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By Andrew Allentuck

Value Discipline

The Value Contrarian Canadian Equity Fund is producing returns for investors that, in the best sense, are right off the charts. For the year ended March 31, 1998, it had a total gain of 38.7 per cent, far above the Canadian equity fund median gain of 24.3 per cent for the period. It's a remarkable return not only for a fund that is barely a year and a half old, but one that is running on the oldest theory of asset management: finding stocks that others have missed.

Montreal-based portfolio manager Benjamin Horwood 40, is a lawyer turned investment counsellor. As president of Value Contrarian Asset Management Inc. Horwood is capturing a lot of attention among professional investors, not only because his performance is very good, but because his measured risk, the volatility of the fund is well below market average.

"I look for 'superior' businesses that generate lots of free cash flow and have high returns on equity together with modest debt and management dedicated to creating shareholder value. I also tolerate cyclical businesses, often in resources, if they can be bought below book value or at low multiples of cash flow."

Horwood sticks to his value discipline. As a result, he holds nearly a third of his fund's total assets in cash. "I wait for bargains. I know this is a good strategy because, as the fund's largest shareholder, I have the most to lose if I am wrong."

Currently in the portfolio are:

Westburne Inc. (WBI: TSE, 52 week high $19.50, 52 week low $ 15.05, cost $ 14.07, recently $19.00), a major North American distributor of industrial and construction supplies that Horwood bought because it generates significant free cash flow and trades at less than 15 times expected 1998 earnings. As a bonus, it has no controlling shareholder and is in an industry that is fast consolidating.

Perkins Paper (PKN: ME, high $7.70, low $6.00, cost $6.15, recently $7.10), a maker of tissue paper that sells in the steady consumer products market but is priced like a cyclical paper producer. Perkins' margins should increase over the next two years, Horwood says, because the firm, which currently processes 60 per cent of its paper into its own products, is moving to convert another 15 per cent to final product, raising margins in the process. The stock, currently trading at 10 times estimated 1998 earnings per share, should move up to the multiple of other consumer products firms, 15 times earnings per share, Horwood says.

Kaufel Group Cl.B (KGL.B: ME, high $4.80, low $2.65, cost $3.58, recently $4.65), one of the largest makers of emergency lighting equipment, was bought for less than book value. Currently, the stock sells for less than 10 times earnings per share. Higher earnings are coming in 1998, Mr. Horwood expects.

Harmac Pacific 8% Convertible Debenture (HRC.DB: TSE, high $113.00, low $97.50 cost $99.00, recently $98.00), a west coast pulp producer that Horwood bought at a recent low in the paper price cycle. "The beauty of our holding is that the debenture gives us 8 percent interest while we wait for the paper cycle to turn."

Philip Morris Companies Inc. (MO: NYSE, high $48.13 low $37.00, cost $12.79, recently $40.00), a diversified consumer products company whose stock price has been hammered to low levels. Philip Morris is trading at 12 times expected 1998 earnings while the Dow is trading at over 22 times earnings, Horwood says. "There is a risk in holding this stock, but at the current share price, we are being paid to take the risk," he says.

Outlook: "Our stocks, bought on strict value principles, are already priced for bad times. But we expect good things for these companies and figure that no matter what happens to the market, our portfolio should do very well."

Winnipeg-based author Andrew Allentuck writes extensively on financial matters.