

“Grab that cash with both hands and make a stash” – “Money”, Pink Floyd

Initial Public Offerings (IPOs) were all the rage during the technology bubble. In 1999 there were a total of 492 IPOs in the United States totaling \$63.7 billion. In 2000, the number was 422 with a total dollar amount of \$97.35 billion. This list contained many names people will remember with disdain such as Priceline.com or Pets.com. They raised money because the market was hot and money was available.

This week we witnessed with mixed emotions memories of the internet bubble with the IPO of Open Table, which takes electronic reservations for restaurants around the world. The anticipated issue price was a range of \$12-\$14. The actual issue price yesterday was \$20; however, the stock closed at \$31.89. All of this hype for an entity that is barely profitable. Money can be raised and executives are “grabb[ing] that cash with both hands!”

We are seeing a lot of money raising in 2009, but mostly from existing publicly traded companies. However, the dollar amounts raised compared to the 1999-2000 period are significantly larger, but the number of companies to get to these large dollar figures are much lower. As an example, Bank of America has raised \$53.6 billion during the first five months of 2009! Citigroup has raised \$35.0 billion during the same period. The capital issued in the market is in the form of equities, preferreds, and bonds.

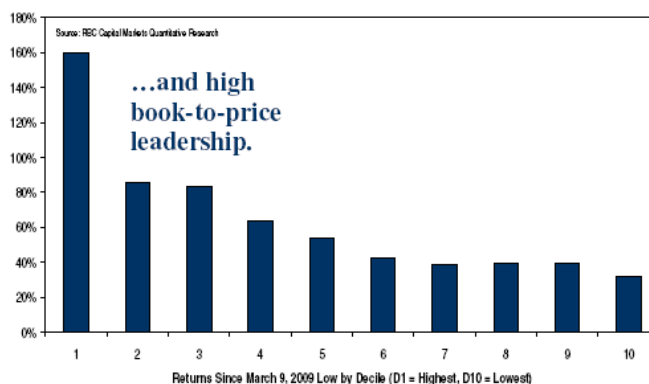
These numbers are staggering. Companies are issuing capital because they need it or companies see it as an opportunity to build up reserves. It is a situation like during a storm when the clouds open up and the sun shines through momentarily. Companies are realizing that if the capital market clouds close up again capital may not be available when it is most needed. Microsoft is an example of a company that does not need money but decided they might as well raise it under favorable terms. Microsoft has \$25 billion on its balance sheet, but decided to raise another \$3.75 billion “for general corporate purposes.” On the flip side is the Canadian company Teck Resources. Teck had purchased Fording Coal’s assets at peak prices and loaded up their balance sheet with debt. Teck was hemorrhaging as their

bridge loans were coming due later in the year and investors began to price in worst case scenarios in March 2009. The stock hit \$3.20. The clouds parted and Teck Resources was able to renegotiate its credit lines, sell some assets, and float some bonds. Current stock price - \$16.00 - a return of approximately 400%.

Would QV like to participate in stocks that move up 400% in two months? You bet! But there is a problem. We are looking for well managed companies that aren’t on the brink of bankruptcy. The upside in these risky stocks might be enormous, but the downside might involve a total loss of capital.

The market has rallied over 30% in both the S&P 500 and the S&P/TSX Composite since March 9, 2009. The bulk of this rally has occurred in those names that would not be considered high quality, such as Teck or Bank of America, which is up 350% from its lows in March.

Myles Zyblock, Chief strategist at RBC Capital markets, notes the stocks which have participated the most in this rally are the ones that are the most expensive, least profitable, and lowest priced. The chart below breaks down the TSX into ten categories. The category labeled one is the most expensively priced group of securities in the TSX. This sector is up almost 160% versus the least expensive securities which are up around 30%.



The companies which have the lowest profit expectations are also up substantially. As put perfectly by a few analysts “this is a mad dash for trash.” Although it is uncomfortable to watch the companies we don’t own outperform, we know that trading speculative securities is not a viable long-term strategy.