COLORFIELD CAPITAL

July 12, 2017

June 2017: Wherever You Go, There You Are

Performance: +3.36% **Benchmarks: TSX -0.76% (total return)**
TSX/Venture/RTY 50/25/25 blend: -0.55%

And here we are. It's been a while. Twenty-eight (?!?) years in the business, nine since beating the retreat from my last partnership (unfortunate but for the best for all concerned), seven since gaining a marriage and dog (decidedly in the plus column, I hasten to add), and three since losing dog (significant minus), and gaining another one (similarly major plus) in the interim, and as of June 1, 2017, Colorfield Capital has hung out its shingle to do whatever it is I do, more on which immediately below. Being childless and in any event unsurprisingly incapable of personally bringing one into the world, a comparison would be inevitably guesswork, but the simile seems apt, with a few differences in degree (less pain, more paperwork, similar expense). And as I write this at the end of the first month of operation, it is not without a degree of satisfaction and gratitude to those who pushed me forward (you know who you are) that I'm able to look back on the six months or so it took to get to the point where the virtual doors were flung open and the first tentative steps towards creating a portfolio began. So, that's where we've gone, and, by gosh, that's where we are.

Why me? Why yet another fund? I'm glad you asked. Aside from the obvious—and not nearly as flip is it sounds—answer that after spending 28 of my 33 years in the workforce in and around the securities industry there's really nothing else I'm qualified to do, I genuinely do believe that there is always room for someone with a focus on making people money to do just that. So, I am delighted and honored to present to you:

Colorfield Capital. For those of you for whom the name means nothing, color field (two words, yeah, but everyone's going to get it wrong and spell it as one, so this way they'll all be right) painting was a short-lived artistic school of the 1950s and 1960s, which one could think of as studied abstraction. Not, on balance, unlike what its namesake fund will be attempting to accomplish in the months and years ahead as we attempt to bring a generalist approach to small and micro-cap investing,

With apologies to the late Gene Davis

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focused but never blinkered, highly opportunistic but never speculative.

Finding the opportunity where others don't

Colorfield, to switch similes from art to baseball, will attempt to be a Wee Willie Keeler of the investment world, following his adage, "keep your eye clear and hit 'em where they ain't," wherever they ain't. And while the investment style won't perhaps hearken entirely back to Keeler's heyday during the McKinley administration, we will, to coin a phrase, do things the old-fashioned way. We continue to believe that there are many underfollowed and misunderstood opportunities out there to be found. By bringing a focus on uncovering these opportunities before most others do (because, among other things, it's a whole lot easier to be early than smart), managing risk carefully, and knowing the difference between taking intelligent risk and gambling and never, but NEVER, stepping over the line, we hope to monetize those opportunities. And with that I'll take your—OK, my—questions.

Will much of what Colorfield invests in be high-beta? Very likely so, though we expect that the risk will go down (and multiples go up) as the companies' strategies and tactics convert to earnings over time, and we believe that, at least for what Colorfield is attempting to accomplish, the ideal risk management practices are appropriate position sizing and using minimal leverage.

Where are we now? Given that July 1 was Canada Day, and the 150th anniversary of the nation, it seemed only fitting that Colorfield's initial influence paid tribute to the sesquicentennial by investing primarily in our neighbor to the north, despite the fact that the fund will likely be a rare investment vehicle that pays a lot of attention to Canada while almost entirely avoiding the resources sectors (for no other reason than focus—I've been in the business nearly 30 years and have done no energy or commodities and am disinclined to dilute my focus by opening that particular can of worms now). Well, that and the fact that there are several highly appealing characteristics to investing in Canadian small and micro-cap stocks at the present time:

1. Baby, Meet Bathwater. US investors appear to have lost interest in Canada several years ago when oil prices declined precipitously and my contacts in the Great White North™ continue to corroborate that that interest has not yet returned, though a deeply promising sign is that Canadian brokerage firms are having increasingly good schedules and interest when they bring managements down to the US.

2. For Sentimental Reasons. Anecdotally, the Canadian markets are generally considered to be even more sentiment driven than in the US, and sentiment turns slowly, meaning that there can be a longer window of opportunity to get involved with Canadian stocks before they take off.

Nat also loves Canada for sentimental reasons

3. *Just Plain Stability.* A huge amount of Canadian institutional investment continues to be centered on large financial institutions, which are inherently among the most conservative investors. The down side is that it can take them longer to get involved in interesting situations, leaving companies frustratingly undervalued for longer. The corresponding positive is that when they do take positions, they tend to be long-term-oriented, exceptionally stable owners.

All in all, then, at least for the foreseeable future, Canada will be a prime focus for investment opportunity for Colorfield, but should that opportunity appear exhausted over the longer term, the fund will absolutely look elsewhere, most likely in the Americas and Europe, as emerging markets, however exciting they may be, are by and large beyond your manager's field of experience.

So how'd it go in the first month? For a fund investing largely in Canada and which was looking to open positions in a difficult market, not badly. The TSE Index was down 0.76% for the month on a reinvested dividend basis, and Colorfield gained 3.4%. Foreign exchange gains accounted for roughly 1.6% of that increase, but although a conscious decision was made in the middle of the month to remove Canadian dollar hedges, we won't take too much credit for that, because nobody's ever going to pay me to be a clever forex trader (and if I ever sound like I'm going to try to be one, I would urge you to fill out your redemption form post haste). What looks to me like some curious end-of-quarter

selling in a couple unloved and thinly traded names may in fact have held gains down, but that's show-biz, and if correct, may have a corresponding positive impact on trading in the third quarter.

The big star of the month was a perennial underachiever that had been on my radar in my consulting business for a year or so, **Novadaq (NVDQ)**, a Toronto-based developer of innovative imaging solutions. NVDQ, which had slipped some time ago into the unenviable but not uncommon category of "perpetual opportunity," managed to get itself taken out of its (and investors') misery by getting itself acquired by Stryker at nearly a 100% premium to its depressed trading price. Unfortunately, it happened so near the opening of the fund that we had only built a 2.5% position in the name, but it's unlikely that it would have ever been too much more than that, and in a month when the primary benchmark index for the fund was down three quarters of a point, a 2.2% gain in a single issue was even more than usually welcome.

If there was a big loser in the month, I'm happy to report that it was a stock that was only an 80bp position (after monetizing a gain in mid-June), though I'm at least as unhappy to report that makes it about a 25bp position now. **Fenix Parts** (FENX), a company whose plan was to create a consolidation play in auto parts yards, had shown itself to be unready for prime time ever since its 2015 IPO. The company had experienced consistency only in its inability to file its quarters and annual reports in any semblance of a timely manner, but, having declined from nearly $10 to $1.50 in two years, and having received forbearance from its principal lender which showed no interest in owning the company, appeared to be priced as a decent warrant on the prospect for future righting of the ship. On June 28, NASDAQ's patience proved not in fact to be unlimited, and after several extensions the shares were finally de-listed, resulting in what is now a 70% decline in share price. The shares had actually appreciated nearly 20% early in the month, and the fund sold almost 30% of its position at a gain before the tsunami hit, but between realized and unrealized losses, the position cost approximately 60bp in June.

The book continues to be shaped, and we'll provide more detail on more positions in future months and quarters. Expect a short monthly letter and longer quarterlys, and more frequent communications as events warrant. I'd be more than happy to hear from any of you any time, so comments, compliments, complaints to john@colorfieldlp.com will be appreciated and responded to in kind (though to be fair, I probably won't answer a complaint with a complaint, but you never know).

With thanks for getting this far, and the hope that you'll come along for the ride,

John Elliott Ford
Managing Partner