



**Tech Futures:  
January 12, 2000**

By [Michael Volker](#)

**Market Commentary, What to Buy?, Hedging your Bets with Collars, and Capital Pool Corps Update**

**Market Commentary**

I'm bullish. I always am. But, there sure have been many not-good news stories and reports which, although I hate to admit it, have dampened even my enthusiasm for the markets. Reports from car makers, Nortel cutting jobs, profit warnings from companies like Yahoo (2001 sales expected U\$1.2Bn slightly below analysts' predictions of U\$1.4Bn, reports that PC (Personal Computer) sales were down last year (30% off in revenues while only 1% down in unit sales, according to PC Data of Reston, VA.) make it tough to get excited about the markets. Doom and gloom.

Invariably when there's bad news, regardless of how bad, companies get hammered. However, when the news is good, we rarely see huge price increases. In fact, prices often stay flat or decline even when good news is reported. This tells me that current holders of stock - not the potential buyers - are the ones who most directly affect the price. Any negative news is unlikely to attract a buyer (only sellers at current prices), hence a downside bias. Positive news, on the other hand, may attract new buyers but it will also attract sellers (i.e. here's my chance to get out of this one!). In my simplistic view of the world, that's why I believe that modest pessimism can have a greater impact in driving prices down than enthusiastic optimism can have in driving prices up (except when everyone is bullish and greedy).

On the bright side, though, market research firm, Forrester Research Inc of Cambridge, MA, predicts that on-line B2B (Business to Business) trade in Canada will reach \$272 billion in 2005. This would represent some 18% of the \$1.54 trillion forecast for total B2B transactions. \$69 billion of the \$272 billion is expected to come from Ontario's motor vehicle trade. Another chunk is expected to come from Quebec's electronics industry.

Here's an encouraging piece which I received from local tech investor and marketing guru, Ullrich Schade of **Ullrich Schade and Associates**. He refers to an article and interview of Don Wolanchuk, an "expert" in market timing.

He predicts that the NASDAQ should go through 5000 this year. He's one of Market Timer Digest's Top Market Timers, having won 17 annual timing awards since 1989. Some of his greatest timing calls were widely ignored by the investment community. Wolanchuk forecast the bull market rally following the 1987 crash and called for aDJIA above 10,000. When NASDAQ traded at 1800, he forecast a NASDAQ 5000. In 1999, at the bottom of the oil market, Wolanchuk called for \$30/barrel oil. He was Market Timer of the Year in 1995, 1996, 1997 and 1999. Good luck again, Don!

Finally, based on my own discussions with investors and brokers, I am encouraged by hearing - for the first time this week in a long while - that things are improving. Many feel that the market has corrected and has bottomed out. Even gloomy news heard this week (Yahoo, Cisco, Nortel) has not caused the huge avalanches that were so common before the Christmas break. Admittedly, earnings forecasts have been reduced. According to First Call/Thomson Financial, S&P500 company earnings should grow by 4.1% which is down quite a bit from the October estimate of 15%. But, hey, it's still positive (and better than GDP growth estimates).

### What to Buy?

So, what are some good buys right now? One of my favorites, which I've mentioned before, is looking even more interesting due to the market's fall-back.

What if I told you that you could invest in a basket of the top 20 info-tech and internet companies (like Cisco, Microsoft) with huge upside potential and a *guaranteed minimum return* on the downside, i.e. a no-lose proposition? Invest U\$7.00 today, with a guarantee of at least U\$10.00, but with unlimited upside potential. Sound crazy?

Then take a look at the **Business Development Bank's Internet Notes** (TSE:BDB.n), a "simulated" basket of 20 stocks. These have been trading on the TSE at less than U\$7.00 (52 week lo-hi of U\$6.00 - U\$16.00). These "notes" (they trade just like shares on the Exchange) are guaranteed by Her Majesty at U\$10.00 (i.e. they can be given to her in Exchange for ten bucks in 2009). But - the upside is unlimited! What a deal!

So, wassup, then? Well, first of all, they have not been promoted. It's even tough to find information about them (try it, you'll see what I mean). No one (except me and a few others) know about them. Secondly, they are thinly traded (hence not of interest to certain investors) and thirdly, the float is very small with few having been sold on the initial IPO. Indeed, there are only 1.5 million outstanding. The third point is a plus for investors because even a modest buying interest will push up the price.

Because of points #1 and #2, the stock is trading around \$7.00. On Dec 29th, 2000, its theoretical "paper" value was down to U\$5.38 whereas the notes were trading at a premium, at U\$6.50. Until recently, they were trading at a discount to the theoretical value. For example, when the notes were trading at U\$12 last Spring, the theoretical value was over U\$20. Both scenarios reflect the lack of interest or awareness of these.

The basket of stocks which the BDB tracks consists of the top 20 internet companies. It includes these companies: Yahoo, Etrade, Ebay, Sun, Microsys, VerisSign, CNET, Amazon.com, Doubleclick, Microsoft, Inktomi, AmericaOnline, CMGI, At Home, Cisco, Entrust Tech, Infoseek, Qwest, Psinet, Macromedia, and Qualcomm. Not bad company(s)!

With respect to investing in emerging tech ventures with a B.C. focus, there are two vehicles available to the general public. These are: the **Working Opportunity Fund** (WOF, see [www.wofund.com](http://www.wofund.com)) and **Discovery Capital Corporation** (CDNX: DVY).

The Working Opportunity Fund is especially attractive to retail investors at this time of year due to its RRSP eligibility coupled with attractive tax credits.

Discovery was written up last August by **Salman Partners** who projected a \$2.15 target. At that time the stock was trading at \$1.40 and today it is less than half that price, trading in the \$.60+

range. Discovery has picked some winners along the likes of **Sierra Wireless Inc.** (TSE:SW), **ALI Technologies Inc.** (TSE:ALT), and **Dees Communications** (acquired by NASDAQ-listed NICE Systems Ltd). This one merits a closer look.

The folks that manage the Working Opportunity Fund, **GrowthWorks Capital Ltd.** (see [www.growthworks.ca](http://www.growthworks.ca)), have launched a new fund - the **GrowthWorks Access Fund**. This unique retail vehicle offers *sophisticated* individual investors the opportunity to invest in the explosive market of early stage information technology and life sciences companies on a pre-IPO basis. This may appeal to the more serious (i.e. minimum \$25,000) investor.

A lot of investors have learned that choosing risky growth stocks is not as simple and painless as it seemed at the start of the year 2000. Are you paying too much for a cute but rather useless technology that will never really go anywhere? Let's face it, it is not difficult to be impressed by fancy technological advances or biotech discoveries that sound awesome but are impossible for most of us to put into proper context. We simply lack the scientific or technical experience. Instead, consider riding the coat-tails of a proven venture capital firm that has earned over \$300 million in gains while losing (on paper or realized) only \$512,000. Their tech and biotech venture capital portfolio returned 68% on average per year for the past seven years. The trick is to invest in the companies in their early stages of growth (well ahead of an IPO) and to take an active roll in ensuring that a sound management team is in place in each investment.

With respect to picking winners, here are a few examples. Their average per share cost in **Angiotech Pharmaceuticals** (TSE:ANP) was \$2.65 (currently \$59.00), in **Stressgen Biotechnologies** (TSE:SSB) it was \$0.63 (currently \$6.26), and in **Chromos Molecular Systems** (TSE:CHR) it was \$2.26 (currently over \$7.00), and in **Anormed Inc.** (TSE:AOM) it was \$3.57 (currently \$18.00). Their best win was **HotHaus Technologies**, in which their \$4 million investment grew to \$170 million when the company was acquired by **Broadcom Corp** (NASDAQ:BRCM).

The Growthworks Access Fund is offered to the sophisticated investors only. This means that the minimum subscription in British Columbia is \$25,000 dollars. It is offered as a limited partnership which gives an investor the opportunity to reduce the capital gains taxes as significant portion of the Fund distributions may be eligible for Canadian Controlled Private Corporation rule for the \$500,000 capital gains exemption (hot damn!).

**Citizens Bank of Canada** offers financing for this issue in the amount of up to \$50,000 dollars.

Thanks to Jarek Matysiak, Investment Advisor at **Canaccord Capital**, for bringing this to my attention. If you wish to receive the copy of the offering memorandum, contact your registered rep or give Jarek a call at 643-7347 (email: [jarek\\_matysiak@canaccord.com](mailto:jarek_matysiak@canaccord.com)).

**Yorkton Securities** has been in the hot seat lately. They've been criticized for their role in various startups, e.g. dot-coms like Book4golf.com, in which certain principals of Yorkton have acquired cheap stock which they then promote to their clients. Scott Paterson, Yorkton's head, has commented that such dealings should be welcomed insofar as it is a tough for junior companies to get risky deals financed. I tend to agree with him on this matter and I think it's good that there is more investment activity in this arena.

Concerns about this relate to "potential conflicts of interest" which arise when an investment dealer is selling shares to its clients in which its own principals stand to benefit.

Over the past year, I've seen numerous such dealings by various firms. Often, they *do* disclose such dealings in order to comply with the regulatory requirements, but such disclosures are often quite subdued. It's a good idea to put these front and centre - not in the fine print. As long as the investing public is aware of any conflict of interest, this information can be factored into one's propensity to invest (or not). In fact, it may even give investors additional confidence. I'm always reluctant to act on a suggestion by an investment dealer who herself has not made a financial commitment to the firm she's touting.

### **Hedging your Bets with "Collars"**

Here's an interesting idea using something called a Put/Call Collar. This will be of interest to entrepreneurs or investors with big stock positions in their companies.

Paul Allen, one of Microsoft's founders recently used this strategy and what he did serves to illustrate the concept.

The strategy involves the selling of a CALL option, i.e. giving the holder of the call the right to buy stock from the holder at a specified price for a certain period of time (just like employee or market stock options) and the buying of a PUT option, giving the holder (in this case, the stock holder) the right to sell, i.e. "put" stock, to the seller of the PUT at a specified price for a certain period of time.

A few weeks ago, when **Microsoft Corp's** (NASDAQ:MSFT) stock was trading down in the U\$41 range, a 65% drop over the past year, Allen set up a "Zero-cost collar". He did this by selling CALLS with a \$130 exercise price (averaged over a few years) and using the proceeds from the sale of these CALLS to buy PUTs with a \$60 average exercise price.

In so doing, he limits the price he can get for his Microsoft stock to \$130 (still 3X above where it was recently), but more importantly, he protects his selling price to a minimum of \$60. So even if MS tanks to \$25, he is still guaranteed \$60 - no matter what. In essence, he's got an insurance policy.

This is a good strategy, especially for insiders, who believe in the future prospects of their company - hence they don't want to bail out in any great hurry - yet at the same time want to be prudent with respect to their investment by covering their downside. It makes a lot of sense for company founders with huge positions that they don't particularly want to liquidate even though market factors might suggest that it is time to cash in.

This strategy works well for anyone with a large exposure in any given stock. Whereas the selling of CALLS by stockholders has always been a good, low-risk way of generating extra income on one's investment, the use of these zero-cost collars should be considered in these turbulent times. At least, you'll sleep well at night.

### **Capital Pool Corporation (CPC) Update**

In this column, I keep track of Capital Pool Corporation ("CPC") companies (see chart below) as defined by the CDNX because they may provide funding and management to, and in the process acquire, technology companies. CPC's are the continuation of the former VCP and JCP programs on the Vancouver and Alberta Stock Exchanges.

I like CPCs from an investment perspective. Although one may regard them as speculative

(indeed, they are), they are also an inexpensive way of getting in early and inexpensively. You can pick up 10,000 shares of a typical CPC for pennies.

However, there's a ton of them now. Over 227 have been formed in the past two and half years. Many are even trading below their IPO prices. I hope that there'll be fewer formed with more emphasis on building value in the existing ones.

New additions to our list are **Predator Capital Inc.**, a B.C. company and **VistaTech Corporation** from Alberta. Predator? Sounds a little ominous, wouldn't you say?

Since the previous update, the following companies have come to trade: **Arsenal Capital Inc.**, **Cross Border Capital Inc.**, **Horizon Industries Ltd.**, **PanGlobe.com Inc.**, **VTEC Capital Corp.** and **WWS Capital Inc.**

Check our [Capital Pool Corporation chart](#) (in .pdf format) for a complete updated list of the CDNX's CPC and VCP companies, thanks to **David Ing** of **Pacific International Securities**

An introductory article explaining CPCs may be found at <http://www.bctechnology.com/statics/mvolker-jun0200.html>.

#### Footnotes

With a mandate to become a national venture capital stock exchange that provides emerging and small companies access to capital, the **Canadian Venture Exchange** (CDNX) ended its first year of operation having helped companies raise \$2.37 billion in equity financings. It also saw 45 of its listed companies graduate to the Toronto Stock Exchange (TSE).

The next [Vancouver Enterprise Forum](#) event scheduled for January 23rd features the very popular annual venture finance session, i.e. who's got the dough and what does it take to get it. Book now to avoid disappointment. This event has been sold out for several years in a row.

For a convenient printable, pdf version of this column, [click here](#).

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#### [What Do You Think? Talk Back To Mike Volker](#)

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**Tech Futures** is a bi-weekly column that focuses attention on new and emerging BC publicly listed technology companies.

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