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Pembroke Virtual Lunch Summary
Jeff Tory: Chairman & Portfolio Manager, Pembroke Management

March 24th, 2020

My name is Ian Aiken and I'm the Managing Partner of Pembroke. I would like to welcome you all to the call. The purpose of this call is to provide insights that will be of help to you during these turbulent times and to share with you how we are positioning the portfolios for the eventual recovery of the economy and the markets.

The pandemic has had a dramatic and rapid impact on financial markets and on our day-to-day lives. I hope that you and your family stay safe and healthy during this challenging time.

While most businesses in Québec and Ontario have been told to stay close for the next two or three weeks, I can report that Pembroke remains very much open for business. As a financial services firm, we are deemed to be an essential service, but with social distancing in place, all of us are working from home. We are operating at 100% in terms of our ability to conduct research, manage the portfolios, access our systems, meet with each other and service our clients.

Many of you are likely interested in fund flows and I can report that in the past ten days we have experienced surprisingly few redemptions and have seen positive inflows into equities as clients rebalance to take advantage of lower stock prices caused by the tremendous uncertainty.

I can also share with you that I, along with other partners of Pembroke, had been putting fresh money into the funds that we manage. Why would we do that now? Because we remain confident in the long-term wealth creation opportunity offered by the companies that we invest in.

Finally, I can share with you that we have reassured all our staff that there will be no layoffs in 2020 as a result of the pandemic.

With that quick update, I would now like to turn the microphone over to my colleague of more than 30 years. Jeff Tory, who is chairman of Pembroke and a portfolio manager, who will make some opening remarks, and then answer some questions that have been submitted by e-mail.

Jeff Tory: Thank you, Ian. I am very sorry that I can’t do this in person, you know that we like to see you face-to-face and through thick and thin in the 38 years that I have been involved in the investment business, and the 33 years now with Pembroke, we have always tried to hold ourselves accountable to you. We have never been afraid to talk about the portfolios and to face the clients in tough times. It’s easy in good times when the portfolios are up. I am very happy to be here with you today.

I am going to make a brief presentation and then we will have a question and answer period. I am going to have my colleague Matthew Beckerleg, who is also operating from home like me, help me answer the questions that Ian Aitken is going to moderate.

To start off my remarks, this is now my 38th year in the investment business and I thought I had seen everything. I lived through many market cycles, multiple bear markets, but this is the first time that we've experienced, certainly me, a black swan where a truly unexpected event has wrought havoc on the markets. We have all been surprised by the rapidity and violence of the sell-off. It has been historic in terms of how quickly things happened and sadly there has been no place to hide in the stock market. I know that we are all going to have a bit of a statement shock when we get our statements at the end of March. It hasn't just been smaller companies that have been hurt. Blue chip Canada has been in a free fall. I looked at the stock charts of many of, what we think of the leading the companies, the banks, the pipelines and REITS, where people thought they were safe. It has truly been a brutal period.

It would be very easy to say to you that this is just an irrational selling panic that is being fuelled by 24/7 news media and all the short-term traders in the world. There is some truth in that, but I think we need to acknowledge to you, that the measures that are being taken at present to slow the spread of the disease, will have a significant negative impact on short-term economic activity and profits. To some degree the stock market is discounting what will be a very difficulty year in earnings in 2020.

I think that we are making a choice as a society to live through this temporary shut down to stop the spread of the disease, to save as many lives as possible. But we're being honest with you and saying that the outcome is uncertain and then, as portfolio managers, which just have to, as we always have, to live with uncertainty and we are managing accordingly.

As Ian mentioned earlier, the team is functioning very well together. We have had two meetings already this morning using Microsoft Teams. Modern communications technology has made this a lot easier and while we are not happy with what is happening in the portfolio, we are also super excited about the opportunities being created by great companies at depressed prices. As I said previously, with few exceptions, the bear market has not been restricted to smaller companies that some people think are riskier, the price declines of even the blue-chip companies in Canada,… and the decline has been breathtaking.

Why do we think the rate of decline has been so rapid? I think what is happening, is when you get into tough stock markets in times of stress, what I call the analytical self, the logical self who looks at numbers, looks forwards and makes projections, we stop looking at the facts and then when the more emotional self takes over, we respond to price movements. When I think back in my career:

- November 1987, about a month after the crash, small companies in the US fell precipitously creating an amazing buying opportunity.

- In 1990, in the depths of the recession in Canada, there were bargains. Ian and I were just three years into our career, we found probably six or eight career-making stocks at the time that went up. Some that 20, 30 or 40 times in the subsequent fifteen years.

- In 1998, the Canadian market fell 20%, investors thought the end of the world was coming.

- Then of course we lived through the tech wreck in 2001.

- Then in 2008, after the financial crisis, the same thing happened.

I think the first point that I would like to make is that in times of crisis, stocks get very cheap and investors get scared. That's just a fact. Then the second thing that I would like to say is that during these junctures, we have all made some of the greatest trades of our careers because even the great companies go on sale and create opportunities.

When I was preparing these remarks, I thought back to 2009, my colleague Matt Beckerleg and I were travelling in California. We were at a growth stock conference. We were amazed at how negative the sentiment was among our peers. The money managers were all worrying about redemptions or their business or their bonuses. The contrast was meeting with the companies. We found that a lot of the businesses were fine. The stock prices were down a lot, there is no doubt. Of course, there was stress in the system. There were questions about the availability of credit. By being at the table, by being gutsy, by staying at the conference, we made a bunch of great investments, a couple which Matt may talk about a little later.

Of course, we get asked by you in these times where there is lots of uncertainty, when we are under great pressure, when all stock prices are down, what are we doing to help you, to help the portfolios, help ourselves? The first thing, starting in early 2019, we became very focused on the balance sheets of our holdings. We had a feeling in our group that easy money, which some had thought was going to persist (I'm going to distinguish between low interest rates and easy access to capital) will when you go into a moment like this, finding fresh capital is not easy. We made a conscious decision for you and for ourselves, because we are the largest owners of these funds, to take the overall debt levels in the portfolio down. When you look at our portfolios compared to indices, we have significantly less debt on a portfolio basis than any of the indices, which if we're in a tough time, is a good indication of survivability as we get through this period of dislocation where some of the business will be closed.

The second thing we are doing for you, is that we have been in contact, over the pas three weeks, with over 70% of the portfolio already. As you know, most of the people running our companies are owners/managers, they are not thinking about their bonus, they are thinking about the shareholders. That's gives us great comfort. When you think of how you endure a period of uncertainty: you have a good balance sheet and you have someone steering the ship that has great alignment with us. What we hope we get out of that, is that at these critical moments, they will make the right decisions even if it means in the short term cutting some staff to ensure survivability.

One of the points we want to make to you about what we do at Pembroke, which is investing in these smaller and medium-sized companies. They are not quite such complex businesses, they area easier to wrap your mind around the scope and scale of the business. This sometimes provides false comfort because they have the will to believe. What we are doing in the process of talking to them is we are asking them what are you doing to adapt to this new work environment? How does it affect your business in the short-term?

This is certainly very sad for the overall economy and some of the private, smaller companies are going to really struggle because of a lack of access to capital. We have been making these calls and we are trying to give ourselves comfort that these companies are prepared to deal with the challenges facing them now.

What's important for you to understand, is that when you look across the board at stocks, all stocks are down. This is the moment where we have to uncouple ourselves from whether we have an emotional attachment to a stock or whether we are making or losing money on the stock. This is the moment where all capital is scarce, and this is the moment when the experienced investment team has to be at its peak level of rationality to make triage decisions among companies. All companies are down. There has been, I think no safe haven.

In this morning's investment meeting, we made the decision to sell two or three of the smaller holdings, that were a little less proven and maybe a little more exposed to the business cycle. Then we are going to take that money, where they then were, either lagging fundamentally or they haven't performed over multiple years as stocks, and we're going to redeploy the money into the longer-term winners in the portfolio. History has shown, and I remember in the words of our founder Ian Soutar, and a lot of you knew him well, is that the stocks that act well and perform well during times of crises are the ones that will lead you out of difficult times.

The other thing that we are doing, which shows that we do not have our head in the sand, is that we are reviewing our research pipeline. The research pipeline is a collection of companies where we have done a lot of research, we've met people, we've prepared, but there was probably an issue around valuation in the last couple of years where we weren't comfortable getting involved. This is now creating an opportunity for us to circle back and revisit some of these holdings. At the same time, we are doing these maintenance calls to see how our existing holdings are doing, we are also taking the chance to revisit some of the pipeline companies. What I can tell you is that in uncertain times like these, when stock markets are down, we found all of these companies to be amazingly receptive to chatting with people. They view firms like Pembroke as long-term partners because they know that we are not an index fund, a hedge fund or short-term traders.

What I want to leave you with is that we own a portfolio of high-quality growing companies. They should react well coming out of the crisis. What we do want you to know, to re-enforce, though is that we are not experts in understanding when the market will turn. If you look back and look at the shapes and patterns of all the market crises going back to the 1920s, you can probably say that we are within hailing distance of the bottom, but we don't know. Peter Lynch had a funny saying that "It is always darkest before dawn, but sometimes it gets darker". I think we all have to realize that the stock market could remain volatile for a period. But what we, really are excited about is that the strong financial positions of our companies help them survive the dislocation and also give them strength to go on the offensive when the smoke clears.

Active management has been under siege for multiple years. We think this is actually a time where active management should shine and while it is a trying time for us as portfolio managers (it's not much fun opening Bloomberg every day), we also have great confidence in our owner managers who will make informed decisions to preserve and enhance shareholder value. When you think of your asset allocation, your exposure to what Pembroke does, we are super excited about our exposure to innovation and the disruptive companies. What has happened in the interconnected world, which has caused some of the down swing, but the global markets that many of these companies address, creates opportunities for much longer runway for growth then may have existed before if you were looking at a small cap company that was dedicated only to the Canadian market.

While we are scared about what's going on and of course we are very sanguine about the fact that it is an uncertain time, the news flow probably will get worse as it relates to unemployment and then certainly the volume of sick people. The stock market is a strange animal in that it discounts the future.

As I have observed these past few weeks, I don't think I have ever seen investors sentiment shift so rapidly in my career. This shift made me think of Warren Buffet's words, which I looked up, when he said: "Be fearful when others are greedy and then be greedy when others are fearful". I think this is not the time to give up on equities, and some of the questions will address asset mix. We remain super optimistic at Pembroke. Having lived through multiple cycles, the ingenuity of the world, what's going on in terms of people trying to find solutions for the disease is encouraging and these things eventually do pass. It doesn't mean that there won't be some pain, but we are very confident that our portfolio of well capitalized growth stocks will come out of it fine.

Ian Aitken: Thank you, Jeff. We now have an opportunity to try and answer a number of questions that have been posed by clients who have sent us e-mails. Where we had multiple questions that were similar, we tried to combine them together. Jeff is now going to be jointed by Matthew Beckerleg, who is a lead portfolio manager at Pembroke, who joined the firm back in 2005. If Jeff can't answer the question then Matt will try.

Q: Ian Aitken: The market is down because of the economic impact of the virus but why is the market so volatile?

A: Jeff Tory: There are a couple of things at work.

- When you're dealing with a global pandemic where we haven't actually seen how this will play out, it is the uncertainty that is weighing on financial markets. That would be number one.

- The second thing is in the last two or three weeks the markets have frozen up a little bit, and there hasn't been as much liquidity as there might normally would have been. What it leads to is, at the margin, exaggerated price changes as people want to buy or sell.

- Then the third thing, which is more complex and would require a longer discussion. There are a lot more constituencies in the market that have shorter term time perspectives. There are not as many long-term holders so you have people at the margin, creating disturbances with their buying and selling, that would be the machine trading. There have been liquidations happening in some hedge funds where people have to sell because they have to sell, not because they want to sell. I think that's why it's so volatile. I would imagine that with little bit more clarity on the timeline of things the volatility would settle down, but I think that volatility will be a feature for the next few months for sure.

Matthew Beckerleg: I think it is also worth mentioning that Ian Soutar, one of our founders, mentioned during the 2008-2009 financial crisis, when people were panicking and criticizing the stock market as a place to invest your money, one of the points that he always made was that at least the stock market was open and you could access your money. Many people have investments in private businesses or have personal needs and the stock market is one place where you could always go and get your money. Sometimes during crisis like these, when people rush to cash or rush to liquid assets, the stock market is somewhere they can access money.

Q: Ian Aitken: How is the current situation different than 1929?

A: Matthew Beckerleg: Many people have started to fear right now that COVID-19 will result, not just in a recession, but that perhaps even a depression. That has started to be talked about, certainly in the popular media, and that is not a word that should be used lightly for anybody who has studied history because there was obviously enormous suffering for a number of years as a result of the Great Depression. While we are living through very uncertain times right now, it is also important to remember that there are critical differences between how the economy and how society is structured today versus how it was in 1929. Now we have coordinated and aggressive actions of central banks around the world to maintain liquidity in the system, that is absolutely critical. You have seen extremely aggressive action, especially on the part of the US and European central banks. We have massive stimulus programs being developed and implemented in some countries. They have already been announced in the United States. They are still debating the plan, and it is always a painful process, but generally we can count on them coming to some sort of reasonable resolution to get money into the economy. Perhaps even more importantly, we have a well-developed social safety net in much of the western world at least, and in some large Asian countries as well. And all these factors make a comparison to 1929 very difficult. That gives us optimism that things won't go that far. There are too many safeguards and too many social safety nets in place for things to get as bad as they did in 1929. We just don't think it's a fair comparison. Also, so I don't go too long here it is also worth mentioning, and I will probably mention this a couple of times on this call, we have a lot of confidence that health experts around the world will develop a treatment eventually, even a vaccine that will put this health crisis behind us. In the case of the Great Depression, it was unclear how to get out of the Great Depression once it had started. They did not have the tools. They did not have the knowledge at the time to act appropriately. In the financial crisis, there were people questioning whether we would get out of that situation. In this case I think the end is clear and it is known, it's just a question of time and effort and we will eventually get those treatments and the vaccine that everyone is waiting for.

Q: Ian Aitken: What can we learn from the great financial crisis of 2008-2009?

A: Matthew Beckerleg: I started in 2005, so I am 15 years into my career, investing in public equities. Before this I worked, in private equity, this is now my second major crisis. I certainly did not expect to be living through two so quickly in my career. I would argue that this even more of a Black Swan than the financial crisis of 2008-2009. It is certainly not something that any of us had expected or had modelled. When we look at the investment opportunities, while history never repeats itself in the exact same way, history does not repeat verbatim, but certainly does rhyme and you know there are comparisons and lessons that we can draw from the 2008-2009 financial crisis. From an investment perspective, I think we learned in 2008-2009 just how much balance sheets do in fact matter. Companies forced to take outside capital, whether it is equity or debt financing, dilute shareholders at the bottom of the market and often see very weak recoveries in their stock prices when the world does eventually right itself. As Jeff mentioned, we were already being very strict on balance sheets, but we've taken that a step further as a result of the COVID-19 crisis.

We also learned that long-term powerful secular trends continue once the crisis subsides. Some trends in technology and healthcare, for example, that were in place in 2007 continued to apace in 2010, 2011 and 2012. We don't expect major trends that were in place to be materially altered by this difficult period, just like they were not by 2008-2009 financial crisis.

As growth investors we are also looking to identify those trends and to find companies that can take advantage of them, and we did that in 2008-2009 and we are doing that today as well.

More broadly, and Jeff touched upon this, we learned to stay true to our process. During the crisis of 2008-2009 we stayed in touch with our companies and we made sure that we were backing well-financed growth businesses. We effectively just stuck to our knitting. Being calm and working effectively together as a team we made some great decisions during that difficult period that helped our clients recover nicely from that crisis.

I would just end by saying that we also learned that while the light at the end of the tunnel seems very dim while you are working through a crisis, it is there, and it is shining. These crises do end, and the world does move forward. It is always difficult to know when you are in the middle of it. History has shown, whether it is world wars or major flus, the world does eventually recover, and the world does move forward, so if you are looking back to history, history will guide you towards being optimistic at this point.

Q: Ian Aitken: You say that the portfolio is invested in high-quality growth companies. What can you tell us about the characteristics of the portfolio to support that?

A: **Jeff Tory:** We are obviously constantly faced with explaining how we differentiate the portfolio we are running against the option of just buying the index. We do this very interesting exercise where we take out seven key criteria that we think matter to the long-term performance of the portfolio and then we roll the portfolio up and compare it to the index. We look at the US, Canadian, the dividend portfolio and the concentrated portfolio on that basis and the portfolio is cheaper or the same value as the index in all the cases, it grows its earnings faster, so the price of growth is cheaper. It is less volatile, similar to less volatile, has a higher return on invested capital or equity, much less debt and importantly in terms of how we look at things, higher inside ownership.

As we mentioned, we have very limited exposure to energy, both in Canada and the U.S. None in the US, very small in Canada. We don't have a lot of airlines, so it is a pretty high-quality portfolio. When I look through the portfolios, I am pretty excited about what we own, and they do fit the criteria of what is a Pembroke stock.

Q: Ian Aitken: Given that you run the portfolio on a fully invested basis, how do you take advantage of market drops like the one that was just taken place? And how do you go on the offensive to take advantage of the crisis?

Jeff Tory: This is when you have to be strict on capital allocation within the portfolio and basically how we keep score is earnings per share, cash flow per share growth and then long-term return on capital and then on a lagging basis, share price performance. Because everything is down a lot, this is a time when you have to be ruthless. You can't personalize the stock ownership and you have to say “Hey, this company's not cutting it and I'm going to roll it into the good ones because everything is on sale”. We call it a competitive force out. Every company has to compete for capital at this time. All capital is scarce.

Q: Ian Aitken: Another Energy related question. The price of oil has collapsed. What is your exposure to Energy in the portfolios in Canada and the US?

Matthew Beckerleg: I can handle that, and I'll be very quick this time. We have no direct exposure to Energy in the US portfolios. We have one energy company in our Canadian portfolios. It's extremely well financed, sitting on a mountain of cash. And well positioned to perform even without with low oil prices. But we have very minimal exposure. There's obviously always indirect exposure.

Q: Ian Aitken: Here's a tougher one. What is the appropriate asset mix now for a 30 year old or for a 60 year old client?

Jeff Tory: I want to take that. There's a great author who wrote the book The Money Game. In the book Jerry Goodman, said the stock market is an expensive place to get to know yourself. So, what I would say for the 30-year old is, the 30-year old has a long time-horizon. The 30-year old, assuming that they're responsible and they save a little money every year, can dollar cost average and so they should be excited now if they have some money coming in because this is a chance to buy the funds or great companies at a lower price. But then at the same time, they do have to be respectful of the fact that, independent of age, the volatility in the stock market is not for everyone.

The 60-year old is slightly different because if they are living on the money then it is more of a challenge. Long-term rates are low so that investments don't produce much. But yet at the same time dividend yields look very juicy right now, if we're not headed into a Depression. So, I think the challenge is to revisit how they felt through this bear market and previous ones. Spoiling your quality of life, if you can't sleep because you're worried about your portfolio, or if you are worried that you your portfolio will go to zero know. then you have too much equity.

My partner, Scott Taylor, gave me an interesting article about market volatility and Ben Graham talked about the fact that if you're in the stock markets, you need to expect that every so often, once every five years or 10 years, there will be a downdraft. Ian Soutar used to say: “don't be in stocks if you're not willing to accept a 30% decline”. Well, we got it. This is where you work with your advisor to establish an asset mix that works for you. The asset mix doesn't just come from something out of the air. It comes from reverse engineering what your needs are and what your capital needs are so that you can live with the market volatility.

Q: Ian Aitken: Given that the news flow could well remain negative, when is the right time to start buying?

Matthew Beckerleg: Our advice today is no different than it ever is. We always tell people not to try to time the market and our advice again today is to continue with that discipline in that view. It is all about "time in the market", setting disciplined long-term strategy and sticking to it, even when it's very difficult to stick to it when you're in a period like we're in today. While many of us believe that we're closer to the end of this crisis than we are to the beginning, at least in terms of market action, we never truly know how and when the markets will bottom. Again, you know the markets have a funny way of looking far into the future, so sometimes it is possible that we could find ourselves right in the middle of the worst part of this health crisis, and you look at the stock market and the stock market is moving up. I am not saying that will happen, but I'm saying that it is entirely possible because the market starts to look through the bad news towards better time.

If you have cash on the sidelines, we recommend simple dollar cost averaging. Slowly putting money to work in a very disciplined manner. But at the same time, it is worth noting that it is at times like these when great fortunes are made by people who have money to invest, who have patience and who have a long-term view.

Q: Ian Aitken: Why is it better to invest in smaller public companies now rather than in large cap companies?

Matthew Beckerleg: At Pembroke, we have a bias towards investing in small caps. That is what we have been doing since 1968 and will continue to do going forward. It is during periods like these that we think you know best opportunities present themselves because the volatility that you see in the marketplace is not reflective in our mind, in many cases, of the true underlying long-term fundamentals of the businesses that we invest in because of factors related to liquidity and we touched upon that at the at the beginning of the call. Sometimes small companies can see their stock prices decline more sharply than large companies, but that has nothing to do with the underlying fundamentals or the long-term opportunity that these companies offer. So it is during very uncertain times like this that we take comfort in the fact that our businesses are very easy to understand, have clear exposures that we can evaluate and decide whether we want to maintain or whether we want to increase or whether we want to decrease and have clear risks that we can evaluate. In the case of many large companies, they have multiple divisions, millions of global customers and so it becomes very difficult to know where their true risks lie. To a great a great degree, they become black boxes when companies become extremely large. It is worth noting that our companies grow faster and as Jeff has just said have better balance sheets than the major indices and that gives us great optimism. Optimism about the fact that they will emerge from the uncertain environment on an even better footing than they went into this crisis.

I will end by pointing out that if you'd known before coming into this crisis, that we were going to go through a crisis like we're experiencing right now, you would have reduced your exposure to equities and certainly reduced your exposure to small cap equities. It's worth highlighting that in nine of the last 10 recessions, small companies outperformed large companies coming out of the recession. Our view would be that you don't want to give up now, this is the wrong time to do that.

Q: Ian Aitken: What do you expect a recovery to look like, and will the world be different after this crisis?

Jeff Tory: That looks like a whole other conference call. Simplistically, some businesses will rebound very quickly and then others it will be more of an “L” shape and at some level consumer behavior might have changed for awhile. I think that assuming credit stays available and that the unemployment shock is not too terrible, animal spirits are such that economic activity will recover quite quickly. But that within industry groups, there probably need be some changes. More money is going to go into health care, preventive health. We're all doing pretty well working from home, so you might argue that businesses will look at the size of their offices over time, maybe do more hoteling like many of the consulting firms and accounting firms do. If there's a wave of short-term defaults, that's going to have some impact on banks and anybody in the lending business. I was thinking of one that kind of makes me smile. There's still something like 40 cruise ships that can dock. When people think of cruise ships as giant Petri dishes, they are not going to rush back onto cruises.

Certain businesses will start to look more valuable. People providing bandwidth to any form of business or home will benefit in terms of how we're all communicating. The data volumes have gone through the roof. There are lots of opportunities to look at in terms of secular changes and make a few shifts and profit from the changes.

Q: Ian Aitken: We have a question here with regards to fees. Will the decline in market-value result in a change in the fees charged for clients who drop below certain thresholds?

The answer is absolutely not. You probably know that if the value of your relationship with our firm is either above one million or above five million, you qualify for a lower fee. Clients who were at five million and as a result of this correction in the market are now below five million, your fee is not going to be raised. So, rest assured about that.

Q: Ian Aitken: Pembroke’s strength has been the thorough attention given to detail on companies you invest in. The shutdowns will almost certainly change circumstances at these companies. Travel is off. Communications have become more difficult. How exactly does Pembroke proposed to deal with this problem?

Matthew Beckerleg: This is one of the advantages of investing in smaller businesses. And again, by smaller we still mean multibillion-dollar businesses in most cases, but not multi-hundred billion-dollar businesses. Well, we're not traveling right now. We clearly can't travel but communications with the management team have actually not been difficult at all. As a result of this crisis, we've been talking to our company more than ever or more frequently than ever. In fact, we have sort of internal goal of speaking to every single one of our companies. We started that over the last couple of weeks and are getting towards the end of that process now. So, we've been leveraging amazing technology. We've made investments as a firm in new technologies that improve communications between portfolio managers, when we're all working from home and those investments have also helped us communicate effectively with the companies that we invest in. As Jeff mentioned earlier, were speaking to companies frequently were assessing their persistency, their balance sheets, and their ability to go on the offense right now. We want to hear that companies can take advantage of weakened competition to make investments with a long-term view. And do M&A that makes them even stronger coming out of this. While it is frustrating not to be able to travel, we have been in constant communication with our companies.

Q: Ian Aitken: Here's another question that applied to some people on the line, but not everyone. For those of us who are forced to take money out of a LIF or RIF, there is a concern that withdrawals are based on 2019 fund values. As the funds are much lower now, to preserve capital, should we delay withdrawals?

I hope everyone has noticed that the government has allowed you to reduce the minimum that you withdraw from a LIF or a RIF. If you don't need the money now, that's probably a good idea. We would advise people to dollar cost average in reverse and to take the money that they need out of their account over the balance of the year.

Q: Ian Aitken: What are the opportunities that might come out of this environment? How can we grow out of this?

Matthew Beckerleg: We have a colleague who reminds us to never let a good crisis go to waste. It is a reminder that there are always companies that are able to actually come out of these difficult periods in better stead then they went into them. It is difficult to believe, but it happened in 2008-2009, and we believe that will happen again. Broadly speaking, we see three types of situations. Delayed purchases with customers, whether it's businesses or consumers, opting to delay some of their purchase decisions. Long-term trends: companies that are in front of large long-term trends that are being temporarily disrupted, but which we expect to resume and then companies that will actually benefit from a crisis like the one we're seeing. I will now give an example of each.

In terms of delayed purchases, we have an investment in the US in a company called Globus Medical. Globus Medical makes components for spine surgeries. They were also the first to market with a robot for conducting spine surgeries robotically, rather than manually by hand. While we expect that some hospitals will put off the purchase of these very expensive robots while they deal with the COVID-19 crisis, we don't expect the trend towards using robots to change in the spinal surgery world over the next 5 to 10 years. We expect that that trend to continue and at the same time clearly there are people who have elective back surgeries or had elected back surgeries lined up. They will be pushing those off, but they will come back to get them done when it's safe to do so. I've had back surgery and I've had enormous back pain in my life, so I can tell you that you might be willing to delay the surgery, but you're certainly not willing to put it off forever. Globus is an example of a company that we expect to see growth slowdown here temporarily; but expect pent up demand to have a significant effect on their future revenue and profitability over the next couple of years.

An example of a company in front of a long-term trend is Gentherm. Gentherm makes heated and cooled car seats and are the leading manufacturer of these products in the world. We invested in them in 2005. We expect car companies to remain focused on improving the consumer experience. We don't expect that trend to change. We expect competition between the car companies to keep driving them to offer more and more features to their customers. At the same time, Gentherm’s heating and cooling systems are much greener and much more efficient than traditional heating and air conditioning system. With a big push to deliver these services with a more environmentally friendly focus, we don't expect the long-term trend to change.

And then finally, there are companies that will benefit from this. There is a company in Canada for example, called Kinaxis that has incredible software that helps people manage their supply chains on a real time basis. There has been enormous disruption to supply chains around the world as a result of COVID-19 and Kinaxis is communicating to investors that, while there could be a short-term disruption or slow down in terms of the implementations, as their clients work through the implications of the COVID-19 crisis the demand for their product is expected to increase. Not wanting to let any good crisis go to waste, we are looking for companies that we think will see, on a long-term basis, uninterrupted demand for their products.

Ian Aitken: We have received quite a few questions related to the fixed income portfolios and how people should be looking at the different types of bonds. I can report that we're not going to answer those questions today because we will be hosting a conference call with Canso Investment Counsel on Friday. It will be focused entirely on fixed income portfolios.

Q: Ian Aitken: So next question. Is it a good time to be buying high yield dividend paying stocks?

Jeff Tory: There was a great strategist that had a saying “that more money is lost reaching for yield than at the point of the gun”. And so, as I look around Canadian dividend paying universe right now, and on Saturday I went through the Globe and looked at all the quotes and the dividend yields. There's some very, very attractive juicy dividend yields. The problem with the knee jerk rush to buy the high yielding stocks is sometimes there is a message in there about the sustainability of the dividends. This is a good time to be looking at the long-term record of the company in terms of the cyclical record paying dividend. Have a good look at payout ratios, so companies where the payout ratios are below 50. The dividend could take a fairly significant earnings decline before it was at risk. But because there is no doubt that many companies will cut their dividends to conserve cash, so it is a time for high-quality research. Someone made the point to me about the Canadian banks that since 1992 only one Canadian bank has ever cut its dividend and that was after they made a bad investment. So, unless we're headed into a housing/financial crisis in Canada, it's probably a better bet that you know they won't cut their dividend, but I can't forecast that. It is a good time, but it is also a time to be very careful and to really understand what you're buying, not just knee jerking into the higher yield.

Q: Ian Aitken: Are smaller public companies riskier than larger companies?

Jeff Tory: Well, I'm probably biased because I have been doing this for so long, but when I have watched all the various cycles in stock market, in the economy and in business, when things turn bad many of the larger companies end up being riskier than the small companies, because there's either a lot of debt or they weren't run by an owner manager so that they weren't responsible with capital etc., etc. But smaller companies often have narrower business models so that's a bit riskier. Below a certain market cap size, probably the talent pool is not as deep. But when you have people running businesses, signing the front of the cheques and not the back, we think that this alignment actually makes, on a long-term basis, the companies less risky. My colleague Andrew Garschagen, in his concentrated fund research, has identified a single factor that seems to correlate with long term outperformance, and it is alignment. I will say that smaller stocks could be more volatile. Sometimes, I might say that they have somewhat narrower business models, so that exposes them to a little more business risk. But in general, they haven't proven to be a lot riskier when they're well financed and run by sensible people. So, you look at what's happened in this last two weeks in the Canadian stock market, some of the blue-chip stocks have gone down as much as anything. It's been shocking.

Q: Ian Aitken: How has the GBC Global Balanced Fund performed year to date, and how are you adjusting asset allocation in that fund?

The global balance fund is down 19.9% as of yesterday, which is in line with the benchmark. This is a fund that has a mix of fixed income securities and equities. The standard mix would be 70% equities and 30% fixed income. On January 22nd we went to 65% equity, 35% fixed income due to concerns over valuations and as the market value of equities has fallen in the past weeks, we have been re-balancing that portfolio, selling fixed income to buy the stocks as they get cheaper. We're currently at 67% equities and 33% fixed income and we're heading back to 70:30. If the sell off becomes more extreme, we have the latitude to go up to 75:25. So that is where we are with the Global Balanced Fund.

Q: Ian Aitken: My thinking is that over the last 90 years that whenever the market has fallen 30% or more it has recovered within 12 to 18 months from its low too to a new high. Would your team think that this is likely to happen again once the Coronavirus has been resolved either by a vaccine or our habits?

Matthew Beckerleg: So, in other words, will the market hit new highs? I think it's impossible to predict that and if anybody could see the future, then maybe they'd be very wealthy. They certainly wouldn't need a job. So, it's impossible to predict. But I will say, that we would have never thought, after the 2008-2009 crisis, that we would have gotten to where we were before this Coronavirus hit. There were many market watchers and very credible investors that were predicting sharply lower returns going forward as a result of the financial crisis. It's difficult again to know how we will come out of this current crisis. If you take the view that we will eventually move forward, but it is worth noting that we have falling interest rates, we have massive stimulus coming from governments around the world, and we have these powerful technology trends, all of which combined to give us optimism that our companies will be bigger and more highly valued in the future than they have been in the years past. Now, does that happen in six months? Does it happen in a year? Does it happen in two years? That's impossible at this point, you know. As this virus passes, there is no reason to think that we can't move forward economically and as we move forward economically, we would expect the stock market to be dragged along and for the increasing size and profitability of our companies to be reflected in higher stock prices.

Q: Ian Aitken: Any comments from either of you regarding how politics is impacting the efforts to respond to the virus in Canada or the United States?

Jeff Tory: They said that they are within the five-yard line on the agreement in the US and that is why the stock market is soaring today. What we are underestimating today is, if we're going to stay in the shutdown mode, just how large the fiscal stimulus is going to need to be to keep things working until we get through to the other side.

Ian Aitken: Thank you Jeff. I hope you found this call helpful. A replay of this call will be available shortly and we do apologize for all those who were not able to connect live to this call as there were a limited number of lines available. I would like to thank Matt and Jeff for their presentations, and I would particularly like to thank all of you, our clients, for your continued confidence in our firm during these uncertain times. Feel free to reach out to me via email or by phone if you have any questions or comments. So, with that, our first virtual lunch conference call comes to an end and I look forward to hosting more in the days and weeks ahead. Thank you very much, everybody.