Laurus MONTHLY COMMENT

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"Most of the annual variation in [investment] performance is due to luck, not skill."

…. Bradford Cornell, California Institute of Technology

As we've written in the past, in investing we generally underestimate luck. Even more interesting is the human tendency to attribute poor results to bad luck and good results to skill. Understanding the relative contributions of luck and skill can help us assess past results and, more importantly, anticipate future results in many such areas.

The outcome of most professional sports are a combination of luck and skill. For example, as highly skilled as the Toronto Raptors are in basketball, luck has considerable influence on the outcome of, not only a game, but the entire season. There is no substantive performance difference between a three-point shot that is blocked and falls harmlessly to the floor, from one that hits the rim and deflects to an opponent, or one that deflects to a teammate and is slam-dunked for two points. While the original shooter may have an excellent three-point shooting percentage, converting the shot is largely a matter of luck (for example, where and how the ball bounces).

In a similar fashion, investing is also largely influenced by luck. Writer Barry Ritholz contrasts trading and investing: "..*trading (as opposed to investing) is more about laying out probabilities of risk versus reward; investing is about valuations within the longer secular macro picture*." Not to be argumentative, but we might suggest that investing is really about finding, acquiring, and holding on to value.

Using discipline, a good investment team can tilt the odds away from pure luck. Finding value via underappreciated assets can come in a variety of ways – businesses that are out of favour, or those that are smaller in market capitalization and therefore not closely followed, are a couple of examples.

Case in point would be our recent discovery of DIRTT Environmental Solutions (DIRTT stands for "Do It Right This Time"). This Calgary-based company designs, manufactures, and installs prefabricated interiors. This may not seem a particularly engaging investment idea, but the half-day we recently spent in their Calgary plant illustrated not only their core competency (mass customized construction at an affordable price with a short lead time), but their capability to be a "distrupter" to the existing industry.

The backbone of DIRTT's competitive edge is their internally developed, and patent-protected, ICE software. This software allows the customer to be engaged in the design of their interior on a stand-alone, 3D platform then integrates manufacturing and on-site installation. Materials costing is produced automatically with a real-time cost estimate available at all times throughout the process. As the customer makes changes to the design – from walls or doors, to finishes, cabinets or even wall plugs – the costing is immediately updated, right down to the last screw.

The visualization aspect of ICE, combined with the immediacy of the costing proposal, provides the customer an accurate representation of what they are purchasing. This reduces the prospect of errors and omissions along the way. The final competitive strength of the process is the ability to deliver the installed solution in three weeks (or less). The end result is a customized space design without surprises at a lower cost and in less time.

DIRTT began trading on the TSX in late 2013. Given its market capitalization of $425 million, there are very few analysts following the company which affords us an opportunity.

Our team's ability to find value via underappreciated or underfollowed assets will provide our clients with strong long-term returns and lower volatility. We are not traders, believing that trying to time a trade brings too much emotion into what should be a disciplined, repetitive process. Instead, our focus is to uncover and own companies like DIRTT for a very long time and thereby tilt the odds in our favour.

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