SEVEN SUMMITS CAPITAL

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NOVEMBER 2017 INVESTMENT COMMENTARY

MAKING A CASE FOR INVESTING VERSUS JOINING THE HERD AND PLAYING THE MARKET

New clients of Seven Summits Capital are many times perplexed by certain portfolio decisions that appear at the onset to be ill-conceived and counter-intuitive. Most individuals are conditioned through financial media sources such as CNBC that the goal of investing is to buy the stocks of companies that are rising and making headlines due to their successes. This approach tends to provide instant gratification, and this gratification tends to reinforce taking such action over and over again. This is the very definition of momentum investing and a herd mentality. Momentum investing is by nature built upon the "greater fool theory," which requires that foolish behavior begets more foolish behavior where each person engaging in foolish behavior continues to do so long as others follow their lead.

The market by definition is the aggregate behavior of all investors, foolish and more foolish alike. The task of riding the hot stocks or playing the market requires an unrealistic assumption that you are not the fool and that you will know when foolish behavior goes too far. The problem with this strategy is that it requires one to be more of a behavior psychologist than an investor. Behavior psychology is an imperfect science under optimal conditions. Divining the underlying psychology of market behavior is far from optimal given that the participants number in the tens of millions and include natural persons with varying objectives, organizations and even computer programs. It is for these reasons that I give very little thought toward trying to figure out the market. Instead, I find security selection within the market to be a far more successful endeavor.

In September 2015 I was searching for attractive investment opportunities as I do on a continual basis. I start with companies and industries that I feel that I can understand. As usual, I identified several companies that I had personal experience with that have been performing very well, and their stock prices were indicating the market believed that the strong performance would continue for the foreseeable future. Two of those companies were Under Armor and Chipotle. I admired these companies, and I was a consumer of both of these companies' merchandise. I passed on investing in both of these companies at the time because their stock prices were not pricing in any deterioration in the hyper-growth rates that had propelled their stocks to valuation multiples which I feared were unsustainable. These stocks were universally lauded by market pundits and the analyst community was extrapolating that these companies' hyper growth rates would continue indefinitely into the future.

It is extremely important to remember that the current valuation multiples of a stock are not supposed to be a reflection of past growth rates, but instead, they are to be based upon a forecast of cash flows expected be generated by future growth rates 3, 5, and ten years into the future. Unfortunately, the shiny object that mesmerizes most investors is the recent historical growth rates and stock performance. Again, the greater fool theory coming into play.

As of September 2015, Under Armor stock had rocketed skyward by 133.5% over the previous two years. The company was a retail growth stock superstar and was universally loved because of its historical performance. Over the previous four years, its stock performance was an even more impressive 343%. On more occasions than I care to admit, I find myself regretting not having bought a stock like Under Armor at a point in time when it was smaller and potentially poised for spectacular growth assuming everything works out as planned. The problem with buying such a stock when it is an unproven small or mid-cap stock is that such a decision typically requires far too much uncertainty and speculation. As I continued my search for an attractive investment opportunity, I came across Garmin. Unlike Under Armor, Garmin's stock had lost 74.50% over the past two years, and the company was seen by most investors as a "has been." Garmin had made their mark in the U.S. as the market leader in dashboard-mounted GPS devices that had been rendered obsolete with the advent of in-car GPS systems offered by most auto manufacturers.

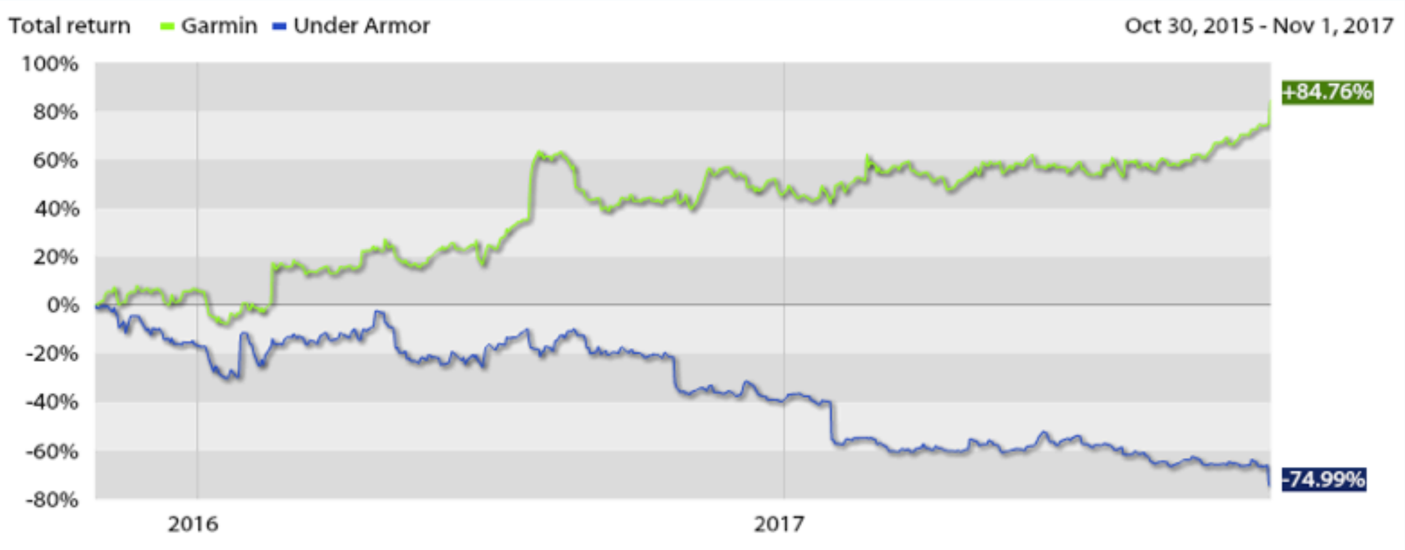
There was far more to the Garmin story than met the eye. The stock was selling at a very low valuation multiple at the time, its dividend yield was 5.50%, its debt levels were low, and cash flow was strong. As I came to understand the company better, dash-mounted GPS devices were just one of many navigation related devices that the company developed and sold. The company was a market leader in both nautical and avionic navigation and its wearable activity devices were the devices of choice for militaries around the world and serious athletes. A big growth initiative for the company was to use their expertise and success that they had in these niche markets and leverage it to gain greater market share at the high end of the retail activity tracker market which was a significant growth opportunity.

I made the first purchases of Garmin stock in portfolios in September 2015 at around $37 per share. My target price on the stock at the time was $52 per share, which met my desire to acquire new positions at a discount of greater than 30% to a 2-3-year target price. The bonus that came with taking this position in Garmin was the 5.50% dividend yield. In essence, investors were being paid a very attractive dividend yield to wait for the market to realize the unappreciated value within this company.

As usual, I did not pick the very bottom in Garmin stock when I made the first round of purchases. In January 2016 Garmin's stock dropped into the low 30's, or approximately 20% below where I first purchased it. I took this opportunity, not as one to lament about the price drop, but instead one to add to existing positions and lower the average cost of this investment. From January 2016 the stock price slowly climbed up to the target price of $52 and even exceeded that target in mid-2016, prompting me to selectively take some partial profits. However, I still really liked what I saw from the company, and I retained a sizable position in the company due to my continued positive outlook and the fact that the dividend yield remained above 4%.

Today, Garmin's stock is around $60 per share. Its dividend yield sits at 3.35%, however, at an average cost of $37.64, the dividend yield on the Seven Summits Capital holdings of Garmin is 5.40%. The stock, including dividends, has generated an aggregate total return over the last two years of 84.76%. Conversely, Under Armor has seen its stock fall 74.99% over the same two years.

(Refer to Chart on Page 3)



Currently the market has a very negative sentiment on Under Armor and the value of the company relative to peers presents what I see as an oversold opportunity. Approximately four months ago I began buying Under Armor stock. Again, I did not enter at the bottom, and I have been given ample opportunity to lower the average cost of the Seven Summits Capital holdings of this stock. I see a significant under-appreciated opportunity today in Under Armor. Unlike two years ago, Under Armor is now an almost universally hated stock because of its dismal stock performance of late. I don't know for sure that the Under Armor purchase will turn out to be as much of a success as the Garmin investment was over a short two year period. However, I do know that I am much more enthused with purchasing Under Armor at current levels than when everybody loved the stock at a much higher valuation. I believe that today's Under Armor stock price is more of a reflection of the negative sentiment caused by poor performance of the stock over the last two years than a reflection of the growth that the company has in front of it over the next three to five years.

I don't play the market or chase high flying stocks because I don't want to end up thinking that someone else is the going to be the greater fool and then finding out that all along I was someone else's greater fool. This is not investing; it is simply playing a game that is only occasionally won through the random attribution of luck.

By now the regular readers of this commentary know how I feel about the current broad investing environment. As with every market cycle that I have invested in, broad markets become much more challenging as they mature, as valuations climb and as investor sentiment becomes exuberant. However, with the approach that I take, opportunities to "zig" always exist when other investors "zag". Finding out-of-favor opportunities, under-valued situations, and a hidden investment opportunity is not that difficult, it simply requires doing the seemingly unpopular thing by looking forward and not backward to build one's thesis.

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