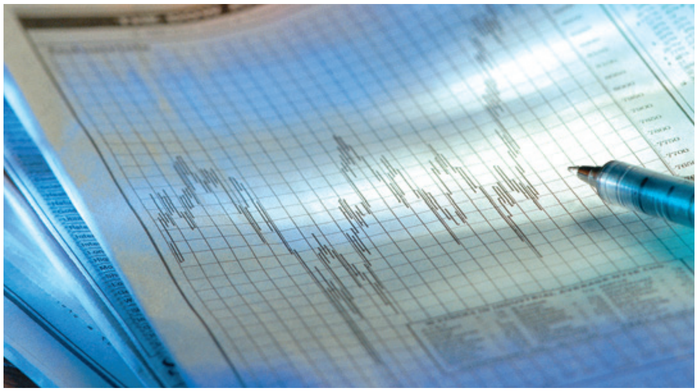
GFI Investment Counsel Ltd.

*Preserving and growing family capital™*

# GoodQuarter

SPRING 2013



## IN THIS ISSUE



*"It's far better to buy a wonderful company at a fair price than a fair company at a wonderful price."* – Warren Buffett *(Source: Letter to shareholders, 1989)*

**Dear Valued Client,**

The first quarter of 2013 saw most global equity markets rise significantly. Economic statistics and political events that occurred during the quarter were both positive and negative for global economic growth. With this as our backdrop, we continued to invest in reasonably valued and very strong businesses. At the end of the quarter, our client accounts had reached all-time highs, earning roughly 12%-16% annualized returns since the lows reached in February 2009. More importantly, since inception in 2005, our client accounts have enjoyed annualized returns of roughly 7% per year.*

With respect to portfolio activity, we sold our investment in The Jean Coutu Group Inc. in the first quarter of 2013. This investment was very successful for us; however, industry fundamentals left us wondering about the company's prospects. Ultimately we decided to exit, given the limited investment returns we expect to see from the company going forward.

Our investment in H.J. Heinz Company ("Heinz") will also conclude soon, as Berkshire Hathaway, Warren Buffett's investment company, along with a Brazilian partner, have announced their intention to purchase the entire company. Heinz has been a successful investment for GFI's clients since June 2008, and the purchase of the company by Berkshire Hathaway is a bittersweet event for us.

As has been a common theme over the past year or so, some GFI client accounts have elevated levels of cash on hand. This cash is earmarked for further investments in fixed income securities. Given the current challenge in finding attractive yields in the bond market, we will remain cautious and wait for greater opportunities. We prefer to be patient rather than stretch for returns and assume unnecessary risk.

We have been busy meeting with many of you during the first few months of the year, and look forward to meeting the rest of our clients in the months ahead. We always enjoy catching up, and encourage you to call us if you wish to discuss your portfolio or any other matter.

Warm regards,

Daniel Goodman, CFA
President and
Chief Executive Officer

Effie Wolle, CFA, MBA
Vice President and
Co-Chief Investment Officer

*Please see our detailed performance figures available at www.gfiic.com

# Our Investment Approach — Change and Brands

With the pace of change in technology increasing every day, our job as portfolio managers has become more qualitative than ever. While recognizing that the impact of change in the technology industry is difficult to predict, it is equally important to recognize the changes taking place in old, established businesses as a result of technological change.

In one such instance, the retail sector is being permanently altered by the continued growth of online retailers such as Amazon.com ("Amazon") and Well.ca. These web-based companies require fewer employees and less real estate than traditional bricks-and-mortar retailers. They, therefore, enjoy greater benefits of scale. The price of products online are similar to traditional retail, and delivery is often within 48 hours. While existing retailers can compete online, many have long-term leases for expensive real estate, and as market share moves online, rents and associated labour costs cannot be reduced as quickly as required to compete with web-only competitors.


One of the ways in which we continue to make strong investment decisions regardless of the rapid technological changes occurring across industries is to purchase businesses that have superb brands. This approach has been espoused by Warren Buffett many times and has become more evident to the astute observer, as companies continue to face challenges in their existing business models.

Regardless of whether we buy Heinz Ketchup online or at the supermarket, Heinz is a trusted and searched-out brand that is generally considered worth paying an extra fifty cents for. While in any given year these characteristics may not be reflected in higher returns, the reduced probability of future losses helps generate strong long-term investment results.

The strength of Unilever NV's brands is one of the reasons that we recently purchased it for client accounts. Unilever is a world-class consumer goods company with brand names that include Dove, Vaseline and Sunlight. Unilever is growing in both developed and emerging markets, and pays an attractive and growing dividend. We look forward to owning Unilever for many years to come.

## Investment Management Fees and Taxes

### *Minimizing taxes is everyone's goal ... including ours*

As an investment counselor, our fees may be considered tax-deductible expenses. Although we refrain from giving specific tax advice, we strongly encourage you to consult with your tax advisor to ascertain whether you can deduct any fees charged by a service provider.

Please also remember that the individuals at GFI are always available to discuss fees — or any other topic — with you and your professional advisors.

## GFI in the News

NATIONAL POST

# More than just doing the math

**Manager:** Daniel Goodman & Effie Wolle, GFI Investment Counsel
**Fund:** Good Opportunities Fund (and private-client portfolios)
**Description:** Concentrated portfolio of high-quality equities and fixed income
**Firm's AUM:** $275-million
**Performance:** 1-year: 17.4%; 3-year: 19.5%; 5-year: 3.8% (annualized as of Jan. 31, 2013)
**Management fees:** Management: 2%; Performance: 20%; with a high-water mark

Investors used to be more willing to give companies the benefit of the doubt in terms of allowing them time to achieve their goals, but Daniel Goodman and Effie Wolle say many of those same businesses are now under tremendous pressure because investors are demanding results, not simply promises.

That's partially why the co-chief investment officers at GFI Investment Counsel, who manage the long/short Good Opportunities Fund as well as segregated client portfolios, spend a lot of time focusing on companies' competitive positions.

"The predictability theme and relying on a company's future prospects is very important today, as opposed to just crossing your fingers and hoping," Goodman said.

As value investors, the managers focus on future cash-flow predictability. "That's what really helps determine the value of a business," Goodman said. "If you can't see out far enough to predict that cash flow, then maybe the business isn't as cheap as the numbers suggest."

For example, he said investors are not granting Fortress Paper Ltd. the same valuation they once did.

"It is leveraged and entering into a new business line," he said. "While the story sounded great, investors were giving the company credit for what it said it could do. Execution has been challenging and now the company's share price is under tremendous stress, declining by 75% over the last 12 months."

Wolle said factors such as competitive position, obsolescence risk and management strength are important. "If it was all about figuring out a number, then mathematicians would be the best investors," he said. "Not all earnings are created equal: A dollar of earnings from a railway does not equal a dollar of earnings from a business in decline."

### BUYS

**JUST ENERGY GROUP INC.** (convertible debentures maturing 2017)

***The position:*** Held in fund and client portfolios for several years.

***Why do you like it?*** This natural gas and electricity retailer recently slashed its dividend in an attempt to bolster its cash position and fund future growth.

"The dividend cut was appropriate and supportive of the debentures," Wolle said, noting the yield to maturity on these securities is now above 10%. "It's positive to see the board of directors address the capital structure of the business."

Goodman notes the company has plenty of cash flow to fund the debenture, while the business is also growing.

***Biggest risk:*** Margin compression due to more competition and lower natural gas prices.

**STAMPS.COM INC.** (STMP/NASDAQ)

***The position:*** Core position in fund, owned on and off for more than five years.

***Why do you like it?*** Stamps.com is one of three companies licensed by the U.S. Postal Service to electronically distribute stamps.

"Its future success is not driven by typical mail volumes," Goodman said. "It's driven by online commerce and the business's ability to help deliver packages through their software."

The managers also like Stamp's strong operating leverage, pristine balance sheet, consistent cash flow and recurring revenue growth.

"They do exactly what we want with capital," Wolle said. "They buy back shares, pay special dividends and always ask shareholders what they'd like to see."

***Biggest risk:*** Lower mail volumes.

**FISERV INC.** (FISV/NASDAQ)

***The position:*** Added to fund in past 10 months.

***Why do you like it?*** This supplier of technology software and back-end solutions does business with every single one of the largest 100 financial institutions in North America.

"The company has wonderful operating leverage since it is mainly software-based and every incremental revenue dollar flows to the bottom line," Wolle said. "They're also tremendous allocators of capital — continuing to buy back large amounts of shares and making quality acquisitions."

The managers see no reason why Fiserv, with its return on equity now in the high teens, will stop those practices.

***Biggest risks:*** An expensive acquisition mistake; technology obsolescence.

### SELL

**CENVEO INC.** (CVO/NYSE)

***The position:*** Short in fund.

***Why don't you like it?*** The managers anticipate shares of this diversified printing company will eventually fall to zero.

"The industry has been in decline for many years and Cenveo has an extremely levered balance sheet with US$1.3-billion in debt," Goodman said.

Wolle noted Cenveo recently refinanced some of its debt at 15%, in addition to other costs, which indicates its lenders are also concerned.

***Potential positive:*** A strong cyclical recovery.

*Jonathan Ratner, Financial Post*

## GFI Investment Counsel

GFI Investment Counsel (“GFI”) provides tailored investment portfolios to families, foundations, trusts and corporations. We work closely with our clients to customize investment accounts that coincide with our clients’ unique requirements. GFI focuses on preserving and growing client capital through intense due diligence, focus, and discipline.

In January 2008, GFI launched Good Opportunities Fund (“the Fund”), an alternative investment fund available to accredited investors. The Fund focuses on a select group of investment opportunities that provide an attractive risk/reward dynamic regardless of asset class or market capitalization. The Fund is managed with a focus on understanding the businesses, their capital structure, and risks and opportunities.

For more information about GFI Investment Counsel or the Good Opportunities Fund,
please call **416.488.8825** or **email info@gfiic.com**.

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