

# FINANCIAL POST

## No time to be passive

Thu Jan 26 2012  
Jonathan Ratner

Manager: Dan Bastasic, IA Clarington Investments

Fund: IA Clarington Strategic Income Fund

Description: Flexible balanced fund focused on income via equities and bonds

Inception Date: August 2011

Manager's AUM: ~\$800-million

Management fee: 2%

It will take eight to ten years to deleverage balance sheets globally, meaning investors can expect more volatility and for the markets to oscillate from being merely okay to not so good, predicts Dan Bastasic, portfolio manager at IA Clarington Investments.

"It's not going to be a passive time," Bastasic says. "We've got growth that is going to be low, and there are global sovereign debt problems and company-specific issues, so it is going to be very important to identify those risks and resulting valuations."

Despite the warning signs and market expectations that things will fall apart, Bastasic has been opportunistically buying relatively safe infrastructure stocks and REITs, as well as U.S. telecoms and utilities that have sold off.

"We're still staying defensive, but playing into the idea that things are getting better," he says. "If we're wrong, the downside is limited with those types of stocks. At the same time, we're not necessarily avoiding the upside if we're right and things continue to improve."

The portfolio manager joined IA Clarington at the end of August 2011, bringing with him more than a decade of experience in both equities and bonds.

Bastasic is a fundamental-based, bottom-up, index-agnostic investor who focuses on cash flows and generating absolute returns. He also uses a macro overlay to manage risk and timing.

In the past six months or so, Bastasic has begun positioning the fund in anticipation of 2.5% to 3.0% growth in the U.S. He is targeting lower-risk names with relatively good valuations that could generate 10% to 15% of upside.

Bastasic thinks the U.S. is going to be in pretty good shape in 2012 relative to the rest of the world. While Canada is exposed to the risk of a slowing Chinese economy, he notes the domestic economy's ties to the U.S. should help offset some of this weakness.

The manager continues to see quite a bit of opportunity in the health care sector and is being selective in the industrial space. He also sees a good chance of low double-digit returns for Canadian REITs.

"In a slow market, there is not a lot of downside risk generally in the Canadian REIT space," Bastasic says.

Diversified infrastructure companies, many of which have been negatively impacted by troubles in Europe and a slowdown in China, are expected to rebound at some point.

Bastasic says there is also a growing opportunity in U.S. financials and is positive on energy stocks, noting that there is too much of a fundamental macro-economic catalyst for oil in particular.

On the fixed income side, which accounts for roughly 40% of the fund, Bastasic has a lot of exposure to telecom and utilities.

"They sold off because of the broader market declines," he says. "But these are high-quality, strong free cash flow producing companies, which are two of the things you really want to see in a high-yield bond investment."

He is also focused on the energy sector, where he notes asset coverage levels are quite high.

"If things go wrong with a company, generally there will be a strong bid on the assets," he says. "We've seen that time and again."

## BUYS

Johnson & Johnson (JNJ/NYSE)

The position: Adding to position since fund launch.

Why do you like it? JNJ provides investors with a diversified product base, and significant scale and scope in all their businesses, but it also offers a relatively safe way to play emerging markets.

"If you believe in the emerging markets story, where growth is better than in developed economies, but you still don't like the risk associated with emerging market securities, this company has what you're looking for," Bastasic says.

He notes that 50% of JNJ's sales are outside North America, so it has access to higher-growth areas. It is also one of the few companies globally that boasts a genuine AAA-rated balance sheet, as well as an attractive dividend and dividend growth prospects.

Biggest risk: U.S. health care reform could impact margins and pricing.

Progressive Waste Solutions Ltd. (BIN/TSX)

The position: Recently added to position established at fund launch.

Why do you like it? As the third-largest full-service waste management company in North America, BIN provides an essential service. "Even in a recession, you're still throwing out trash," Bastasic says.

He notes that the company can adjust prices as inflation rises, thereby protecting its income stream.

The stock is also trading at a significant valuation discount. "If the economies of North America start to show some better strength, you have to believe it will start trending toward its historic mean, which means some pretty decent upside."

Biggest risk: A recession that leads to pricing weakness in the commercial business.

Cascades Inc. (7.875% due 2020)

The position: Has owned this bond on and off for past 10 years.

Why do you like it? This Canadian container board company also has a large proportion of earnings coming from its tissue paper business. "As long as people are going to the bathroom, this should be a pretty safe business, and it always has been," Bastasic says.

He says Cascades carries a higher-than-average multiple given the high value attributed to the company's established presence in this space, has plenty of flexibility to protect its coupon payment and has been reducing debt in recent years.

Biggest risk: A lag in pushing price increases through to customers as a result of rising input costs would create earnings volatility.

SELL

Bank of Montreal (BMO/TSX)

The position: Sold in recent months.

Why don't you like it? Although BMO's valuation is somewhat inexpensive relative to its long-term average, Bastasic highlights the bank's inconsistent operating results in recent quarters as a reason to sell. Specifically, he points to weakness in BMO's domestic, personal and commercial division. Couple that with challenging capital market conditions and the manager sees better opportunities in other financials.

Potential positive: BMO should emerge as a defensive play if Canadian commercial real estate experiences a correction, because the bank is pulling back from that part of the market.

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