



**We are here**

30Sep09

## **To my Partners:**

You will notice a couple of changes with this quarter's report. I have added a section called "What we have been up to" in order to give you an idea of the things we are doing. I have also tried to ask myself some of the tough questions you may be thinking.

You will also find enclosed a copy of our revised monthly price email. If you wish to be added to our email list, please contact Diann at [diann@mcelvaine.com](mailto:diann@mcelvaine.com).

**Q: *I am extremely concerned with the continuing under performance of the Trust. I was reluctantly willing consider 2008 as a write off, but 2009 is shaping up to be at least as bad - relative to the TSX (trailing in the double digits). I am looking for more information to help me decide whether to continue investing in the Trust.***

**A:** I know one of the reasons you invested with me is that in the past I have managed to protect our downside. I apologize for letting you down in 2008 and giving you an outcome different from what you expected of me.

I realize you would have expected more of a bounce this year as the market rebounded especially given how much we were down in 2008. I estimate we have rebounded about 27% from February while the TSX/S&P Total Return Index has rebounded 43%. Looking at our holdings, I continue to believe we still have some "bounce" left but I understand you may be tired of me making such comments.

If you recall I said there were a couple of reasons for our underperformance:

1. Impact of specific investments

I estimate since June 2007 about 70% of our net loss was due to the following 4 securities: Citadel Broadcasting, Canwest, Rainmaker, and Glacier Media.

Canwest and Citadel will not be a negative drag going forward. We have sold our entire Citadel position. We have also sold part of our Canwest position and the balance has only a nominal value in the portfolio. I had underestimated the financial risk in these two holdings.

We continue to hold Rainmaker and it represents about 5% of assets. Rainmaker does have some significant issues which we are working through. The people are good but the environment is tough. I am currently Chairman.

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We have added slightly to our Glacier Media investment. It represents about 13% of our assets. I think it is a cheap stock run by people I respect. It is very cash flow generative, has a high return on capital and low capital requirements. Glacier also has a number of opportunities for strategic and operational growth. In other words, while the performance of this stock hurt our results over the last 2 years, I think it is worth a lot more than where it is trading.

## 2. Portfolio Structure

Our large position sizes mean our performance is very dependent on a few securities. For example, Glacier Media and Indigo have not really moved in 2009. I have met with both companies recently and feel good about our investments.

In retrospect, I realize I have held too few securities so am broadening our portfolio somewhat. I do not intend to hold 100 stocks but believe our best performance came when we had a slightly wider portfolio.

The purpose of the above comments was to show I have identified shortcomings and taken action to improve our results. I established the Trust in October 1996 so have been managing it for just over 13 years. I am proud of the performance of the first 10 ½ years or so to June 2007. We substantially outperformed the indices over this period. I have been embarrassed by our performance since June 2007 and apologize for the anxiety and loss of wealth I have caused.

**Q:** *My spouse/partner wants to redeem his/her account. I don't think it's the right time to sell, but what can I tell him/her to help him/her reconsider?*

**A:** I often get asked, "Why should we invest with you?" I am not much of a salesperson but the key points I think are:

- I have been doing this for a long time. Without a doubt I have had some bad years but my good years outnumber my bad. I am confident in my abilities.
- This confidence is backed by a personal commitment. I have all of my investments in our stuff.
- We have taken action to correct the reasons for our underperformance.
- Because of the performance shortfall, our fees are relatively low. In fact, I would suggest at this time they are significantly lower than most retail mutual funds.
- The Trust has a tax loss carryforward.
- We have had good returns this year from a number of our positions including Sotheby's, GMP Capital Trust, Canaccord Capital and more recently Livingston International which just received a takeover bid.
- We own a number of interesting companies.
- Finally, and I do believe this is important, my name is on the door.

**Q:** *I don't think that you should try to explain away poor performance. Writing that you feel that our stocks are "cheap" doesn't mean anything, every value investor thinks the same thing. Cheap just keeps getting cheaper.*

**A:** I agree, sometimes cheap just keeps getting cheaper but my experience is that price and cheapness do matter. If a stock doubles in one year that is great and you look like a genius. If it takes 3 years to double, that is still a 25%+ rate of return. If it takes 5 years to double, that works out to about 15% per annum. All of these are good outcomes but waiting can be both frustrating and boring. I hasten to add I realize you have been extraordinarily patient with me, thank you.

Going forward, by broadening our portfolio a little, we will allow for a better mix between the “bloomers” and the “incubators”.

**Q:** *I cannot recall you ever having as much cash as you have right now. Is this largely a defensive position relating to client losses, or is it a result of how you see the markets right now?*

**A:** Our cash holdings are about average. As of October 15<sup>th</sup>, we have approximately 18% of the portfolio in cash. Having said that, simply put, cash is a residual: what is left after all of our buys and sells. We sold a number of positions over the last quarter or so and hence our cash has increased. In the short term, I would expect our cash to decrease. We tend to find things to do in the fall especially as this is the time of year when people clean up their portfolios and “kick stuff out”.

The bottom line is our redemptions have not caused us any difficulties this year. I would quickly add that we have had purchases too and I appreciate your trust.

**What we have been up to:**

Investments made during quarter: \$3,200,000

Positions in 5 new holdings were established in the quarter. Four of these were what I call “broken down trusts”. These are income trusts that have fallen significantly from their highs (and issue price). We were able to buy these at attractive prices because investors were selling either due to a distribution reduction and/or as part of a portfolio cleanup.

Subsequent to quarter end, we added substantially to one of these positions while we received a takeover bid for our holding in another.

Investments sold during quarter:      \$4,400,000

We eliminated our holdings in Sotheby's and in Citadel Broadcasting. We also received a pleasant surprise in the receipt of proceeds from our CINAR litigation stub. This stub had been carried at zero in the portfolio.

**Performance:**

The 30Sep09 price for the Series B units of the Trust was \$14.65. This represents a gain for the first 9 months of 2009, net of all fees and expenses, of 6.6%. During this period, the S&P/TSX Total Return index rose by 30.0%.

**Conclusion:**

As always, many thanks for all your support and confidence. I appreciate your trust.

All the best,

A handwritten signature in black ink, appearing to be 'Tim McElvaine', written in a cursive style.

Tim McElvaine  
15Oct09