These 4 TSX Stocks Are Failing Shareholders

Description

Which pensioners do you think will fare better? The former employees of Sears Canada or its parent, **Sears Holdings Corp.** (NASDAQ:SHLD)?

If you answered the Canadian employees because we're so much more benevolent a country, you'd be wrong.

A recent article about this very subject in Benefits Canada got me thinking about pension deficits, which are defined as the difference between a pension plan's assets and obligations — something that's far more common than anyone would like to admit.

The U.S. vs. Canada

Sears Canada had a $267 million pension deficit when it applied for protection from its creditors last June, while Sears in the U.S. has a US$1.5 billion pension deficit but is still open for business.

I can remember writing about the Sears Canada debacle last October and getting an email from a Sears employee in the U.S. who worked in its automotive business wondering about his pension.

I'd suggested he contact the Sears alumni person responsible for helping retired employees maneuver through all of the various issues related to a pension in distress. I hope he did.

However, after reading the Benefits Canada article, it appears he had a better chance of seeing some or all of his pension than his Canadian colleagues, and that's a darn shame.

"There's no guarantee, of course, that Sears's U.S. operations will survive. But even if they don't, the government-insured pension scheme there is far more generous than in Canada," wrote Julie Melnitzer April 30. "To begin with, Ontario is the only province in Canada that provides any form of guarantee to its resident pensioners. Pensioners elsewhere in the country have no such protection."

In Ontario, pensioners are guaranteed a maximum of $1,500 per month, according to Melnitzer, while in the U.S. the cap is more than four times the amount when converted to Canadian dollars at US$5,420.

Capital allocation includes pension top-ups

The Canadian Centre for Policy Alternatives (CCPA) published a report last November that examined pension deficits and shareholder payments of S&P/TSX 60 companies — 60 of Canada's largest public companies.

It found that of the 39 companies that had a non-executive defined-benefit pension plan in 2016, only 12 were fully funded (defined as assets covering at least 95% of obligations), another 16 had a shortfall between 80% and 95%, and the remaining 11 were below 80% funded.

Like corporate debt, pension obligations are a liability, or at least they are supposed to be; pension shortfalls, the CCPA argues, should be a higher priority for capital allocation than shareholder payments such as dividends and share repurchases.

I couldn't agree more.

It was so sad to hear that comedian Mike Myers's brother Peter was out of a job after 36 years at Sears Canada with no severance and a reduced pension.

So, the CCPA further argues that the laws should change, so public companies are prohibited from making shareholder payments if there is a pension shortfall. Many experts have suggested that pensions get treated equally to senior creditors.

It's hard to fathom that Canada hasn't legislated this into the securities laws.

The worst offenders

I went through the list of 39 companies looking for three things:

1. A pension deficit.

2. Dividend and share repurchases in 2016.

3. Share repurchases that exceeded the pension deficit.

I came up with four companies.

Company	Pension Deficit	Share Repurchase	Dividends
Magna International Inc. (TSX:MG)(NYSE:MGA)	-$294M	$913M	$385M

National Bank of Canada (TSX:NA)	-$67M	$176M	$600M
Saputo Inc. (TSX:SAP)	-$31M	$92M	$210M
Thomson Reuters Corp. (TSX:TRI)(NYSE:TRI)	-$655M	$1.67B	$982M

If you own any of these stocks, you might want to look more closely at where they sit today. The numbers above are from 2016, but I highly doubt they've changed all that much.

These four stocks are failing shareholders for the simple reason that this shouldn't be a problem in the first place, because each of these companies has significant free cash flow with which to top up the pension shortfalls.

By failing to do so, the CEOs are thumbing their noses at the very people who generate the free cash flow in the first place.

Capital allocation is critical to a company's success. Sometimes, the right thing to do isn't always what's best for shareholders.

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