

Joe Jugovic credits his father and mother for planting the seed that would eventually grow into a job handling investments.

"At the end of the day, the biggest influence was that both my parents were immigrants from Croatia," says Mr. Jugovic, a fund manager with Calgary's QV Investors, which is also a sub-adviser to the Ethical Funds Co. of Vancouver.

"They not only instilled in me the value of money, but how hard you had to work to save it. And if this notion is put into your head at a young age, you want to figure out how to do it."

It also didn't hurt that there were folks around who could point him in the right direction.

"I had a couple of very good high school teachers who had an interest in investing. And when they found a young person with similar interests, they took me under their wing."

Born and brought up in Calgary, Mr. Jugovic, 34, manages the Ethical Special Equity Fund, a small-cap portfolio.

### Because your portfolio is a sub-advisor to Ethical Funds, the stocks you buy must meet specific standards.

So, we'll avoid those companies that are polluters or which have mistreated suppliers or customers. We'll also steer clear of outfits that have wronged their workers. It's important, after all, that a company have good relations with its community. It's also important that a company have a good health and safety record. More no-nos? Corporations that get 10 per cent or more of their revenue from tobacco, weapons sales or uranium mining.

### But don't all these restrictions make it difficult for you to find good companies?

Not at all. Being both ethically responsible and profitable go hand in hand. After all, a company that respects the environment, its customers and its suppliers is less likely to incur the financial liabilities that unethical behavior often causes. Just the opposite, however, is likely to occur when a company breaks the rules. Consider a base metals miner that's slipshod in disposing of its waste. The next thing you know, it will likely have a spill. This, in turn, will result in a financial liability that may ultimately drag down its stock.

### So, first off, you're looking for businesses that make money

That's right. We're not picking companies based solely on their sense of right or wrong. We're picking good businesses that meet Ethical Funds' standards for socially responsible investing. You know, a lot of people have the impression that a fund like ours will invest only in green technology outfits of the type beloved by David Suzuki. But this isn't what we do at all. We simply try to buy sound companies that are good investments.

## THE INVESTOR'S DIGEST INTERVIEW

# Psst: A fund that practices ethical investing can still make money

*Mention socially responsible investing and tree huggers often come to mind. But the linkage is inaccurate, says Joe Jugovic, who runs a small-cap portfolio for the Ethical Funds Co. of Vancouver. Indeed, for Mr. Jugovic, a good company above all is one with a healthy balance sheet and solid returns*

**Still, in some cases, you've been able to get a socially responsible company to become even more so.**

That's true. Take Cascades, the Quebec-based forest-products firm and one of our long-term holdings. Although Cascades was well run and had high ethical standards when we bought it, we were able to convince it to join the Forest Stewardship Council, an international body for the promotion of sustainable forestry. Still, we didn't originally buy Cascades because it promised us it would join the FSC. We bought it because it was a good company—and a fairly priced one at that.

**Your portfolio only holds small caps. But most small caps pay no dividend.**

Yet, two-thirds of ours do. So, we're different from other small-cap funds. But even if a small cap doesn't pay dividends, it's still often a good investment. Small caps, remember, are able to grow faster than large caps. They also tend to have fatter returns. Then, too, all good big caps initially started out as small caps.

### STOCKS JOE JUGOVIC LIKES

Canadian Western Bank  
(CWB-TSX; \$27.84)  
Phone: 780-423-8888

Empire Co. Ltd.  
(EMP-A-TSX; \$49.40)  
902-755-4440

CCL Industries Inc.  
(CCL-A-TSX; \$44.20)  
Phone: 416-756-8500

Richelieu Hardware Ltd.  
(RCH-TSX; \$24.34)  
(800-361-6000)

Uni-Select Inc.  
(UNS-TSX; \$30.90)  
Phone: 450-641-2440

**So, what do you look for in the companies you buy?**

A significant ownership stake by the managers or the insiders. When a company official has his dollars on the line, he's much more likely to want to make the company a success. We also look for managers who've shown they can grow shareholders equity or earnings over time. We want to see that they've been able to deliver the goods. A management team that has great promise, but which has yet to prove itself, is of little use. That's why many of the new green technology outfits seldom make it into our fund. Being relatively untried, they don't yet have much of a track record.

**What else do you look for in sizing up management?**

candor and honesty. We want people who tell the truth when describing their companies. Do they understand risk and do they know how to handle it? Indeed, many managers can talk a good story, but still be unaware that their business may have a downside.

**You put a lot of stress on a company having a good business model. Why?**

Because without it, an outfit may not survive. Any company can look good when its sector is going great guns. Take the oil-patch. Two years ago, all energy plays seemed great. After all, commodity prices were red hot, cash flows were strong and equity investors were champing at the bit. So, it was tough to find a money-losing outfit. But back in 1998 when oil prices were falling, things were very different. For every company that was making money, 10 were not. And the one that was in the black was probably the one with the superior business model.

**You obviously consider a solid balance sheet as another important investment criterion.**

We do. In fact, many of the companies we own have zero debt. They also have a lot of free cash. Both attributes give a company flexibility when times are bad. Yet, another thing we will look for is good valuation. We like companies that trade at a discount to their net asset value, or at an earnings multiple that's rea-



sonable. Then, too, we want an outfit with the ability to generate free cash flow. Not only does this allow it to pay out a dividend, but it also allows it to plow money back into its operations.

**Your investment style, you say, is one that's based on risk management.**

Which means our price-to-earnings ratio averages less than that of our benchmark, the Nesbitt Burns Small Cap Index. Right now, for example, our P/E is roughly 15 times 2007 earnings. With the index, by contrast, it's over 22. So, in effect, we're taking considerably less risk. By the same token, however, we're offering a better payback. Indeed, while our return on equity is now around 13, that of the index is less than 11.

**Canadian Western Bank has focused on small and medium-sized businesses — primarily in Western Canada.**

And as such, has carved out a profitable niche. Meanwhile, Canadian Western, of all of Canada's banks, probably has the least amount of balance-sheet debt. And because the bank steers clear of the capital markets, it isn't hit as hard as its rivals when the stock market starts to shake. Then, too, because its primary focus is Western Canada, the bank is good for investors who want a piece of Alberta action, but who don't want to buy energy stocks to get it. Of course, because the bank is small cap, it has more room to grow its market share than its big-cap brethren back East.

**Empire, you say, has a solid record of finding good value.**

Indeed, it does. Over the last couple of quarters, for example, it bought the remainder of Sobey's that it didn't already own. And because Sobey's, when it was still a public company, was one of the world's cheapest grocery chains, Empire managed to get a good grocery retailer, without having to shell out a lot of cash. Then, too, the company also has a good record of boosting its dividend. And because people will always need to buy groceries, Empire will likely remain in business, regardless of what ultimately happens to the economy.

**CCL Industries, you say, has shown itself capable of making hard-nosed decisions.**

Consider what it did with its custom manufacturing division. Although that division had long been CCL's backbone, CCL realized that its future lay in pressure-sensitive labels, a smaller part of its business. So, in May 2005, CCL sold its custom manufacturing operations to KCP Income Fund. And the decision has proved to be a good one. Meanwhile, CCL, through its customers, has a good entree to the world's emerging markets. Indeed, because it sells to such giants as Procter & Gamble, CCL offers investors a good play on consumer spending, but without the risks involved in buying, say, commodity stocks. Moreover, CCL is investor-friendly, having consistently paid out dividends over the past two decades.

**Richelieu sells specialty hardware to both retailers and wholesalers. As such, it does business with everyone from the Home Depot at the mall to the do-it-yourselfer down the block.**

Which gives Richelieu a diversified customer base. The company also creates shareholder value, having averaged a 15 per cent-plus return on equity annually for the last decade. Indeed, Richelieu, which is based in Quebec, is a superb model of growth that is at once both disciplined and profitable. As such, it's exactly the type of company we like to buy.

**In 2004, Quebec's Uni-Select, an auto parts distributor, bought Mawdi, a U.S. company in the same business. In making the acquisition, Uni-Select signalled it was moving aggressively into the American market. Yet, many Canadian companies that have tried to do so have come a cropper.**

But we don't think Uni-Select will meet the same fate. For one thing, it didn't just jump in, choosing instead to think seriously about what it was doing before making its move. Then, too, Mawdi is well-established in America. So, rather than going into the U.S. and starting afresh, Uni-Select chose instead to partner with an existing player, thus hedging its bets.