for exporting into Canada. Thus, Canada adopted import substitution as a development policy just as much of the rest of the world achieved an apogee of free trade. Tory manufacturers were able to inextricably and permanently link Canadian nationalism with high tariffs.

These protectionist measures did succeed in fostering a large branch plant economy. For example, Alexander Graham Bell entrusted his father, Alexander Melville Bell, to set up a Canadian telephone company - American Bell of Boston held Bell's patent from the 1880s on. Canadian municipalities everywhere, eager to attract these sorts of high tech ventures, offered increasingly competitive "bonuses" – up front cash subsidies – to manufacturers. A multitude of bidding wars, often financed with municipal debt, erupted across the country, with *The Monetary Times* reporting in 1895 that

> American firms of every description 'seeking a new site' or 'wishing to extend their business by establishing a Canadian branch' have only to make public their designs and be inundated by letters from Canadian municipal authorities.[30]

[30] Quoted by Bliss (1986) p. 304.

Despite their success in generating branch plants, the overall efficacy of these industrial policies as a development strategy remains a topic of debate. For example, Naylor (1975) argues that their side effect was Canada's marginal position in the wave of technological innovation in the 1890s and early 1900s.[31] Bliss (1986) argues that the National Policy "created distorted hot-house growth in manufacturing that had serious, often harmful consequences," and cites a vast overcapacity in chic high-technology industries like textiles and steelmaking. Irwin (2002) argues that rapid growth in Argentina and Canada, two high-tariff, high-growth outliers in the late 19th century, was based on commodity exports, not industrialization based on import substitution. He argues that the tariff was a revenue source, not a spur to industrialization.

Another distortion was smuggling, which became a major industry. Although this had some beneficial results, such as fueling the growth of Fort Whoop-Up in the part of the Northwest Territories that would become Alberta, its effects were probably mainly negative.

The National Policy also fostered inefficient and high cost production. Few Canadian firms were capable of exporting. Notable exceptions were the farm machinery firms of Hart Massey and Alanson Harris, both based on Canadian patents and American prototypes. Domestically, the competing firms prospered as farming in Ontario, and later Québec, modernized. By 1891, when the two great family firms merged, both had robust export businesses in Argentina, Australia, and Great Britain. Patent law technicalities initially limited their US exports.

[31] Naylor (19xx), Vol. II p. 47.

Also, reciprocal trade barriers stymied creative entrepreneurs. Thus, J.L. Kraft moved his cheese business from Ontario to Chicago in 1905.

By subsidizing manufacturing, the National Policy probably delayed the exploitation of Canada's vast mineral wealth. Remarkably, at the end of the 19th century, Canada was regarded as virtually bereft of exportable mineral deposits.

Finally, nationalist support for economic walls created opportunities for political entrepreneurs. Members of Parliament and other politicians, such as Manitoba Premier John Norquay, routinely empowered each other to develop and run coal mines, lumber companies, and land companies.[32] An 1875 requirement that insurance companies invest domestically repelled foreign insurers and opened the field for a spate of new Canadian insurers. Confederation Life was run by Sir Francis Hincks, then Finance Minister. Prime Minister Mackenzie took charge of North American Life after losing power in 1878. Prime Minister MacDonald served as president of Manufacturer's Life while in office. Sun Life was run by Matthew Gault until MacDonald intervened to oust him.

In summary, Canada's early industrialization was a textbook example of import substitution. High tariffs were erected to protect local business and to force foreign companies to establish Canadian branch plants, rather than export to Canada. Foreign patents remained unprotected unless the patent holder established a Canadian production facility. Family controlled pyramids gained importance and freestanding widely held firms remained rare, save for the unlisted, though widely held Hudson's Bay Company and the Canadian Pacific Railroad. Senior politicians routinely ran major corporations while in office, accepted kickbacks, and saw this as a normal perk. Politics and

[32] Myers (1914) chapters 16 and 17.

government still registered corruption levels well into the present day third world range, as did investor protection and disclosure standards.

Thus, political independence did not change the institutions greatly. Although more fortunes were associated with heavily subsidized nation-building projects like the CPR, genuine entrepreneurs such as Eaton created new wealth. While many economic historians believe less corruption, more openness, and better institutions would have sped growth, gross corruption and heavy handed protectionism clearly did not obstruct it entirely.

4. Industrialization

The Liberals took power in 1896, and ushered in a booming economy, with the new Québecois Prime Minister, Wilfred Laurier, famously proclaiming "Canada will fill the twentieth century." This seemed not absurd at the time, for Canada's population and industrial production were growing at unprecedented (and unsurpassed) rates. A popular diversion of the time was forecasting when Canada's population would exceed that of the United States by extrapolating the two countries' growth rates. An immigration boom settled the new provinces of Alberta and Saskatchewan, and greatly expanded the populations of the older provinces. New technologies seemed designed to create opportunities in Canada. The fat Hudson's Bay Company dividends of this era, shown in Figure 1, as well as the more direct measures of growth in Figures 2 and 3, all also attest to the country's prosperity.

Visionary politicians seriously advocated imperialism, envisioning Canada taking on weary Britain's role as the center of a worldwide Empire. This too seemed not unreasonable, as Victorian capital flooded Canada. More foreign investment actually flowed into Canada per year in absolute terms during the boom than into the United States. Laurier himself was a dedicated imperialist.

During this period, Canada developed a vigorous financial sector. Max Aitken's Montréal Trust and Monty Horne-Payne's British Empire Trust funneled this last great wave of British foreign investment into Canadian start-up ventures and corporate takeovers. A domestic securities industry grew fat off the proceeds of public issues as domestic demand for investments rose. George Cox, despite the obvious incompetence of all his sons, entertained visions of a dynasty. In 1905, James Henry Gundy and George Herbert Wood quit Cox's Dominion Securities to form Wood Gundy Ltd., which quickly grew to dominate the industry. Banks and insurance companies, as well as trust companies and the new securities firms, directed Canadian savings into industrial ventures *via* bonds, preferred stock, and common stock.

These developments permitted another wave of mergers and acquisitions. By raising cash through bond issues *via* their securities houses, raiders could finance corporate takeovers. By swapping shares, they could undertake mergers. Figure 4 shows a second burst of M&A activity in the early 20th century.

In 1899, Henry Melville Whitney issued shares to consolidate several collieries into Dominion Coal, and then to diversify into steelmaking with Dominion Coal and Steel. The Cox family responded by setting up the country's first true pyramidal group, with public shareholders holding minority interests in Crow's Nest Pass Coal, Canada Cycle and Motor Co., and a host of other firms. Panics in 1903 and 1907 soured many of the old families on equity holdings, but public demand continued.

As the stock market deepened, widely held industrial firms also appeared. The Hudson's Bay Company had never had a single dominant shareholder, though its Chief Factor often seemed to rule the company and its shares did not trade on exchange. The Canadian Pacific had also been widely held from its outset. By1900, Bell Canada too was widely held. All three firms remain widely held and still trade in Toronto.

The Laurier Boom also sustained itself by expanding the market available to Canadian industry. Three major factors contributed to this: a rapidly growing domestic population, declining freight rates, and foreign investment by successful Canadian firms.

An immigration surge caused Canada's population rise by 44% during the period. The rapid growth of the new provinces of Alberta and Saskatchewan, as well as a sustained growth of British Columbia, Manitoba, and Ontario made the Canadian domestic market increasingly able to provide the economies of scale needed to support entrepreneurship.

Alexander Tilloch Galt, whose family had helped settle English immigrants in both Upper and Lower Canada in the 19th century by buying land from Loyalists and reselling it to settlers, repeated this model in Alberta with more success than in either previous venture. Hugh Allen made another fortune off his vast ranches in Alberta as meat production shifted west. The semi-literate Patrick Burns built a huge beef packing empire based in Calgary. But the pork business remained in the east, primarily because Toronto pork packer William Davies made his best manager, Joseph Wesley Flavelle, a major shareholder. Flavelle built Wm. Davies & Co. into the Empire's largest pork packer, winning the engaging nickname "Hog Town" for his hometown.

Robert Dunsmuir grew wealthy from his Union and Wellington Colliery, Esquimault and Nanaimo Railway, and especially his land grant from the government at the CPR Pacific terminus, an obscure village called Vancouver. As the local population surged, Dunsmuir's coal operations far outstripped his core demand from the railroad. He also served as Premier of British Columbia through much of the new century's first decade.[33]

Freight rates fell as the Manitoba entrepreneur William Mackenzie and his partner, Donald Mann, strung bits of railroad together to compete with the CPR in its most profitable runs. This competition ultimately lowered rail shipping costs substantially, providing further scale economies.

Fresh from building the now world famous Canadian Pacific Railroad, the longest in the world, other railroad barons looked abroad, setting up railways in Brazil, Cuba, Guatemala, Mexico, Spain, and the West Indies. Once established in those countries, they moved on to trolley systems, electric power and light systems, and sundry other enterprises. Canadian banks followed into these new markets.

The old Cox group, now ably managed by Mackenzie and advised by the legal virtuoso Zebulon Lash, also rapidly expanded into Latin America, Spain, and the Caribbean. In 1912, Mackenzie and his chief engineer, F.S. Pearson, combined these holdings into Brazilian Traction, also called *o pulve Canadenses* (the Canadian octopus). The Mackenzie family still controls one of Mexico's main pyramidal corporate groups.

The National Policy had produced enormous overcapacity in stylish industries, with many plants run by certifiably unskilled managers and financed with public share offerings. This overcapacity later allowed moneyed individuals and families to enter

[33] Myers (1914) chapter 16.

those industries at discount prices. Thus, A. F. Gault amalgamated about half of the country's cotton mills into Dominion Cotton Mills by 1890, and David Morrice amalgamated most of the rest into Canadian Colored Cotton by 1892. After fairly overtly fixing prices for many years, the two eventually merged into Dominion Textile in 1905.

Having exhausted the old forests of Eastern Canada, lumber companies looked west. Canadian lumber barons, such as John Hendry of New Brunswick and the Maclaren family of Québec, began major operations in the new provinces.

But new industries also arose. John Bayne Maclean, a clergyman's son, launched the *Canadian Grocer*, Canada's first weekly newspaper. He quickly launched a succession of other newspapers: *Hardware and Metal*, *Books and Notions*, *Dry Goods Review*, and *Canadian Printer and Publisher*. His most enduring companies were the *Financial Post* and *The Busy Man's Magazine*, which he later unassumingly renamed *Maclean's*. The Southam family of Hamilton used profits from their *Spectator* to acquire a steel company, printing plants, and a chain of newspapers in other cities.

Indeed, a series of technological advances also favored Canadian development, allowing entrepreneurs to grow wealthy in previously marginal or unknown businesses. Firms in these technology-intensive industries were continually *in play*, contributing to the merger wave visible in Figure 4.

Canada was designed for hydroelectric power. Dams went up everywhere. One of the largest projects was by William Mackenzie, who, briefly tired of his railroads and Latin American investments, built hydroelectric turbines under Niagara Falls and a system to transmit the power to Toronto.

New technology made it possible to use wood pulp, rather than rags, to make paper. This created new opportunities for firms that developed hydroelectric power sites to grind low-grade trees into pulp to produce paper. Hector Clergue built a hydroelectric generator to power such a mill at Sault Ste Marie, and the railroad tycoon Angus and Van Horne acquired another by squeezing the entrepreneur John Foreman out of his company, Laurentide Pulp. The first Québecois entrepreneur, Alfred Dubuc, built the *Compagnie de Pulpe de Chicoutimi* because, as he admitted to his banker, "*Je n'ai pas d'argent*."[34] Established lumber barons, including matchmaker E. B. Eddy and J. R. Booth, also moved into paper making.

This period also saw the beginnings of Canada's minerals industries. Discovering iron ore near his Sault Ste Marie mill, Clergue formed the Algoma Steel Co. to extract and smelt it and Algoma Central Railway to ship it out. Samuel J. Ritchie gambled on the discovery of low-grade copper and nickel ores in Sudbury, and won hugely when military demand associated with the Boer War pushed prices up sharply. A takeover of Ritchie's mining operation and an amalgamation with several other mining and smelting companies organized by Robert Thompson's smelting firm created International Nickel. When formed in 1902, it was the world's largest nickel producer. The CPR also entered the field, forming the Consolidated Mining and Smelting Company of Canada, or Cominco Ltd.

The mining business built more fortunes when gold was discovered, first in British Columbia in the early 1890s and then in the Yukon in 1898. A booming industry of fraudulent penny stock IPOs sprang up in Toronto, fleecing investors from across

[34] Bliss (1986) p. 323.

Canada and around the world. Two additional exchanges were formed in Toronto to handle the boom.[35]

A government-subsidized railway into Northern Ontario in 1902 brought a fabulous return, as minerals were discovered all around it, and is still used to justify publicly-financed development schemes. Gilbert Labline and Noah Timmins developed Hollinger Mines. J. P. Bicksell took over Porcupine Mines after its original owners were imprisoned. These firms, and the new Dome Mines, fueled a second wave of penny stock speculation. Over five hundred new mining companies were listed in Toronto to meet investor demand at the end of the new century's first decade.

Max Aitken, a passionate imperialist who purchased the title Lord Beaverbrook, assembled Canada's largest pyramidal group. The son of a Presbyterian minister, Aitken attracted notice by running Royal Securities for John Stairs, heir to the old Nova Scotia merchant family. In 1906, he used his earnings to buy Montréal Trust, and then used that firm to take over Royal Securities. Aitken began issuing debt in London on a very large scale and used the proceeds to buy up steel mills, cement companies, power companies, and other firms all over Canada. Aitken's merger activity established the Steel Company of Canada from Montréal Rolling Mills, Hamilton Steel and Iron, Canada Screw, and Canada Bolt among others. Aitken also formed Canada Cement out of twelve of the country's thirteen Portland cement makers.

By 1909, the inflation was rising, but the merger wave thundered on. From 1909 until 1912, when the economy abruptly slowed, 275 of Canada's largest firms coalesced into 58 in half a billion dollars worth of M&A transactions.

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[35] See Armstrong (1997) for details.

As the boom redounded, Laurier concluded that Canada needed more state-subsidized transcontinental railroads. The Liberals had indignantly opposed the Tory plan to build the CPR, and had been proven wrong. Laurier now undertook ending the CPR monopoly by extending the old Grand Trunk into a second transcontinental line - at public expense.

Meanwhile, the entrepreneurs William Mackenzie and Donald Mann, backed by Manitoba government money, and rebuffed by the Grand Trunk principals, set about forming a third transcontinental line with the keen backing of George Cox and his Canadian Bank of Commerce. Francis Hector Clergue, who lost control of his companies at Sault Ste Marie in the 1903 Panic began promoting a fourth transcontinental line.

[Figure 5 about here]

It is in this period that we can first construct a broad, though approximate, cross-section of the ownership structures of large Canadian companies. Figure 5 classifies the top one hundred firms by ownership structure in 1910 – at the height of the Laurier boom. It shows that four widely held firms accounted for twenty-nine percent of the assets of the corporate sector. This is primarily due to Bell Canada and the Canadian Pacific Railway. However, the greatest part of the corporate sector, forty percent by assets and forty-four firms were firms in pyramids controlled by individuals or families. A large number of smaller firms are independent corporations controlled by a family or individual. About one fifth of the corporate sector is foreign controlled, primarily by Britons.

The 1911 election was a critical turning point for Laurier. During MacDonald's long tenure, the Liberals had railed against the National Policy. The party won power after Laurier promised business leaders the trade barriers would stand. On the crest of a booming economy, Laurier decided to reinstate free trade as a key plank in the Liberal platform for the 1911 election.

With Laurier's renewed triumph and free trade both in sight, investors ploughed yet more money into increasing the capacity of Canadian industry. An investment boom swept new industries like pulp and smelting. But, according to Naylor (1975), merchants and the owners of older businesses were furious. Intensive lobbying by the Canadian Manufacturers Association split the Liberal party, and key members of parliament associated with the Cox-Mackenzie pyramidal group crossed the floor to the Tories. Laurier lost the 1911 election, dooming free trade. The Great War interrupted the flow of British capital, halted most transatlantic shipping, and choked off immigration, underscoring an end to the boom. The new Tory government of Prime Minister Borden, another ardent imperialist, stalwartly declared Canada "Ready, Aye Ready" and delivered full support to Britain despite anti-conscription riots in Québec.

The boom had created a new industrial elite of multimillionaires alongside the old-money elite. The ostentation of these *noveaux riches*, with real Scottish castles in Toronto and Tudor palaces on Vancouver Island, seemed incompatible with the probity of Empire. That the major charitable foundations active in Canada were the Ford Foundation and the Carnegie Foundation also contributed to a growing backlash. The McGills and Molsons of Montréal, the CPR tycoons and lumber barons, and the non-smoking tobacco king William MacDonald all supported specific local good works, but none of Canada's multimillionaires remotely considered charitable giving on the scale of Bell, Carnegie, or Hershey. Instead, the new rich, like the old, planned family dynasties.

There had been sporadic strikes and occasional labor unrest throughout the 19th century, but organized labor was really due to a campaign by the American Federation of Labor to expand into Canada. The whole idea of labor unions was deeply antithetical to the traditional Catholic values of Québecois habitants and the Tory traditions of United Empire Loyalists. Voices for both condemned unionization as the lamentable Americanization of the country. Robert Dunsmuir instantly fired any employee he thought was even contemplating any connection to organized labor, probably setting the stage for British Columbia's damaging union militancy.

Parliament had passed an Anti-Combines Law in 1889, but its actual effect was to legalize price fixing, for the law held restraints on trade actionable only if they "unduly" or "unreasonably" lessened competition. Thus, cartels were a recurring feature of the time. For example, two leading oil refiners, Patrick Fitgerald and Jacob Engelhart, organized the Imperial Oil Co. in 1880 to fix prices. Standard Oil promptly invaded Canada pushing prices down until 1898 when Standard acquired Imperial, and again established something approaching a monopoly.

There were attempts to build the moral case for restraints on trade. For example, the *Journal of the Canadian Banking Association* wrote in 1898 that

> "[T]here should be certain things universally considered unprofessional within our ranks. Giving service without profit or at an actual loss should be unprofessional. Solicitation of business by offering to work more cheaply should be as unworthy of a banker as we consider it unworthy a doctor."[36]

[36] Quoted by Bliss (1986) pp. 360-61.

The Canadian Bankers Association was formed in 1891 to fix interest rates and other bank fees. Small merchants across Canada pointed accusing fingers at Timothy Eaton's catalogues and department stores for just such unprofessional conduct.

To many Canadians, though, Eaton was a hero. The flawed Anti-Combines Law seemed a deliberate shot into its own net by a government of vested interests. The National Policy, which elevated the prices of most everything, seemed the fount of all price fixing. And the powers granted the CPR still chafed in the new western provinces. The attitudes of great industrialists further stoked popular ire, as when the CPR baron Van Horne quipped "people who put pigs in office ought not to complain if they eat dirt and are bought and sold."[37]

And many industrialists were guilty of more old-fashioned unprofessional conduct. A 1906 Royal Commission on Life Insurance exposed extensive tunneling in the Mackenzie-Cox pyramid, with money flowing from insurance companies to power companies, as well as extensive insider trades by the pyramid companies in each others' stocks.[38] The result was a 1910 law tightening investment rules and reporting standards, but only for insurance firms.

Canada's corporate governance laws during this era were extraordinarily weak in general.[39] Corporate governance was essentially a matter of private reputation, constrained loosely by vague and often contradictory provincial statutes and common law precedents. No federal corporation law existed until 1910, and that law required no annual general meetings. Until 1917 they needed only hold meetings every two years,

[37] Bliss (1986) p. 368.
[38] Bliss (1986) p. xxx.
[39] See Armstrong (19xx) for a detailed review. A good summary is provided in Boothman (2000).

and then only to elect the board. Only Ontario required annual shareholder meetings. The law mandated neither minority shareholder rights nor fiduciary duties by officers and directors to shareholders. Directors and officers had a "duty to the corporation" under common law, which was interpreted as trumping any duty to shareholders. Conflicts of interest were of no concern to the courts. Shareholders had no rights in common law to inspect books or records unless they could persuade a judge of a definite legal objective and could identify the specific records that would certainly contain the information. Auditors had no duty to inform shareholders of potential or actual misconduct; their duty was purely arithmetical. One key precedent held that auditors were "justified in believing tried servants in whom confidence is placed by the company".[40] Another warned that an auditor who opines on governance "does so at his peril and runs a very serious risk of being held judicially to have failed to discharge his duty."[41]

The political movement that rose to combat these and other ills associated with highly concentrated economic and political power in Canada came to be called the Progressive Movement, and its growing strength probably factored large in Laurier's unpropitious decision to make free trade *the* issue of the 1911 election. A "people's power" campaign of Progressive agitation and lobbying by electricity hungry businesses in Ontario led that province to establish Ontario Hydro, a state-owned power company that would compete with privately owned power companies.[42] A similar campaign in Alberta led to the state-owned Alberta Government Telephones.[43]

[40] Re Kingston Cotton Mills (1986) 2 ch. 279 at 688, 65 LJ ch 673.
[41] Re London and General Bank (1895) 2 ch. 685, 64 LJ ch 866.
[42] See McKay (1983).
[43]

The new Tory government of Prime Minister Borden continued Laurier's railway construction programs, and by 1915 the National Transcontinental Grand Trunk Pacific was complete. The same year, William Mackenzie finished his Canadian Northern. Both new transcontinental lines were hopelessly insolvent almost immediately. The new railways were both "too big to fail", and after a series of bailouts, the government bowed to populist pressure and nationalized both new lines to form the Canadian National Railway.

In summary, public investors were an essential part of Canada's large-scale industrialization. Old wealth still controlled many of the new industrial ventures that were transforming the country. However, the scale of investment opportunities available demanded external capital. Pyramidal groups were a device that allowed continued family control while bringing in external capital from public shareholders, and were consequently extensively used. Max Aitkin and other takeover entrepreneurs set a merger wave in motion, buying up family firms and combining them into large-scale corporations, often within even larger pyramidal groups. Bond issues in London were a key source of financing for these deals. Many industries were probably highly cartelized. Still, *noveaux riches* entrepreneurs were genuinely important for the first time in Canadian history. Outright scandals involving covert deals between the political and corporate elites became rarer, but government subsidies, bailouts, tariff protection, and protection for cartels indicate continued devotion to Canada's venerable mercantilist heritage.

[Figure 6 through 9 about here]

4. The Interwar Economy

We can now track the evolution of the ownership structures of large Canadian firms over time. Figures 6 through 9 show little change in the corporate ownership structure of large Canadian firms between 1910 and 1920, but a discernable increase in foreign control and, to a lesser extend, widely held firms from 1920 on. This is mainly at the expense of narrowly held pyramidal group firms.

Before we turn to explaining these developments, a brief overview of changes in the economic environment is useful first. The 1920s began with a sustained deflation, a collapse of the businesses sector, and an exploding government deficit. However, beer and liquor exports soon created new opportunities, and by the latter half of the decade, the economy was booming.

In August of 1914, Canada left the gold standard and the government began printing money to pay for the Great War. Inflation roughly doubled the cost of living by 1920. With the war won, holding down wages could no longer be justified out of patriotism, and union membership grew by 50% in 1919. A series of strikes paralyzed Canada's major cities, with the bloody Winnipeg General Strike attaining Bolshevik proportions. In 1920, prices "broke", and several years of sustained deflation set in. Deflation caused a wave of business failures in the early 1920s that was not surpassed even in the 1930s. This, in turn, triggered a wave of bank failures. Hugh Allen's Merchants' Bank, first to fail, was rolled into the bank of Montréal in 1921. By 1928, Canada had only ten remaining chartered banks, down from thirty in 1910. The last narrowly held family bank, Molson's Bank, was taken over by the Bank of Montréal.

Mistiming the new boom, Izaac Walton Killam, now running Royal Securities, organized the world's largest pulp and paper company, Riordon Co., through a series of amalgamations. Killam was wiped out. Roy Wolvin and a cadre of other former Beaverbrook associates combined Nova Scotia Steel and Coal, Dominion Coal, Dominion Iron and Steel, Dominion Steel, a Halifax shipyard, and several other companies into the British Empire Steel Co. The postwar world turned out to be awash in surplus capacity, and the venture collapsed. As it died, Wolvin tried to force ever greater concessions out of labor, triggering Canada's worst class war. By 1922, one third of the Canadian army was maintaining order around BESCO facilities. One commanding officer even called for air strikes. Nova Scotia labor was irredeemably radicalized, and Atlantic Canada never recovered its leading industrial position. And one of the great pyramidal groups from the Laurier era was in tatters.

As the economy stagnated, the government found itself pouring ever rising subsidies into the Canadian National Railway, in addition to servicing its war debts and providing for veterans. In 1916, parliament had passed an excess corporate profits tax to fund the war. When this lapsed, it enacted a permanent manufacturers' sales tax at six percent. Corporate and personal income taxes, enacted in 1917, rose sharply with top marginal rates for both soon above fifty percent. To avoid double taxation, dividends and capital gains were exempt. In 1926, dividends became taxable personal income, but intercorporate dividends remained exempt, allowing pyramidal groups to continue.

As more companies failed, government finances teetered, and taxes rose. Immigration fell to about one third of its prewar level, and bold new initiatives like BESCO and Riordon had failed spectacularly. The great business leaders of the prewar era were dead or retired. The new Tory Prime Minister, Arthur Meighen, though a capable corporate raider in his own right, seemed out of his depth. Things looked bad.

Amid the stagnation, a new progressive party, the United Farmers, broke Canada's two-party system and took power in both Alberta and Manitoba in 1921. The same year, its federal counterpart, the Progressive Party became the Official Opposition to the new Liberal government of William Lyon Mackenzie King. This movement, mainly representing new immigrants, seriously rattled the Anglo political establishment.

New business opportunities were more dependent on happenings in the United States than in previous decades. The most significant opportunity for Canadian business in this era was provided by the Prohibition laws effected in the United States from 1919 on. These made the manufacture, sale, or transport of alcohol illegal, but permitted its consumption.

Abe and Harry Bronfman, who built a chain of hotels in western Canada, discovered the highly profitable business of selling mail order liquor. His attention to quality and cost soon made Harry the biggest liquor wholesaler in Saskatchewan, with most of his business in border towns. By 1927, having gained control of Seagram's, an old family distillery in Ontario, the Bronfmans were among the richest families in Canada. Their heirs would later control the largest family controlled pyramidal groups in the country.

Meanwhile, the Ontario hotelier Harry Hatch took over the established Gooderheim and Hiram Walker distilleries, and set up a rival mail order and wholesale liquor business. The staunchly religious Labatt family turned over management of their breweries to Edmund Burke, an Irish catholic who cheerfully maximized exports. By the mid 1920s, competition in beer and spirits exports was so intense that profits were dangerously thin and Canadian exporters organized to fix prices.

All of these enterprises owed a deep debt to the Molson family, who vigorously worked their political connections to keep Canada, and especially Québec, from succumbing to the foreign hysteria of Prohibition.

The new high technology industries of the 1920s - automobiles, airplanes, motion pictures, and office automation - were slower to make an impact in Canada than elsewhere. Fossmobile, Maxmobile, LeRoy, Bourassa, Mottette, Neff, Redpath, London, and Lavoie were all much touted Canadian automobile manufactures that filled the dustbin of business history. Canada Cycle and Motor made the most viable product, the Russel. Sam McLaughlin put Buick engines in luxury bodies, and Gordon McGregor founded Ford Motor Co. of Canada. McGreggor died in 1922, and Ford subsequently integrated its Canadian and US operations. General Motors bought out the McLaughlins and Chrysler bought the Russel from CCM. By 1926, Canada was closing on the US in car ownership, and had tens of thousands employed in auto making and related industries. The Bank of Nova Scotia's president SJ Moore created a series of companies to produce paper forms and cards for use in Hollerith's IBM tabulating machines. He amalgamated these into the Moore Co. in 1929.

As the world economy recovered in the 1920s, demand for pulp and paper and minerals picked up again. But now the capital was from New York, not London. By the late 1920s, pulp and paper investment was booming. Family controlled mills disappeared in a second wave of mergers, with American money involved at every level. The major player was Harvey Reginald MacMillan, a forestry student who stayed on in British

Columbia after a summer job. MacMillan Export Co., formed in 1919, came to dominate the industry, and shipped wood around the world on its Canadian Transport Company chartered fleet.

International Nickel, selling an alloy developed by its metallurgist president Robert Stanley, also dominated its industry. The Mackenzie pyramid's British American Nickel failed in 1924, and International Nickel took over its last major competitor, Mond Nickel, in 1928, giving it a 90% world monopoly. The monopoly broke when Falconbridge, controlled by Thayer Lindsay, developed a major rival operation.

A new mining enterprise, Noranda, developed a large gold strike in northern Ontario and was partially bought by Hollinger. Hudson Bay Mining and Smelting developed new mineral discoveries in northern Manitoba. In 1925, Alcoa bought a range of prime potential hydroelectric power sites from the Price and Duke families, and formed the Aluminum Company of Canada (Alcan) to develop them as smelters for local bauxite. All of these firms would later become widely held.

Stock prices picked up from 1926 on, and old families began selling out *via* public equity issues. The Massey family sold out when Vincent resigned the presidency of Massey-Harris to enter politics and his brother Raymond took to the stage. The surviving Dunsmuir sons and grandsons were wastrels, and ultimately sold out to Mackenzie and Mann. Harris Abattoir, controlled by McLean, took over Wm. Davis & Co. to form Canada Packers. CL. Burton bought out the old management of Simpson's, and T.P. Loblaw built a continent spanning chain of grocery stores.

As the economy prospered, other old family controlled companies were resurected as widely held firms. Wood Gundy floated a new Dominion Steel and Coal Co. from the ruins of BESCO.

New pyramidal groups also formed. Killam, now in control of Royal Securities, reassembled the pieces of Max Aitken's pyramid into a new Killam group. Nesbitt, Thompson organized the publicly traded Power Corporation to hold utilities in a pyramidal group. Other major holding company groups were Canadian Pulp and Power Investments and Hydro-Electric Bond and Share Corp. One of the most important pyramid builders of this period was Prime Minister Arthur Meighen, briefly back in office in 1928. Meighen issued debt to acquire companies for his Canadian General Investment Trust pyramidal group.

A.E. Ames & Co., Dominion Securities, Royal Securities, Nesbitt, Thompson, and Wood Gundy all underwrote new debt and equity issues, and organized mergers of constantly rising value. Ike Solloway and Harvey Mills established a chain of Solloway, Mills, & Co. offices across the country to handle the surging investor demand for penny mining stocks. By 1929, the firm, now based in Alberta, had forty offices, fifteen hundred employees, and 13,500 miles of private wire. McDougall & Cowans, Greenshields & Co., and Watson & Chambers also became major players in the investment banking and retail brokerage businesses.

The market continued rising through 1928, when investors valued the troubled radio company Canadian Marconi, with $5 million in assets, at over $130 million. Sir Henry Thornton, president of the Canadian National Railway determined that the time was ripe to make the CNR the greatest railway in the world. Thornton ploughed public money into a fleet of CN steamships, a chain of CN luxury hotels, and a vast expansion of the CN rail system. Not to be outdone, the CPR expanded its own existing operations in all these areas. In 1928, over 2,000 miles of new rail lines were laid and the expansion continued through 1929.

By 1929, the world was awash in minerals, paper, wheat, and manufactured goods. Commodity prices collapsed and so did corporate valuations. In 1930, the United States enacted high tariffs that crippled Canada's exports. Industry after industry collapsed, hiring stopped and layoffs began.

Following the Crash of 1929, the *Financial Post* published exposés of the investment industry. As the government struggled with a huge foreign debt run up by the CNR and an expanding trade deficit, Ike Solloway was arrested and jailed.

Securities and investments regulation had been delegated to the provinces in the 1867 legislation that created Canada. The provincial authorities eschewed a regulation-based clean-up as undue Americanization. Although provincial securities commissions were established in the 1930s, disclosure remained piecemeal and trading on insider information remained legal. High-pressure "boiler room" sales techniques remained an esteemed institution of Canadian finance.[44]

Unemployment relief was also a provincial matter, and the provinces needed tax revenues desperately. Ontario had introduced a "succession tax" in 1892, and by 1894 all the other provinces had followed suit. Death taxes had been introduced in England in the 18th century, and many US states had levied death taxes since the 1820s. Thus, succession taxes were seen as further Americanization of the country.[45] Although the

[44] See Armstrong (1997) for details regarding the lack of reform.
[45] For example, Bayley (1902) writes that the "Ontario Act of 1892 was purely American in origin."

original rates had been only in the five to ten percent range, by the 1930s top marginal rates were as high as thirty percent. Smith (1993) finds that succession duties accounted for a significant share of provincial revenues during the 1930s. As the patriarchs of family firms passed on, their heirs could not afford to retain full control and pay their succession taxes. Many sold out, contributing further to the continued decline of family control during this period evident in Figures 5 though 8.

The Liberal Prime Minister MacKenzie King attributed the growing unrest among the unemployed to subsidy-seeking provincial governments, and lost power in the 1930 election after quipping that he would not give a nickel to help a Tory provincial government alleviate alleged unemployment. The new Tory Prime Minister, R. B. Bennett, was a corporate lawyer and long-time associate of Max Aitken. Married to the heiress to the E.B. Eddy Company, he was also a millionaire.

Bennett's solution to rising unemployment was to raise the tariff higher and abandon the gold standard. When this became evident, the Canadian dollar fell precipitously and foreign lenders called in their loans. Major investment houses, including McDougall & Cowans, Greenshields & Co., and Watson & Chambers, promptly failed. To avoid a complete collapse, the Cabinet issued Orders In Council authorizing Canada's major banks and insurance companies, almost all of which were now bankrupt, to use "special valuation methods" to convince the public of their soundness.[46] Bennett barely prevented a sovereign default by raising funds through a National Service Loan, sold to the public using wartime rhetoric in a huge advertising campaign. The prices of the top fifty stocks dropped an average of 85% from their October 1929 highs to their May 1932 lows.

[46] For details, see Kryzanowsky and Roberts (1996).

Although deflation reduced the cost of living by over 20% from 1929 to 1933, wages fell by much less. This, combined with sharply reduced demand, caused prolonged depression in most industries – automobiles, base metals, oil, railroads, pulp and paper, and steel – collapsed. But precious metals mining prospered because investors viewed gold and silver as safe-haven assets. By concentrating on refining these metals from composite ores, the widely held firms Noranda and Cominco flourished.

At the Ottawa Imperial Economic Conference of 1932, Bennett organized an Empire-wide retaliation to US tariffs. The new Imperial Preferences abruptly shut US and Baltic lumber and paper out of Imperial markets, reviving the British Columbia economy. Canada Packers could now survived by undercutting Danish pork producers, and US firms had to establish more branch plants in Canada to re-enter Imperial markets.

The Retail Merchants Association of Canada gained national prominence through loud charges that 'big business' was destroying jobs through predatory pricing. Bennett responded in 1934 with the National Product Marketing Act, which enforced the cartelization, through marketing boards, of any industry whose producers so desired. Businesses from barbers to taxicabs were quickly cartelized under the direction of trade associations. Reynolds (1940) writes

"The Canadian associations perform scarcely any of the service functions which characterize trade associations in the United States. General statistical services, institutional advertising, cooperative research, and the like are very rare. The Canadian associations center upon the maintenance of 'fair prices' and it is judged largely by its success or failure in this field. One trade association secretary, indeed, remarked that 'manufacturers up here wouldn't be bothered with an association that couldn't control prices.'"[47]

[47] Quoted in Bliss (1986), p. XX.

Of course, the tariff was essential to supporting most of these cartels.

This seeming adoption of planning and state-control now looks socialist, and Bennett vigorously denounced *laissez faire* in a cross-country radio address in 1935. But neither he nor his Tory government was remotely sympathetic to the left. Bennett was an enthusiastic imperialist and thoroughgoing Tory. His prime objective was to protect established business, much like the Tories of the Family Compact a century earlier. Hankin (1933) summarized the prevailing philosophy thus:

"There must be planning, order, and cooperation in economic affairs between individuals, groups, and nations or disaster will overtake us all."[48]

However, the economy deteriorated further, and Bennett lost the 1935 election to King's Liberals. King repealed some of the enabling legislation for cartelization of the economy, but similar provincial legislation supplanted the federal laws in everything except agricultural products and banking. Federally enabled cartelization remained in place until quite recently for those industries, and still endures for some agricultural sectors.

Perhaps the most important of the industry associations was the Canadian Bankers Association. Parliament granted it the legal power to block charters for new banks. It coordinated reductions in deposit interest rates and increases in loan rates, and successfully lobbied for an abolition of government savings accounts that "drained the lifeblood of the country." Naylor (1975) argues that the banks, which were joint stock companies founded by commodities merchants, adhered to the real bills doctrine that

[48] Quoted in Bliss (1986), p. XX.

loans be backed by inventories, and that this substantially slowed growth by precluding loans for capital.

Genuine Keynesian economics came two Canada in two waves. In the first unsuccessful wave, the progressive United Farmers of Alberta lost the 1935 election to the Social Credit Party, which promoted the quasi-Keynesian ideas of Major CH Douglas. The province issued scrip and tried to regulate banking to increase the money supply. Unfortunately, the province refused to accept its own scrip for tax payments and the federal parliament declared its new banking regulations unconstitutional.

In the second successful wave, industry associations representing various parts of the construction industry lobbied heavily for a public works program. King's Liberals responded enthusiastically. Arthur Purvis, president of Canadian Industries Limited, pushed the Liberals further, arguing that the state should take on a broader insurance role. His advocacy was instrumental in establishing unemployment insurance in 1940.

Some family fortunes were wiped out in the depression. But new family fortunes were also made in the 1930s. Demand for Armand Bombardier's "snowmobiles" soared in the late 1930s. Kenneth Colin Irving expanded his family store business into a new pyramidal group of gas stations, busing, trucking, auto sales, and bus making. Roy Jodrey, who had lost a considerable fortune, established his United Service Corporation bus line, as well as a chain of gas stations and auto dealerships, building a new pyramid. John and Alfred Billes built Canadian Tire Corporation into a large national firm during the 1930s. Roy Thompson, after failing in several ventures and accumulating a bad credit record, acquired a radio station and then a newspaper. After paying US back taxes, the Canadian whiskey and beer firms of the 1920s did well in the legal US booze market, and

Edward Plunkett Taylor built a new major player, the Brewing Corporation of Canada. Charles Trudeau sold his chain of gasoline stations and his Automobile Owners Association service clubs, and bought into stocks precisely at the 1932 low, greatly magnifying his already creditable fortune. This provided his son, Pierre, the life of a millionaire playboy.

In summary, the weak economy of the early twenties ruined some older groups that expanded too fast. Then the strong market of the late twenties allowed many families to sell out. Selling out was increasingly necessary as provincial succession taxes rose, especially as they became hungrier for tax revenues in the 1930s. The 1920s bull market also capitalized new widely held companies and allowed new pyramidal groups to form and expand. The new businesses of the 1930s were predominantly narrowly held family ventures, for public equity issuance had largely dried up.

The crash of 1929 did not lead to an expansion of shareholder rights, or to perceptibly better regulation of financial markets and institutions. Incestuous ties between politicians and business remained evident, and perhaps grew deeper. And the government organized the wholesale cartelization of the economy. By any plausible measure, the quality of Canadian institutions was deteriorating. Yet despite this, widely held firms were becoming more commonplace and family control was starting to wane, at least within the ranks of the country's largest firms.

5. The New Dirigisme

Clarence Decateur Howe, an MIT graduate and engineering professor at Dalhousie University, had drifted out of academia to build a huge empire of grain elevators, which he lost in the Depression. C.D. Howe was well disliked and diplomatically inept. The president of the CPR remarked that “He is not able to deal with ordinary individuals except on the basis of a superior dealing with inferiors.”[49] However, as Mackenzie King’s “Minister of Everything”, Howe was unquestionably the most powerful force in the Canadian economy through the middle of the 20th century.

In 1935, needing work, Howe ran successfully for Parliament and became Transportation Minister in King’s new Liberal government. His first major effort was airline regulation, when in 1935 he squashed a private-sector attempt to establish a national airline by the Winnipeg grain merchant James Richardson, who had invested heavily in airmail delivery and wanted to expand into passenger service. Instead, Howe organized Trans Canada Airlines (TCA, subsequently renamed Air Canada) as a subsidiary of the state owned Canadian National Railway. All the senior managers were hand-picked by Howe. Richardson and Edward Beatty, the president of the CPR, which had backed his venture, were infuriated.

By the beginning of World War II, Howe had become King’s right hand man and took charge of the centrally planned wartime economy as Minister of Munitions and Supply. Howe subordinated the private sector to government planning by taking key industrialists into the government as “dollar a year men” and assigning them production targets. The War Measures Act and Wartime Prices and Trade Board kept down wages and prices while industrial production surged. The War Contracts Depreciation Board arranged special accelerated depreciation tax deductions on a case-by-case basis. Whenever a contractor’s profits looked to high, Howe sent someone to renegotiate the depreciation deductions down, and where that failed, applied a highly discretionary

[49] Quoted in Bliss (1986), p. 443.

Excess Profits Tax. Whenever no private company promised delivery on Howe's terms, he established a new state-owned enterprise. Both new entrants and business failures were vanishingly rare. Howe's dirigisme was wildly successful. By 1945, with European and Asian factories in ruble, Canada was the third largest economy in the world by some measures.

Canada's wartime alliance with the Soviet Union, and memories of the Depression amid the new centrally planned prosperity, boosted the popularity of the socialist Cooperative Commonwealth Federation (CCF), later renamed the New Democratic Party (NDP). The CCF outpolled both the Liberals and Tories at the federal level in 1943, and took power in Saskatchewan in 1944. This, even more than the earlier Progressive victories, deeply disturbed the country's polity.

King countered by moving the Liberal Party leftward, absorbing moderate socialists so as to leave the CCF unappealingly radical. In 1944 the King issued an Order in Council (executive decree) granting trade unions the right to organize and compelling collective bargaining, and appointed Howe Minister of Reconstruction and Supply. In 1945 Howe explicitly committed the Liberals to Keynesian countercyclical fiscal policy.

Following the war, Howe moved quickly to liberalize the economy - over the objections of the CCF and business groups who wanted state enforcement of cartel prices. He sold off state-owned enterprises in droves, adding further to the stock of widely held firms in Figures 5 through 8. However, he retained state ownership in key industries, keeping Polymer, a plastics manufacturer, and El Dorado, a mining firm with uranium holdings Howe had nationalized in 1944. Howe also provided extensive subsidies to aircraft manufacturing – most notably to A.V. Roe (Avroe), Canadair, and De Havilland.

As Howe moved from Minister of Reconstruction and Supply to Minister of Trade and Commerce to Minister of Defense Production, control of the state airline TCA moved with him. After Canadian Pacific Airlines (CP Air) emerged during the war to provide air transportation in the arctic, Howe tried to squash it to preserve the state airline's monopoly. CP Air only survived because TCA adamantly refused to fly trans-Pacific routes, and Howe begrudgingly let the private airline step in. He granted or denied import permits on a case-by-case basis, favoring some firms over others. To mitigate unemployment in northern Nova Scotia, he directed an increasing flow of subsidies to Dominion Steel and Coal.

Howe ended wage and price controls, though officially-sanctioned price fixing by industry associations remained until 1951, and key agricultural prices are still set by government marketing boards. In the late 1940s, Howe pressed for a final abandonment of the National Policy, and the Liberals negotiated terms for free trade with the United States. However, fearing a replay of Laurier's 1911 defeat, King quietly shelved the plan and opted for slow multilateral tariff reductions through the General Agreement on Tariffs and Trade instead.

But Howe was no libertarian. High taxes were now institutionalized, and Howe quickly realized that the tax system was now his major tool for micromanaging the economy. Most importantly for this study, the federal government entered the previously provincial arena of death taxes in 1941. The federal succession tax was enacted to generate war revenue, but always envisioned as permanent tax. Rates rose quickly and approached provincial levels by 1947. In 1947, the federal government doubled the rate to fifty-four percent and offered half its take to provinces that withdrew their taxes.

Seven did. Ontario and Québec retained their own succession taxes, which could be credited against federal tax. As the business elite of the 1920s passed away, a succession of family firms became widely held.

Major new private sector companies were also formed in these years. The Iron Ore Company of Canada was organized by Hollinger, Timmins, and the Hannas of Cleveland. Gunnar Gold Mines, run by Gilbert LaBline, whom Howe fired from El Dorado, developed a huge new uranium mine. Joe Hirshhorn developed the biggest ever uranium strike, sold out, and left Rio Tinto and Rio Algom running the operations. A Czech migrant farm worker, Stephen Roman, took an option on some claims near Hirshhorn's operations and struck uranium, and developed Consolidated Dennison Mines into a major producer.

And the widely held sector expanded. MacMillan took over Bloedel, Stuart, and Welch to form MacMillan-Bloedel, which later became widely held. Alcan Aluminum became widely held after a US court order required its parent, Alcoa, to divest. Hiram-Walker, Hydro-Electric, Fraser, Shawinigan Water & Power Co, and Great Lakes paper also passed from family control to become widely held.

But pyramidal groups and family-controlled firms were also on the rise. The Sobey and Steinberg families grew rich in food retailing. Simard, Demarais, and Basset appeared in Québec. Several older corporate empires also flourished in the immediate post war period. These include the Irving group in New Brunswick, the Billes family's Canadian Tire Corp., Roy Thompson's newspapers and radio stations, and the Bronfman's distilleries.

The most important creation of this period, however, was the Argus Group, a huge pyramid organized by EP Taylor, whose rapidly growing Canadian Breweries gave him a steady cash flow. He expanded into food with Canadian Food Products and into soft drinks with Orange Crush. He took over Massey-Harris and, working with Eric Phillips, the heir of an auto glass firm, took over Standard Chemicals. In 1945, he reorganized all his holdings, plus William Horsey's Dominion Stores and various other firms, into a classical pyramidal form. Argus Corporation, the apex firm, was 50% owned by Taylor, with Horsey, Phillips, MacMillan, J Wallace, EW Bickle and McCutchean (a lawyer) owning lesser stakes. Taylor believed that all industries evolved towards monopolies, and his strategy was to take advantage of this by building market power in carefully chosen industries where market power was most useful. This merger strategy, and the services of George Black as top professional manager, helped Argus companies grow substantially faster than the economy from the 1940s to the 1960s.

Argus expanded rapidly into Europe, buying the British tractor firm Ferguson and merging this into Massey-Harris. The group acquired control of a posy of family forestry firms, consolidating them into British Columbia Forrest Products Corp. Standard Chemicals completed a hostile takeover of Dominion Tar and Chemical (Domtar) and the pulp and paper companies St. Lawrence Corporation and Donnaconna Paper. Argus moved into broadcasting by taking control of Standard Broadcasting Corporation. British Columbia Forest Products took over a series of family-controlled firms. Taking a lesson from the Galts of the 19th century, Taylor got into the land business too, building the new city of Don Mills, Ontario, as a single project.

While the predominance of Argus signaled a move away from the old money controlled groups that had previously dominated Canadian business, the country was still very much a relationship economy. Argus, after all, was simply a pyramidal corporate group with newer wealth at the top, though some of the control blocks holding it together were now as small as twenty percent. Intercorporate dealings among Argus firms may have circumvented oligopolistic and crony-ridden markets. But those dealings were themselves between cronies. Old family pyramids, including the Killam Group (descendent of the old Beaverbrook group), the MacKenzies, and others, still held commanding positions in the economy. Canadian business was still in the hands of a small network connected by ethnicity, school ties, and family connections.

And C.D. Howe had a personal relationship with every member of that network. Corporate presidents routinely turned to Howe to recommend high performing bureaucrats for corporate management jobs. Years later, the top executives of the country's biggest firms owed their careers to Howe. Howe invested heavily in the stocks of such companies, and his policies often greatly affected their profits. For example, James Dunn, the CEO of Algoma Steel, refereed to Howe, whose policies saved the company and who (through a trust) was a major investor, as the "great white father in Ottawa".[50] The recipient of major government contracts, CD Howe & Co. was run by Howe's son and son-in-law. All the while, the socialists of the CCF, deeply confused by Howe's apparent oscillation between state intervention and favors to business, alternated between praise and condemnation.

In summary, the depression and wartime economies were highly regulated and officially cartelized. After the war, the government undertook a rapid, though incomplete

[50] Quoted by bliss (1986), p. 472.

liberalization against the combined opposition of the socialists and business interests seeking cartels. State owned enterprises were privatized. A high succession tax further encouraged heirs to sell out, contributing to a further growth in the number of widely held firms. A strong stock market allowed the capitalization of yet more widely held firms. Shareholder rights remained weak, ties between government and business elites remained strong, and CD Howe kept faith with Canada's mercantilist heritage.

6. The Apogee of the Widely Held Economy

The 1950s and 1960s in Canada were a near continual boom, though not as energetic as the Laurier years. The growth rate fell after 1957, but revived in 1961 and sustained high levels through the sixties. European and Japanese reconstruction and world economic growth fueled demand for metals and wood. The federal government withdrew its hand visibly, and the economy took off.

In 1956, with subsidized construction of the St. Lawrence Seaway nearing completion, C.D. Howe decided that Canada needed a transcontinental oil pipeline to move Alberta oil to Ontario and Québec. Howe unreservedly believed that Canada needed a procession of huge publicly subsidized projects to stimulate demand. The aging "dictator" pushed enabling legislation through parliament, invoking closure from the outset to end debate, and then wielded his war powers to organize its construction by American oil companies. Howe won the pipeline debate, but Mackenzie-King's Liberals lost the 1957 election because of it. C.D. Howe lost his own seat to a socialist schoolteacher.

The new Tory Prime Minister, John Diefenbaker, an upstart lawyer born in a shack in rural Saskatchewan, immediately found himself caught in leftover Liberal nation building schemes. The most important was a government subsidization of the A.V. Roe Company to produce a state-of-the-art jet fighter called the Avro Arrow.[51] Plagued with design problems and delays, the Arrow was a turkey. But Roe was using its cost-plus government financing to build a pyramid of engine and steel makes, railway car builders, and finally to acquire DOSCO, a pyramid of Atlantic steel and coal companies. The new prime minister pulled the plug just as the economy slowed in 1957 into the so-called Diefenbaker Recession.

The substitution of American for British capital, first visible in the 1920s, was now complete. Much of this was foreign direct investment (FDI) in new industries, such as the burgeoning oil and gas businesses of Alberta. However, a few high profile takeovers of established Canadian companies by US firms, such as Gulf's acquisition of British American Oil, made headlines. Although studies such as Safarian (1969) failed to find any negative economic consequences of American investment, this flow of FDI was far more controversial than that overseen by Laurier or King. Imperialists saw increasing ties to the US undermining the unity of the Empire. Socialists, with surprising success, gained media attention by condemning multinational corporations for any number on sins. Some top managers at widely held firms chimed in with unexpected support.

Diefenbaker, the prairie lawyer, was unimpressed by both. An outsider to the British corporate elite, he was disinclined to interfere in the market for corporate control. The farthest he went was to permit defensive tactics like the mutulaization of the largest

[51] The company also received subsidies from the US Defense Department to produce the Avrocar, a small flying saucer.

insurance companies, including Canada Life, Confederation, Equitable Life, Manufacturers, and Sun. This allowed their delisting, and so blocked takeovers (not just foreign ones) and ensconced their top mangers.

Howe had angered nationalists by turning construction of his pipeline over to Americans. Then Diefenbaker infuriated them by canceling the Arvro Arrow. That fury contributed to his loss of the 1962 election, which returned the Liberals to power under Lester Pearson. An old guard rebellion within the Tory Party forced Diefenbaker out as opposition leader a few years later. However, the Pearson Liberals remained non-interventionist for the most part. An early exception set this tone. In 1963, the Liberal Finance Minister, Walter Gordon, announced a 30% takeover tax on the sale of publicly traded companies to foreigners. Amid a storm of controversy, the tax was quickly withdrawn.

The Liberals quickly realized that political reality meant leaving the business sector alone. Yet the party's embrace of economic nationalism in its campaigns against the Diefenbaker Tories left it exposed to charges of hypocrisy. When the takeover of a small bank by US interests triggered another nationalist outburst, the Liberals responded in 1964 by legislating ownership caps. These forbade any single shareholder from holding more than a ten percent stake in a financial institution, and capped aggregate foreign ownership of such an institution at twenty-five percent. Both restrictions were enshrined in the 1967 revision to the Bank Act. Garvey and Giamarino (1998) conclude that these restrictions "were put in place to prevent American ownership of Canadian banks and there is little indication that consideration of economic costs played a significant role in the decision."

The other major economic initiative of the Pearson Liberals was a half step in the opposite direction. The 1965 Auto Pact rationalized the North American automobile industry by allowing free trade in automobiles and auto parts. This pact was a deliberate probe towards dismantling the National Policy tariff system. Its success in stimulating Canadian employment in this sector would become critical to future public support for liberalization.

The 1960s was, in many ways, a high water mark of laissez-faire in Canada. With C.D. Howe gone, nation building seemed almost out of style. However, province building was on the upswing. Newfoundland's government embarked on a costly and ultimately failed programs of government-led industrial diversification through subsidies to business. Provinces everywhere built hydroelectric projects, pipelines, and the like.

The noisiest flurry of intervention was in Québec. *La Révolution tranquille* of the early 1960s dislodged and then marginalized the Roman Catholic hierarchy, opening the public mind to increasingly radical ideas - first secular education and divorce, then socialism and separatism. The province established its own steel industry, built vast state-owned hydroelectric projects producing for export, and hugely subsidized aluminum smelting ventures. The Québec government's most daring venture was the Caisse de Dépôt et Placement du Québec. This state-owned enterprise was designed to purchase control blocks of publicly held corporations in order to establish a pyramidal group controlled by the provincial government. The motive behind the Caisse appears to have been that government controlled pyramidal groups of publicly traded companies were a much cheaper way to take charge of the economy than the outright nationalization of the same firms.

While inward foreign direct investment by Americans made headlines in Canada, outward foreign portfolio investment led to outrage south of the border. The United States had established the Securities and Exchange Commission and other regulatory systems to clean up its stock markets in the 1930s. C.D. Howe, no socialist, felt such regulation had no place in a capitalist country. Besides, stock market regulation was an area of provincial jurisdiction. Consequently, Canada's stock markets in the 1950s still resembled the NYSE in the 1920s. Disclosure was often minimal, insider trading was viewed as a perk, and anything short of outright fraud was fair game. Hearing of the vast riches in oil and minerals north of the 49th parallel, small U.S. investors responded in droves to telephone pitches from Canadian boiler rooms. The lucky widows and orphans across America found themselves the humiliated owners of worthless moose pasture. The unlucky ones lacked such title, for they had all bought the same patch.

Senators and congressmen in Washington, prodded by their outraged constituents, repeatedly demanded that Canada do something. The response was always that stock market regulation was not a federal matter in Canada. After a series of especially egregious swindles, the United States threatened an embargo on investment in Canada unless the Toronto market was cleaned up. Under heavy federal pressure, the Ontario government established the Ontario Securities Commission, mandated standardized disclosure, and moved to curtail insider trading in the mid 1960s.

There was a changing of the guard in top corporate offices. Isaac Walton Killam and Sir James Dunn both died in the mid 1950s. C.D. Howe decided that Algoma should become widely held, and sold Dunn's shares in several small blocks. Inheritance taxes took a huge bite out of both the Killam and Dunn estates. The $100 million boon was used to finance university expansions across the country and to establish the Canada Council. Their heirs sold control to pay the taxes and a new cadre of widely held firms came into being. These included Calgary Power, once part of the Killam group, the Algoma Central & Hudson Bay Railway, formerly controlled by the James Dunn, and many other firms. Free standing family firms, for example Burns & Co., also became widely held upon the death of their patriarchs.

This growth of the widely held sector occurred despite the takeovers by the Quebec government of the formerly widely held firms Shawinigan Water & Power Co, Saguenay Power Co. Ltd, Gatineau Power Co, Dominion Steel & Coal Corp. and other widely held firms.

Also working against the growth of the widely held sector were further foreign takeovers of the widely held Algoma Steel by Mannesmann and of Westcoast Transmission by Philips Petroleum

And the Argus pyramid retained its integrity. A new generation of professional managers led by Albert Thornborough, a Harvard MBA, took charge at Argus, as E.P. Taylor stepped aside. Argus was extraordinarily successful during this period, with Canadian breweries, Dominion Stores, and Massey-Ferguson all growing at sustained double-digit rates. By the 1960s, Massey Ferguson had become a major multinational business in its own right.

Fueled by its oil and gas wealth, Alberta was now a major center of economic activity. New widely held companies, like Alberta Gas Trunk Lines, Dome Petroleum, Hudson's Bay Oil and Gas, and others rose to national prominence. Vancouver also became a major center to rival Toronto and Montreal.

However, much remained unchanged too. In a landmark 1965 book entitled *The Vertical Mosaic*, John Porter argued that an Anglo-Scots elite still held virtually all the levers of economic and political power in what was now a distinctly multicultural country. The need to dislodge this elite would become, in many guises, the central political issue of the next quarter century.

7. Social Democracy, Nationalism and the Return to Family Values

Lester Pearson resigned as Prime Minister in 1968, and a playboy bachelor and part-time University de Montréal law professor, Pierre Eliot Trudeau, won the party leadership and took power. Trudeau saw himself as a scholar, interested in philosophy, social justice, and constitutional law. He was profoundly bored by economics, and his main training in the field was disinterestedly auditing a Harvard class taught by John Kenneth Galbraith. Since he inherited a vast fortune from his entrepreneurial father, Charles Trudeau, Pierre was platonically untainted by commerce.

Thus, Trudeau delegated economic issues to Marc Lalonde, his college chum and fellow Liberal. LaLonde was a committed nationalist, who aspired to break American dominance of the Canadian economy and establish countervailing links with Asia and Europe, especially France. This philosophy acquired deeper roots between 1972 and 1974 when the Liberals ran a minority government dependent on support from the socialist and now highly nationalist New Democratic Party.

While the left propounded nationalism, the right argued amongst themselves. Though economic openness had support in some quarters, especially among entrepreneurial businesses, many venerable Tories were at least as anti-American as the socialists. Canadian executives feared US takeovers as career disasters and old families were also upset by FDI. Publishing companies, like the Southam group and Maclean-Hunter, stepped up their already clamorous lobbying for foreign content rules to drive US competitors, like Time and the Wall Street Journal, out of Canada. Canadian filmmakers lobbied successfully for generous tax subsidies in the name of Canadian culture. The Canadian Radio and Television Commission mandated that Canadian-made programs constitute set fractions of broadcasting schedules, and licensed entry into broadcasting to create profit cushions to finance this programming. The regulation, cartelization, subsidization, and protection of "cultural industries" became national policy

Canadian content regulations did succeed in relocating substantial parts of program and film production to Canada as "cultural products" are considered Canadian if they are partially produced in Canada. Thus, many US network programs and films now count as "Canadian culture". Television content regulations also made Canada a world leader in cable television technology, as Canadians subscribed to cable in droves to receive foreign programming.

In 1971, the Liberals set up the Canada Development Corporation (CDC) to serve as a 'white knight" in takeovers by foreign firms. In 1973, they established the Foreign Investment Review Agency (FIRA) to vet foreign takeovers. FIRA took its work seriously, and began blocking foreign takeovers with considerable energy. The spike of takeover activity visible in Figure 4 in the early 1970s corresponds to multinationals exiting and selling their Canadian operations either to state organs or to private sector Canadian firms.

The acme of Trudeau era interventionism occurred when Energy Minister Marc Lalonde proclaimed a National Energy Policy (NEP) - exactly one week before Ronald Reagan won the US presidential election. The program provided a subsidy of up to 80% of drilling costs for operations in Federal Territories (the arctic), but only for 75% Canadian owned companies. Less than 50% Canadian ownership disqualified a company from operating in Federal Territories. This provision was designed to discriminate against foreign-controlled companies and to lessen Alberta's importance by finding and developing oil and gas in the arctic, where the federal government owned the mineral rights. But the most controversial element of the policy was the direct expropriation of twenty-five percent of the properties of all foreign controlled companies already active in Federal Territories. These properties could be transferred either to PetroCanada, the new federally owned oil company, or to other government organs. PetroCanada was also to buy out foreign-controlled oil companies with money from a new "Canadian Ownership Account" to be financed with a new federal tax. All current and future prices for energy were set by the Federal government, and announced at the time.

The government began acquiring an array of industrial firms, including De Havilland Aircraft, Westcoast Energy, and many others. Air Canada began acquiring private airlines, and other state-owned enterprises began expanding. Government ownership, control, and regulation were dominating the land almost as they had during the war.

Businesses either learned to navigate the new environment or floundered. Swatsky (1987) writes that business leaders "yearned for the not so distant time when they could phone C.D. Howe and resolve their problems on the spot." Prior to Howe, self-interested politicians routinely and overtly undertook joint ventures with business leaders, and these "business government partnerships" enriched both. Howe professionalized the civil service, and insulated it from political pressures other than his own. With the economy liberalized and Howe gone, business leaders continued to lunch with politicians, but the urgency of such meetings had faded as the government withdrew its hand from the economy. Now suddenly, the Trudeau government's hand was visible everywhere.

The new social democratic Canada that Trudeau was building had a large and complicated government, with interconnected lines of control that did justice to the most complicated corporate pyramids. Increasingly estranged from this new public sector, business leaders were repeatedly hit with new regulations, laws and decisions that seemed to come out of the blue.

Swatsky (1987) describes how some of the most brilliant young Canadians of the 1970s came to realize that "business was fundamentally incompetent in dealing with government" and that the increasing complexity of government created golden business opportunities. These young entrepreneurs built a new industry of consulting firms to monitor government, alert clients about impending problems, coach them about how to deal with different government organs, and to intervene on their clients' behalf.

The necessity of doing business with these new entrepreneurs became increasingly evident. Swatsky (1987, p.98) recounts how a multinational consortium invested $150 million dollars in an application to build a natural gas pipeline along the Mackenzie valley and then lost out to a hastily conceived, ill-prepared, and under-financed rival through "bad lobbying". The business of helping business deal with government grew in leaps and bounds, creating a new collection of millionaires.

Companies that learned to build their strategies around government policies prospered. Nova, a new widely held pyramidal grew rapidly undertook a spate of takeovers, cheered on by the supervisors of the NEP as it Canadianized business after business. While most oil and gas companies railed against the NEP, Nova learned to love it. Of course, the firm was also buttressed by its legislatively protected cost-plus natural gas transmission monopoly. Dome Petroleum also earned laurels from the NEP for its purchase of Conoco in a complicated takeover deal involving Mesa and Occidental Petroleum. BC Cellulose acquired control of Columbia Cellulose from its former US parent, Celanese Corp.

As governments expanded, income taxes rose to Scandinavian heights. However, Alberta had begun competing for wealthy family investments by promising to rebate its shares of the succession taxes collected by the federal government. This tax competition threw the entire succession tax system into disarray, and Trudeau decided to abolish it entirely in 1972. Inheritances were now tax-free income. In place of the old estate tax, the Liberals now decreed the realization of capital gains upon death. However, they created a huge loophole by allowing the transfer of assets to a family trust, which deferred capital gains taxes for two generations. The Bronfman heirs were allowed to escape capital gains taxes entirely by moving their wealth out of Canada when they sold Seagram's and bought Universal Studios.

Sam Bronfman had passed control of the central companies of his empire to his sons and grandsons, but his nephews had to be bought out. Sam's brother had been a partner early on and his nephews therefore had a legitimate claim. Thus, Edward and Peter Bronfman obtained a cash hoard to establish a second, separate "Edper" Bronfman pyramid that would eventually overtake the first. Indeed, the venture into motion pictures proved catastrophic, and Sam's direct descendents lost much of their wealth.

Figures 6 through 9 show an abrupt turning point for Canada at this time. The steady growth in the importance of widely held firms is reversed. A few large widely held firms, such as Hunter Douglas, failed during this period. But the main reason for this reversal seems to be a flurry of acquisitions of control blocks by new and old family controlled pyramidal groups.

In 1978, after the death of Bud McDougald, Conrad Black inherited a large block of Argus and acquired full control in a series of complicated deals. He then proceeded to "bust up" the pyramid. His motives for doing this are unclear, for diversification was not yet out of vogue. Newman (1998) notes that EP Taylor had fired Conrad's father, George Black, as head of Canadian Breweries. George invested successfully through the 1960s and put the money into Argus. Breaking up the largest corporate group in Canada required the sale of many control blocks, and this corresponded to the beginning of the merger wave of the 1980s, evident in Figure 4. Black sold some Argus companies to other wealthy families, publicly floated others, like Massey Ferguson, and retained yet others, including Dominion Stores, in his Hollinger group. He then used the cash he raised to buy control of newspapers across the country, notably the Southam group, and around the world.

The Edper pyramid grew through the 1970s and 1980s by acquiring control blocks in a broad portfolio of companies. In doing this, it assimilated several large widely held firms, including Brascan, Norcen Energy, and Noranda, accounting in part for Figures 6 through 9. Noranda, in turn, took a controlling interest in British Columbia Forest Products, once controlled by Argus, and later amalgamated it with Crown Forest Products Ltd. to form Fletcher Challenge Canada. Noranda also took a 48% control block in the widely held MacMillan Bloedel. Meanwhile Brascan took a control block in Great Lakes Power, which was also formerly widely held.

Many large widely held firms were taken into the other great pyramidal groups during the Trudeau years. The Power group took a controlling interest in Dominion Glass. The Reichmanns took over much of E.P. Taylor's Toronto real estate holdings *via* the Cadillac and Fairview companies, which the merged into Cadilac-Fairview. Their flagship Olympia and York acquired control of Abitibi Paper, Abitibi-Price, and Gulf Canada – the last after its parent spun off its Canadian operations.

And family firms took over widely held firms too. Molsen and Labatts, together, took control of the formerly widely held Canada Malting. The Gordon family assembled a control block in Canadian Corporation Management

Although most of the federal government's corporate acquisitions were of formerly foreign controlled firms, provincial governments – especially Quebec, were less fussy. The separatist Parti Québecois had a staunchly leftist ideology, and valued state ownership *per se* . Quebec's state controlled pyramidal group, the Caisse de Dépôt et Placement du Québec, consequently acquired control of Dominion Textile, the former Argus company Domtar Inc., and many other firms.

In summary, the Trudeau years saw a transformation of Canada from a liberal democracy into a social democracy. Simultaneously, inheritance taxes on large estates were greatly reduced or eliminated. During this period, the importance of widely held firms fell markedly and that of family controlled pyramidal groups rose. The reasons for this are not entirely clear.

8. The Tory Liberalization and the Liberal Retrenchment

The socialist experiments of the Trudeau era fractured the economy and the country. In 1985, Brian Mulroney's Tories routed the Liberals.

Mulroney rapidly redirected the country onto a free markets path. He abolished the National Energy policy and rechristened Foreign Investment Review Agency as Industry Canada, with a new mandate to attract foreign direct investment. He reduced the top marginal federal tax rate to twenty-nine percent, cut taxes on capital gains, and pruned regulations. In 1987, the Tories relaxed the rules forbidding banks from owning other companies. The major banks quickly acquired control of all the main trust companies, investment banks, and other financial services companies. And in 1989, Mulroney signed a free trade agreement with the United States, finally burying MacDonald's National Policy.

The Tories also embarked on a privatization program, floating Air Canada, the Canadian National Railway, PetroCanada, Polysar Chemical and Energy, Westcoast Energy, and other state-owned enterprises. Though the processes were often lengthy and multistage, all these enterprises eventually became free standing widely held firms.

But the expansion of the great family groups *via* the greatest merger wave in Canadian history swamped these privatizations. The Reichmanns took control of Hiram Walker Resources. Control of Consumer's Gas was acquired by Interprovincial Pipe

Lines, which was then acquired by the Reichmann group. The Edper group took control of Falconbridge and Fraser, and expanded its existing businesses with debt financing.

However, in the early 1990s, both the Reichman and Edper Bronfmann groups encountered financial difficulties. Edper divested John Labatt & Co. as a widely held firm, though it was later taken over by a Belgian conglomerate.

After the Tories enacted an unpopular consumption tax, the Liberals under Prime Minister Jean Chretien took power in 1993. Chretien was a Liberal of the Trudeau era, but the party was now full of pro-business elements too. Pragmatically, the Liberals continued the then still incomplete privatizations of Canadian National and PetroCanada. However, more nationalistic than the Mulroney Tories, they reinvigorated the rules and regulations protecting "cultural industries".

Newman (1998) makes much of a new elite taking charge of Canadian business in the 1990s, writing of the death of the "Jurassic Canadian Establishment." He correctly notes (p. 5) that the old elite

> "practiced insider trading with exuberance, feathered each others' nests with considerable grace, maintained their workers in patronizing insecurity, and, with the instincts of an unregulated oligarchy, gleefully forced competitors out of their misery" and "operated in what was a virtually risk free environment .. nurtured by government subsidies having formed a cozy marriage with the political establishment."

Several grand old families, such as the Eatons and Woodwards did indeed reap the fruits of long years of mismanagement in the 1990s, and largely disappeared from the headlines. Newman may be right that the old establishment lost influence because of its British ideal of "lovable dimness" (p. 13). But much remains the same.

Figures 6 through 9 attest to the continued dominance of family controlled pyramidal groups. The dominant figures of the corporate sector remain largely unchanged. The lineal descendents of Sam Bronfman were ruined by their foray into Hollywood, but the Edper group remains the largest in the country. The Reichmann group, after stumbling badly in British investments, recovered and still ranks second. The Thomson group acquired control of the venerable Hudson's Bay Company.

The Power group, a pyramid formed in the 1920s, has grown rapidly. Power is now controlled by Paul Desmarais. Although Demarais is a genuine entrepreneur, in that his first venture was to buy a bankrupt one-line bus route in Sudbury, his Power group is similar to the other pyramids. That Desmarais' son Andre is married to Jean Chretien's daughter, France, is not associated with any improprieties. Nor is the fact that the Finance Minister, Paul Martin, ran Canada Steamship Lines, a Power Company.

New corporate groups have formed. For example, Jimmy Pattison turned a used car lot into the largest group of British Columbia. Peter Munk, a penniless Hungarian Jewish refugee, built a huge corporate empire. Tainted with insider trading allegations, Munk moved to the South Pacific and built a large hotel chain. His success in plowing his hotel profits into Barrick restored his social standing, but eyes were once again averted when he posted bail for his longtime friend, the Arab arms dealer Adnan Kashoggi. It is perhaps a tribute to Canada's maturity that such slips no longer trump genuine success in business. Semour Schulich, another new baron of Canadian business, noted famously "reputation is character minus what you can get away with."

But some major new corporate groups often bear disturbing resemblance to older ones in their dependence on government connections – real or perceived. Izzy Asper built a “cultural industries” group, Canwest Global Communications, from his base in Winnipeg. Gerry Schwartz, Asper’s one-time protégé, used ONEX to launch a series of LBOs of major firms in the 1990s, and his wife, Heather Reisman, took control of Cott Bottlers and then Chapters/Indigo. Newman notes in passing that “it can’t hurt that Gerry Schwartz happened to be Canada’s chief Liberal bagman for most of a decade.” Issadore Sharp’s flagship company, Four Seasons Hotels, has a second class of “variable vote shares” with voting rights that change continuously so that Sharp always has two-thirds control.

9. Conclusions

Family controlled pyramidal business groups are theorized to facilitate business transactions in economies with poor institutions and widespread corruption. Khanna and Palepu (1997, 2000, 2001) argue that such groups have a survival advantage in India and other developing countries because group member firms can deal with each other without fear of being cheated. In contrast, intercorporate transactions between independent firms are costly because of a thoroughgoing absence of trust. They further argue that, in such an economy, a reputation for fair dealing can have large economies of scale. They note that the Tata family has such a reputation, and that member firms in its pyramidal group are consequently preferred as business partners over other family pyramid firms and independents.

The Canadian economy a century ago was much like a modern third world economy. We have shown that colonial Canada was deeply corrupt. The relationship between economic and political power in New France and in British North America compares unfavorably to most modern sub-Saharan African states. Politicians routinely used their offices for personal enrichment, directed state funds into their own companies, altered laws and regulations to suit themselves, and erected trade barriers to protect their monopolies. This situation improved only very slowly after Confederation. Prime Ministers continued soliciting bribes and kickbacks, running businesses out of their offices, and using their political influence for personal gain. The civil service remained highly politicized and the courts did not intervene.

Thus, it is not surprising that Canadian business a century ago looked much like Indian business now. Family controlled group companies could avoid relying on shady markets and corrupt institutions by dealing with each other. The controlling family could move goods, capital, and labor from firm to firm as needed. Oligopolistic and opaque product, capital, and labor markets could be circumvented. When such a family did acquire a reputation for honesty, it could leverage that reputation into an advantage in numerous lines of business.

Khanna and Palepu (1997, 2000, 2001) show that business group firms outperform independent firms in the developing countries they study, and argue that diversified groups might be an optimal corporate strategy in developing countries. However, Khanna and Palepu (2002b) are careful about drawing normative conclusions. Good government policy might involve fostering such groups, however social welfare might be increased more by improving institutions to the point where groups no longer have an advantage over independents.

Indeed, Khanna and Palepu (2002a) find that the advantages enjoyed by pyramidal groups in Chile fade as that country's institutions improve. La Porta *et al.*

(1999) show that family controlled pyramidal groups are by far the dominant corporate organizational form in most countries.[52] La Porta *et al.* (1997, 1998, 2000) link poor investor protection laws and government corruption to reluctance by small investors to hold corporate equity. Burkart *et al.* (2002) argue that the poor institutions of most countries limit founding families' options to sell out, and thus lock in old family corporate control. Thus, the steady replacement of family pyramidal groups by free standing widely held firms through the first half of the twentieth century can be explained by an exogenous steady improvement in Canada's institutions – its political system, courts, and general standards of business behavior. However, this improvement was not monotonic. For instance the economy became highly cartelized in the 1930s and subject to wartime central planning in the 1940s. These shorter term deteriorations in institutions do not correspond to short term rises in the importance of family groups. Also, overvalued stocks in the 1920s may have induced insiders to cash out.

Controlling families' decisions about whether to cash out or not depend on their ability to extract private benefits of control from their pyramidal corporate groups. Dyck and Zingales (2001) and Nenova (2003) present empirical evidence that these private benefits are economically large, and that they are larger when institutions are weaker.

Such private benefits can take various forms. One is simple utility from "being in control" of a corporate empire. Good institutions dethrone unqualified managers, and so limit such control. Another form of private benefit derives from self-dealing and other transactions that are not permitted in economies with stronger institutions. A third form

[52] See also Agnblad *et al.* (2001), Becht and Böhmer (2001), Becht *et al.* (2001), Bianchi *et al.* (2001), Bloch and Kremp (2001), Crespí-Cladera *et al.* (2001), De Jong *et al.* (2001), Gulgler (2001), and others.

of private benefits involves using corporate assets to influence the development of institutions. Again, this is easier in countries with weaker institutions.

Top executives often retain control despite being liabilities to the companies they run. Johnson *et al.* (1985) show that stock prices often rise upon CEOs sudden deaths. Morck *et al.* (1988) show that CEOs with large blocks of their firm's stock, old CEOs, and heir CEOs are associated with depressed share values. Morck *et al.* (2000), Palia and Ravid (2001), and Pérez-González (2001) show that heir-control firms lag in a variety of performance metrics. Although a variety of explanations are conceivable, the simplest is that CEOs gain utility from control, and unqualified CEOs therefore seek to entrench themselves.[53] This utility might be entirely psychological, or it might derive from private pecuniary benefits of control.

Pyramidal corporate groups are associated with pecuniary private benefits from self-dealing in many countries. Bebchuk *et al.* (2000), Morck *et al.* (2000), and others describe how non-arm's-length transactions between related companies can transfer wealth from public investors to controlling shareholders. Johnson *et al.* (2000) provide detailed examples of this in European corporate groups, and dub such transactions "tunneling". Faccio and Lang (2000) and Faccio *et al.* (2000) present econometric evidence of tunneling in European pyramidal groups. Claessens *et al.* (2000, 2002) and Bae *et al.* (2002) present similar evidence regarding East Asian groups. Attig *et al.* (2002) show that traders have relative difficulty valuing Canadian pyramidal group stocks, possibly consistent with such problems. Bertrand *et al.* (2002) find evidence of tunneling in India.

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[53] See Barclay and Holderness (1989) and Barclay et al. (1993). Stulz (1988), Shleifer and Vishny (1989), and others derive models of managerial entrenchment.

Benefits of control may also derive from political influence, as argued by Morck *et al.* (2000), Morck and Yeung (2003, 2003), and Faccio (2003). Fisman (2000), Johnson and Mitton (2002), and many others demonstrate a strong linkage between political influence and benefits of control. Faccio (2003) argues that such influence is more valuable in countries with weaker institutions.

Whether private benefits are purely psychological or pecuniary, their extractors should regard their disappearance when institutions improve as a serious loss. This reasoning leads several scholars to propose that the elites of countries with poor institutions prefer things that way. Rajan and Zingales (2001) argue that entrenched elites in many countries acquiesced to leftist policies that eroded their financial systems for precisely this reason. Weakened economic institutions acted as barriers to entry, entrenching their control, and made the extraction of private benefits easier by limiting competition. These arguments parallel those of Olsen (1963), who argues that rapid growth dislodges entrenched elites, and that these elites consequently lobby to preserve institutions that end up retarding growth.

Is the reversion to large family controlled pyramidal groups in Canada's corporate sector indicative of such misdirected institutional development? To answer affirmatively, we must identify the institutional changes underlying this reversion. Rajan and Zingales (2001) argue that a deliberate dismantling of the financial system was historically important in many countries. There is little evidence of this in Canada. The regulation of stock markets is thought to have improved markedly in the 1960s, just before the resurgence of large pyramidal groups. La Porta *et al.* (1997, 1998, 2000) argue that the nature of a country's legal system is the paramount factor. We are unaware of any evidence that Canada's legal system became more corrupt or politicized after the middle of the century, though Trudeau's constitutional reforms may have done this. Olsen (1963), though he makes no mention of pyramidal groups, argues that an onerous regulatory burden and extensive state intervention in the economy can act as barriers to entry.

Certainly, Canada's government became much more interventionist again in the 1970s under the Trudeau Liberals. The Foreign Investment Review Agency, the National Energy Policy, and the Canadian Radio and Television Commission are but a few examples of what mid-century Canadians would have regarded as radical interventionism, inappropriate except perhaps in wartime. If private benefits of control in Canada relate to business-government relations, "bigger" government, all else equal, would magnify the value of those benefits.

Such a magnification would almost certainly be socially undesirable, all else equal. It is well established that when political entrepreneurship, or rent-seeking, is more remunerative, resources are shifted to that end and away from investments in real economic growth. Consequently, widespread rent seeking is regarded as a serious impediment to growth. See Baumol (1990), Kruger (1974), Murphy and Shleifer (1991, 1993), and Olson (1963).

But the retention of control by unqualified heirs contributes to poor corporate governance and widespread self-dealing undermines public confidence in financial markets. These problems, associated with other private benefits of control, might also impede growth.

At present, however, our hypothesis remains speculative. More prosaic explanations must be excluded. Canada altered its tax regime in the 1970s to facilitate the tax-free inheritance of large estates. Discrete increments in the importance of widely held firms in the first half of the century correspond to sales of corporations by heirs to pay succession taxes, or by patriarchs to avoid them. Discrete decreases in the importance of widely held firms in the second half of the century correspond to purchases of control blocks in widely held corporations by heirs. The tax reforms explain how heirs came by the money to expand their groups, but not why they chose to do so. They could, for example, have diversified abroad instead. Why did they instead build larger Canadian pyramids?

Further research is clearly needed to confirm or falsify the hypothesis that private benefits of control rose in the second half of the century. We are currently attempting to devise tests of this hypothesis. Meanwhile, we enthusiastically invite alternative explanations of our empirical finding.

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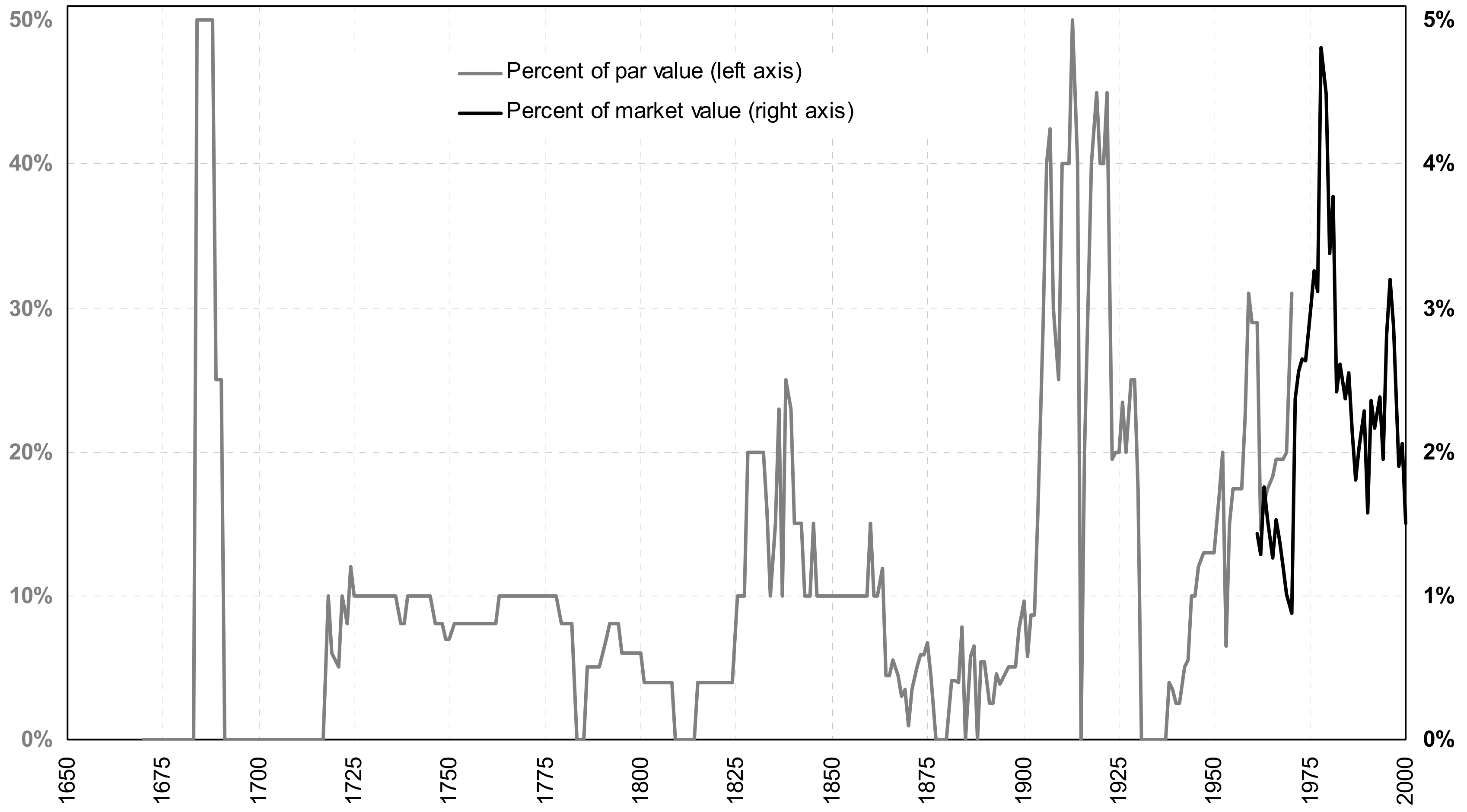
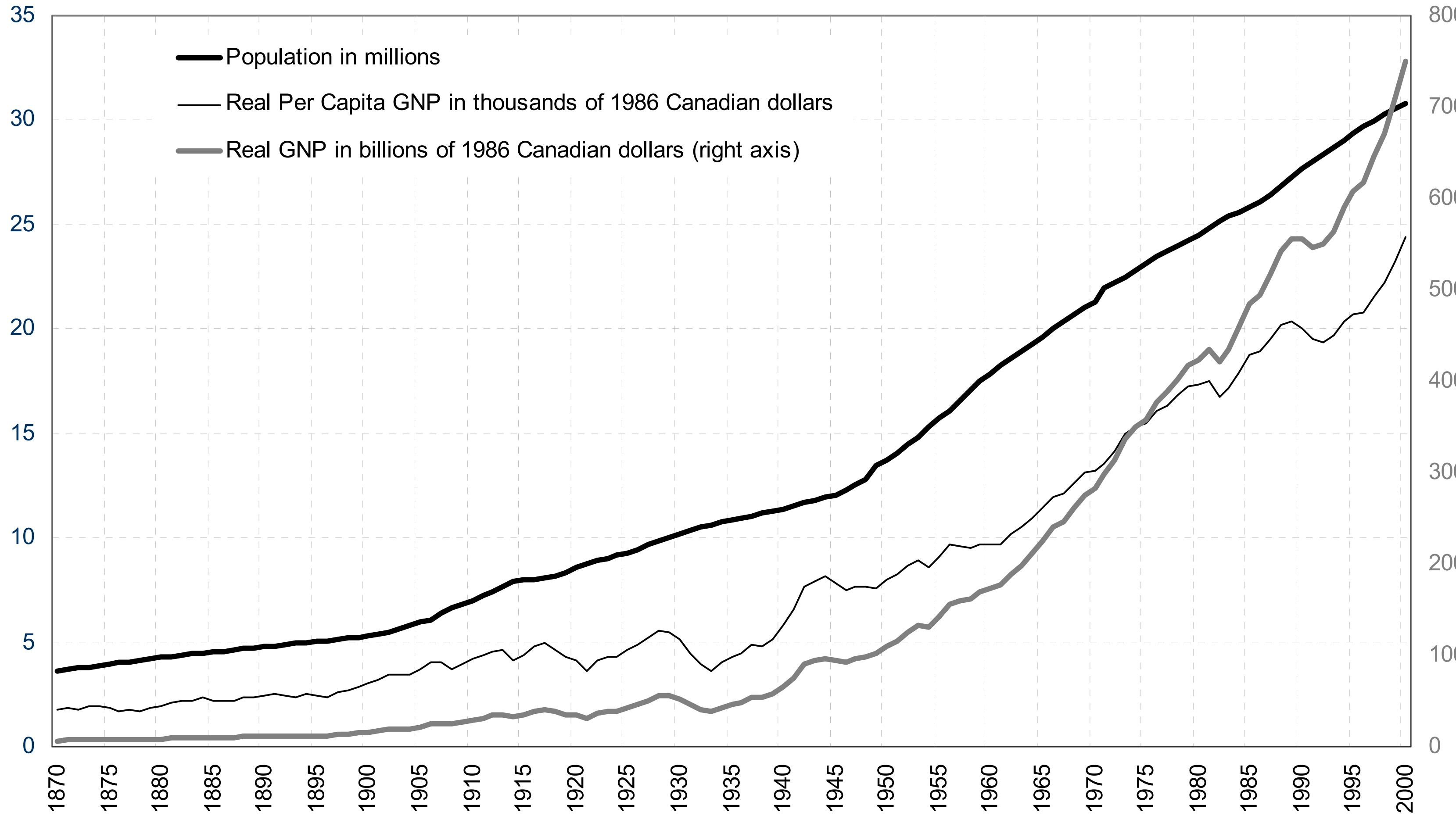
Figure 1. Hudson's Bay Company Annual Dividend, 1670 to 2000
Expressed as percent of par value until 1970 and as a percent of equity market value from 1961 to 2000.



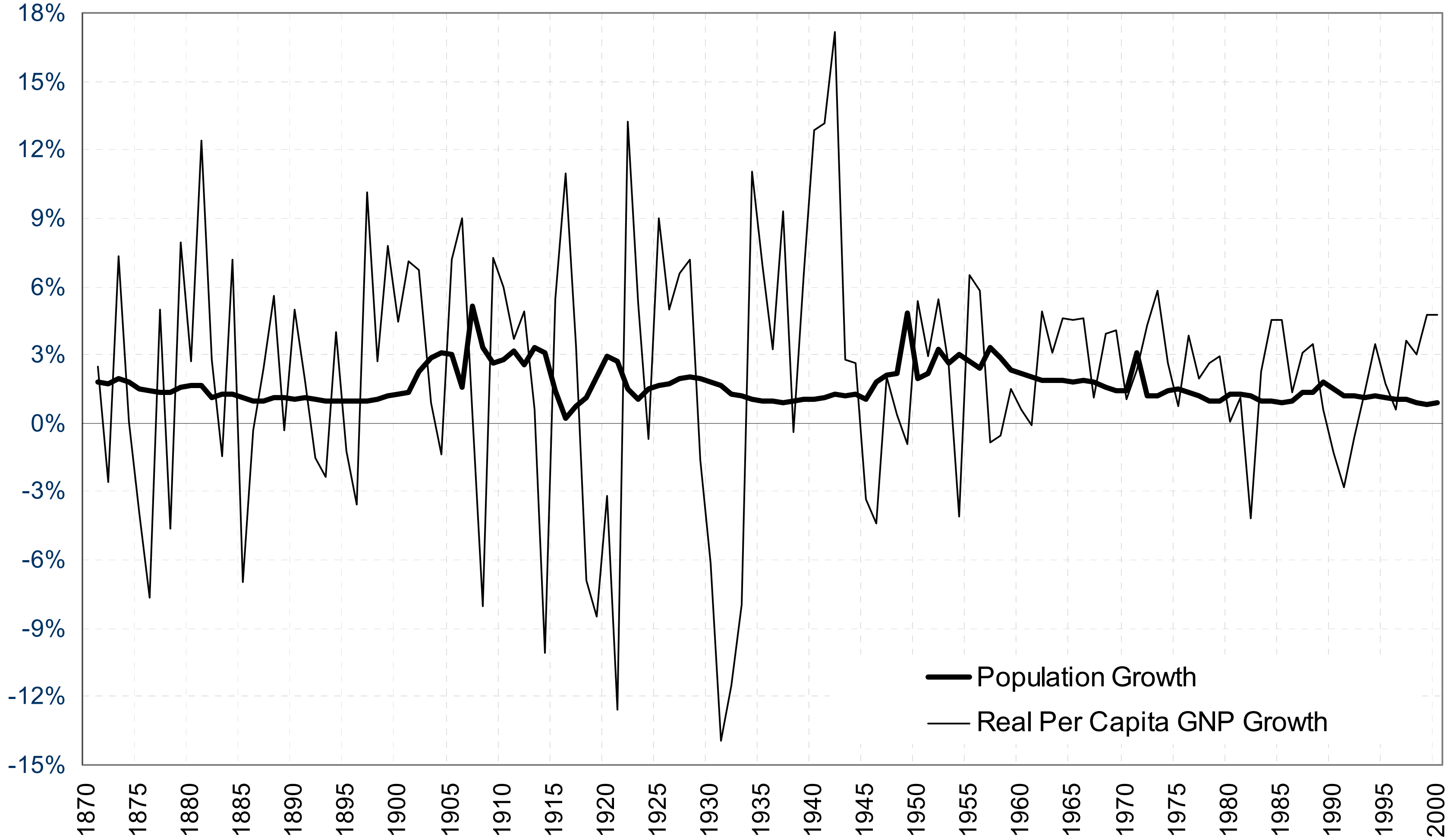
Source: Newman (1998) and *Financial Post Historical Report* for Hudson's Bay Company.

Figure 2. Overall Economy Growth, 1870 to 2000
Population in millions and *per capita* Gross National Product (GNP) in 1986 Canadian dollars are measured on the left axis. Total GNP in billions of 1986 Canadian dollars is measured on the right axis.



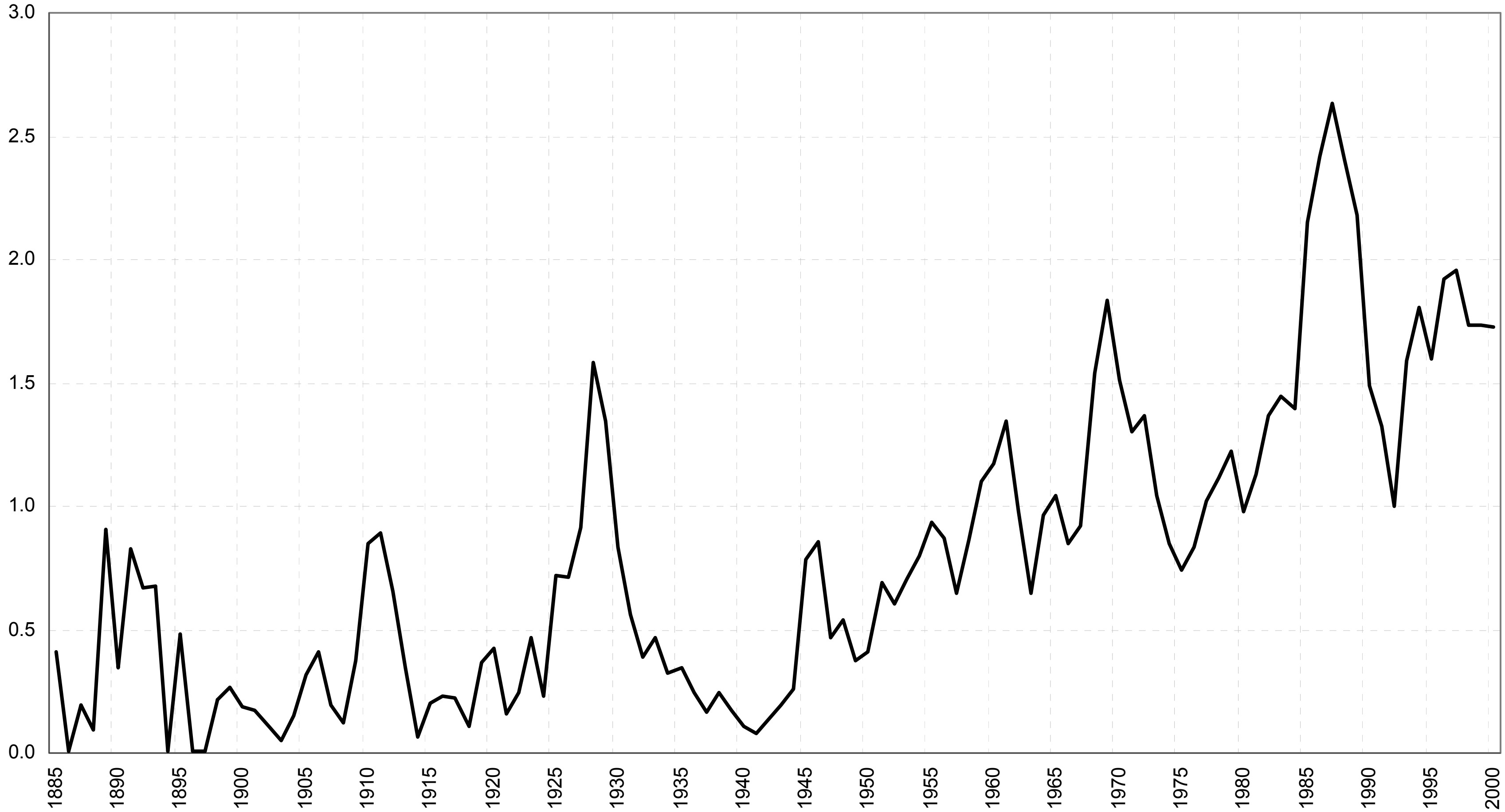
Source: Data up to 1926 are from Urquhart (1993). Later data are from Statistics Canada: Historical Statistics of Canada.

Figure 3. Economic Growth, 1870 to 2000
Annual growth rates in population and per capita GNP in 1986 Canadian dollars.



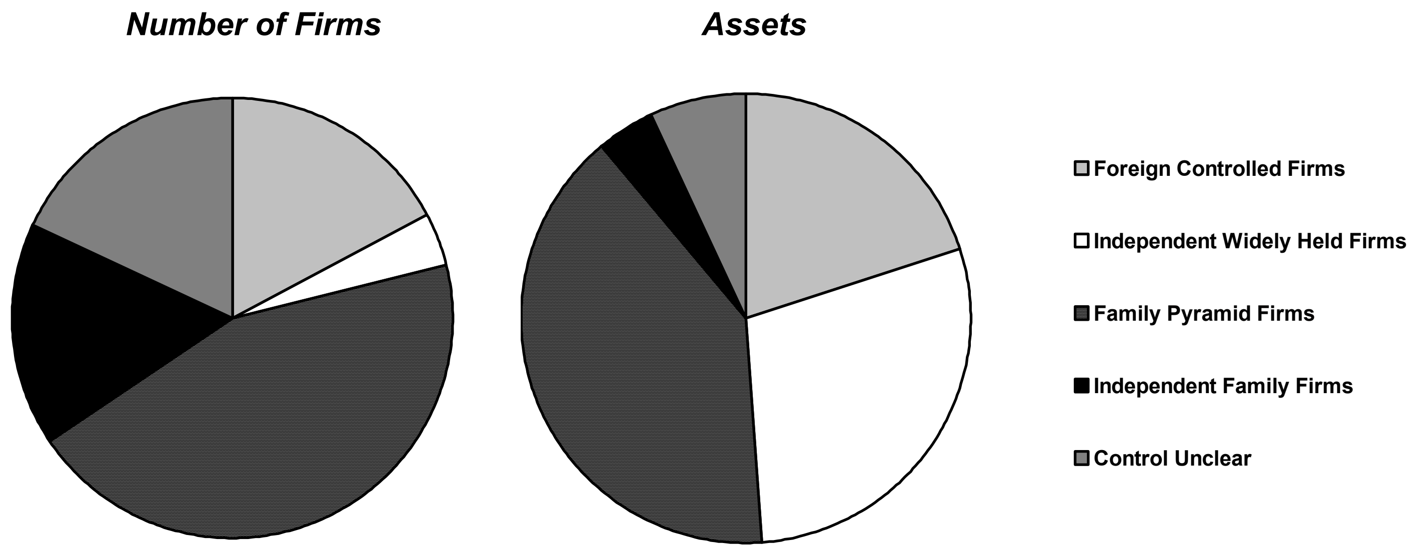
Source: Data up to 1926 are from Urquhart (1993). Later data are from Statistics Canada: Historical Statistics of Canada.

Figure 4. Merger and Acquisition Activity, 1885 to 2000
Number of mergers and acquisitions per million 1986 Canadian dollars of GNP.



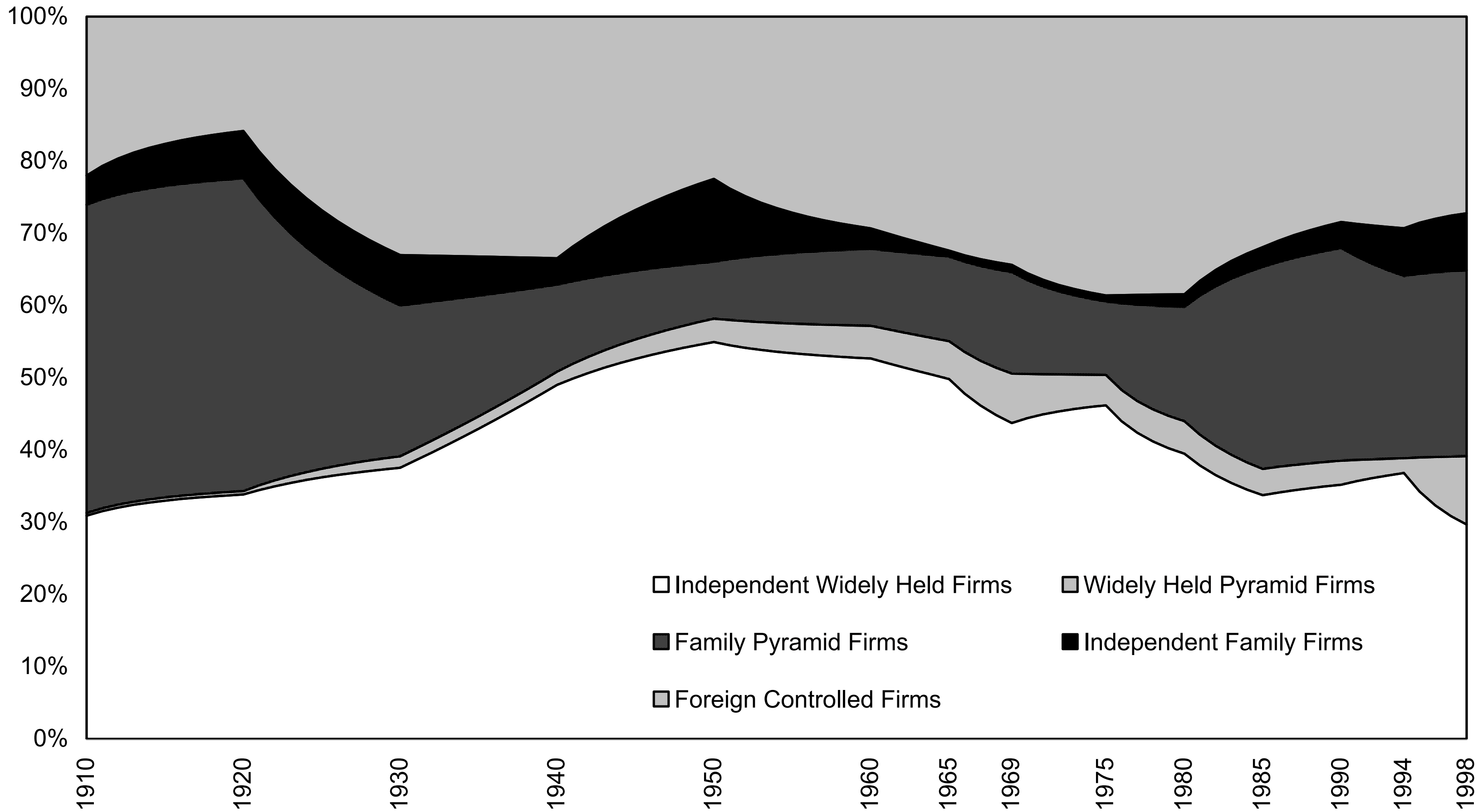
Date for 1885-1918 are from Marchildon (1990), data for 1900-1963 are from Maule (1966), data for 1970-1986 are from Globerman (1977), and data for 1985-2000 are from the *Directory of M&A in Canada*. Because discrepancies exist across different sources, we apply linear transformations to each overlapping period and move different series up or down to generate a single time series.

Figure 5
Ownership Structure of the Larges 100 Canadian Firms in 1910



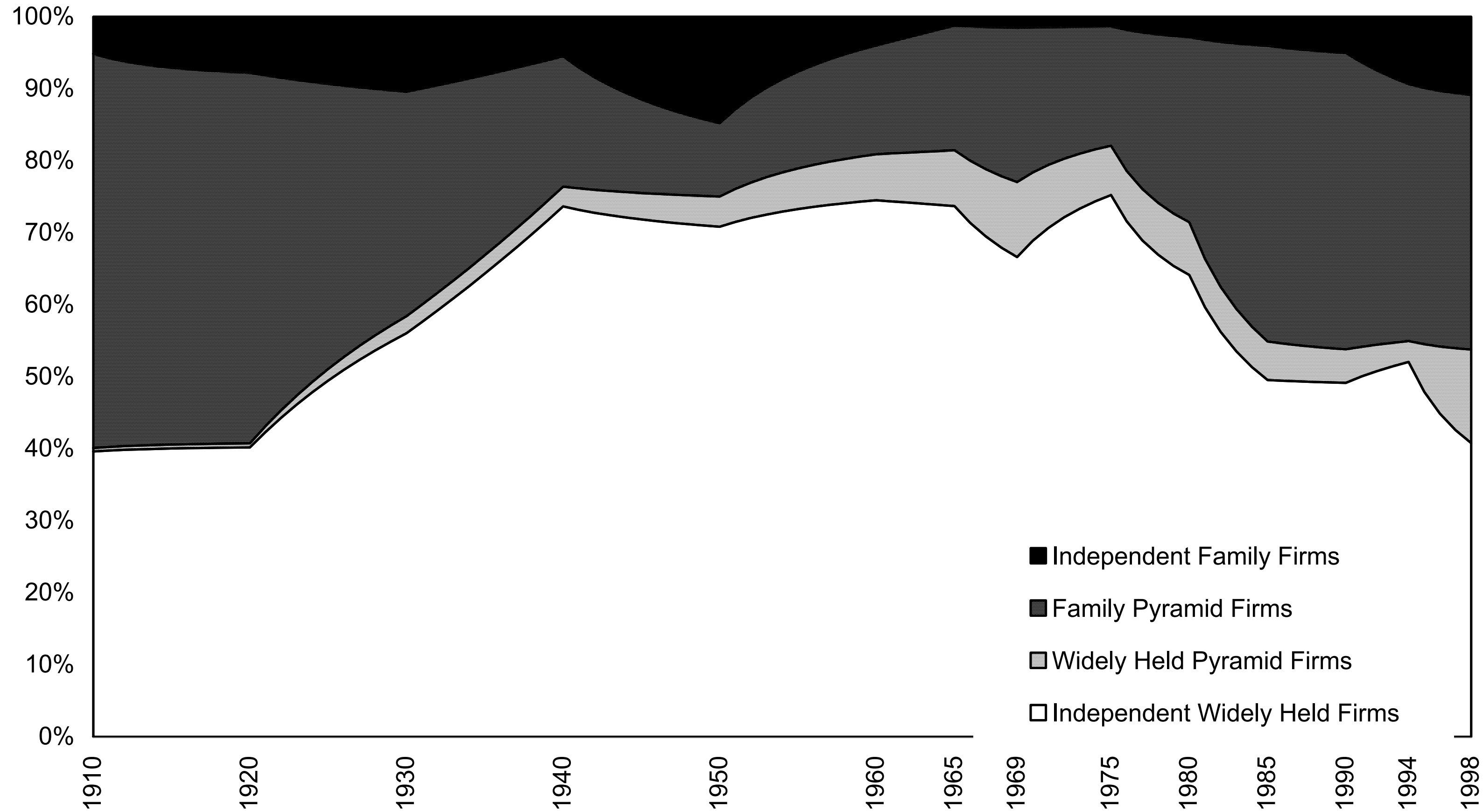
Source: Compiled from the Canadian Annual Financial Review and many history books, as described in the text.

Figure 6
Ownership Structure of the 100 Largest Firms in Canada, 1910 to 1998
Importance of firms with various ownership structures expressed as a fraction of corporate assets, at book value.



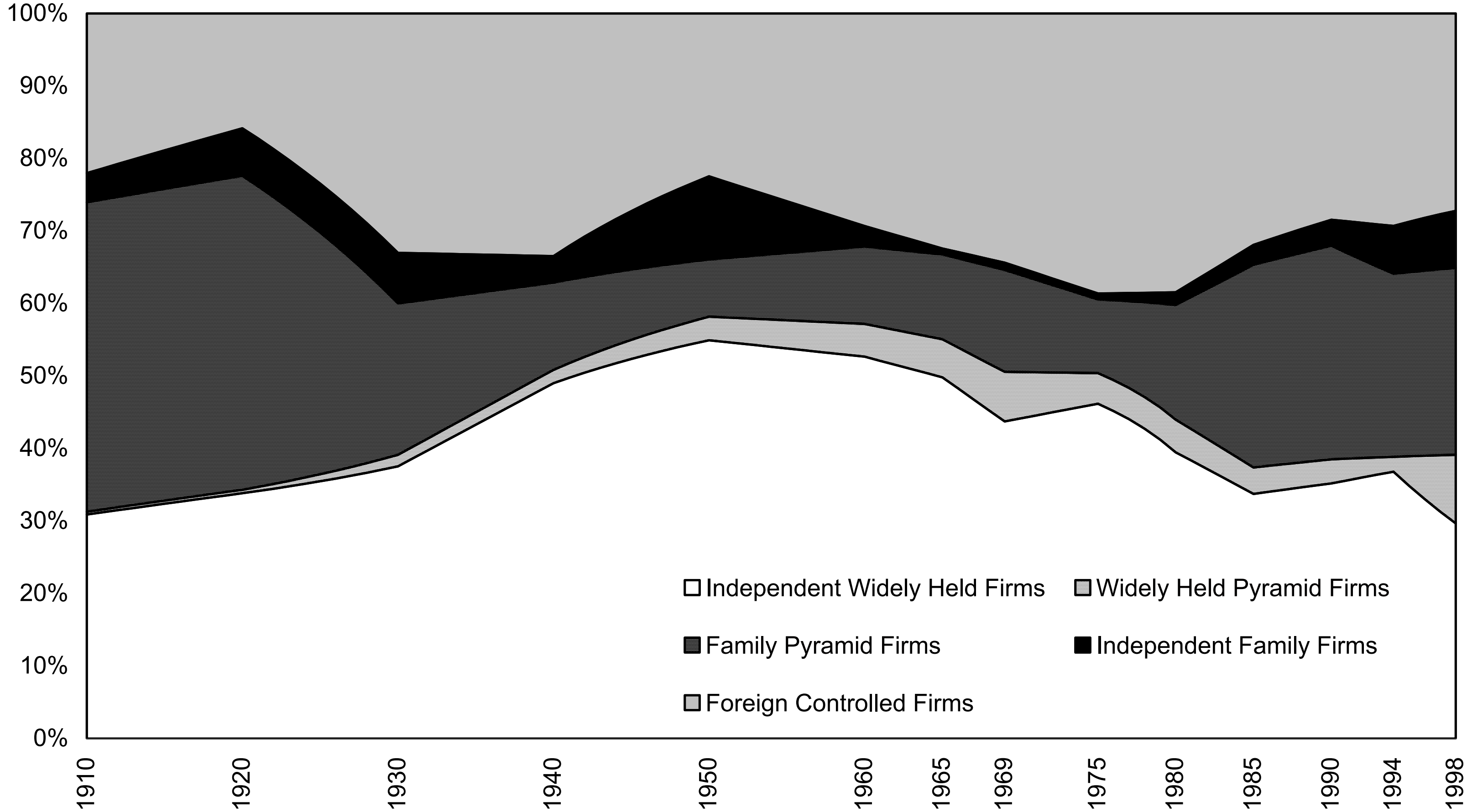
Sources: Past issues of *Statistics Canada's Directory of Inter-Corporate Ownership*, the *Financial Post, Canadian Annual Financial Review* and *Financial Post Corporate Securities*; supplemented by Baskerville and Taylor (1994), Bliss (1986), Myers (1914), Naylor (1975), and individual corporate histories.

Figure 6
Ownership Structure of Domestically Controlled Firms Among the 100 Largest Firms, 1910 to 1998
Importance of firms with various ownership structures expressed as a fraction of corporate assets, at book value.



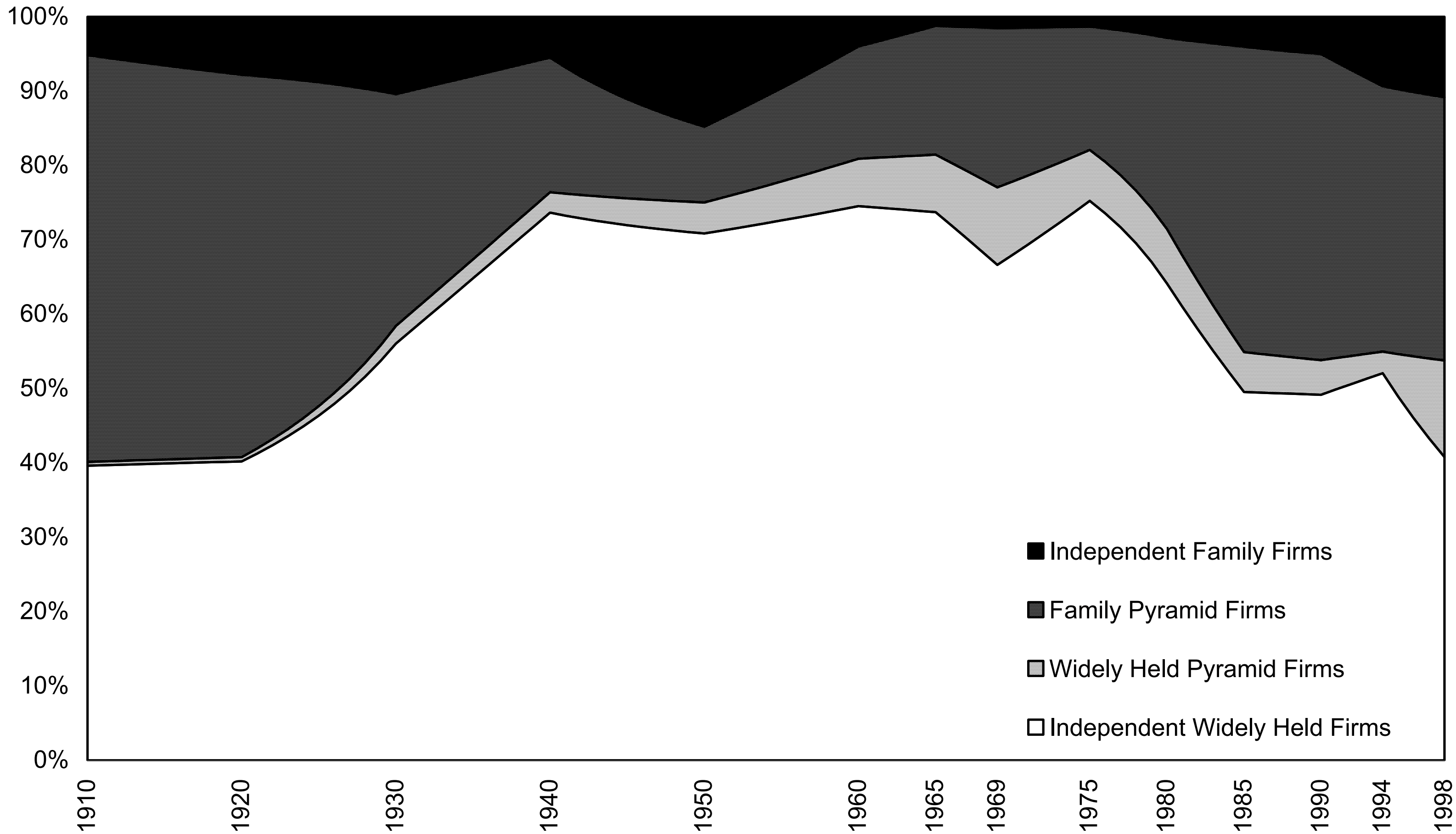
Sources: Past issues of *Statistics Canada's Directory of Inter-Corporate Ownership*, the *Financial Post, Canadian Annual Financial Review* and *Financial Post Corporate Securities*; supplemented by Baskerville and Taylor (1994), Bliss (1986), Myers (1914), Naylor (1975), and individual corporate histories.

Figure 7.
Ownership Structure of the 100 Largest Firms in Canada, 1910 to 1998
Fraction of firms with various ownership structures.



Sources: Past issues of *Statistics Canada's Directory of Inter-Corporate Ownership*, the *Financial Post, Canadian Annual Financial Review* and *Financial Post Corporate Securities*; supplemented by Baskerville and Taylor (1994), Bliss (1986), Myers (1914), Naylor (1975), and individual corporate histories.

Figure 8
Ownership Structure of Domestically Controlled Firms Among the 100 Largest Firms, 1910 to 1998
Fraction of firms with various ownership structures.



Sources: Past issues of *Statistics Canada's Directory of Inter-Corporate Ownership*, the *Financial Post, Canadian Annual Financial Review* and *Financial Post Corporate Securities*; supplemented by Baskerville and Taylor (1994), Bliss (1986), Myers (1914), Naylor (1975), and individual corporate histories.