

Giving Thanks

October 12, 2020

The Value Fund was up +4.1% in Q3 and is down -3.2% year-to-date through September 30. The strengthening of the Canadian dollar (the Value Fund's reporting currency) lowered our Q3 returns by approximately -2.0%. A more detailed explanation of our view on currency hedging (and our bias for not doing so) can be found [here](#). Year-to-date the TSX Index is -3.1% and the S&P500(CAD) +8.3%.

Markets continued their rebound from the steep Q1 selloff despite the negative headlines: a COVID-19 half-speed economy, an ugly US election, etc. Given the gloomy environment I hope that the cartoon below brings a little cheer to your day. We are all looking forward to putting 2020 in the rear-view mirror and getting back to normal.

Despite life's daily challenges, I suspect that if we take the time to reflect, we can all find things in our own lives to be thankful for. As the Stoic emperor Marcus Aurelius correctly noted, our life is what our thoughts make it. In honour of Canadian Thanksgiving, I decided to share a few of my own thoughts on the matter. But first, a review of the Value Fund portfolio.



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The Value Fund Portfolio

The market environment is much the same as we reported in our [Q2 letter](#). Equity valuations are generally rich and there are pockets of outright froth (many SaaS companies). Low interest rates and TINA (there is no alternative) are goosing asset prices.

Given this environment, we remain cautiously positioned with the portfolio including an 18% cash position at present. We prefer to assume the risk of lagging the indices when markets are frothy in exchange for preserving your capital (and ours) by only making bets when the odds are decidedly in our favour.

Our best performer for the quarter was our largest holding: **Berkshire Hathaway** (BRK.A/B) +19.7%. As we wrote about last quarter, many have written off the Oracle as being washed up. Given the quality of the machine that he has built, Berkshire's \$140 billion of cash on hand and the company's current valuation, we view it as a core holding.

Facebook (FB) +15.3% was our second-best-performing stock for the quarter. Everyone hates the company. Except for the 2.7 billion people around the globe that use one of its platforms (Instagram, WhatsApp and Facebook) regularly. And the advertisers that want to precision target those 2.7 billion people. The stock is no longer cheap but given Facebook's secular tailwinds and our low cost basis (\$141.29), the stock will likely remain in the portfolio.

During the March 2020 selloff we added several big-pharma names to the portfolio including **Pfizer** (PFE) which was up +12.2% in Q3. We like the stock given the company's broad product portfolio, strong free cash flow and attractive valuation.

Cisco Systems (CSCO) -15.5% was our only negative contributor for the quarter. The company issued disappointing guidance in August due to customers pulling back on equipment orders due to the economic environment. We have owned Cisco for years and given the current valuation and their long-term prospects, are happy to own it.

On top of adding to existing positions, we added **Intel** (INTC) to the portfolio in Q3. Intel is a company that we have previously researched and monitored, waiting for an opportunity to purchase it at an attractive price. We finally got our chance.

In July, the company reported a delay in the manufacture of its next-generation 7nm chips and the stock sold off by -22%. We immediately pounced. There is little doubt that Intel has lost its chip manufacturing leadership to **Taiwan Semiconductor Manufacturing Company** (TSM). But given Intel's scale, product breadth, geopolitical importance to the US and dominant market share in its segments (>60% in PC CPUs, >90% in data center CPUs), we believe the selloff is overdone.

Competitors will undoubtedly grow faster and take some market share from Intel. But with **Advanced Micro Devices** (AMD) trading at a 59x forward P/E, **NVIDIA** (NVDA) 55x and **TSM** 25x, you can probably understand why we prefer an investment in Intel at 11.5x. Given the company's historical leadership and financial strength, we believe that in time, Intel can get things back on track. At current prices, any change in sentiment to the positive should lead to a market re-rating.

Our portfolio remains highly concentrated in the US with approximately 73% of the portfolio in US-domiciled companies. Approximately 9% of the portfolio is invested in companies domiciled in Europe (UK and Denmark) and the Middle East (Israel) with the remaining 18% of the portfolio sitting in cash at the end of the quarter.

As a “go anywhere” fund, we are open to investing in businesses around the globe provided that the country respects the rule of law and we understand its culture and business environment. That said, most of the world’s great companies are found in the United States and hence our heavy weighting in US stocks. It is important to highlight that while many of our companies are based in the US, most are multinationals that sell their goods and services throughout the globe.

The Role of Luck in Investing

I was recently invited to write an article for an investment blog on the topic of the role that luck plays in investing. An excerpt is reproduced below, and the full article can be found by clicking on the link that follows.

Just because the future is far from certain, does not mean that it is entirely unpredictable. Lessons gathered across wide-ranging disciplines – from quantum mechanics to professional poker – teach that the way to deal with the inherent uncertainties of life is to think in probabilities. Investing is no different. [Link to full article.](#)

Capital Gains Tax Changes Coming to Canada?

Last week I was asked by a professional tax preparer for my thoughts on the rumoured changes to the capital gains inclusion rate in Canada and how one should position their portfolio. An excerpt is reproduced below, and the full letter can be found by clicking on the link that follows.

I think that there is a better way to approach this. Instead of trying to read the tea leaves to determine what the current and future governments will do with the inclusion rate, we try and take advantage of the fact that capital gains are only triggered once realized.

Unrealized capital gains essentially embed an interest-free loan from the government until you sell a stock or have a deemed disposition (e.g. on death without available offsets or rollovers). We try and take advantage of this free loan by investing in companies that are growing and tend to compound their value at attractive rates over long periods of time (e.g. businesses with tailwinds). Using this approach, the tax bill rarely comes due and the effect of the interest-free loan is to deliver superior after-tax returns to clients in taxable accounts. [Link to full article](#)

Gratitude

The global pandemic has impacted every one of the 7.8 billion human inhabitants of planet Earth. Some tragically so. Being in my middle years, lately I find myself drawn to reflecting on the big existential questions.

To my thinking, an essential part of the miracle that is life is struggle and overcoming hardships. But the timeless wisdom of the ancient Stoics teaches that we can train our minds to be resilient. It teaches that every one of us can find joy and things in our life to be thankful for.

It can be something as simple as a nature walk. A pleasant memory. Pavarotti singing the climax of *Nessun Dorma*. Random acts of human kindness. Appreciating the improbability that our species even exists and possesses the ability to contemplate the wonders of the universe.

In the spirit of Canadian Thanksgiving, I feel inspired to give thanks for these and a few more of my many blessings.

To the firm's clients, thank you for the privilege of managing your capital alongside my own. GreensKeeper will celebrate its 10th anniversary next year and the firm has grown every year since inception. It would not have happened without your trust and support.

Reading and lifelong learning are my passions. I am blessed to work in a profession that rewards those skills, challenges me daily and fosters my creative expression via stock picking, portfolio construction and writing.

Value investing has also introduced me to a community of like-minded investors around the globe whose friendship and generosity in sharing ideas continues to humble me. I suppose this sharing culture stems from the fact that we are all disciples of Buffett and Munger who themselves selflessly share their wisdom openly. If you haven't studied both of their lives, you should.⁽¹⁾ They are a true gift to the world—far, far beyond the realm of investing.

I enjoy teaching others about value investing and watching our four summer analysts progress was immensely rewarding. I am thankful for the gift of working with people who challenge me and whose company I enjoy—thanks Michelle and James!

Finally, I have been blessed with two daughters who I am immensely proud of and whose progress in life bring me much joy. I am fortunate to be surrounded by a family whose guidance, support and unconditional love enriches my life. I have much to be thankful for.

Happy Thanksgiving!



Michael P. McCloskey

President, Founder &
Chief Investment Officer

⁽¹⁾ I recommend *The Snowball: Warren Buffett and the Business of Life* by Alice Schroeder and *Poor Charlie's Almanack: The Wit and Wisdom of Charles T. Munger* by Peter Kaufman.