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Nexen deal: The only standard is reciprocity

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The CNOOC takeover bid for Nexen demonstrates once again that while a given government policy tool may have a bright, sunny face, it often simultaneously casts a dark, problematic shadow.

The Canadian policy tool that will be used to determine whether this takeover will be permitted is “net benefit.” This means that after all the capital-market formalities are taken care of – which should be pretty straightforward due to the 61-per-cent premium being offered – the government will declare whether the takeover produces net benefit for Canada.

Thus far, the net benefit tool has been all happiness and light for Ottawa. The handy thing is that the government can make up any conclusion it wants under the as-you-like-it construct of net benefit. The prima facie evidence for making stuff up is the BHP Billiton bid for PotashCorp, where the government determined that the bid didn’t provide net benefit to Canada and disallowed the takeover. I suspect the government felt pretty chuffed about the power of the net benefit tool. In the face of a legitimate bid, it was able to declare on the basis of nothing particularly useful or intelligent that there wasn’t net benefit to Canada and, in doing so, ensured the goodwill of the Saskatchewan electorate for the Conservative Party.

But the dark side of this tool is that it is totally obvious to the rest of the world that Canada’s government can make up absolutely any story it feels necessary to disallow a takeover. Other countries understand the picture really clearly. Net benefit as a standard is intellectually and procedurally bankrupt, and any result of its use is simply a reflection of the government doing whatever it wants vis-à-vis the acquirer. It is similar to when France declared yogurt to be an industry essential to France’s national security. The world got the picture: France would stoop to whatever intellectual depth required to prevent anyone from taking a run at Danone.

In the BHP/Potash bid, Canada had a manageable adversary. Australia is a smaller country, one step below the G7. It’s never going to be a critical trading partner for Canada because it looks a lot like us: few people and lots of natural resources. It doesn’t really matter if we annoy Australia. So we declared that the BHP acquisition didn’t produce net benefit despite not having a single compelling

argument supporting that.

In contrast, China matters – a whole lot. So what has to be understood is that Beijing knows, absolutely, that if Ottawa invokes net benefit to disallow the takeover, it is just making up an argument to thwart China. Beijing would take that as a major affront, and we don't really need another one of those.

This is why, as I have argued previously, the standard on foreign direct investment should be the standard of all other trade matters, not the vapid standard of net benefit. That standard is reciprocity – i.e., if we allow X in our country, will you allow the same sort of X in yours? The principle has guided all trade advances in the past century. We certainly wouldn't have a free-trade pact with the United States and Mexico had we used net benefit as our principle.

That is why we should ask China to sign a foreign direct investment treaty specifying that if a Canadian company attempts to take over a Chinese company of similar size – for the sake of argument, \$10-billion to \$20-billion in acquisition value – China will automatically approve it. If the answer is no, we should turn down the Nexen acquisition on the principle of the absence of reciprocity. If the answer is yes, we should approve it and not engage in another net benefit charade.

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