GFI Investment Counsel Ltd.

Preserving and growing family capital™

"I think the reason why we got into such idiocy in investment management is best illustrated by a story that I tell about the guy who sold fishing tackle. I asked him, "My God, they're purple and green. Do fish really take these lures?" And he said, "Mister, I don't sell to fish."

Charlie Munger, 1994

Second Quarter 2014 Commentary

Good Opportunities Fund

Good Opportunities Fund gained 2.5% over the second quarter of 2014. The Fund closed the quarter with long holdings of about 80% in equities and 3% in convertible debentures. The Fund is short one company that totals 4.0% of assets, and holds roughly 16% cash.

We began selling our convertible debenture holding during the second quarter, as its price had increased following a restructuring of the company's finances. We do not believe that this holding's current yield-to-maturity warrants further ownership, given the Fund's objectives.

We continue to strongly believe that the Fund's short sale investment will, in due time, face financial peril. However, we do not know the timing of this event. To our benefit, the company pays no dividend and we are able to borrow the stock at a very low cost. However, given its highly leveraged balance sheet, the company's equity has been volatile and, at times, has been a drag on the Fund's performance.

Owning and shorting a collection of 12 businesses – as opposed to an index of 100 or more businesses – will inevitably lead to some lumpy results. Our first objective is not to lose capital. We have accomplished that goal thus far in 2014. We also need to ensure that we produce adequate returns. Although we are quite pleased with the operating performance of our holdings, the stock prices of our investments have not moved in tandem thus far in 2014. This is part of the ebb and flow of investing and a fact of life in managing public securities. We will not deviate from a proven approach to rational investing.

We continue to research various companies and securities in which to allocate the Fund's cash. We are confident that our approach of purchasing cash-flowing businesses that allocate capital well will lead to continued successful investment results.

We are enclosing a feature article about the Fund that ran in the Financial Post during the second quarter.

Warm regards from the entire GFI team. We hope you enjoy the improving weather!

Sincerely,

Daniel Goodman, CFA
President and Chief Investment Officer

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VP and Co-Chief Investment Officer

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FINANCIAL POST

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Managers following in Warren Buffett's footsteps

By Jonathan Ratner

Warren Buffett never really focused on the macro, and GFI Investment Counsel portfolio managers Daniel Goodman and Effie Wolle are comfortably...

Managers: Daniel Goodman and Effie Wolle, GFI Investment Counsel
Portfolios: Segregated Client Accounts, Good Opportunities Fund
Description: Value-oriented securities, focused on North America
Firm's AUM: $350-million
Performance (Fund): 1-year: 15.5%; 3-year: 16.3%; 5-year: 20.6% (as of March 31, 2014)
Fund fees: Management: 2% (Class A); Performance: 20%

Warren Buffett never really focused on the macro, and GFI Investment Counsel portfolio managers Daniel Goodman and Effie Wolle are comfortably following that roadmap.

The bottom-up value investors focus on buying great businesses that have attributes such as pricing power, operating leverage and some form of competitive advantage, and believe the best risk management and return opportunities come from companies that are not over-leveraged.

"They come out stronger because competitors are often unprepared," Goodman said, noting such companies often end up taking market share or gobbling up other businesses.

GFI offers high-net-worth clients separately managed portfolios, with the Good Opportunities Fund holding a more concentrated basket of securities.

As the firm's co-chief investment officers, Goodman and Wolle don't try to time the market, but low interest rates are making it very comfortable to invest in high-quality companies.

"It appears that we're likely in a low-rate environment for a prolonged period," Goodman said, highlighting similar comments from Bank of Canada Governor Stephen Poloz recently. "Great businesses are responsibly using this to increase earnings and cash flow by refinancing their debt at a lower rate."

He also thinks companies are far less cavalier than they were heading into the financial crisis, so there is less risky leverage in the system.

"Credit expansion is just starting to pick up and in the businesses that we focus on, it is happening at a responsible level," Goodman said.

One area the managers tend to avoid is the fast-changing technology sector.

"You won't see Apple or BlackBerry in our portfolio," Wolle said. "Trends change quickly, so it is a lot harder to be comfortable with what a business will look like in five years."

(continued)

BUY

Whistler Blackcomb Holdings Inc. (WB/TSX)

The position: Purchased in past six months

Why do they like it? GFI went back about a decade to analyze this ski resort operator's pricing power and the math indicated that it has increased the price of lift tickets well above inflation.

Wolle also pointed to the company's operating leverage, as the variable cost for an additional skier coming to the mountain is next to nothing.

"With extraordinarily low variable costs and some pricing power, if you slowly grow your customer base, your profits go up dramatically," he said. "It's also a world-class asset and the competition in the Vancouver area are smaller hills with less appeal.

Biggest risk: Prolonged bad skiing conditions.

Visa Inc. (V/NYSE)

The position: Held for about 3 years

Why do they like it? GFI considers this global payments giant a royalty company linked to global consumption.

"Businesses like this have built-in inflation protection because when prices go up, so does the royalty," Goodman said. "It is a tremendous business model and its operational scale is very powerful."

Wolle noted that Visa doesn't have to worry about increasing prices as industrial companies do, because it takes "the same percentage and the total amount just grows over time."

Biggest risk: Regulatory changes.

Guardian Capital Group Ltd. (GCG/TSX)

The position: Held for more than 3 years

Why do they like it? Guardian is a growing asset manager with more than $22-billion in AUM ($1.8-billion in private wealth), and GFI estimates its corporate portfolio's net asset value is worth about $14 per share.

Most of this portfolio is Bank of Montreal stock, so Goodman noted investors get Guardian's wealth management business for about $3 per share.

"The ability to buy this division for such a low price is a great opportunity," he said.

Wolle noted that the knock on Guardian used to be that its core business was near break-even, but said it's "really turned a corner," having made about $10-million before taxes last year.

Biggest risks: Prolonged weak performance; staff turnover.

SELL

Cenveo Inc. (CVO/NYSE)

The position: Short for more than five years

Why don't you like it? GFI took a short position in this envelope and paper company when it was trading around US$15 per share. It now trades at about US$3.

"They have a very leveraged balance sheet and sell a commoditized product as opposed to something unique," Wolle said, noting it has little pricing power. "The business is declining as people use less envelopes and print fewer documents."

Potential positive: The company is able to raise prices.

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