

CANADA TIP SHEET: Law Hunts For 10-Baggers

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OTTAWA (Dow Jones) -- As a small-cap fund manager, Jennifer Law tries to sniff out potential "10-bagger" stocks. She thinks Katanga Mining Ltd. (KAT.V) may eventually prove to be a winner.

Ten-baggers are stocks that increase their value 10-fold.

Law bought Katanga earlier in the year for the CIBC Canadian Small Companies Fund that she lead-manages. But it could take about a couple of years for the company, which owns a big copper project in the Republic of Congo, to show its potential.

"You don't expect them to produce immediately, but you watch as they come on production in 2007, I think that will give a nice lift to the portfolio," Law said in an interview.

"With Africa becoming a more important copper producer, we're sort of taking a little bit more risk, branch out a little bit and finding a next winner," she said.

She builds smaller positions in established winners, such as First Quantum Minerals Ltd. (FM.T), which she bought a few years ago and which emerged as a 10-bagger.

"We try to layer on some more smaller positions that we can build into core positions over the next two years if management delivers what they promise," Law says.

HudBay Minerals Inc. (HBM.T) is another stock that has been an "exceptional performer" for the fund since Law bought it at the initial public offering for C\$2.20 a share. The stock came with warrants.

She bought more warrants at 3.5 Canadian cents each and that has risen to become "almost a 10-bagger." She bought more of the stock and warrants in anticipation of strong fourth-quarter earnings, and describes subsequent gains as "pretty sweet."

HudBay is trading at C\$13.33 in Toronto Thursday.

Recipe For Making Money In Small-Caps

As a bottom-up investor, what attracts her the most about a company are the qualitative aspects: the management, the product or service, the competitive landscape, how a company sets itself apart to compete, and catalysts for growth.

She keeps sector bets "small and measured" and says she runs a balanced portfolio with exposure to all 10 sectors. Nearly half the fund is invested in energy and materials stocks, reflecting their dominance in the market.

Law says the key to making money in Canada's small-and- mid-cap market is to get a foot in the door early before a company's earnings are included in forecasts.

"If you're there early, you get to know management well, really understand the business, that's where you can outperform and that's when you can make good money," she says.

Law has spent nearly her whole career managing small-caps funds. She started managing the Canadian Small Companies Fund in 2003 and helped turn it from a fourth-quartile fund to the current second-quartile ranking. As of April 28, the fund had assets of C\$123.9 million (US\$112 million).

The portfolio is run on GARP principles - growth at a reasonable price - but has a lower beta than is typical for the riskier small-and mid-cap asset class.

"The beta for this portfolio tends to be 10-15% lower than the benchmark. We're not taking as much risk as the benchmark," Law says.

The price-earnings multiple is also lower, and the return on equity tends to be better than the benchmark. "I think as an investor, you get the best of both worlds," Law says.

She can hold winner stocks until they reach a market capitalization of C\$6 billion, unlike other small-cap funds where the limits are much lower.

"That's a really nice flexibility within this mandate (the Canadian Small Companies Fund) that the unit-holder is probably not aware of," says Law.

Law doesn't see "lots of great new ideas" in the market right now.

"We'll continue to dig and find some little nuggets here and there, but overall, I think the biggest call this year is when to take profit on the commodities and the rest of it is just really boring, bottom-up work," she says with a laugh.