A View From Here - October 2018

The best way to predict the future is to create it - Peter Drucker

Underneath It All

In the face of political and economic fear revolving around worldwide and North American trade wars, the U.S. market continued to increase throughout September on the narrow band of technology companies we know all too well. In Canada, we have seen a renewed surge in the cannabis space with the kind of volatility reserved for the not-so-faint of heart. This may have cast the illusion that all is well in the markets, but that doesn't seem to be what's going on underneath the major indices making the headlines. In fact, the Canadian benchmark TSX Index is now down on the year and is lower than it was just before the financial crisis 10 years ago. While U.S. markets are making all-time highs, it seems that memories of that catastrophic event have started to slip. In Canada, it seems like a lot of frustrated investors are succumbing to the excitement of the looming October 17th legalization of recreational cannabis.

Outside of the headline stocks, many companies that we track are suffering significant share price losses. This redeemed our view that one of the best actions we have taken over the past year has been to limit new investment positions and concentrate on the ones we currently own. Thankfully, the commitment to our current portfolio has collectively provided our accounts with returns well into the double digits over the past year. Having said that, September saw these values consolidate a few percentage points. Still, our 12-month and year to date numbers are remain enviable.

September saw the release of quarterly results in some of our investments that confirm our continued commitment to their value proposition. We just need the market to see what we are seeing in these valuations. All good things in time I suppose (or hope!). This is especially true in instances where some of our retail and media-based investments seem to be going nowhere, bringing a sense of anxiety to some clients. However, I remain firm in my belief in their value proposition.

But I would be remiss if I did not admit that it feels strange out there in 'market-land' right now. It is almost as if we are on the verge of a breakout...or breakdown. As such, I suspect that the best course of action is to have cash on hand and carry a big stick. Experience has taught us that there is no sense in trying to anticipate a weak market and that the best course of action is to buy our way out of weakness, if it indeed occurs. I sense that there is a belief among most investors that the current trend will continue and that markets will remain buoyant, but we have also learned that surprise, not consensus is what really moves markets.

Speaking of Weak Markets & Recovery

September is the 10th anniversary of the start of the financial crisis, which ushered in one of the most difficult periods in stock market history. The major indices collapsed almost 50% while investors witnessed their net worth cut in half between September 2008 and March 2009. Interestingly, while many waited for signs of the proverbial 'other shoe to drop', (which never happened) a very powerful rally began to take place in late March 2009 and we saw recovery in prices that was equally as stunning. At that time, our most passionate holding was a company called Softchoice which saw its share price fall throughout 2018 from a high of over $24/share to under $1. This was based on fear that they would not be able to refinance maturing debt. Interestingly, when they were able to do so by year's end, the shares still suffered losses. Yet by the spring of 2009, the shares recovered to almost $8 and, despite strong earnings and cash-flow growth, remained there for three years. We had used that weakness and share-price stagnation in the years which followed to augment investment positions and ultimately sold it when it was taken over at $20. This was indicative of many of our holdings and we used the weakness during that period to augment existing holdings. My experience is that the best time to purchase companies is when they are not popular and represents the best risk-reward opportunities for the patient investor

What is often not spoken of about that period and is worth repeating is how stunning the recovery was in the aftermath of the economic tsunami which had occurred. In terms of today that recovery, particularly in the United States, has remained unabated and now counts as one of and, by some measures, the longest bull market in the history of the stock market.

Does any of this mean that markets won't remain strong? No one knows. Records are always broken, but I find that markets tend to surprise investors with a problem that is not currently in the headlines of concern. These days they include geo-political fear, trade wars, China or corporate debt. It's almost impossible to know what will bring about the next crisis, but suffice it to say, we'd like to be able to buy our way out of it, because in my experience, that recovery is where we will build wealth and anticipating it is almost impossible. The other thing we know is that these things do not last that long. Think about it, the last crisis was only 7 months and it was a doozy. More money is lost reacting to weakness in share prices, and for better investors, a lot of wealth was reclaimed and built upon in its aftermath.

With that said, for the first time in the long time that I have been publishing this note, I am cautious of the current environment, but remain excited about our existing holdings.

Thanks for taking a look, and as always,

All Good Things

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