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EWING MORRIS & CO. 3RD ANNUAL LIMITED PARTNERS MEETING

Toronto Reference Library, October 15, 2014 – Toronto

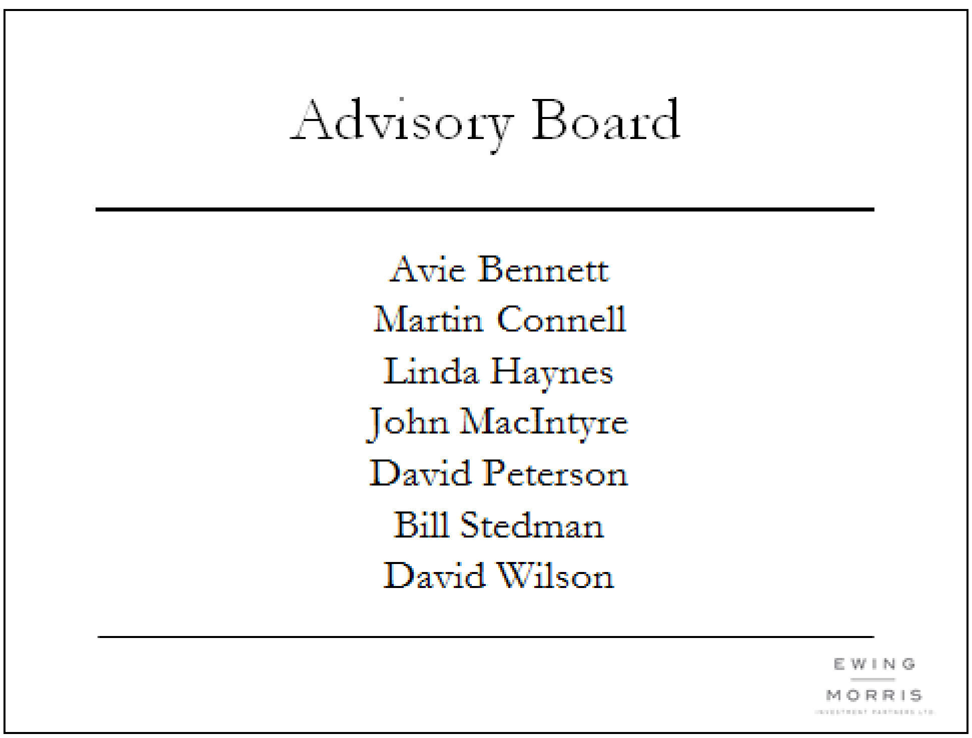
Remarks have been edited for clarity.

Darcy: It is wonderful to see so many people here - old friends and new friends. This is our third annual meeting and the numbers have grown. Every year when my father gets his invitation - he happens to be a limited partner as well - I get a phone call and he says, "I have two questions in advance of your annual meeting. What's for lunch and when is it over?" So if that is the standard of questions today, it should go pretty smoothly.

Before we get started, I wanted to make a couple of quick introductions; I think everyone here is familiar with John and myself. Some of you are familiar with Matt Irwin, but for those of you that are not, Matt is our third partner and he runs operations for Ewing Morris. He is also our Chief Compliance Officer and he is the defensive core of our operation. I would also like to introduce Jill Hamblin; Jill is our office manager and she makes sure that John and I get to our meetings on time with our shirts tucked in and our ties on straight. She also has a lovely British accent, so we consider her the Ewing Morris Moneypenny. Events like this do not organize themselves so thank you Jill. My mother-in-law, Linda, and Devin also had a big hand in organizing this. Lastly, I would like to introduce Alexander Ryzhikov - with a name like that, you would be forgiven if you thought he was the newest left winger for the Montreal Canadiens. He is our new investment analyst and we have known him for a number of years; he is a brilliant investor and we are absolutely delighted that he has decided to join us and I think everyone in the room should be pleased as well.

The outline for today is that John and I are going to give short prepared remarks; I am going to give an overview of the philosophy of our firm and an overview on where we have been, where we are going and then John is going to give a short presentation on our investment approach. Then we are going to open it up for Q and A. The real objective for today is to discuss what is on your mind.

Many of our service partners are here with us today and we believe that these guys are the best in the business.



We also have many of our Advisory Board members with us as well. They are all limited partners and all have a vast background of personal achievement in business and philanthropy. It has been great to have them as part of our team.

For the year to date, the fund has returned about 5% net of all fees and expenses. I think that the underlying growth of our businesses has been in excess of that number and we are happy to discuss that more. You will see that since we started in September 2011, it has been just over three years, the fund has returned, on a cumulative basis, about 45%, net of all fees and expenses; on an annualized basis that is about 13%. Our investment objective has been to compound money at 10-15% annually, doubling money every five to seven years. We are three miles into our marathon and we are on pace. I show the TSX and S&P 500 here, not because the underlying characteristics of those indices reflect the underlying characteristics of our partnership - in fact they are vastly different - but what they do signify are two well-known and widely-followed indices that reflect your opportunity cost of investment in the fund. As you can see, they have done quite well over the last few years. Over time, the long run average for both those indices is about 7%, including dividends. So if we are successful in reaching our investment objective over time, we should outperform those indices.

With respect to our strategy, John and I have never found terms like "value" or "growth" to be a very enlightening way to describe how someone makes money. In fact, I am not sure how you can have value without growth being part of the equation. So that is not the language we use when describing our strategy. What we use is the analogy of a sports playbook. The idea is that a championship sports team will have perfected and practiced a number of different plays, so when they get into a game situation, no matter what the defense does and no matter what the external factors are, you will always have a strategy to score. We have four plays in the Ewing Morris playbook. The first play is the Great Business. Those are investments in situations where you have a company with wonderful economic characteristics, sustainable competitive advantages and one or more compelling growth opportunities. John is going to speak in more detail on that play. The second play is what we call the Great Capital Allocator and those are situations where we are investing in businesses that have a great investor at the helm. Warren Buffet would be the archetype for that type of investment and I am pleased to say that there are probably a few of them in this room today. Actually I know there are a few of them in this room today! The third play is the Cheap Asset and those are businesses where the market value of a company is trading at a significantly lower price than what their assets would fetch if the business closed tomorrow and the parts were auctioned off. You can think of that as though we are buying dollars for fifty cents. It works well with businesses that have hard assets so we have made investments in companies with drilling rigs, timberland, helicopter fleets and things like that in the past. And the fourth play is shorting Broken Businesses; those are situations where we short companies that are in fundamental decline or failure.

Profit breakdown

as of September 30, 2014

Ewing Morris Playbook	Profit ($)	Profit (%)	Batting Average (%)*
Great Capital Allocators	11.4 million	66	100
Great Businesses	4.3 million	25	100
Cheap Assets	1.6 million	9	78
Broken Businesses	(3.2 million)	n/a	25
Total Profit	14.1 million		

* Percentage of investments with return > $0

Here is where we have made money by play. Since we started, the Great Capital Allocators have accounted for the bulk of our profit, almost $11.5 million. The last column from this slide is batting average and that signifies the percentage of investments within each play that we have made money on. So we have been batting 100% there. The second area that we have made money in is the Great Business, almost $4.5 million and again our batting average has been strong there. In the Cheap Assets, we have made a little bit of money, but the batting average has not been quite as good. In shorting Broken Businesses, we have actually lost money.

It is important to note that most of these are unrealized gains and losses. I think the number that will jump out at everyone is the Broken Business number. While that number is negative, I think that number could swing positive very quickly and perhaps sooner than we think.

The Big 5

* Investments with over $1m profit

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My mother-in-law told me that I should be quiet about our successes and trumpet our failures. This is the opposite of that; this is the Big Five. Internally we describe this as the Million Dollar Club. These are five investments that we have made over one million dollars in profit on and we can happily discuss those in more detail.

Portfolio Summary

as of September 30, 2014

Ewing Morris Playbook	% of Portfolio
Great Business	21.5
Great Capital Allocators	44.1
Cheap Assets	24.5
Total Longs	90.1
Broken Business	(15.3)
Hedge & Arbitrage	(1.9)
Total Shorts	(17.2)
Free Cash	9.9
Cash From Shorts	17.2
Total Cash	27.1
Net Investment	72.9
Total	100.0

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Here is where the portfolio stands today. You can see the Great Capital Allocators account for the bulk of the partnership assets - about 45%. I want to draw your attention to the free cash number, which is about 10% today and that is the type of cash that you would have in a long only portfolio. Hence, there is 10% of partnership assets that are at our disposal to make investments. The cash from shorts is about 17%. As a reminder, when we short businesses, it is the opposite of the old business adage, "buy low sell high". When we short, we sell high, we receive that cash on day one and set it aside in order to buy back those stocks at a later day and a lower price. That gives us total cash of 27%, which is a little misleading. I think the most important number there is the 10% free cash.

As a firm, we have three structural advantages that, regardless of how hard-working, smart or charming we may or may not be, give us a leg up in competing for results on behalf of our partners in the capital markets. Those three advantages are size, flexibility and focus. We run a relatively small pool of capital and that gives us the opportunity to take advantage of investment situations that the larger players cannot. There are certainly people just as capable as us to spot investment opportunities at Fidelity, Blackrock, RBC Asset Management, etc., but when you are managing tens of billions of dollars, it can be hard to move the needle with small cap investments. So we skew towards small cap investments in the fund to take advantage of our size.

The second structural advantage is flexibility. If you are focused on building a firm that gathers as many assets as possible, the most intelligent way to do that is to structure the business with a number of different funds and products. We call it the Baskin Robbins style of fund-for-every-flavor. If you run an investment business that has 25-40 different products, on sheer probability alone, one of those products is probably going to be doing well. So you will always have something to sell. However, if you are building a firm that is focused on investment results, which is what we are trying to do here, we think the most intelligent way to build that firm is to have a single investment vehicle but to have a flexible mandate within that vehicle in order to take advantage of opportunity wherever you may find it. That relates to market cap, geography, capital structure and the ability to short.

The third advantage is focus. We have no interest in watering the wine with our 100th or 200th best investment idea so we put a meaningful amount of capital behind our top investments.

So how are we employing these structural advantages today?

Size Advantage

as of September 30, 2014

	Ewing Morris LP	S&P/TSX Index	S&P 500 Index
Median Market Cap – Long	$516 million	$2.3 billion	$17.3 billion
Median Market Cap – Short	$1.2 billion	n/a	n/a

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Well, today the median market cap on the long side of our portfolio is just over $500 million and on the short side it is just over a billion. Both of those numbers skew much lower than the TSX and the S&P 500 median market capitalizations.

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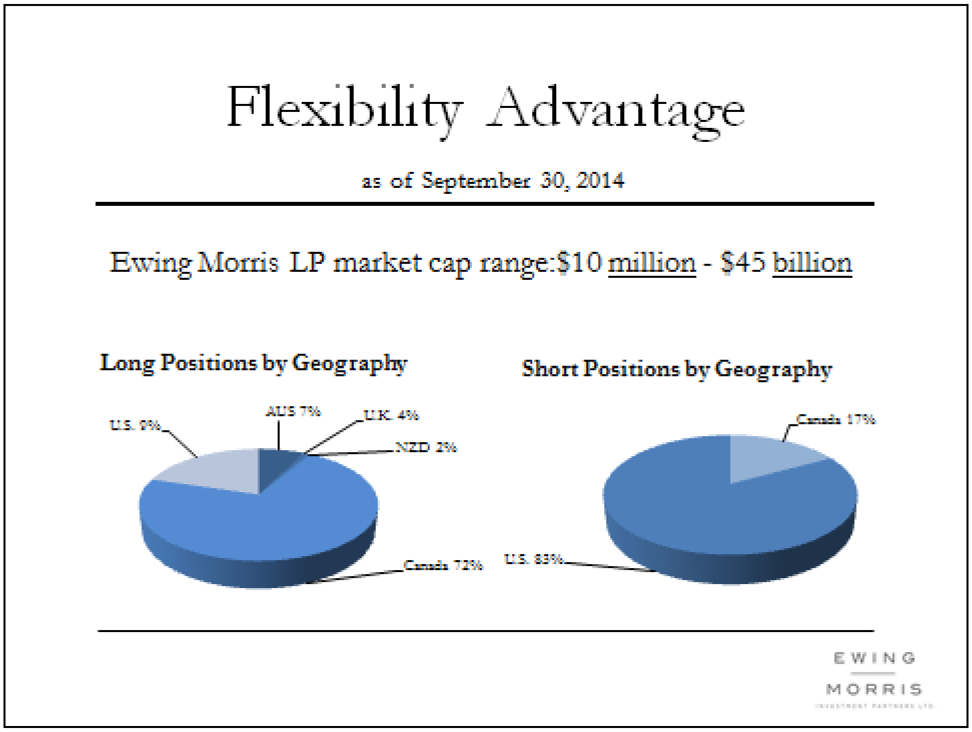

In terms of flexibility, today we own a $10 million market cap company and we also own a $45 billion market cap company. That is a range of market cap investments that I think is very rare in any single investment vehicle. Geographically, we continue to focus on North America as those are the markets that we know best. Just over 70% of the portfolio on the long side is invested in Canada and we have also been expanding internationally. On the short side, we skew towards the U.S. with 83% of our assets there

Focus Advantage

as of September 30, 2014

	Ewing Morris LP	S&P/TSX Index	S&P 500 Index
Top 10 Positions	80%	35%	18%

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And focus? As you can see, our top ten positions account for 83% of our portfolio. Contrast that with the TSX and S&P 500 index and it gives you an idea of the level of focus within the partnership.

Partnership Overview

as of September 30, 2014

Limited Partners	69
Mutual Fund Trust Investors	77
Firm Assets	$83,000,000
Management Ownership	17%

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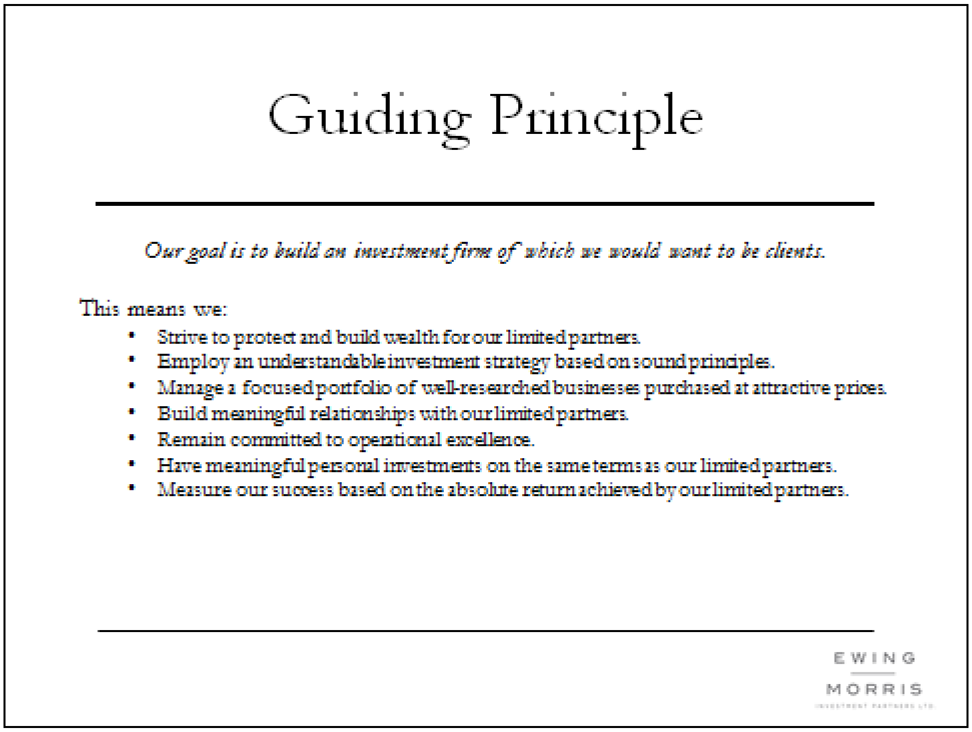
Here is where the partnership as a whole stands. When John and I founded the firm just over three years ago, we only had a handful of limited partners, we were managing about $5 million and we had a great story to tell about how we would build and protect capital. Fast forward to today and the family of partnerships has grown significantly and assets have grown to about $83 million. There is still a large insider ownership, so we continue to eat our own cooking.



Before I turn it over to John, I want to touch on the guiding principle of our firm. Ever since John and I had our very first breakfast to sit down and discuss the blueprint for Ewing Morris, the guiding principle was: "Let's build a firm that we would want to be investors of". Once we had that lens, it made a lot of the more difficult decisions that we faced, and continue to face, a lot easier. Furthermore, what stems from that vision, are these core principles. We strive to build and protect wealth on behalf of the limited partners without taking excessive risk, we employ an understandable investment strategy based upon sound principals and common sense, we manage a focused portfolio of well researched businesses purchased at attractive prices run by management teams that we trust, and we usually invest with the intent to hold for several years. We build meaningful relationships with our limited partners based upon candid communication, whether it is good news or bad news. We remain committed to operational excellence; things like accurate and timely reporting when it comes to taxes and performance. We all have meaningful investments on the same terms as our partners. And, lastly, we will measure the success of our firm based on the absolute net return that accrues to our limited partners over time.

Now, as much as we wish that the stocks in our portfolio, especially in the past few weeks, would incrementally tick up each and every day, we all know that the world does not work that way. The investment management business is tough and it is highly competitive - hard work and passion are mandatory. So while we cannot guarantee results, we can guarantee that these are the principles that will guide our operation and that we expect to be held accountable. With that said, I will turn it over to John and then we will open it up for questions.

John: In this setting last year, I spoke in great detail about the Great Capital Allocator play in the playbook. So this year I would like to talk about the Great Business play and tell you a little bit more about what we mean when we say we are making a Great Business investment. Before I start, I want you to pause for a moment and think of a company that comes to your mind when you think of the words "great business" - maybe even write it down - think about it because we are going to be coming back to it.

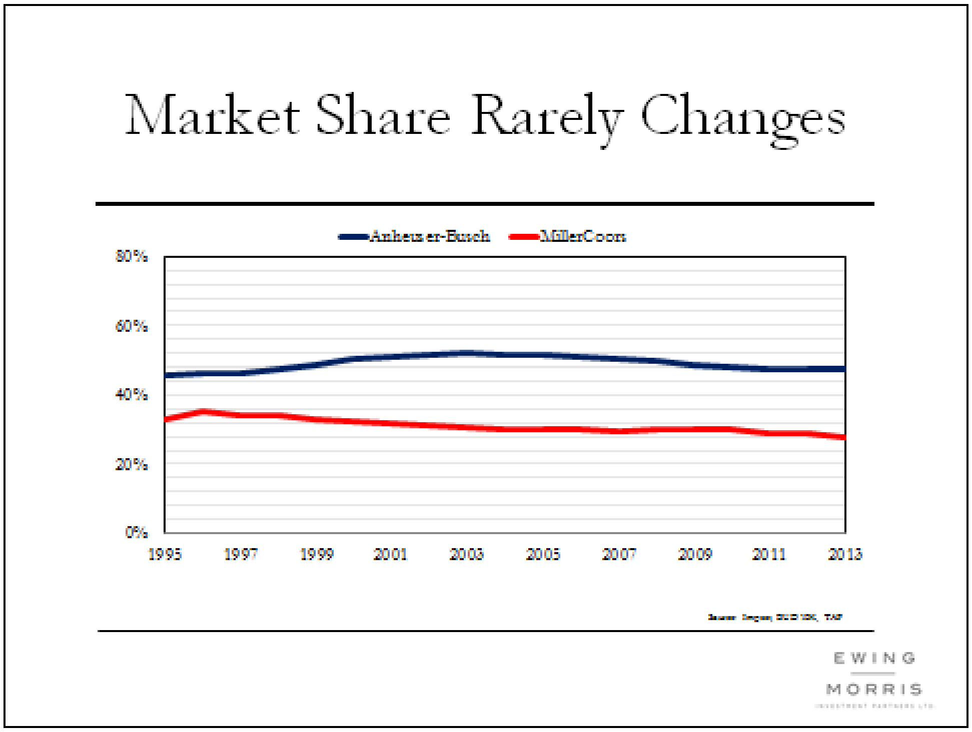
When we talk about a Great Business, we think it needs to have three characteristics. It needs to make a lot of money, it has to make more money tomorrow, and it needs to be able to keep making money for a long time. When we say a company makes a lot of money, what we really mean is how many dollars do the owners need to invest to get a dollar of profit back? That is what we call return on tangible capital.

When we say that a company needs to make more money tomorrow, what we really mean is: how long is the runway for growth in this business and how close is the company to the end of that runway?

And when we say that a company needs to keep making money for a really long time, what we really mean is that we think capitalism works and, when you make money, you tend to attract a lot of competition. A favorite example of mine is high-end burger restaurants. I am not sure that all of these people will still be in business ten years from now. So what we are looking for is a business with the economic equivalent of a moat around a castle, which keeps competitors on the other side.

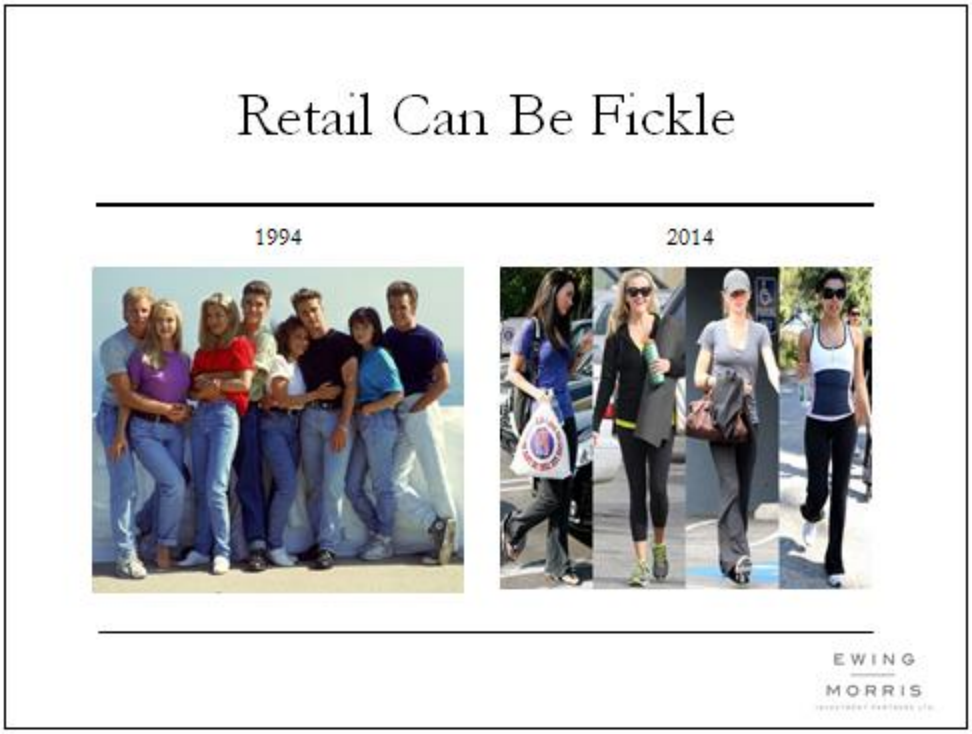
I think a really important point is that a Great Business needs to have all three. I had an old wrestling coach and, when people tried to make excuses or tell him how they came close to winning a big match or things like that, he used to remind us that close only counts in horseshoes and hand grenades and this is true with Great Businesses as well. Close is not good enough, you need to have all three. To make this a little more tangible and real, I am going to go through a couple examples of widely recognized companies and show you how they have two of the three characteristics and how missing one disqualifies them from the Great Business discussion for us.

The first company, Anheuser InBev, is the largest beer company in the world; maker of iconic brands such as Heineken, Corona, Stella and Labatt. Last year, Anheuser made $13 billion on operating profit on $43 billion in sales. To get that, they needed $8 billion of inventory, about $21 billion of fixed assets, which are things such as; breweries, tanks, delivery trucks and they get to offset that with about $16 billion of interest-free advances from their suppliers. If you add it up, they had about $13 billion invested in the company. You take those two together - it took $13 billion of assets to get $13 billion of operating profit, that's 100% return on capital and that is really good. They make a lot of money, number one. This slide shows the market share in the U.S. of beer over the last twenty years from 1995 to today.



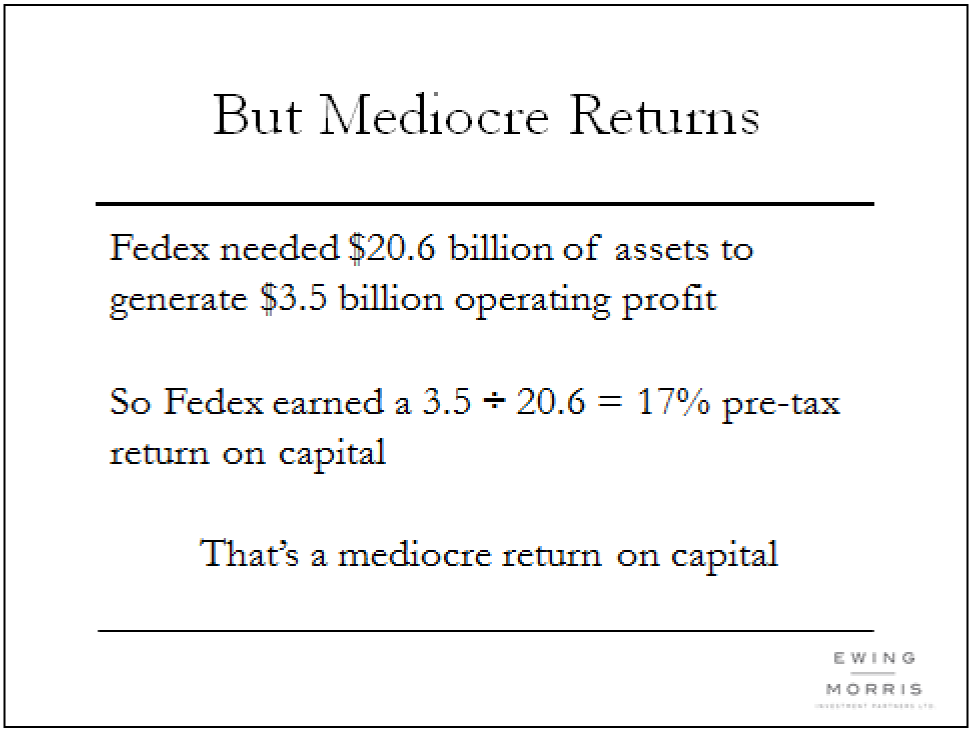
The blue line is Anheuser Busch and the red line is a combination of Miller and Coors. The key point on this slide is that essentially the lines are flat and the market share does not really change even over a long period of time. The reason market share does not change is, when you have iconic brands with big ad budgets behind them and you have pervasive distribution, it is really hard to compete with that. So beer companies have a wide moat and, if we came back twenty years from now, I would be very confident that Budweiser would still be the number one market share beer in the U.S. So they make a lot of money *and* have a wide moat. The problem for us with Anheuser is that there is not a lot of growth opportunity in this business. Consumption of beer is flat, maybe growing 1% a year and they already have 50% market share and we have seen that it is really hard to change market share in this business. The odds of Anheuser growing earnings 15% per year in the future are pretty low. They are close: make a lot of money, wide moat, but not a lot of room for growth. For us, Anheuser Busch is not a Great Business.

I am going to go to the second example which is Lululemon. They made about $400 million of operating profit, on about $400 million of assets yielding about 100% return on capital. Once again, that is really good - they make a lot of money. In 2008, Lululemon had about 50 stores in the United States and, if you come forward to today, it is about 180, so they have tripled in size – that is a lot of growth. But if you were to compare them to something like Victoria's Secret, which has over 1,000 stores in the U.S., you would realize that there is still a long runway for growth ahead for Lululemon. So we have growth opportunity. For us I think it is important to remember that fashion is fickle and we are not sure how popular yoga pants are going to be 20 years from now.



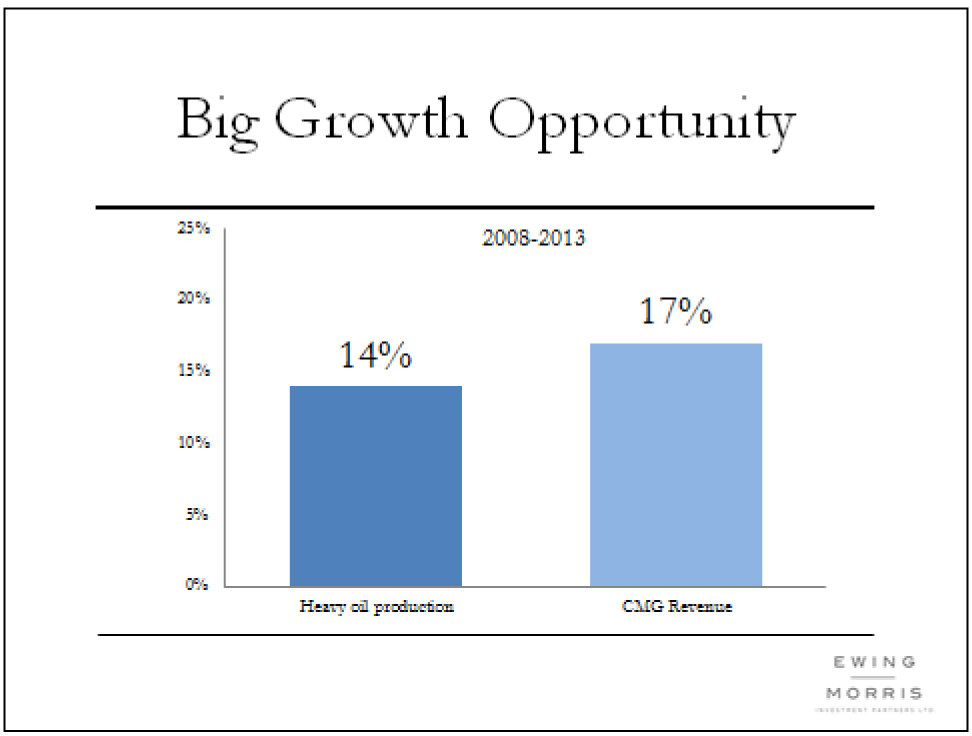
For that reason, we are not convinced that Lululemon has a moat. They make a lot of money; they have a long runway for growth, but I am not sure about the moat; they have two out of three. It is close but not a Great Business for us.

The third example is FedEx, again a widely recognized company. If you went back to 2003, DHL, a large German company, decided to enter the U.S. market to try and compete with Fed Ex and UPS. Five years later, they closed up shop and exited completely. It was a big disaster; they lost $10 billion in five years. If someone can spend $10 billion to try to compete with you and they cannot take a dent out of your business that is a really wide moat. If you think about the trends in e-commerce, that is a really big growth opportunity for companies like FedEx and UPS. There is a runway there, but the problem for us with FedEx is that it really does not make that much money.



It had an operating profit of about $3.5 billion on assets of a little over $20 billion for 17% return on capital. It is not bad, but it is certainly not the 100% that we saw with the first two companies. When you think about FedEx - wide moat, long runway but it does not really make a lot of money. It is close, but not a Great Business for us. The reason that I bring these three up is not to pick on these companies, they are wonderful iconic companies in the grand scheme of things and I think there is a good opportunity now to reflect on the company that you thought of in the beginning and test it against our three characteristics. Does it make a lot of money? Does it have a long runway for growth? Does it have a wide moat? Chances are that it is missing at least one of those three. If the one you had in your mind has all three, you should come tell us afterwards because I think we would like to buy it but it probably does not. Again that is not to pick on the company that you thought of, but I just wanted to remind you that these things are really rare.

But Great Businesses do exist and I am going to tell you about one that we found and have successfully invested in. The company is called Computer Modeling Group. Computer Modeling Group is a software company based in Calgary and they make reservoir simulation software which, in laymen's terms, the best way to think about it is the carpenter's maxim of, "measure twice and cut once". Reservoir simulation allows you to simulate twice or a hundred times before you drill a multi-million dollar well and figure out exactly how you want the well to be designed. Computer Modeling sells this software to big oil companies such as Shell, PetroCanada and Suncor and the software is particularly useful for drilling heavy oil which is what you find in the oil sands, but not isolated to Canada. If you think about the economics of a company like this, last year they made an operating profit of about $40 million. A wonderful thing about a software company is that you do not have any inventory; you don't need that many fixed assets. You have office furniture and a few computers. The real beauty is that you can get your customers to pay you in advance so that the customers, not the owners, are actually financing the company. The return on capital is essentially infinite here, so that is really good. They make a lot of money. I do not know if anyone has tried to switch banks before, it is a really painful experience. You have to set up all sorts of direct deposits and bill payments. That concept is what we would call switching costs. So the switching cost with something like reservoir simulation is a magnitude higher than switching banks. You have to retrain all of your people and these are highly skilled people that you are going to be paying a lot of money just to retrain on a new software product. You have to recreate the simulation model for each property that you have. It is a really expensive and time consuming process and, at the end of the day, you are not really going to be further ahead so companies are very reluctant to switch and, for that reason, we would say Computer Modeling has a wide moat.



In the last five years, heavy oil production in Canada has grown about 14% per year and during the same period Computer Modeling revenue grew at about 17% per year. You look out at the next 5-10 years and Canadian heavy oil production is expected to grow at about 10%. We do not know exactly how fast the industry will grow, but I believe it is reasonable to think it will be similar to the nine plus the ability to raise prices. This is a business that should be able to grow revenue and earnings at double digit rates for a long time. CMG actually does have all three; they make a lot of money, they have a wide moat and there is a long runway for growth. For us, CMG is a Great Business and it has also been a great investment. This is something that we invested in, in a large way from day one of the fund and the return to all of you has been over 100% in the three year period and we still have a big position today.

That really sums up what I wanted to say about Great Businesses. I hope that helps you understand a little bit better what we mean when we use the phrase "Great Business" and I hope it helps you understand what we are doing when we are making what we think is a Great Business investment. That is the end of the formal remarks for today.

Matt: Now we are going to take some questions; I will be moderating. I have prepared a handful of softball questions, but it is really a day about you and we hope that you ask the majority of the questions. Anything about the portfolio, the business, the current market environment are all on the table so fire away.

Question 1: How do you incorporate macroeconomic analysis into your investment decisions?

Darcy: In our approach to investing, there are things that are important and there are things that are knowable as well. When we think about the macro economy, it is important but it is essentially unknowable so we make no attempt to time the markets when we make an investment. There is a lot of smart macro-economic forecasters out there, but I do not think that anyone of them has made their way to the Forbes 400 list yet.

John: History will tell you that there is going to be a recession once every five or so years. If you buy a company that you expect to own for a long time and the success of your investment is based upon smooth sailing the whole time, you have set yourself up for disappointment. We are going to expect that there are going to be better years and worse years over the holding period of an investment and, if you go into an investment and handicap it with that in mind, it does not really matter when the bad years hit. If you have built that into your thought process during the research period, then you will be able to sleep at night and you do not need to worry.

Darcy: In the heart of the 2008-09 meltdown, Jamie Dimon, the CEO JP Morgan, said his daughter came home from school one day and said, "Daddy, what is a financial crisis?" He replied, "Honey, it is just something that comes along every 5-7 years". I think there is a lot of truth to that. We cannot forecast the timing but we can prepare accordingly for a financial crisis of some sort every five to seven years.

Question 2: What have you been doing given the sell-off in the oil related stocks?

John: So I think that if we were to look at what we have done in relation to some of the energy related companies that have sold off in the last few weeks, we have added to almost all of those positions. There are some really talented executives of medium sized oil companies that I have admired for years and the stock prices were not at levels that I thought were all that attractive that have found their way into the fund in the last couple of days. I think that the environment has created an opportunity to make the portfolio stronger than it was a month ago.

Darcy: We were out in Calgary last week and we met with four CEOs of companies that we are invested in and, while there seemed to be a lot of fear out there, it was not evident in the managers that run our businesses. They are looking at this as an opportunity as well.

John: One last thing that I would like to add on, when we make an investment in an energy-related company, it is almost universally because of the people running it and not because we have some particular view on oil. A lot of the best business talent in Canada has gravitated towards the energy industry and if we look at the energy related companies that we are invested in, they all have outstanding balance sheets, run by terrific people. If oil prices stay low or get lower and stay there for any prolonged period of time, these are companies that have the balance sheets to withstand that and the type of people who should be able to make the most of that opportunity. If oil prices stayed low for an extended period, I would be surprised and disappointed if these companies had not each made a wonderful acquisition in a period such that they would come out on the other side a lot stronger. That is what you get when you are investing behind great people.

Question 3: What are your thoughts on industries that stand to benefit from lower oil prices such as transportation?

John: We think oil should track the marginal cost of production over the medium to long term. Today that is somewhere between $80 and $100, probably closer to the high end. Investing in something that only benefits when oil is at $70 doesn't make sense to us because I think it's unlikely oil will stay there long enough to have an impact. But there are a few companies in the portfolio that would benefit from lower oil prices. We don't own them for that reason but they create a natural hedge. One example would be a company called Boyd Group which owns the largest chain of collision repair body shops in North America. When oil prices are low, people tend to drive more and the number of accidents you get into is more or less a function of the amount of time you spend on the road. It is probably not good for society, but there will probably be more car accidents, all else being equal than if oil is high. That would benefit Boyd's business. We do not own it because we think that is going to happen, but it is a natural hedge when you look through companies in the portfolio and think about how things like oil prices impact them - both good and bad.

Question 4: You walked us through about what makes a great business, but how does valuation figure into your decision to hold or sell stocks? You might have a great business where valuations have run-up to an unreasonable level, what do you do then?

John: Valuation matters a lot and you cannot own them at any price. I think walking through our history with Boyd probably helps you understand our thinking on that. When we first found Boyd in late 2012, we had done extensive work on it. We were quite attracted by the industry and the people. One of the biggest uncertainties with it was that there had been a founder/CEO who appeared to have had a meaningful impact on the business, but had left the business about a year prior, in 2011. The subsequent CEO had also been in the company and had been the right-hand man all along. But it was hard to tell from the outside how much responsibility was assigned to each one and how much of a negative impact the founder being gone would have. We started off with a 2% weight with the view we needed to meet management and we would come back from meeting him in Winnipeg and it will either be a 0% weight or it will be something like 5%. We go and see him, feel more comfortable with him talking the talk but you still do not know - 5% weight seemed reasonable at that point. From there forward, the stock went on a huge run and, at that point, we still loved the business just as much as we did before, but we did not love the price nearly as much, so we trimmed it from 8% to 5%. The stock kept going up and we trimmed from 5% to a 2% weight and the stock kept going up and so this is one that we still love, but the price is not great. If we found a Great Business at a much more attractive price, we would switch, but I think our experience with Great Businesses is that they tend to surprise you to the upside and they tend to figure out better things to do. You really want to be a reluctant seller of these kinds of things that is why it is a 2% weight and not a zero today. That is the way we think about valuation and the life cycle of a Great Business investment. I think that you want to have a lot of money behind them when you find them, but it is not just a binary decision of zero or a lot. The thinking that is involved and valuation plays a big part in that.

Darcy: We are inherently long term and play a long game. Even John and I, sitting up here, we think decades out on the Great Business or Great Capital Allocators potentially more and I will give you two examples of why that makes sense. In a great business, an example of a wonderful business would be the 407 highway - we have talked about it before. It is an easy to understand business - it is a slab of concrete across a fast growing population density. If someone came to us and showed us a 50-year discounted cash flow model on the 407 toll highway, we could say with near probability whether it was correct. Whereas, if someone came to us with a five-year discounted cash flow model on a Facebook or something that we did not quite understand, we would have to throw that out. With a Great Business - as long as we can see that pathway - we are going to be very reluctant to sell. We might trim on valuation, but the idea is to hold long because if you exit that position unless you time the market perfectly, which we are not trying to do, you are probably going to be a net loser. On the Great Capital Allocator side, if you were invested in Berkshire Hathaway in 1965, you would have compounded at close to 20% and three times in the history of that stock, and I think it is four times, you would have been down 50%. If you tried to time the market on valuation within Berkshire Hathaway and you got it wrong, you still would have been a net loser. You would have a bumpy path along the way, but you would have made more money by holding it. So that is the framework in the Great Capital Allocator - we really want to hold on as long as the facts remain the same. In the Cheap Assets and Broken Businesses, there is higher turnover. We have turned over virtually 100% of the names in the Cheap Assets and almost 100% in the Broken Businesses as well. We use that framework when thinking about buying and selling.

Question 5: What are your thoughts on ethical investing as well as investing in new technology?

John: We have no interest in investing in things that make money at the direct expense of society. Handguns and tobacco do not appeal to us.

In the history of the world, there have been technological advancements that have changed the course of humanity yet they have not translated into positive economic returns. I think flight is a great example. The opportunity for commercial air travel changed the lives of people in remarkable ways. For instance, when people used to emigrate from England, the odds were high that they would never see their families again. Air travel has had a positive impact on everyone's lives, but the airline industry has cumulatively lost money over history. A more recent example would be something like solar. I think there is a very high probability that solar plays a major role in displacing coal and even natural gas to a degree in the future. Electricity generation is going to be great for society and the environment, but the solar industry is a tough industry to make money in as private investors. Trying to invest in things because they are good for humanity doesn't necessarily work together with making money. If you can do both together, that is terrific.

Darcy: Our fiduciary duty to our investors is to protect capital and build capital at a reasonable pace. I think it would be too challenging if we went through a list of companies and tried to determine which businesses are ethical and which businesses are unethical and try to get consensus on that in a room like this. To John's point about things like alcohol, gambling and guns, a lot of these things are self-regulated by society. If you look at gun control laws or gambling laws, even take something like alcohol prohibition in the 1920s, on that basis alone, these would have been bad investments. So I think if you are looking at a business that happens to be too close to the line ethically, it does not make economic sense to be there. We really focus on people and we want to make money in an honorable way. Avie Bennett, who is not here today, said, "Darcy I have never done a deal with someone that I did not feel comfortable inviting over to have dinner with my wife and kids." To a certain extent, that is how we feel.

Question 6: What has been your biggest mistake?

John: The investment that we have made in the past three years that put the most egg on our face is a company called TeraGo. They provide high speed internet access to companies operating in suburban business parks, across Canada. We invested in early 2013 at about $9 a share. The company, at the time, was going through an auction process. We had identified a number of logical buyers, we thought that the assets were worth at least $13 a share and that is why we made the investment. As it turned out, the auction fell through and the stock price tanked. The largest shareholder who had board representation exerted a lot of pressure on management to change the strategy pretty dramatically. The CEO correctly resisted that push and was fired. At this point, we found ourselves holding a company controlled by an irrational shareholder run by unproven management. It was still a cheap stock and a business that in the right hands, I think, would be a successful investment. I think it is important to remember that you do not need to make it back the way you lost it. The situation that I described is not the best place to have your capital and we moved on to better ideas.

I think there were two things that we got wrong; one, when an auction has gone on for a while and has not ended with a buyer, chances are that it will not. I think that we were too optimistic about the auction's outcome. The second one was that I do not think that we appreciated this large shareholder, who owned 30% of the company, had nuanced incentives. This was a venture capital fund with a large investment in their first fund. The returns of the fund had been terrible; the likelihood that they would ever raise a second fund was close to zero and so, if they were to sell the investment, they would get the cash back and give it back to their investors, and be out of business. Or they can continue to not sell the company, continue to charge management fees and hope for a blowout price. Their incentives were not lined up with ours to just maximize their return in this particular auction. We did not fully appreciate the shareholder's incentives and that was the second thing that we got wrong.

Question 7: You have mentioned that you invest in companies that you understand, in this context can you talk about how you define your area of expertise and what are you doing to expand in order to take advantage of the newly emerging technologies?

John: We think about what we call circle of competence; what are the areas where you think you have an edge? What are the areas that you do not have an edge? You have to know the difference between the two. There is the old phrase that, if you have been playing poker for thirty minutes and you do not know who the patsy is, then it is you. When you are outside of your circle of competence, that is when you are the patsy, so you only want to play when you are the shark and the others are the patsies. Most broadly, I would say our expertise is business to business companies. I think that, at the very core of understanding a business is why do the customers buy the product? The reasons why businesses buy products or services are more predictable and narrower. I know why we have a Big Four auditor as the auditor for the fund because it makes a difference and maybe the quality of the auditor is the same but the credibility that comes with Big Four matters. I understand how businesses make decisions; business to business is the unifying theme of what we look at. I think it is a lot harder to understand why someone buys a Mars bar and not an Oh Henry bar. Consumer related things are generally not what we do.

As a subset of that, there are two particular industries that I think we know really well. One is enterprise software - we have talked about Computer Modeling Group a little bit - and this is a big part of what we do in the portfolio. The nice thing about enterprise software is there are companies of all different sizes, many of them small, with wonderful economics and operating in all sorts of geographies in the world, but the things that you need to know to understand a software company are surprisingly universal. Armed with this one knowledge base and expertise, we can cover a lot of companies. Whereas, if you thought you understood financial services, how many banks could one person reasonably cover - the answer is probably zero. I do not think that most bank CEOs know that much about their own businesses because they are so complex.

The second industry would be distributors and that is a company like Sysco; you see the trucks dropping off food early in the morning to restaurants. Whenever you have fragmented customers, fragmented suppliers and no way for them to go in between, that makes a good distributor. Again there are hundreds of distribution companies in all sorts of industries. The knowledge base is very applicable to many of these companies. We recently made an investment in a company in Australia that is an auto parts distributor. The knowledge base that we needed to understand that is very similar to what we used to understand Richelieu Hardware, which is a Canadian distributor of kitchen renovation products. Those are the two industries that are the most unifying themes of what we own and the beauty of them, as I mentioned, is that both of those areas of expertise are applicable to many different companies, so you can have a small team cover a lot of companies really effectively. That helps us reinforce the advantage of size.

The third one are any industries that we are trying to learn. I would say the biggest one that we have added to our area of expertise over the last three years is thinking a lot more about real estate. Real estate is meaningful to lots of different businesses; retailers often own real estate. Companies owning real estate are able to assess what the real estate is worth as a source of investment opportunity and it influences a lot of different industries. Real estate is something that I have not paid much attention to before, but we have spent a lot more time thinking about it over the last couple of years.

Matt: One thing to add is how Alexander fits into the research process.

John: We have been asked since day one, "When do you think you might add an analyst?" If you were to look at the great investment track records, whatever your favorites might be, they have almost universally been produced by either individuals or people working in very small teams and yet the default question is always when are you going to have more analysts? So everyone seems to think that big research teams beat small research teams and yet the reality is that small teams almost universally beat big ones.

And so the hurdle to have anyone in the research team is pretty high and I think one of the reasons why big research teams do not do that well is because the expectations and the job description are wrong. Most people hire analysts to come up with more ideas and ideas are not the bottleneck; I have a bunch of ideas and almost all of them are bad ideas, but I just do not know why yet. Alex is here to help me figure out why this idea is bad so that we can go on to the next one. Let us say that 1 out of 100 ideas that we come up with, we can work our way through, is going to be a good idea that we are going to put money behind. That is roughly the hit rate. If Alex can help me get through 200 ideas a year instead of 100, then we are going to find two good investments a year, rather than one, and that is really going to have a big impact on the results. Analysts are typically hired to put more ideas into the hopper and that just jams up the system. Alex joined us to help do the deep digging on the companies that are already in the hopper so that we can get more ideas flowing through the system. I think that is a really unusual way to use an analyst and structure a research team. I used to run a research team and I think I saw all the things not to do. And true to form, Alex has boosted productivity to everyone's benefit.

Darcy: When you take the perspective that the markets are there to serve you rather to instruct you then, even though you might not see a lot of activity in our portfolio, the work that is being done is still cumulative so in terms of pipeline of ideas and potential future investments. We use something that we call a wish list. When we look at a business, the last thing we do is look at price and valuation. We are analyzing the economics, talking to the management, going back and reading annual reports and that is really where Alex comes in. Having Alex gives us the added horsepower where we are increasing the wish list. When you have market dislocations or corrections, we have a greater capacity to act; this has been getting stronger with Alex's addition.

Question 8: Do you think that if this correction continues, it will offer you an opportunity to jettison "Cheap Asset" and "Broken Asset" plays?

John: If you think about the playbook, and were to overlay a market cycle, there are going to be years when markets are at peak valuation and periods when they are near troughs. In Great Businesses, the times when you are going to get shots at those are in market declines and we have made some new Great Business investments recently. Those are rare all the time and they are even rarer, especially at reasonable prices, through most of a market cycle. I had a friend in high school who wound up playing varsity basketball who just needed a tall person to practice with. I would go play basketball with her and kids would show up at the park and they would want to play two on two. I was the tall guy and she was the girl; I would usually get double teamed and she would be left open; I was terrible at basketball and after she hit about five open shots in a row, they would figure out maybe we should cover Laura. The Great Capital Allocator is sort of the same in the market; it is really hard to appreciate and it does not get quantified very well. That play is almost always open even when markets are high. The underlying business might be fully valued, but you very rarely have to pay for the Capital Allocation and the Capital Allocation is really valuable. That gives you something to do even when markets are near tops. The Cheap Assets tend to be, available to one degree or another, throughout a cycle, but there are certainly more available at bottoms, but that is the only time that you get to buy the Great Businesses so that is a period when you want to migrate the fund from Cheap Assets to Great Businesses. The Broken Businesses, at the core, are something that we are looking at - businesses that, regardless of where the market goes, these are things that are going to be in structural decline and are not going to be around in five or ten years from now. Sometimes, the thing that makes the market go down, a recession or something to do with oil price, is the trigger for people to realize this business is really about to collapse. The Broken Businesses are better investments near market tops then they are at market bottoms. The playbook gives you the opportunity to do different things at different times at a market cycle. I think it is somewhat premature to judge the returns to any of the plays, good or bad, when you have only had the up years of an up and down cycle.

Darcy: If the market continues to decline then the short book should outperform, which it hasn't in a bull market. So in that context, as the broad markets are declining, the shorts are doing well. We will be harvesting returns from that short book and redeploying that capital back into the Great Business and Great Capital Allocators through a market trough. In that sense, our short book might disappear entirely in a period like that if that makes sense. It will certainly be getting larger as markets increase and should be getting smaller as the market comes down.

Question 9: A lot of investors talk about margin of safety, but it appears to be little more than a marketing device, how do you think about the margin of safety?

John: Margin of safety is an engineering principle. The idea is that when you design a bridge, you do the math to the best of your ability but you might get it wrong. Or there might be factors that you did not appreciate; the welders will not get every connection perfect, the concrete might not be poured right and the wind might be stronger than you expected. So you build in a margin of safety and design the bridge to be a little bit stronger than it needs to be. If the bridge is a footpath over a shallow creek, you don't need all that much margin; but if you're going to drive transport trucks over the Grand Canyon, you will want a larger margin. Margin of safety is the foundational concept of engineering; it has been borrowed and frequently misapplied by finance. I think the key point is that there is not one correct margin of safety, it depends on the circumstances. With a pre-production copper mine in Tanzania – 50% margin of safety might not be enough to know for sure that you won't lose money. Whereas a company like Anheuser Busch where market share never changes you do not need much margin of safety to protect yourself from losing money. You probably won't make 15% per year buying Anheuser today but the odds of losing money after paying a reasonable price are pretty low. We think about it a lot more qualitatively than quantitatively focusing on figuring out how we could lose money.

Darcy: It is largely conceptual, it is there to remind us not to cut an investment too close to the line and so, when it comes to margin of safety, we would rather be approximately right than precisely wrong. There is the analogy that, if someone walked into this room, you would not have to know if they were 300 lbs. or 350 lbs. to come to the conclusion that they are overweight. That is the idea when it comes to an investment. The other thing we try to do is make it simple. I've told John that, if it takes anything more than high school algebra to understand the investment, then I am not interested. Those are the types of things that apply in our margin of safety.

Question 10: How do you leverage your Advisory Board in your investment process?

Darcy: On investment decisions, it is good to get their feedback but they don't get a vote. The Advisory Board is really there to guide us in running our company, not only the investment operations, but the business side. That could be things like structuring healthcare benefits for the firm and negotiating our operating lease for our office space. On the investment side, I think the biggest help and benefit has been introductions. It is not uncommon that we might have an investment in an industry and they will have a relationship with the CEO in the Canadian division. So introductions there help and it also helps to have that voice of reason behind you when you are making difficult decisions.

John: In the last year, something that is new with the fund is that we have made some international investments. The Advisory Board has some interesting thoughts and input regarding how to think about what can go wrong with international investments and how to think about building on the ground relationships to minimize some of those issues. That is an example of how they can make an impact on the investment side as opposed to should you buy this or not.

Matt: Just in case someone did not read the last letter, how do you think about making investments internationally? Up until a few months ago, it has primarily been North American and now we own some companies overseas? How is the investment process different?

Darcy: Well firstly you do not invest in countries that you are scared to visit. Number two, our investments outside of North America have been in the U.K., Australia and New Zealand. And these are countries with language and customs similar to North America. We have taken comfort in that and the other thing is that we have dipped our toes in rather than jumping head first. We have taken smaller positions in those businesses than we would if they were located in Canada or the U.S. They also happen to be in industries and sectors that we know well through past investments in North America.

John: I think the reason for that foray is instructive too. When we started three years ago, attractive valuations and investment ideas in North America were available, but they were scarce and they have become increasingly scarcer over the last three years. Darcy spoke earlier about the importance of flexibility. Most funds have restrictive mandates; when you are required to be fully invested and are restricted to North America and can't find good investments, most people would just lower the bar until something can get over it and that's what they buy. That is not in the clients' best interest. But that is what a lot of people are forced to do when they have restrictive mandates. So the fact that we have this flexible mandate, allowed us to say, look we are having a hard time finding compelling ideas in North America, why don't we look in countries that we would be comfortable investing in, with industries that we have past experience in and let's see if we can find something that looks a lot like something that we know that just happens to be located in another country. That has led us into an auto parts distributor in Australia and a software company in the U.K. These are the kinds of things that we have invested in North America before.

Matt: Just staying on flexibility, from the beginning you said that you had the ability to go up and down the capital structure. In the portfolio today we own a debenture, how do you think about making investments in debt versus equity?

John: At the end of the day, we are looking for, as Darcy mentioned, things where we think the odds of us losing money are close to zero and we think we can make ten to fifteen percent a year over a multi-year horizon. It does not really matter if that is a bond or equity or whatever.

Looking at Atlantic Power, which again really reflects our flexibility, this is a company that we first looked at and saw that its bonds were kind of cheap. Looking through it actually, it turns out this is a high dividend paying company, the investors had bid up the price of the stock well in excess of the underlying assets. Just because of the dividend, we wound up shorting the stock on the expectation that eventually they would cut the dividend and the market price would more accurately reflect the underlying assets, which proved to be the case. They cut the dividend in September and the stock was down 40%. At that point, the bonds actually sold down pretty heavily over the year that we had been following the company. We had got to know the assets quite well and thought that these were money good bonds and you were definitely going to get paid when they mature in 2017 and they were priced at a yield of plus 13%. So now this is something where odds of losing money are virtually zero, 13% expected return and assets we had gotten to know well. We thought, let's buy that, it totally fits the mandate, even though it is a bond and not a stock. So that ability I think shows how we have been able to use the flexibility to short things to make money and also the ability to move around on the capital structure to make money.

Darcy: It is always looking at the opportunity cost of your next investment. If we can find something that offers higher return at similar risk, we are going to make that trade. If we can find something that can offer similar return at lower risk, we are going to make that trade as well regardless of the capital structure.

Question 11: Have you looked at making investments in insurance companies with a good capital allocators at the helm such as Berkshire Hathaway, Fairfax, or Markel?

John: We don't own any of those companies. Insurance is a business that has skeletons in closets you didn't know existed. The business does have some positive attributes and if you can find one run by the right people it can work it. Insurers are obligated to hold a lot of their assets in bonds which I think is unlikely to turn out well, but they don't really have a choice. That's going to be a big handicap. If we found one run by the right people at the right price we would consider it.

The problem with Berkshire specifically is that it has gotten so big that it becomes really hard to compound at high rates. Today, Berkshire seems more interested in deploying a lot of capital at decent rates rather than maximizing returns. So I think we can do better than Berkshire, not because we're smarter but because we are working with a lot less capital and we should be able to find something better to do than buying a $300 billion market cap company.

Darcy: However, we do think Berkshire is an interesting substitute for the S&P 500 index. You own a cross-section of the American economy, you don't pay any fees and there's still some juice left in Warren

Question 12: Do your think that Berkshire is worth more as a holding company or broken down into smaller pieces?

John: If I was CEO I would keep it together. They own a lot of businesses that can benefit from a low cost of capital. I don't think they've pulled very hard on that lever but there is probably a lot of untapped value within Berkshire because of its cost of capital.

Matt: If there are no more questions then we will stop it there. Thank you for all of the great questions that you asked and thank you very much for joining us today.

About the Ewing Morris Opportunities Fund LP:

The Ewing Morris Opportunities Fund LP was established by John Ewing and Darcy Morris in September 2011 to achieve preservation and growth of capital through superior securities selection. The Partnership invests in securities that are inefficiently priced based on a number of factors. The Partnership is focused on North American-based small-capitalization companies.

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