3 Stocks to Buy From 1 of Canada's Most Successful Hedge Funds

Description

Canadian investors 50 or older might remember the Montreal brokerage firm Marleau Lemire. Founded in 1989, it specialized in financing Canadian small- and mid-sized businesses and, for a few years, had a pretty good run until it was sold to Dundee Bancorp in 1999.

One of the co-founders, Hubert Marleau, moved on after the sale, setting up Montreal boutique investment firm Palos Management with his son Charles in 2001. The father and son team's first product out the door was the Palos Income Fund, L.P., a long/short hedge fund sold to accredited investors and the offering memorandum exemption.

Only 25 at the time of the fund's inception, Charles Marleau has managed to deliver positive returns in 13 out of the last 16 years–an excellent performance to the say the least. Even more impressive is Palos Income Fund's compound annual return of 11.1% since inception–466 basis points better than the S&P/TSX Composite Total Return Index.

Flying under the radar, Marleau has done a good job delivering for investors.

Here are three stocks he's currently interested in. As one of Canada's most successful hedge fund managers, you might want to consider one or more of them.

Pick #1

Learning from talented investors is a key component of getting better at managing your own personal portfolio. Fortunately, Marleau writes a weekly commentary that's available for viewing on his company's website. I recommend you avail yourself of this useful resource.

Marleau's first pick is **Superior Plus Corp.** (TSX:SPB), which is best known as one of the biggest distributors of propane in this country. He believes that the collapse of its merger with **Canexus Corp.** over the summer combined with the almost simultaneous sale of its construction products division for $420 million have put it back on track toward growing its two primary businesses: propane and specialty chemicals.

As a result, its balance sheet in much stronger, putting it in the perfect position to make an acquisition. Marleau sees Canwest Propane, a division of **Gibson Energy Inc.**, as an ideal target, given that Gibson is highly leveraged with debt four times EBITDA.

I said almost the same thing in August minus the takeover candidate. I too like Superior.

Pick #2

Up until reading *Market Masters* by Robin Speziale, I had never heard of Charles Marleau, but I'll be sure to keep an eye on his recommendations in the future.

Marleau's October 20 commentary discusses the lack of love for Canadian auto parts manufacturers. He sees the weakness as a product of investors rotating out of the sector as a result of slowing auto sales, which have led to attractive valuations for both **Magna International Inc.** (TSX:MG)(NYSE:MGA) and **Linamar Corporation** (TSX:LNR).

"LNR and MG trade at 4.1x and 4.5x EV/EBITDA respectively, which is at the low end historically and relative to the industry average trading roughly around 5.5x," wrote Marleau in his October 20 commentary. "The opportunity for multiple expansion as well as new technology reaching manufacturers are why we are bullish on both the names going forward."

If you're a big believer in free cash flow, Linamar definitely should be on your list.

Pick #3

Up until this point, I've been on the same page as Marleau but it's this third and final pick where I respectfully disagree.

Marleau's September 29 commentary highlights specialty retailer **Aritzia Inc** (TSX:ATZ) and its recent IPO. He points to the company's planned push into the U.S., where it will open 15 stores within the next five years. Sure, it could go fabulously well, as was the case with **Lululemon Athletica Inc.'s** American expansion, or it could be a disaster as so many Canadian retailers have experienced over the years (Joe Fresh being the most recent example).

"We believe that ATZ has the team, drive and discipline to continue growing the company's revenue, EBITDA and bottom line by 20%, 25% and 45% respectively," wrote Marleau in his September 29 commentary.

While this might come to fruition, one must also take into account the possibility that Aritzia fails to meet these lofty growth projections. Does it really deserve a similar valuation to Lululemon, despite the fact its operating margins are about half those of the athleisure-wear champion and the fact that it's an unknown commodity south of the border?

I don't think so, but you be the judge.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:MGA (Magna International Inc.)
2. NYSE:RY (Royal Bank of Canada)
3. TSX:LNR (Linamar Corporation)
4. TSX:MG (Magna International Inc.)
5. TSX:RY (Royal Bank of Canada)
6. TSX:SPB (Superior Plus Corp.)

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