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Investment Commentary

Markets were lacklustre in the third quarter as the TSX Composite declined just over 1%, while the S&P 500 increased by a similar percentage over the same period. The real market action started in September and has continued into October as we write this report. Over a several week period straddling September/October, the S&P 500 declined 7.4% and then quickly rebounded 6.1%. The decline in the TSX Composite started earlier and declined further by 11.4% and then climbed back 5.3%.

We had remarked in our last quarterly letter that market volatility had been at all -time lows in the summer. Since then, the CBOE Market Volatility Index (VIX) has increased threefold from a low of 10.3 in early July to a high of 30.9 in mid-October. Following this sharp spike, the VIX declined to 15 and it is now tracing lower.

We actually see this turmoil as healthy as the stock market's steady increase over the last several years along with abnormally low volatility was concerning. It suggested a certain level of investor complacency and insensitivity toward investment risk, which can lead to excesses in market valuations.

The minor correction in equities was precipitated by increasing investor concerns over weak global growth (particularly in Europe and China), ongoing conflict in the Ukraine and Middle East, democracy protests in Hong Kong, the ongoing Ebola scare and the end of the Fed's quantitative easing project.

Weakening global demand dragged down commodity markets across the board in the third quarter and through October. This has been felt here in Canada as Q3 returns for the TSX Energy and Materials indices were down 7.3% and 10.5%, respectively.

Bridgeport's focus on quality businesses with sustainable revenue and earnings has served us well during this period, although we remain somewhat cautious as (i) undervalued equities are still difficult to find (notwithstanding the recent pullback), (ii) corporate profit margins are at all-time highs (and likely have little room to grow) and (iii) economic growth is likely to be modest for the foreseeable future.

Many of you may have noticed that our Equity portfolios have taken on a decidedly larger cap focus of late. This is because, for some time, we have had greater success in identifying undervalued large company stocks, while finding that many smaller cap companies were "priced to perfection".

Despite this recent trend, we are actually more interested in investing in the small and midcap sectors of the market as in the long term those segments tend to be less efficiently priced and offer better growth prospects. We are hoping that more investment opportunities emerge among smaller company stocks going forward as we note that the small cap-oriented Russell 2000 index returned -7.6% in Q3, suggesting that some buying opportunities may lie ahead. The key takeaway here is that we take a disciplined approach to finding investments that meet our criteria. We do not deliberately target segments of the stock market; rather, we take a "bottom-up" approach and seek to invest in the right businesses when their stocks are selling at attractive prices.

In keeping with our low turnover approach, we only added one new position to our High Income Portfolio during the quarter which was a new preferred share issue from Equitable Group. Equitable, through its Canadian banking subsidiary, provides a variety of mortgage products and savings solutions to retail and commercial customers across Canada.

We look forward to speaking with you soon and wish to reiterate that we appreciate the trust you place in us as your advisors.

Yours truly,

John Fisher

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