

**We did it again!**

**We managed to post a positive return in an environment where almost every global equity market suffered substantial losses. The TSX lost 8.7% in 2011. European markets lost on average more than thirteen per cent and emerging markets such as China and India dropped more than twenty per cent. The S&P was one of the few equity markets to post a positive return in 2011 with a total return of 2.2%. The vast majority of equity managers lost money last year irrespective of their mandate. Our focus on absolute value once again held us in good stead.**

**The underlying cause of the disappointing returns during 2011 was the weak economic conditions in the developed countries. Global growth expectations have declined over the past year as market observers have come to realize that the two largest issues facing the developed world are not going to be quickly or easily resolved. Extremely high levels of government debt and high levels of unemployment in the United States and Europe are structural long term problems that will take many years to work out. As a result, economic expansion over the next several years in the developed economies will be modest.**

**Negative returns bring out all of the doomsayers and pessimists. The siren song today is that investing in equities is no longer a sound strategy for a myriad of reasons. The sovereign debt crisis in Europe has been a very real source of concern. Many are worried that Europe will not be able to solve its debt problems resulting in serious financial problems that could result in a severe economic crisis. Others point to increasing levels of debt in the United States and a gridlocked political system. A potential economic slowdown in China is another cause for concern. In addition, investors have been so traumatized by the events of 2008 and 2009 that for some equity investing has become inconceivable. These attitudes have become so prevalent that prominent long term value investors have now started to incorporate macroeconomic analysis into their stock selection process; a prospect that was unthinkable before the financial crisis of 2008.**

---

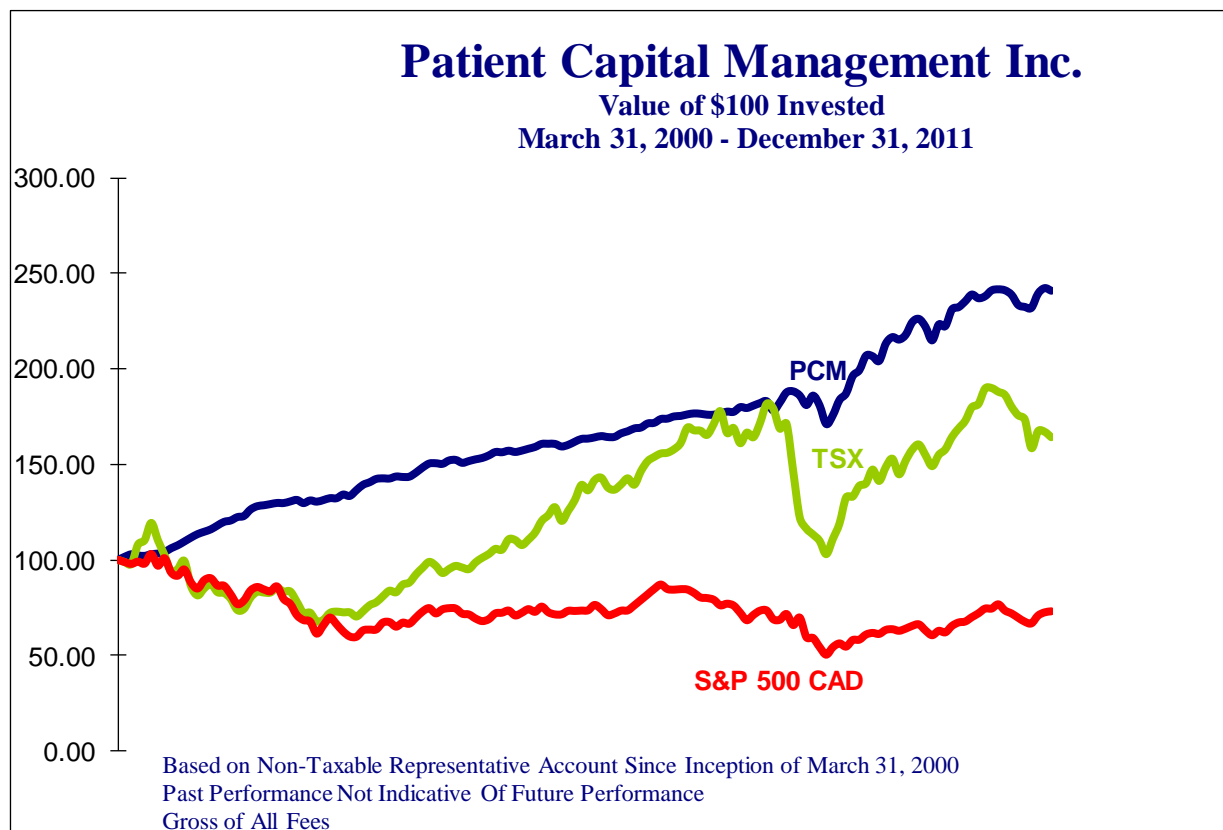
---

Being the stubborn lot that we are, we continue to exclude macroeconomic factors from our decision making process. Our focus is entirely on finding and purchasing high quality businesses trading at a substantial discount to intrinsic value. We refuse to tamper with a philosophy and process that has proven to be so successful for a very long time. Warren Buffet says it best in his 1994 Berkshire Hathaway Shareholder Letter:

*"We will continue to ignore political and economic forecasts, which are an expensive distraction for many investors and businessmen. Thirty years ago, no one could have foreseen the huge expansion of the Vietnam War, wage and price controls, two oil shocks, the resignation of a president, the dissolution of the Soviet Union, a one-day drop in the Dow of 508 points, or treasury bill yields fluctuating between 2.8% and 17.4%. But, surprise - none of these blockbuster events made the slightest dent in Ben Graham's investment principles. Nor did they render unsound the negotiated purchases of fine businesses at sensible prices. Imagine the cost to us, then, if we had let a fear of unknowns cause us to defer or alter the deployment of capital. Indeed, we have usually made our best purchases when apprehensions about some macro event were at a peak. Fear is the foe of the faddist, but the friend of the fundamentalist."*

We started PCM on March 31, 2000 at the height of the tech boom and with equity valuations at extreme highs. Over the past twelve years we have had several crises: a terrorist attack in the United States; two major wars; a loss of thirty per cent of the TSX Composite with the collapse of Nortel Networks; SARS; a large run up in commodity prices; a housing bubble and subsequent collapse; and, the worst recession since the Great Depression. Had one been able to predict these events in 2000 “run for the hills” may have been the strategy! However, as the chart below indicates PCM managed to earn an acceptable rate of return. Our returns were higher than both the TSX and S&P 500. Just as importantly, our cumulative returns have outpaced inflation since our inception.

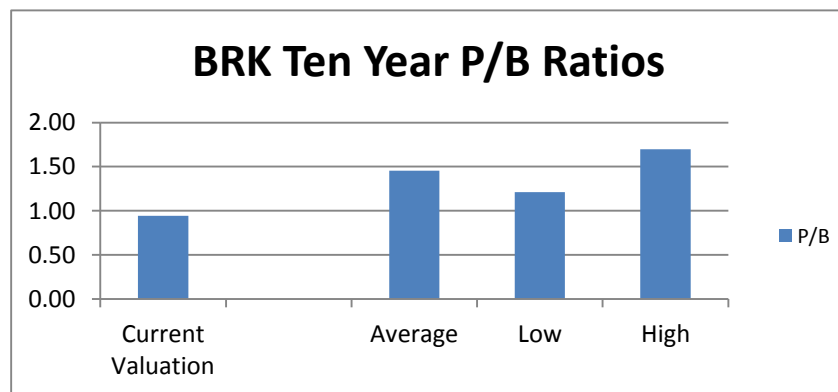
---



We were able to achieve these results because we focused on analyzing and valuing individual companies. We were not distracted by the noise of “big picture” forecasts. In fact, we buy when the investing macroeconomic environment looks particularly grim, when a specific industry is facing challenges or when a particular company has a temporary setback. For example the bulk of our investments were made during the depths of the financial crisis of 2009; perhaps the most severe economic crisis in many years. One of our most successful investments was National Oil Well Varco; an oil services company with significant operations in the Gulf of Mexico. We purchased the shares during the BP oil disaster when all oil and gas operators in the Gulf of Mexico were tainted with the same brush. We bought Bell Canada when the anticipated takeover didn’t materialize and the shares fell dramatically over a few days. Had we been concerned about the “big picture” we would have missed these great opportunities and many others like them.

Today as in March of 2000 the prospects for acceptable long term returns do not look appealing. However, we believe that our process supported by a track record of nearly twelve years, gives us the potential to earn somewhat higher returns than the overall market. Just as importantly, we have the potential to earn these higher returns with substantially less risk. Our optimism is supported by the quality of the business that we own in our portfolios and the prices they were purchased at.

As a result of last year's volatility we were able to purchase some very high quality businesses at valuations that offer the potential for substantial long term returns. For example, we purchased Berkshire Hathaway, the conglomerate run by legendary investor Warren Buffet. Berkshire Hathaway (BRK) is recognized as one of the highest quality companies in the S&P 500. The company's collection of businesses are for the most part leaders in their particular industries and generate substantial amounts of cash that is "sent back" to headquarters for Warren Buffet to reinvest. BRK's insurance operations are widely recognized as amongst the best managed and financially strongest in the world. The company also has a long record of growing and reinvesting its capital. Most importantly, as the Bar Graph below indicates we were able to buy this very high quality company at a discount to its book or equity value per share; the most attractive valuation that it has traded at since 2000.<sup>1</sup>



<sup>1</sup> Current Valuation Refers to P/B at Initial Purchase Price

**Our internal calculations indicate that from our initial purchase price we have the potential to earn a fifteen to twenty per cent compound annual rate of return over the next five years. Shortly after we bought the shares Warren Buffet announced that he believed Berkshire Hathaway shares were undervalued and that the company would buy back its own shares for the first time in its history!**

**Berkshire Hathaway has all of the characteristics that we look for in a business and then patiently wait to buy:**

- ✓ **Strong Businesses and Franchises**
- ✓ **Sound Balance Sheets**
- ✓ **Long Operating History**
- ✓ **Conservative Accounting Practices**
- ✓ **Free Cash Flow Generation**
- ✓ **Very Attractive Valuation**

**The one investment that many of you have asked us about is Nokia. The company's share price has declined and management has undertaken a significant restructuring. When we first analyzed Nokia we thought that the company had all of the above characteristics; in particular a very strong brand and excellent distribution capabilities in Europe and in the emerging markets. The company also had a sound balance sheet and a long history of generating substantial cash flows. At the time of purchase we estimated Nokia's value to be substantially higher than its share price.**

**We didn't anticipate the seismic shift in the smartphone market and Nokia's lack of a competitive product in that particular segment. However, the board has moved quickly to respond to the situation. A new management team was put in place and Nokia has partnered with Microsoft to launch a new smartphone based on Microsoft's mobile operating platform. Initial reviews have been positive and management's plans are well**

---

ahead of schedule. The company's balance sheet is still very strong and Nokia continues to generate excess cash. Management recently signaled a vote of confidence in the future as Nokia's dividend was increased. We still believe that Nokia's brand name and distribution capabilities are significant long term competitive advantages that will anchor the company through this important product transition phase. At current prices we continue to believe that the potential for substantial capital appreciation is quite high.

Our business has continued to grow quite strongly. For many of you this may be your first newsletter from us. We think it is important to reiterate PCM's Promise:

**We will Always Act as a Fiduciary**

**We will be Uncompromising in Applying our Investment Philosophy & Discipline**

**We will Invest Our Capital Along with Yours**

**We will Always Tell You What We Believe**

These promises based on investment and business principles have stood the test of time and served us well over the past twelve years. We think that they will continue to serve you well for many years to come.

We thank all of you for your continued trust and confidence.

Vito Maida

February 7<sup>th</sup> 2012.

---