

## IRA'S MUSINGS

April 14, 2010

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Last quarter I was pretty frank in my assessment of my new life at the Firm. Even some of our veteran readers claimed to be surprised at all the personal revelations that came forward. Don't expect the same today. Nothing much has changed in my world. Obviously I am not working as hard as I have in the past and I am not likely to get any smarter, so the obvious difference is our team's tenacious work habits and overall investment smarts. I have a little secret. Over a period of decades I was on balance successful.

One of my favourite columnists in the world is Lucy Kellaway at the *Financial Times*. In her March 29<sup>th</sup> column she reviews the importance of good luck on success. I echo this, but I have never underestimated the rewards that emanate from old fashioned hard work. Over many, many decades I cultivated an image of myself playing golf all the time and generally enjoying life. This was a half truth. I worked very hard for decades and only recently have I truly begun to work less intensively. We have a team of very hard workers and this offsets my retreat to more normal working habits.

I am sticking with my statement from January that this year is going to permit old fashioned stock picking to flourish. The best proof is in the oil and gas sector, where some stocks are booming because of technology-induced finds, while others are in the doghouse because of depressed natural gas prices and failures to increase production. During 2008 and 2009 all that mattered in the stock market was the industry you were in, as most stocks in a sector acted the same. This was not our type of environment, so I am a little biased.

I have not forgotten to pay attention to the world. How can I, when my colleague David Rosenberg is widely followed and quoted. Here I am sitting quietly at breakfast in Florida reading the March 26<sup>th</sup> *Financial Times* when I spot an article entitled "Treasuries - will they prove a good bet over the long term?" Suddenly I am confronted with David Rosenberg's debate with Jim Grant at a recent spring conference. The following Monday the *New York Times* quoted David saying that the market was too complacent.

My friend David reminds us at least once a day not to get complacent so don't worry. I try to think about what the downside risk is to stocks if his outlook for more trouble in the U.S. comes to pass. I doubt that it will be as bad as 2008. Admittedly there is more speculation in the air than a year ago. There has been a strong recovery in many asset classes, but the world doesn't have anywhere near the same degree of leverage it did three years ago. I am not talking about highly publicized Donald Trump-type debt-laden companies. I am talking about normal operating companies who three years ago had normal amounts of debt as determined by debt-to-cash ratios and a variety of such basic measures. What happened in the financial crisis of August 2008 was that all companies with short-term debt maturities were declared to be guilty by the market. The credit shortage made many companies seem vulnerable even if the operating

business was still coasting along. If the operating company with some debt also happened to contain some cyclical aspects then chaos ensued. Thus many, many stocks declined in price by 90% as fears of widespread bankruptcies were commonplace.

You can now see why so many stocks have recovered so dramatically in the last year and a half. Many companies reduced their leverage by hook or by crook. They sold assets ferociously and issued equity at every opportunity and lastly issued corporate bonds to retire bank debt at whatever spread happened to be available. Thus, there is much less risk to the companies overall because of the drop in leverage and the increase in corporate liquid assets. I review these events only to point out that the stock market decline, if it happens again, should not be as bad. Over many decades I was always asked about the downside in various stock markets. I always thought 25% was a good answer to give and I would provide it again.

I have always been an avid reader, which I attribute to my late mother the librarian. Obviously I have more time for reading than ever before and I am taking full advantage of the opportunity. Whether my mother would have approved of my racing through the three Stieg Larsson novels is another story. Despite this literary background nobody asks me my view on the future of the world, or the future of contemporary art, or any such weighty measures. Instead I am asked about real estate because of my background and the big question of course is what should I do with my money. Having kept roughly the same asset weights for the last three years, I am no maven. I understand the reluctance to go too strongly into equities after a strong market rally. History is littered with examples of people pouring into the market at or near the top – for me, I'm a long-term guy, so the recent experience of quarter-to-quarter and year-to-year increased volatility is less worrisome than it is to most.

I find that the increased volatility has also impacted behaviour in the charitable world. Three years ago capitalists were very generous in their donation practices. When the market crashed so did the world of donations. Two years later, the world inhabited by wealthy donors is in remarkably good shape, especially in Canada. The asset values of the affluent class are relatively healthy and not too far below the peak values of 2008. However, donation patterns are far from recovering. Inevitably donors will be back as the trend to U.S. style giving is in its early stages.

How is life at the Firm? Quite exciting. We continue to add great talent. Geordie Young has joined our investment team after 8 years at Goldman Sachs in London, England. He's a legitimate rocket scientist, having his undergraduate degree in Astrophysics from Harvard. How many of those also have an MBA from Stanford? I don't know, but my guess is the number is close to 1. He's also a nice guy to boot. As well, Jim Bantis, a former head of research with Credit Suisse, has joined us on the client side. Being able to attract this kind of talent gives me great confidence in the future.

Lastly and for many people the big question – how is my golf game? Before answering, a little background is necessary. I have played golf forever, but my skills have been declining for decades, regardless of the state of the financial markets or time spent on the game. It does not bother me. I am not a fanatic. At least that's what I tell myself.