

THE INVESTOR'S DIGEST INTERVIEW

Here's one marathoner who's not running with the pack

Gaelen Morphet pilots the Renaissance Canadian Core Value Fund for CIBC Asset Management. She's also a marathon runner, but she'll seldom chase the latest hot stocks. They're fine, she admits, when Bay Street is on a tear. But they'll provide little protection when markets go into a slump



Gaelen Morphet is slim, svelte and toned — hardly the tough jock you'd expect a marathon runner to be.

But Ms. Morphet, 46, is a top-notch racer, having successfully completed five major North American marathons over the last six years.

What's the attraction? The sheer challenge — that and the side benefits of stronger muscles and less stress, says Ms. Morphet, who helms the Renaissance Canadian Core Value Fund for CIBC Asset Management in Toronto.

But perhaps an even more important benefit is the cultivation of those traits necessary for success in value investing — the philosophy Ms. Morphet herself follows.

"As a value investor, you have to be patient and wait for value plays to improve and get better," she notes.

"So, in this sense, the discipline and patience of value investing is similar to the discipline and patience involved in marathon running."

You didn't enter marathons until your late 30s. But you started running years earlier.

In Grade nine, to be precise. I took up running at lunchtime just to keep in shape. But I had to give it up later when my children came along. (I have three boys and one girl). Now, however, I run every weekend on Toronto's Belt Line trail, starting out near my home in Leaside, going six miles out and then six miles back. And I plan to keep working out as long as I can.

But don't you sometimes get the urge in a marathon to throw up your hands and quit?

Not at all. By the time you get to the starting line, you're determined to finish under any circumstance. After all, you've put so much time and effort into your training — largely at the expense of your family.

But your husband, Derek, is right there with you. In fact, both of you often run in the same marathon.

Allowing the two of us to spend time together which, given our hectic schedules, is often hard to come by. In the meantime, my husband is getting better. He even beat me in the 2005 Houston marathon. It was an exciting moment because I usually outrun him.

So which marathon has been the most enjoyable?

New York's. Not only does it take you through many different neighborhoods, but there are these enormous crowds all along the route. You're also serenaded by jazz and calypso bands. The Boston Marathon is also memorable, if only because it's the top such event in the world. Unlike other marathons, however, you can only enter after you've passed the qualification race.

Unlike most of your peers, you studied psychology, not business, in college. How did you end up in investments?

Ra research assistant at McLeod, Young Weir — now Scotia Capital. And I was hooked. For one thing, it was a great introduction to the world of business. More important, it was fascinating to be exposed to so many companies in so many sectors.

And 23 years later, you're still working on Bay Street.

I love my job because I get paid to read about so many things: the North American economy, globalization and fixed-income investments, to name a few. I also like the fact that this business is based on merit. It's not focused on whom you know or where you went to school. Indeed, when I started out, I was told that if I worked hard and proved myself, the sky was the limit.

Before this fund, you managed some mining portfolios — a job for which your childhood stood you in good stead.

From kindergarten to grade six, we lived in Northern Ontario;

my father was a doctor in Swastika and Porcupine. And while I did the usual outdoorsy things like climb trees and run through fields, I also hung around abandoned mine sites, if you can believe it. So, I had a bit of a feel for mining when I began investing in the industry many years later.

For whom is the Renaissance Core Value Fund best suited?

For conservative investors. Yes, we aim to grow the fund — but not at the expense of capital preservation. People can buy our units, safe in the knowledge that they can hold them for the long term. During the tech meltdown, for example, we actually made money. In 2001, the Canadian portion of the fund rose 12.5 per cent. By contrast, our benchmark, the S&P/TSX Composite Index, tumbled 12.57 per cent. Meanwhile, as of mid-April, we had \$650 million in assets under management.

Over the course of the current bull market, a lot of value investors have strayed over to the growth camp. But you've stuck to your guns, say.

Because in a rising market, anyone can make money. But in a falling market, the watchword must be capital preservation. And when it comes to preserving capital, a value investor is better than one who's obsessed by growth. True, because we hold no speculative stocks, we've lagged the overall market. But when things roll over, as they invariably will, we won't fall as far. We're happy, in other words, to yield some of the upside in order to be well-protected when hit on the downside.

Still, there's always pressure to jump on the bandwagon.

You said it. And people do climb aboard. But inevitably, things go too far, and the situation ends badly. You have to learn how to grow money, but not be swept along by the herd. And the herd is always chasing after something — like China, for example.

True, many think China is on a long-term secular rise.

But there will be ebbs and flows along the way. And even though such setbacks may last only a year, they can still hurt.

So Canadian investors might do well to exercise caution before investing abroad?

Definitely, yes. In fact, Canadian equities should do as well, if not better, than their foreign counterparts. For one thing, Canada is anchored by a solid financial-services industry — one that's both big and well-diversified. Moreover, the loonie is likely to remain strong. Then, too, we have a balanced budget. In addition, we're politically stable. All these things help explain why many of our companies are being snapped up by outsiders. Yes, holders of Canadian stocks will be hurt when the market rolls over. But they won't be bruised any more badly than those Canadians who are now heavily invested abroad.

What do you look at when actually buying stocks?

The current return on equity, for starters. If a company is trading at a lower ROE than it has in the past, or if its ROE seems as if it's going to grow more than before, we'll consider that company a "buy" candidate. We'll also look at the balance sheet. After all, a company's financial house should be in order. Of course, many other fund managers will tell you the same thing, although they'll conveniently skip over financial deficiencies if the company is the flavor of the month. Another area we'll look at is corporate governance. We don't want to buy a company that's under investigation for, say, accounting irregularities. In sum, we seek out stocks that are overlooked, underfollowed and in a spot of trouble. In other words, we try to find diamonds in the rough.

Because its modular buildings are heavily used in the resource sector, Atco stands to do well as the oilsands ramp up.

Indeed, it should. But Atco is also into electric power generation, with approximately 4,900 megawatts of capacity. And because power generation is regulated, Atco's income stream is highly predictable. Meanwhile, the company is well-managed, boasts a good return on equity and plows money back into its own operations. In short, it's an investment that's dependable.

Linar is based in Guelph. But it's a world-class maker of automotive parts.

And cheap as well, given a price-to-book ratio of just 1.3. Getting a quality company like Linamar at such a low price is rare. In addition, it has a solid ROE, a strong balance sheet and very little debt. Moreover, having done a major stock buyback last year, Linamar has shown itself to be onside with its shareholders. The company is also profitable, having made money even at the bottom of the business cycle. A parts maker like Linamar can only benefit as the Big Three North American automotive companies outsource more and more of their production.

Thomson is a byword in publishing. But for years, its revenue grew at a snail's pace.

But its sales should now start revving up. Indeed, its revenue is poised to grow seven to eight per cent a year, and its profit margins should increase by 20 per cent a year. Thomson's biggest problem now is its huge pile of cash — something that could be a drag on its ROE. But the cash hoard could turn out to be a plus if put to work, say, on the acquisition trail.

Canadian Tire is often only thought of as a parts and hardware outfit. Yet, it has a successful credit card business too.

Which it hopes to expand into other financial products, such as GICs. Meanwhile, thanks to increased floor space, along with jazzier merchandising, the company is posting heftier sales. Other Canadian Tire pluses include a strong balance sheet and, in its subsidiary, Mark's Work Wearhouse, a brand that's almost as well-known as the parent's.

Quebecor owns Videotron, a Quebec cable provider.

With the highest rate of subscription growth in Canada, as well as the highest rate of hookups to the Net. Yes, Rogers is a cable company every bit as good as Videotron. But it's a growth play with high valuations. So, because Quebecor trades at a discount and because we're value investors, QBR is how we've chosen to play Canada's cable sector.

STOCKS GAELEN MORPHET LIKES

Atco Ltd.
(ACO.X-TSX; \$48.04)
Phone: 403-292-7500

Linar Corp.
(LNR-TSX; \$17.10)
Phone: 519-836-7550

Thomson Corp.
(TOC-TSX; \$48.50)
Phone: 416-360-8812

Canadian Tire Corp. Ltd.
(CTC-TSX; \$92.40)
Phone: 416-480-3000

Quebecor Inc.
(QBR.A-TSX; \$45.40)
Phone: 800-567-7070