



McElvaine
Investment Management Ltd.

**Presentation to
The Ben Graham Centre for Value Investing
The Richard Ivey School of Business
January 27th 2011**



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FINANCIAL PLANNING SERVICES



**" The sports car and sailboat are investments
for my retirement. I'm using them to attract a
younger woman who can support me in my old age."**



Things my Lawyer told me to Warn you About!

- *I am not offering to sell you anything; this is a presentation for information only*
- *My facts may be wrong so do your own work*
- *This presentation contains my opinions, believe them at your own risk as I am often wrong*

What we will cover

- Who I am
- How have I done
- What is risk
- Our approach
- A couple of things we see today
- Couple of Observations
- Q & A



Who is Tim McElvaine?

Investment Experience – Cundill

- 1991 – 2003: Peter Cundill & Associates
 - CIO (1998 – 2003)
 - Co-manager of Cundill Value Fund (1998 – 2003)
 - Lead manager of Cundill Canadian Security (1992 – 1999)

Business Management – Board of Directors

- 2007 - present: Board of Directors Member (Chairman since 2008) of Rainmaker Entertainment
- 2005 – 2006 Director, Humpty Dumpty Snack Foods
- 2001 - 2005 Director, Sun-Rype Products

Investment Experience – McElvaine Investment

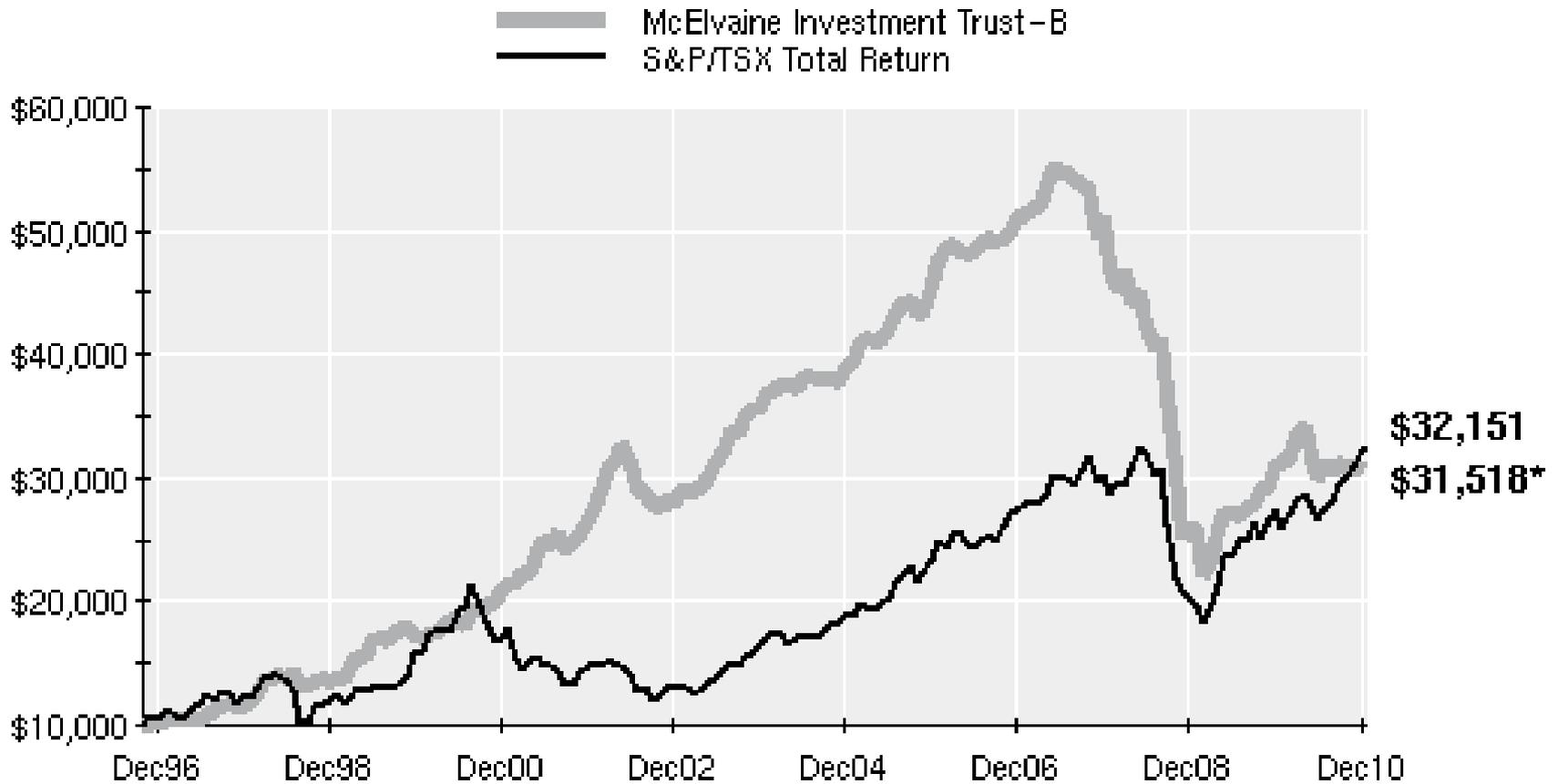
- 1996 – Present: President, McElvaine Investment Management Ltd.
 - The McElvaine Investment Trust since inception in 1996

Education

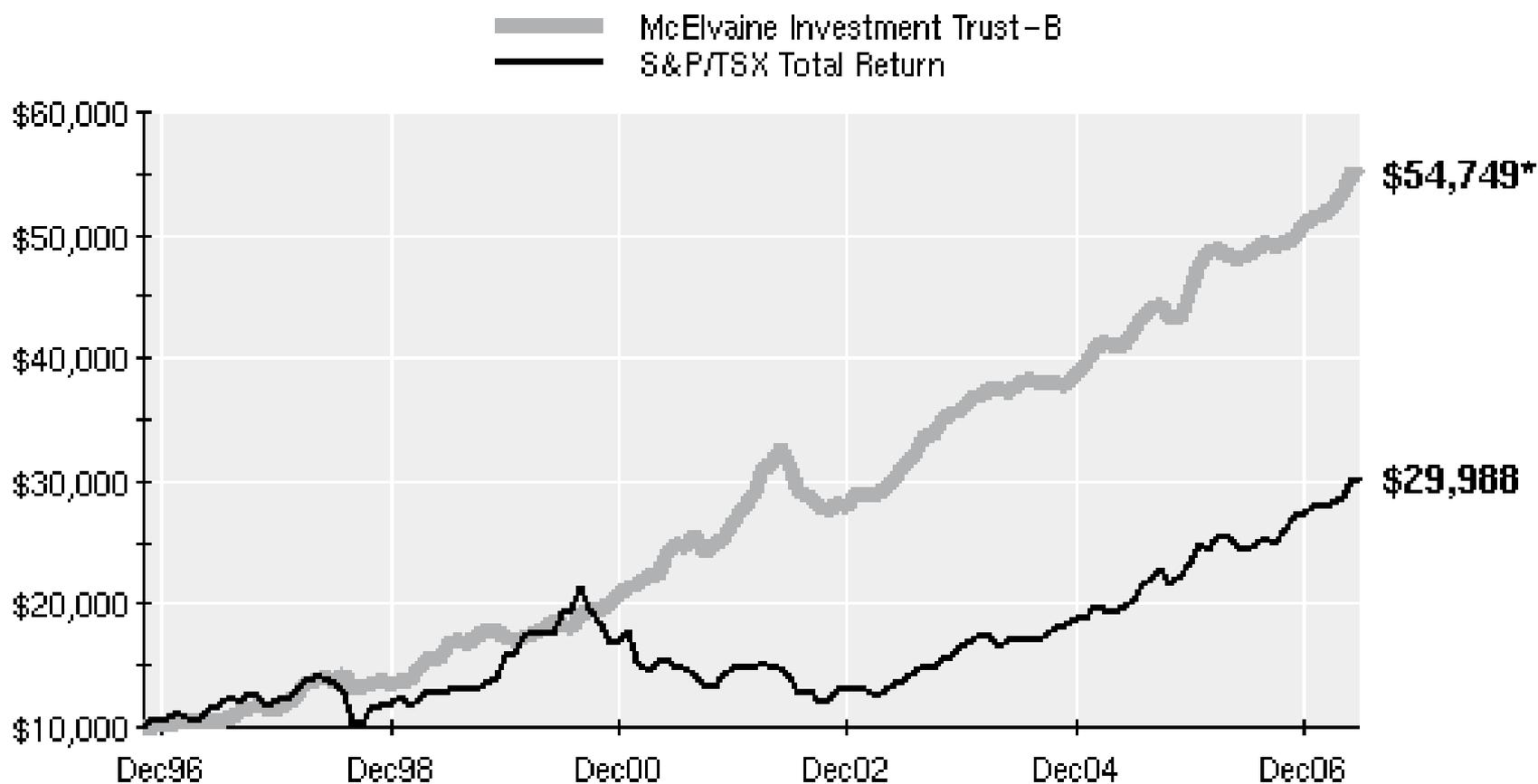
- Qualified as Chartered Financial Analyst (1991)
- Qualified as Chartered Accountant (1988)
 - Touche Ross, Toronto (1986 – 1989)



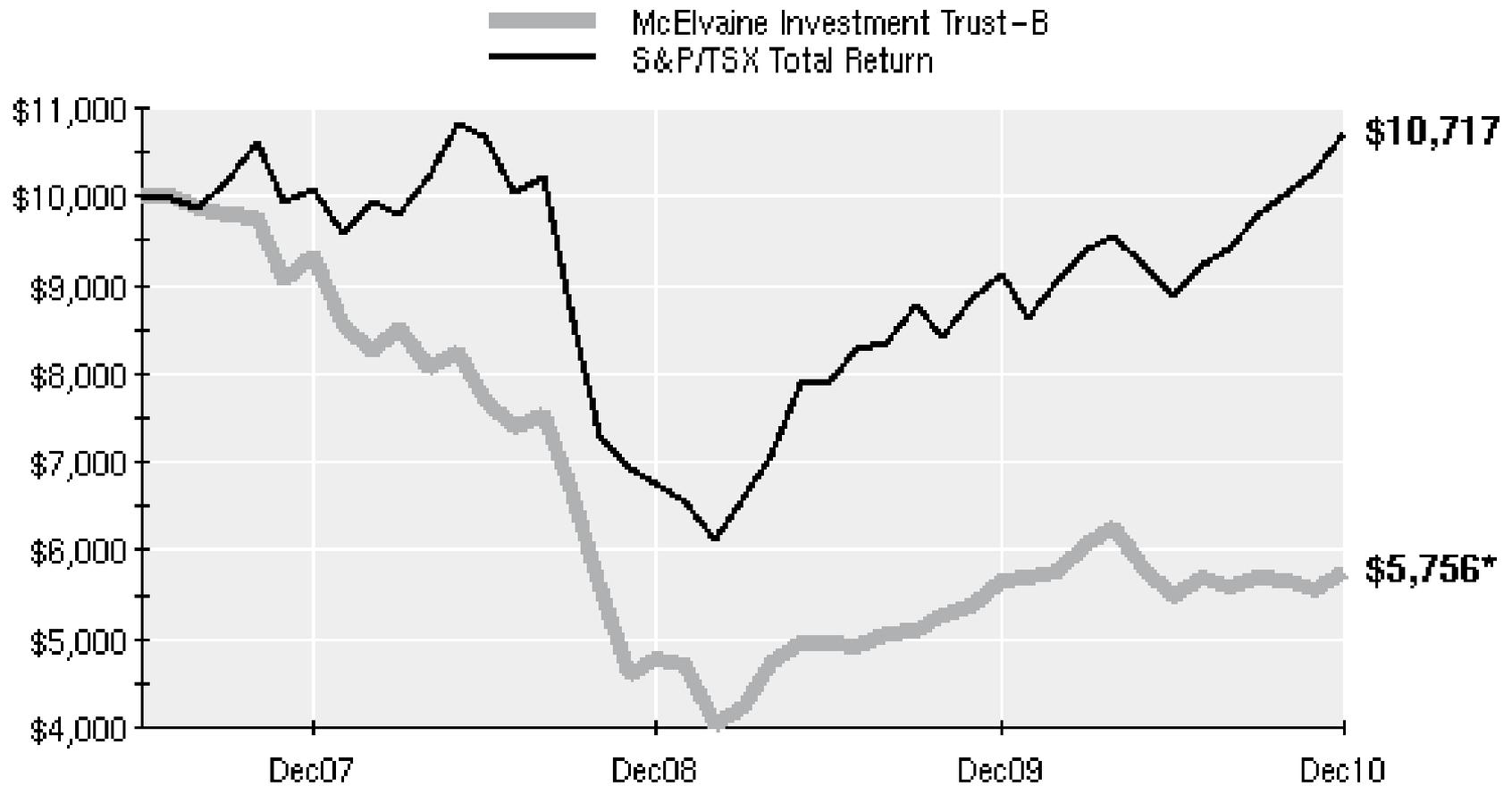
Since inception- Oct96



Glory days – 1996 to mid 2007



The humbling period mid-2007 to 2011



Lessons

- Lessons:
 - Citadel and Canwest
 - Went to zero
 - Large positions
 - Both were delevering plays and environment changed
 - Issue was position size and averaging down
 - Rainmaker
 - Financial and operating leverage
 - Position size
 - Glacier, Indigo, Arlington, Sun-Rype
 - Primarily volatility but balance sheets okay
 - Consider balance of small cap/big cap



RISK

Investments and Retirement Planning

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**“Okay, this time we’ll try it *your way*: 3% in stocks,
2% in bonds and 95% in lottery tickets.”**



RISK

To a Finance professor

Volatility of a stock (or portfolio) relative to the market. Measured by *BETA*.



RISK

To a portfolio manager

Relative performance



RISK

To us

Permanent loss of capital

To a lesser extent: time value of money



RISK

To investors

Time horizon and need for cash



My Investment Criteria – “ABBA”

Accidents

Bird in hand

Brick (cheap) house

Avoid Lola (or alignment of interests)



Criteria 1: Accident

“If you’re going to buy the best bargains, you have to buy the things that people are selling.” – Sir John Templeton

- Look to buy when people are selling for reasons other than price
- Examples:
 - Sectors, industries or regions that people are avoiding
 - Bad news (i.e. dividend cuts, unexpected poor results)
 - Special situations (spin off, emergence from bankruptcy, rights issue)



Criteria 2: Bird in hand

“Protect the downside. Worry about the margin of safety.” – Peter Cundill

- Want margin of safety based on purchase price
- Also consider what the stock may be worth in 3 years (bird in the bush)
- Examples of things considered when valuing a company:
 - Replacement value
 - Liquidation value
 - Private market value
 - Sum of the parts value



Criteria 3: Brick house (but cheap)

“To finish first, you must first finish.” – Rick Mears (4 time Indy 500 winner)

- In the Three Little Pigs story, the brick house survives the wolf
- There will always be wolves in business and our job is to look for cheap brick houses
- Things considered include:
 - Balance sheet strength
 - Free cash flow generation and capital requirements
 - Market share, competitive positioning, relative cost of production



Criteria 4: Avoid Lola (or alignment of interests)

“If you’ve been playing poker for half an hour and you still don’t know who the patsy is, you’re the patsy.” – Warren Buffett

- In 1970s, the Kinks had a hit song “Lola” about a story of a young man who meets a lovely lady who he fancies called Lola. He later was unpleasantly surprised to discover that Lola is a man and not a woman
- Similar to this story, we prefer to avoid unexpected surprises by understanding the motivation and interests of the Board of Management before investing
- Things considered include:
 - Stock ownership of directors and management
 - Insider buying
 - Management compensation program
 - Independence of Board



My Investment Criteria – “ABBA”

Accidents – Seller who does not care about price

Bird in hand – Discount to Net asset value – margin of safety

Brick (cheap) house

– Good bones?

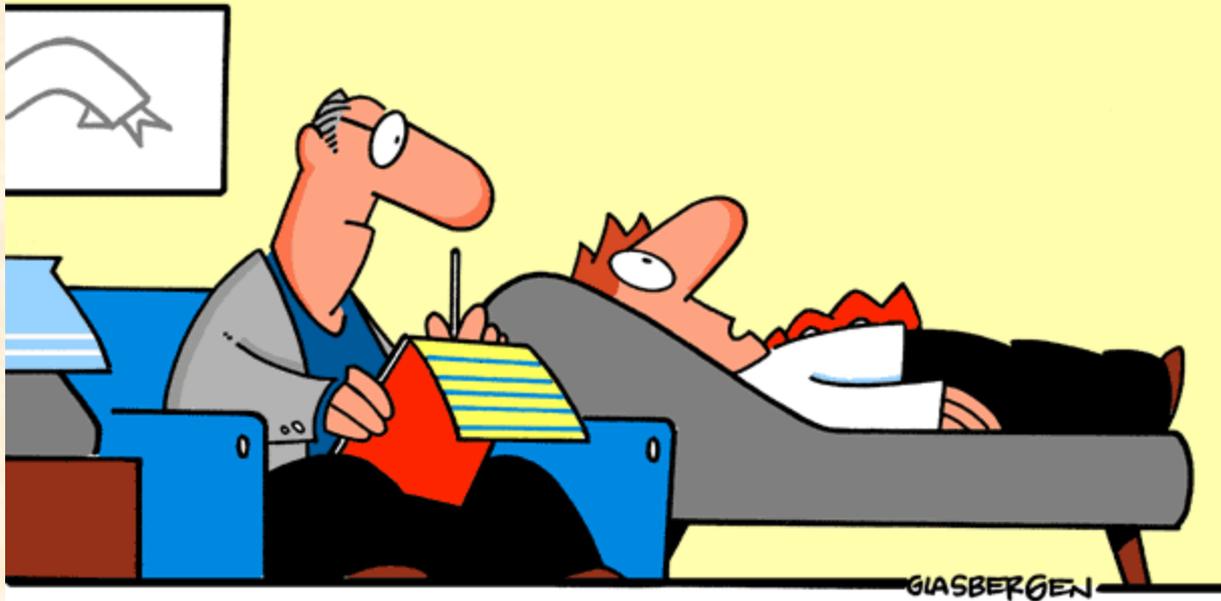
Think about the story of the Three Little Pigs and their houses

Avoid Lola (or alignment of interests)

– Board and management incentives/focus on shareholder



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**“I’m finally learning how to relax.
Unfortunately, relaxation makes me tense.”**



Some things we see today



Fear vs Greed

Where is the Greed today



Fear vs Greed

Charlie Munger paraphrasing Ben Graham:

It's not the bad investment ideas that fail; it's the good ideas that get pushed into excess



Indigo Books and Music

- Accident was sentiment following disappointing results post Chapters takeover
 - Created one dominated national book chain
 - In 2002, Indigo did a rights issue backstopped by Gerry Schwartz
- Plan was to:
 - Improve margins through store rationalization and implementation of SAP system
 - Generate free cashflow and reduce debt
 - Grow sales



Indigo Books & Music



Which Company would you buy?

Example 1

	Company A	Company B
Market Capitalization	5.5B	11.0B
Net extra assets (debt)	1.4B	(2.4B)
Enterprise value	4.1B	13.4B
Op inc (est next fiscal yr)	600m	1.4B
EV/Op inc	7X	10X



Which Company would you buy?

Example 1

	Makita Corp (6586 JP)	Stanley Black & Decker (SWK)
Market Capitalization	5.5B	11.0B
Net extra assets (debt)	1.4B	(2.4B)
Enterprise value	4.1B	13.4B
Op inc (est next fiscal yr)	600m	1.4B
EV/Op inc	7x	10x





Date: 21 January, 2011
Price: ¥3,300
Shares Outstanding: 138 million
Market Cap: ¥455 billion
Yield: 1.58%

Our position: 4.66% of net asset value
Average cost: ¥2,408



Description of Business

Makita, based in Japan, is a premier brand which specializes in cordless power tools, particularly drills and drill accessories. It also produces a full line of hand-held cutting, grinding, sawing and planning tools. In addition, it produces gardening tools and also derives revenue from after sales and service support business. Makita today derives 84% of its revenue from overseas markets with majority of the production based in China and Japan.

Accident

- Capital spending and housing starts is at record lows in many developed economies
- Makita derives a majority of operating profit from Europe, which is mired in bad news, with countries implementing austerity measures
- Yen has appreciated significantly compared to other major currencies

Bird in Hand

Replacement value of the business is higher than the current share price. In addition, from an earnings perspective, the stock is trading below our estimates of equity value measured using depressed earnings and a depressed multiple.

bird in bush

Exposure to developing economies and cyclical upturn resulting in modest sales growth, without assuming any operating margin expansion will lead to a share price much higher than today. In addition, there is a free option in the Yen depreciating.

Brick House

- Balance sheet strength:
- Fortress balance sheet with Net Cash
- Free cashflow generation and capital requirements:
- High ROIC
 - Depreciation equals maintenance capex
- Market share/competitive positioning:
- Strong brand and quality products
 - Major presence in Europe and Japan
 - Major presence with superior growth in developing economies
 - Maktec brand introduced to compete at lower price points

Avoiding/understanding Lola

- Stock ownership:
- Management owns 1.52% and CEO owns 1.44%
- Insider buying:
- None
- Mgmt compensation program:
- Very reasonable
 - Linked to the stock price
- Independence of Board:
- One independent director out of eleven. Four independent auditors.

Disclaimer: We may be wrong and you should do your own work.



Which Company would you buy?

Example 2

	Company A	Company B
Market Capitalization	850m	11.7B
Tangible equity	700m	500m
Assets/tangible equity	6x	25x
P/TB	1.2x	23.5x
PE (next fiscal year)	9x	14x



Which Company would you buy?

Example 2

	Monex Group (8698 JP)	TD Ameritrade (AMTD)
Market Capitalization	850m	11.7B
Tangible equity	700m	500m
Assets/tangible equity	6x	25x
P/TB	1.2x	23.5x
PE (next fiscal year)	9x	14x





Date: 21 January, 2011
Price: ¥22,070
Shares Outstanding: 3.14 million
Market Cap: ¥69.5 billion
Yield: 2.72%

Our position: 7.49% of net asset value
Average cost: ¥24,756



Description of Business

Monex Group, Inc. is the second largest online broker in Japan in terms of assets. The company serves various financial services needs through its stock brokerage, asset management, investment education, M&A, and FX businesses. Monex also acquired Boom Securities in Hong Kong for its foray into Mainland China.

Accident

- Selling pressure. Citigroup is selling its stake from 20.64% to 2-4%.
- Trading volumes in Japan have come down from ¥272 trillion in 2006/2007 to ¥167 trillion in 2010

Bird in Hand

Customer accounts and Customer assets. Purchase was made close to Book Value.

bird in bush

As volumes return to the Japanese bourses, Monex will be a beneficiary and with its built in operating leverage the EPS is expected to increase substantially. In addition, Monex is increasing customer accounts at a brisk pace.

Brick House

Balance sheet strength:

- Capital adequacy ratio of 400% vs. 150% regulatory requirement

Free cashflow generation and capital requirements:

- Almost no maintenance capital requirements
- FCF approximates Net Income over a cycle

Market share/competitive positioning:

- Second largest broker in Japan in terms of customer assets
- Differentiated service with a focus on advice and alternative investments
- Prudent China strategy

Avoiding/understanding Lola

Stock ownership:

- CEO, Oki Matsumoto owns 8.71%
- Orix Corp. owns 22.60%

Insider buying:

- None

Mgmt compensation program:

- Not disclosed
- New age management

Independence of Board:

- Board of Directors comprises ten directors, of which three are external and independent directors and one is an external director.
- Women on the Board

Disclaimer: We may be wrong and you should do your own work.



Dollar bill for 50¢

Cash and loans	€167m
Legacy industrial hldgs	378m
Financial services	<u>282m</u>
Total	€827m
Per share	€10.30
Stock price, 01Dec2010	€5.33





Date: 21 January, 2011
Price: €6.41
Shares Outstanding: 85 million
Market Cap: €540 million
Yield: 0%

Our position: 8.40% of net assets
Average cost: €5.95



Description of Business

RHJ is a based holding company. On July 1st 2010, RHJ acquired Kleinwort Benson, a wealth management company based in the UK and Channel Islands. Timothy Collins, Chairman of Investment Committee, previously worked with Onex and founded Ripplewood Holdings.

Accident

- RHJ was taken public in March 2005 at €19.25
- RHJ was associated with Ripplewood Group and expectations were that it would invest in industrial companies in Japan and elsewhere
- Significant losses sustained in investment portfolio, particularly auto part companies
- Confusing structure and foreign listing

Bird in Hand

Post Kleinwort Benson and related acquisitions, net asset value estimated at approximately €11.

Bird in Bush

Expected disposals of industrial assets and focus on private banking should not only provide for portfolio gains but also potentially eliminate the holding company discount.

Brick House

Balance sheet strength:

- Post Kleinwort Benson acquisition, net cash of €146 million
 - Industrial company debt is non-recourse
 - Kleinwort Tier 1 ratio in excess of 20%
- Free cashflow generation and capital requirements:
- Kleinwort expected to earn €20million
 - Little required capex
- Market share/competitive positioning:
- Industrial assets slated for sale which would generate about €400 million at current valuation
 - After recent acquisitions, has over €10 billion in assets under management
 - Strong brand name

Avoiding/understanding Lola

Stock ownership:

- Timothy Collins, director, owns 13% of shares
- Directors and senior management own shares

Insider buying:

- None noted

Management compensation program:

- Leonard Fischer, CEO, has modest salary and significant share holdings under grants

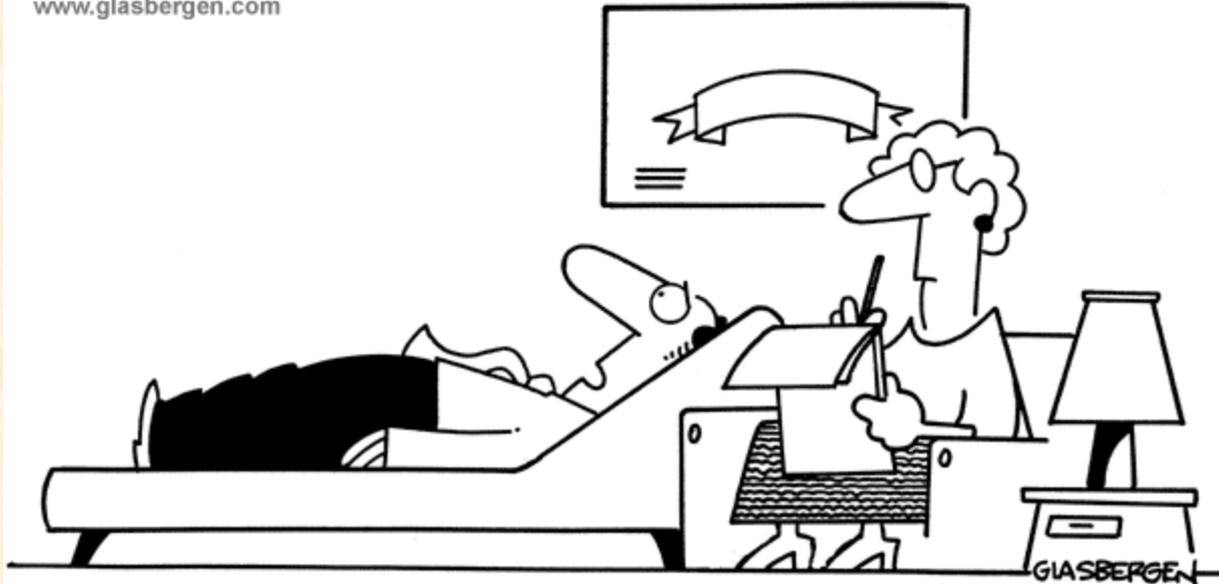
Independence of Board:

- 9 directors, 3 considered independent under Belgian law

Disclaimer: We may be wrong and you should do your own work.



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**“I’m a fun-loving shopaholic trapped
in the body of a prudent investor!”**



A couple of observations

- Ethics
 - Put yourself in your clients shoes
 - Align interests
- Job search
 - Focus on relationships you respect
 - Tailor correspondence to firm





*“Buy stocks like you buy groceries,
not like you buy your perfume.”*

Benjamin Graham



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