RESEARCH CAPITAL CORPORATION

HENNIC WEALTH MANAGEMENT

YOUR FUTURE IS WORTH MORE

A View From Here - September 2023

"Couldn't be happy in the city tonight, I can't see the stars for the neon lights. Sidewalk's dirty and the river is worse, underground trains all run in reverse. Nobody here can dance like me. Everybody's clapping on the one and the three, am I, the last of my kind?" – **Jason Isbell**

Last of Our Kind?

Unlike most investment managers, we are part of a minority who research and create holistic portfolios of actual share/bond ownership as opposed to a structured produced created in a boardroom.

It's viewed from the perspective of a large fast-food chain where everything from the product to marketing is carefully curated by different departments.

This isn't necessarily a bad thing as long as there is an acceptable bottom line, but I have seen that this is not the case. Returns are most often anemic but the illusion of stability and safety of a large brand hide the underperformance while the fee structure is created to offers the illusion of goodwill.

The best investment managers have their name on the door, taking on the painstaking work of managing portfolios. It's not hard, but it isn't easy either. One has to have the passion of their craft and mix it with a good dose of benevolence and common sense. As most of you know by now, my team and I own the same

investments as our clients and our long-term performance that favors deep value dives into the companies we own has over time, produced favourable returns.

However, most advisors take the approach to build their practice through scaling as much of their assets into their employers' 'recommended' portfolios of too many well-known names that complete the slick portrait.

We independent thinkers call these portfolio's 'Happy Meals'. It's becoming clearer that the advisors are (not so) subtly coerced into this scenario for their clients using the brand to promote security and long-term stability while using props such as portfolio reviews and financial planning as a gateway to client assets, in an effort to sell products and services that they don't need. Again, this is all good as long as it provides satisfactory bottom line, and the side effect is little return at all. Are we the last of our kind?

To date, 2023 has been an excellent year for our portfolios culminating with July's parabolic performance thanks to a few positions that have increased exponentially more than outshining our most challenged holdings.

Our investments often take a long time to reach fruition, but when they do, it occurs over a short period of time. Take our holding of Hammond Power. When we started buying this investment in 2019, the share price was well below $10/share with a view that it could be worth $25 - $30. It worked a lot better, and we began to sell some in the $40s and recently more in the $50s as many lights have been shining on this area of all things electric.

Like our investment a few years back in Stelco, when steel prices increased

exponentially in 2020, we happened to be in the right investment at the right time, but when we took that position, the company was cheap on valuation, management held a large stake and there was a large net cash and real estate holdings. To us, it just made sense, as it did when we sold off the final shares as steel prices consolidated from its highs.

In the case of Hammond, few of us may have noticed that we've held this name for over four years, and it took three of them before the share price began to increase. Conventional wisdom might have suggested that we sell when we made a good profit (can't go broke taking a profit sort of thing), but we are value investors and what comes with that inoculation is constant revaluation of an investment, and that work suggested that we remain invested.

However, there is another view one must take from a portfolio management perspective, which is to protect the account from having too much exposure, so we sell off small pieces, as if we are doing the reverse of what we do when we accumulate a position.

This was a hard learned lesson over many years. In the old days of creating portfolios, we would spend most of the allocated funds to create their portfolio, then a market sell-off would manifest and positions would get even more attractive, but we had used up most of our capital. The reality spoke loudest in late 2007 and early 2008, before the financial crisis revealed itself.

From that point on I vowed that constructing a portfolio is going to have to take 18-24 months and developed a view that all new funds into equities would be done so methodically over a period of time to take advantage of pricing from a

manic/depressive called the stock market.

As with all of my investment heroes, I had finally understood a reality that no matter what the outcome of an investment, they always seem to disappoint on the downside, even if the business is performing as expected (Tucows). Further, if we've done our work and the thesis remains intact and we have faith that an investment continues to deliver on a corporate level, the share price will ultimately take care of itself.

Thankfully our long-term performance is part of what gives us enough confidence to pursue this process because it has worked well for us. As I write this note, we have been adding to existing positions that are going through the same situation. We believe that underflowed and misunderstood names offering a unique value proposition will eventually be found and become the overnight success they aren't right now…we just don't know when.

That is why we must have a long-term view and the optimism that in a portfolio of disparate holdings, at least at some point, each can perform in their own right. Having some of our names scale the heights they've seen recently is a testament to this view.

Portfolio Management As it is Practiced

Portfolio Management, as it is generally practiced, preaches long-term, fee based diversified portfolios of investments that look safe but ultimately don't perform as advertised. That's because they are so diversified that when one area is doing well, another is not, and the offset leads to meandering results. I have not seen this

approach work, but it is preached and sounds like a logical theory.

Yogi Berra once said; “In theory there is no difference between theory and practice - in practice, there is.” I believe, with relative confidence that this practice does not work, or at least we have not seen it work in the over 30 years that we’ve been doing this job. Ultimately, it relies on the efficient market thesis, that all things are valued appropriately.

I believe they aren’t.

The market is manic and no AI solution is going to change human behavior. The best results come from well researched investments held in a relatively concentrated portfolios.

The world’s best investors who we hold in the highest regard practice the same view and ironically, even though most advisors quote these heroes often, the portfolios created by their companies that pay them annual fees, underperform, not always matching the index that it is being benchmarked against.

Basically, as I see it - it’s a racket designed to create recurring fees and scale as much as you can. The real retirement plan isn’t the one created for the client but rather the advisors who hopes to sell that recurring stream at some point in the future.

When considering an advisor, two important questions come to mind: Proof of performance, particularly for accounts that resemble the one they are attempting to

provide you with and secondly, does the advisor eat their own cooking? The answer will surprise you, particularly the second one. I'm happy to show my RRSP to any potential client, its value speaks for itself.

Every once in a while, we are surprised to see an account fall for the financial planning/portfolio management approach that comes across with charts and graphs and shining colors, but short on the details of the real thing - long term performance. That's because they are disappointing - it's the dark secret of the advisory world.

We recently have moved over a few accounts that held a long shopping list of mutual funds and well-known stocks and bonds where their long-term performance was under 4% annually. In these cases, one could have simply purchased GICs, had no volatility, slept at night, paid less fees and still performed better.

Maybe that's why these Questrade ads freaked out so many advisors. The advisors who lost those accounts to us warned their outgoing clients that our process and independence creates an environment where their capital might be at risk of total loss, despite having no knowledge of what we have achieved. Perhaps, they should have re-thought exactly why they lost the accounts.

Independence allows investment managers the right to make the best decisions for their clients, not what the institution they work for wants because it is the most profitable approach for the firm.

Recently a bank manager told me that the posted GIC rates from institutions are

negotiable. That means, if you call our banker and ask them for their best rate, they have discretion to offer a higher one, only when the client is willing to take it elsewhere. Shouldn't they always be offering the best rate?   The most important thing ultimately is the return but for over 90% of financial managers do not create this, so they hide behind the brand names of their firms and speak to the safety of the investments and a dream of the long-term despite not having lived up to the promise over, well, the long term.

We are blessed, I hope it continues to be the case and thank you for having the confidence in our unique offering that has been able to produce returns that few are able to achieve.

Thanks for taking a look, and as always,

All Good Things

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