The McValue Portfolio Newsletter

November 2010

I'm Out.

This will be my final edition of the McValue Newsletter and a little more personal than the previous editions for reasons that I set out below.

As most of you know, I recently resigned from my investment banking position that I began nine years ago with Cormark. The smile on my face tells me that taking some time off after 15 years on Bay Street seems to agree with me. I have finally decided that instead of reading Annual Reports and Proxy Statements while on vacation with my family, its time to do this as my full time job. I am therefore proud to announce that I have formed my own investment management company – GreensKeeper Asset Management Inc. Writing this newsletter has helped me to recognize what I really love to do. Thank you for taking the time to read it and provide me with such wonderful feedback. Your encouragement has helped me to make the move.

One of my investment heroes recently remarked:

> *"…the basic idea is that if you want to succeed in life in a capitalistic world, go where the competition is low… A very flawed person like me can do pretty well if he seeks out competition that is inferior."*
>
> *Charlie Munger, Outstanding Investor Digest (Aug. 9, 2010)*

I think that the investment management industry has largely lost its way. Don't get me wrong - there are some very talented managers with decent results and plenty of integrity. Unfortunately they are too few and far between. The industry is rife with closet indexing, excessive and often hidden fees and managers that constantly underperform. It has largely become a sales and marketing game. Given my passion for investor education and through the formation of my own Fund, my goal is to start to remedy some of these industry shortcomings. Remember my lesson from McValue #1 – unless a money manager can beat the benchmark over a period of time (after fees) there is no reason for them to exist.

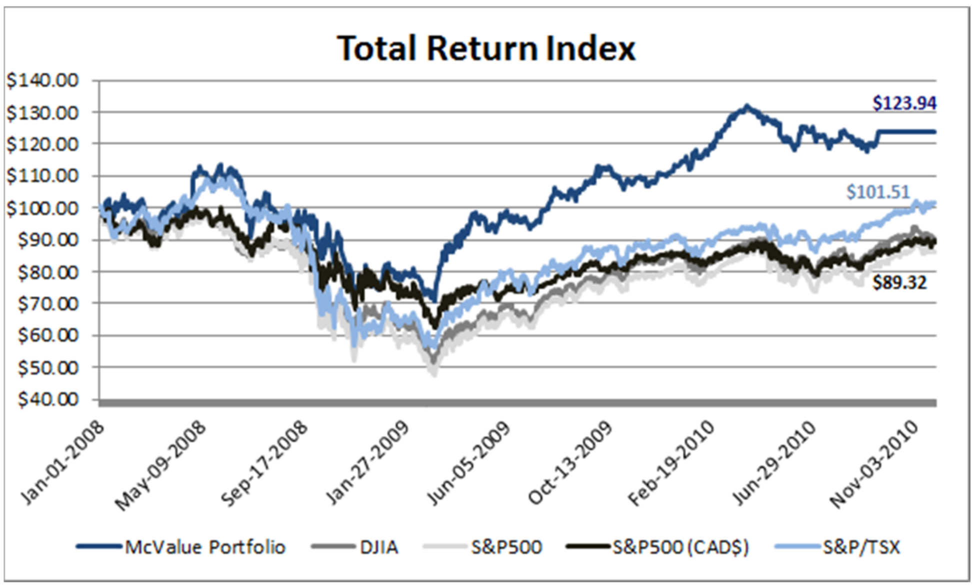
I plan to launch the GreensKeeper Value Fund early in the new year subject to receipt of all necessary regulatory approvals. The Fund will be open to "accredited investors" and others that invest a minimum of $150,000 and I will keep you posted in the coming months. I will most likely be the largest single investor in the Fund from day-one and will have the bulk of my net worth in the Fund alongside my clients. As you know, I believe in eating my own cooking. Let's just say that I will be motivated to focus on the task at hand.

The McValue Portfolio

In light of the foregoing I have liquidated my entire investment portfolio and only hold cash and short maturity Canadian Treasury Bills at the moment. Don't confuse this move as a market call (despite my slightly negative view of current equity valuation levels). This portfolio shift was necessary to allow me to deposit the proceeds in my Fund. Unfortunately my timing was poor. As soon as I went to cash (~Sept. 1) the equity markets have rallied significantly. Overall my move to cash has cost me around 10% in performance over the past three months. There is a lesson here – you can't time the markets or predict their direction in the short term despite the many market pundits that try to suggest otherwise.

My portfolio's performance has lagged the market indices during the third quarter and into the fourth. The timing of my move to cash was the main culprit but I have to admit I have been a little distracted lately. The reality is that one quarter's performance is largely irrelevant (or one year for that matter). What's important is whether you can outperform over several years, cumulatively. Given my current portfolio makeup my performance for 2010 is now set in stone at 11.11%. My relative performance for the year will be determined by how the markets finish the year. I'm keeping my fingers crossed for a major correction before I go shopping for stocks in the new year.

Overall the portfolio is up 23.94% since January 1, 2008 which compares quite favourably with the major indices: S&P500 (-14.07%); S&P500 in $CAD (-10.68%) and S&P/TSX 1.51%. And this was accomplished with lower volatility (less risk according to the academics). If I'm totally honest with myself I have to say that I delivered great relative performance but mediocre absolute performance. I'm looking forward to seeing what I can deliver when I do this full time.



	Performance Results				
	McValue Portfolio[1][2]	S&P 500 [2]	McValue Outperformance	S&P/TSX[2]	McValue Outperformance
2008	-19.55%	-37.00%	17.45%	-33.47%	13.93%
2009	38.66%	26.46%	12.19%	35.05%	3.60%
2010 YTD[4]	11.11%	8.29%	2.82%	12.98%	-1.88%
Total Return 2008 - 2010[4]	23.94%	-14.07%	38.01%	1.51%	22.43%
Annual Compounded Return	7.64%	-5.06%	12.70%	0.52%	7.12%
Standard Deviation[3]	19.34%	21.59%		20.11%	

[1] Based on invested capital (ignoring cash)
[2] With dividends included.
[3] Annualized and based on monthly returns since Jan 1, 2008.
[4] To Nov. 30, 2010.

Protect the Downside

In the presentation that I gave to my daughter's class and distributed with McValue #4 I illustrated the power of compounding. Let's go through a simple exercise that builds on that lesson. I find that the result often surprises people.

Suppose that you start with an investment portfolio of $100,000. You are a savvy investor or have a good financial advisor who puts your money into some successful funds and have gains in each of the first three years that you invest this money. Assume that your portfolio earns 20% in Year 1, 25% in Year 2 and 10% in Year 3 (all returns are after fees). Very good numbers based on historical returns from equities. Year 4 is tougher as it brings a major market correction (think 2008) and your portfolio gives back 40%. How do you think that you've done over that four year period? Most people are surprised to learn that they are actually *down* from where they started ($99,000 to be exact) despite peaking at $165,000 at the end of Year 3. The lesson here is that compounding is a very powerful force (the eighth wonder of the world according to Einstein) however it also works in reverse when you incur losses.

I have a mouse pad on my desk that I picked up in Omaha a few years back with Buffett's cardinal rules of investing inscribed on it. I keep it in such a conspicuous place as a constant reminder of the double-edged sword of compounding:

Rule #1 – Never lose money.

Rule #2 – Never forget Rule #1.

When equity markets are rallying and everyone around you seems to be making money your instincts will tempt you to try and join the party. It is in our nature – a remnant from our primitive instincts formed when we fled predators on the open plains. There is often safety in numbers and in following the crowd. Unfortunately it is exactly the wrong thing to do in the investment business. When everyone loves equities they are priced dear but when panic ensues they are effectively being given away. However, it is painful to sit on the sidelines when everyone around you is having fun. Chuck Prince (former CEO of CitiGroup) gave an interview to the Financial Times of London in July 2007 and said:

> *"When the music stops, in terms of liquidity, things will be complicated. But as long as the music is playing, you've got to get up and dance. We're still dancing."*

CitiGroup's equity valuation peaked at $277 billion in 2006. It is now worth approximately $160 billion *less* than that. I'm not sure that CitiGroup made enough money dancing to make up for the destruction of wealth that has ensued. I think that the following quote from the Oracle himself sums it up best:

> *"I will tell you how to become rich. Close the doors. Be fearful when others are greedy. Be greedy when others are fearful."*
>
> *Warren Buffett*

Current Holdings
Cash
Canadian Treasury Bills

***Selected* Former Holdings**
Astral Media
Berkshire Hathaway
Equitable Group
Grey Horse Corporation
Hammond Power
Home Capital
MacDonald Dettwiler
Nike
Precision Drilling
Royal Bank
Sprott Inc.
Starbucks
TD Bank
TMX Group
Urbana Corp.

The New Newsletter

In my time off I have managed to take in a value conference in NYC and to witness first-hand the Hawaii Ironman World Championships. Very inspiring. The picture below gives you a hint at my new website that will launch some time in the new year. I couldn't resist the prospect of some free advertising on NBC. I will send out an announcement once my website (and business) is up and running.

I plan to run the GreensKeeper Value Fund the same way that I have managed my own portfolio over the past three years. I hope that this newsletter has given you a good understanding of my investment philosophy and how I approach stock picking. The only difference is that I will devote much more time to the task.

I will continue to write a quarterly newsletter but under a new name better suited to my new company – The Scorecard. I admit that "McValue" was a little cheesy and I would prefer to avoid any unnecessary litigation with the McDonald's Corporation. I will make sure that you remain on the distribution list for future issues. In the interim I would be happy to discuss stocks, the market in general or my new Fund with any of you if you are interested in doing so.

Wish me luck. Michael.