

October 27, 2008

Groundhog Day Part II

As October comes to an end as one of the most volatile months ever in the stock market, I am left almost speechless. Like many of you, I sit in front of my television screen or computer terminal with my jaw on the ground. When large, seemingly sound companies like Fannie Mae, Freddie Mac, Lehman Brothers, Washington Mutual, Wachovia, and AIG Insurance, go bankrupt, it is not too difficult for investors to be concerned to the point of panic. The month of October reminded me of the 1993 movie *Groundhog Day*. The movie involves a television reporter (played by Bill Murray) who goes to a small town in Pennsylvania on February 2nd to report on whether the groundhog has seen his shadow. For various reasons, the reporter cannot move on with his life. He reports the actual events on Groundhog Day, goes to bed at night, and wakes up and repeats the previous day again. Regardless of what he does (including driving off a cliff) he wakes up and Groundhog Day is repeated. Well, the month of October felt like the movie. Despite what global governments were doing to help the situation, we did not seem to be moving forward. Every day felt the same, just different companies or economies reporting collapse or near collapse. As October draws to an end, I am beginning to feel the repetitive declines in the markets may be ending, although progress may take longer than many of us would like.

With the Dow Jones, S&P 500 and TSX all down 30% to 40% from their highs, investors are looking for some type of stability. Once investors feel the market has stabilized they will be more confident going forward. We feel that central banks around the world are taking the appropriate steps to help ensure that the financial system continues to function properly, but it will take time for the measures to take effect. Primarily, central banks are lowering interest rates, providing financial aid for troubled institutions, companies and countries, and providing liquidity to the financial system. The one other important variable which should help consumers, is the decline in oil prices. The drop in oil prices from a record US\$147 per barrel to the current level of mid \$60s and the corresponding drop in gas prices at the pump should provide additional discretionary income for the consumer. Accordingly these factors will eventually lead to more consumer confidence which should lead to a gradual recovery. But confidence has been shaken tremendously and it will take time for it to be restored. The decline in stock markets around the world has been so dramatic that it has left investors shocked and dismayed. However, we feel that some of the fear in the market is more psychological than real. Assume for example an investor purchased shares in Company A at \$10 a share. The shares proved to be a

prudent investment and the share price rose to \$30 during the first two years of the investment. In year three the stock dropped \$10 and closed the year at \$20 per share.

Initial Purchase Price	\$10
Stock Price End of Year 2	\$30
Stock Price End of Year 3	\$20

The investor can look at his investment in two ways. The first scenario considers that the purchase was made for \$10 and three years later it is now \$20. They have doubled their money in 3 years. Most investors would consider that a good return. The second scenario considers the same investor looking at his investment at the beginning of Year 2 at \$30 per share and then at the end of Year 3 at \$20 per share. Although the stock has been a good performer over three years it has not done well recently and the investor feels he has lost 33% of his investment. I am not trying to minimize the losses that have occurred, but unless you are forced to sell the stock or the company has some permanent negative changes, a decline in stock price although concerning is not necessarily catastrophic. In our example, as long as Company A continues to pay a dividend, the decline in the stock price could be viewed as temporary, since as the economy picks up again, share prices should rebound.

Overall, we continue to feel comfortable with our portfolios despite the sudden declines. Only one of the companies we have invested in has cut their dividend distribution to date. We are not aware of any further dividend cuts to come. Our weighting in oil & gas stocks of approximately 15%, compared to 30% for the TSX index, as well as avoiding heavy composite weighting stocks such as Potash Corporation, has insulated us somewhat from the market declines. However, with declines for all markets throughout the world and for all sectors of the economy, our portfolios have experienced some uncomfortable declines. The central banks of the world are addressing the economic issues as best as they can, but it will take time for the fiscal stimulus to take effect. There is little doubt that the US and probably Canada are either in or heading towards a recession but we believe the markets have bottomed or are close to the bottom. We feel that the companies we have invested in will survive the economic slowdown and a slow recovery in stock prices will occur. Consumer and investor confidence has been hit hard and regaining that confidence will be a gradual process.

Sincerely,

Stephen Sisokin
President