

RULES #19 & #20: DID YOU MISS IT and ANCHOR THEORY

Instrument (Inception)*	September 2014 Return	Year-to-Date Return	Compound Growth
Venator Founders Fund (March 2006)	0.0%	21.0%	15.5%
Venator Partners Fund (July 2014)	-0.4%	5.5%	-
Venator Income Fund (August 2008)	-0.8%	10.0%	15.9%
Venator Select Fund (September 2013)	-1.3%	27.7%	44.9%
S&P/TSX Total Return (March 2006)	-4.0%	12.2%	5.9%
Russell 2000 (March 2006)	-6.1%	-4.4%	6.3%
S&P Toronto Small Cap (March 2006)	-9.3%	7.0%	2.2%
S&P 500 (March 2006)	-1.4%	8.3%	7.4%
Merrill Lynch High Yield Index (August 2008)	-2.1%	3.6%	10.6%

Our Funds "hung in there" admirably amidst a tough month for the market. While the S&P 500 managed to avoid substantial losses, the Canadian market and US small caps got hit pretty hard. I won't bother reciting why there was apparent weakness because all the explanations after the fact just sound like poor guesses based on variables that were in place months ago. Sometimes the market just goes down, with any minor piece of conjecture providing the 'catalyst', no matter how stale or benign the information may be. We had the benefit of one developing activist situation which positively affected both the Founders/Partners Strategy and the Income Fund (Epiq Systems), while a takeover on the last day of the month positively affected the Founders/Partners Strategy and the Select Fund (Move Inc).

With regard to Rule #19, we have a saying: anything that goes from \$1.00 to \$10.00 has to go through \$3.00 first. In other words, don't be so quick to sell that double, because you will never enjoy the benefit of the 10-bagger if you always sell just because it went up too quickly. On the other side, **Rule #20 regarding Anchor Theory** tells us not to discount the future potential of a stock just because it has doubled.

The simplest illustration is to look at any 'winner' you may have read about over the past several years and see that this is an important discipline at all times. For example, applying Rule #19 to Tesla, if you bought at \$30.00, would you have made the right decision to sell at \$60.00 if you thought it was going to \$200.00 (currently around \$250.00)? You would have missed the vast majority of the gains. Conversely, in applying Rule #20, was it too late to buy the stock at \$60.00, even though it had doubled in a short period of time? Apparently not as most of the gains were still in front of it. Any stock that goes from \$30.00 to \$250.00 has to go through \$60.00 first.

We have our own perfect illustration of the application of these rules in Boyd Group Income Fund (yeah, we reference this winner a lot, but it is a prime example of what we do well in terms of finding companies early, with no brokerage coverage, and developing an ongoing relationship with a smart management team). When we first bought Boyd in the \$4.50 range, it had already more than doubled as it was in the earlier stages of what was then a turnaround situation. But if the stock was going to go from \$2.00 to \$10.00 (our then target) it had to go through \$5.00 first, so the short term move up didn't discourage us from starting the position. As the company built out their business model we kept holding our position as our target evolved with the business

(when we initially bought it we were expecting EPS of \$0.60-\$0.80, now we can see \$3.00 in the not-so-distant future).

With the stock now over \$40.00, we are pretty happy we didn't succumb to the anchor theory (whereby your impression of something is anchored by where it's been, when what should be of greater importance is where it's going) and didn't hold out for a better purchase price. We are also happy we didn't take our profits at \$10.00, or \$20.00, or even \$30.00.

As a corollary, you also can't enjoy the full benefit of a 10-bagger if you need to 'lighten up' as it goes up in order to keep your portfolio from being too concentrated in a single stock. Generally, when an individual stock exceeds a 10% weight in the Founders/Partners strategy it comes under daily scrutiny in terms of its weight in the Fund. This often means that we sell 25%-50% of our holdings every time a stock doubles. In contrast, our Select Fund, which was designed in part with this dilemma in mind, can ride the full 10-bagger to its conclusion, even if that means that the stock in question reaches over 50% of the total assets of the fund.

As always, we reserve the right to change our mind.



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