

# NATIONAL POST

## It's a risky time for short sellers

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Short sellers have to be cautious in the face of the strong cyclical upturn in earnings and an equity market that is showing such vigour, says Peter Puccetti, chief investment officer at Goodwood Inc., a long/short hedge fund manager.

"But this bull market might not be sustainable given the array of economic headwinds that could batter the United States, and it might be appropriate to have a larger short position at some stage, just not yet."

Toronto-based Puccetti, who founded Goodwood seven years ago, says about 76% of the \$160-million in assets under management is in long ideas, 17% in short sells and the remainder in cash. The fund does not use derivatives, but can use leverage.

The Goodwood fund is value-driven. "We see ourselves as value managers that can also short stocks." Goodwood runs a concentrated portfolio, which currently has a distinct long bias. There is, says Puccetti, a modest short position in the S&P/TSX60 iUnits (XIU/TSX) a basket which represents the S&P/TSX Index. Units closed recently at \$43.68 and trade in a 52-week range of \$44.21 to \$35.10).

This holding represents a 5% weighting in the funds managed. There is also a modest short position in the Nasdaq 100 Index Trust (QQQ/AMEX) US\$35.23 (US\$35.84-US\$23.31) which tracks this tech index. "If the major technology stocks "start to break down, I would increase this short position."

"There is more upside in long positions," says Puccetti. "While, a short can yield up to a 100% return if the stock collapses, a long has the potential to offer higher rewards."

A long idea that is relative new to the Goodwood portfolio that Puccetti is selecting for the column is:

- Kingsway Financial Services Inc. (KFS/TSX) \$13.05 (\$19.60-\$11.29). "This stock is cheap." This North American property and casualty insurer specializes in non-standard automobile insurance. The company has delivered negative surprises year-to-date, says Puccetti, in that it had to take two additional charges against earnings for business it had written in previous years.

"These adverse surprises and reserve increases are part and parcel of this business," says Puccetti, "the Street was disappointed and took the stock down." The upshot of these additional charges, he adds, is that its Canadian business now has a good reserve cushion. Another plus, he says, is that the company is boosting its business in the United States, where the pricing environment for its products

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### IMAGES

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Yvonne Berg, National Post

"We see ourselves as value managers that can also short stocks," says Peter Puccetti, chief investment officer at hedge fund Goodwood Inc.

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has improved substantially. The United States accounts for 90% of its business. In June, the company completed a bought deal at \$16.70 per share, which provided a boost to capital. Goodwood participated in this issue and subsequently bought more in the market in the \$12 range. In September, the company delayed the offering of US\$50-million in preferred shares in the United States and will likely revive this shortly, he says. The stock is cheap both relative to the book value per share of the company and on a P/E multiple basis. His target price on the stock is \$24.

Another long that he is selecting for the column:

- Creo Inc. (CRE/TSX) \$15.77 (\$15.94-\$7.50). This stock represents a 3.5% weighting in the funds under management of \$160-million. Based in Burnaby, B.C., Creo provides digital solutions (both hardware and software) to the graphic arts business. Its products help to automate the pre-press phase of commercial printing. Goodwood has held this stock for more than a year. This is an earnings turnaround story, says Puccetti. Creo, which has a fiscal year ending September, should turn a profit in fiscal 2003 of US13 cents a share., he says. (The company reports in U.S. dollars). For fiscal 2004, the company could produce earnings per share in the region of US50 cents-US60 cents. The company has undertaken extensive cost cutting and the demand for its product should revive as the printing industry recovers, he says. Also, it has made some canny acquisitions in related fields that will boost revenue and its profit margins.

A smaller cap name that he has held for some time:

- Belzberg Technologies Inc. (BLZ/TSX) \$3.35 (\$4.70-\$2.60). Based in Toronto, this company provides Internet-based trading systems for the routing, execution and management of trades for financial institutions and brokerage houses in the United States, Canada and Europe. The bulk of its business is south of the border. The company's system is connected to all North American stock and option exchanges. The company recently announced that its U.S. transaction-based equities trading volume (generating revenue on a per-share basis) reached 263 million shares for the month of September -- a 42% increase over the previous year's high of 185 million traded in July. As Belzberg Technologies' volumes increase, profit margins will follow. The company has a "decent" balance-sheet with 80 cents per share in cash and no debt. The company could turn profitable in the first quarter of 2004 and produce EPS of 20 cents to 40 cents for 2004. It could be an attractive takeover target, he adds.

Puccetti continues to champion Extencare Inc. (EXE/TSX) \$10.62 (\$10.44-\$3.10), a Canadian company that runs long-term care centres and retirement homes in North America. He has held the stock for three years and its has quadrupled in value. The earnings, he says, are "finally coming through."

The company has \$2 a share in cash from its holding in Crown Life, which is being wound down. The company sold out its operations in Florida and Texas markets, which have a high incidence of liability suits.

His call is that this stock is worth around \$14, which includes the \$2 a share in Crown Life.

A long position where he has taken some profits recently because the stock has done "extremely well," is CanWest Global Communications Corp. (CGS.s/TSX) \$12.35 (\$12.70-\$4.11).

Fears concerning CanWest's debt levels are receding, which is helping the stock to rally. This media stock has been a major holding in Puccetti's hedge fund for some time.

