LIONRIDGE
QUARTERLY REPORT
winter | 2017

Feeling Bloated After The Festivities

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Dear Clients,

The holiday season is always lots of fun, but come January 1st I'm ready for a break from rich food and festive beverages. It's easy to get carried away by the plethora of treats that are abundant in the latter half of December, and overconsumption of calories seems to go hand in hand with all the socializing and merriment (if you can get through a Christmas party consuming only mineral water and carrot sticks, my hat's off to you!). The sluggishness I felt on New Year's morning was not so much the result of that extra glass of wine as it was from the large amounts of rich food that I mindlessly scarfed down in the preceding days. It took a number of days before my appetite was back to normal.

There's an analogy with financial markets. Periods of binging are often followed by periods of temperance (or worse!). The severe corrections in 2008, 2001 and many times prior were preceded by the type of investment gluttony that we've seen in recent years. Unlike my personal eating habits, as an investor I have less of a tolerance for binging than do the financial markets. I tend to start pushing away from the stock market buffet while the frenzy of speculative buying is in full swing (we might miss out on that last chicken wing, but when the market tosses its lunch I want to be well away from the splash zone!). Just as I started off the new year with a (short-lived) preference for mineral water and carrot sticks, over the last couple of years I have gradually been shifting Lionridge's Total Equity Portfolio from a diet of stocks that became richly-priced to one rife with a large proportion of cash (around a third at this time). To continue with the food analogy, as pieces of lean fish turn into chocolate cake, and I can't find new pieces of lean fish to buy, I prefer to trade the chocolate cake in the portfolio for some lettuce!

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Based on different measures it appears that stock markets are clearly overheated. Although enjoying positive returns in 2016, the Total Equity Portfolio did lag its benchmark* last year. This was largely due to the high cash position plus the fact that I avoided exposure to resource and commodity stocks (very deliberate decisions that give me no regrets). I'll continue to be patient with your money (and my own), waiting only for the right opportunities to use this cash to buy stocks of good companies at attractive prices. That time will inevitably arrive, although we might have to forego a few more chicken wings in the meantime. It is with this type of selectiveness and patience that the Total Equity Portfolio has outperformed its benchmark since inception.**

A note on our bond strategy; although I tend to focus on the equity investments in my commentaries, a number of you have significant fixed income allocations as well. The focus of Lionridge's bond strategy is preservation of capital and liquidity to meet your personal cash flow needs, with income generation being secondary to those criteria. My focus is primarily on low risk government debt, with a smaller amount in high-grade corporate debt. In order to protect your capital, I've focused mainly on shorter-term debt as well. One can get higher interest yields investing in long-term debt, but those investments are much more susceptible to falling market values when interest rates begin to rise.

This strategy paid off in the last quarter of 2016, which saw a modest increase in interest rates. During that period, the TMX Canada Universe Bond Index, which is representative of the overall bond market, fell by 3.44%. The TMX Canada Long Term Bond Index fell by a whopping 7.54% in the quarter. By contrast, Lionridge's bond portfolio barely budged in the quarter, down only 0.2%.

Protecting your capital so it can grow for you and be available when you need it: that's a primary objective at Lionridge. ■

At your service,

Hardev Bains, LLB, MBA, CFA
President and Portfolio Manager

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*Benchmark: 45% TSX Total Return; 35% S&P 500 Total Return (Cdn $); 20% MSCI EAFE (Cdn $).

**The inception date of the Total Equity Portfolio was March 30, 2011.

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