



July 2008

Confucius say; “*Our greatest glory is in never failing but in rising every time we fall.*”

Investor Behaviour – See Chart “*Bull & Bear Markets*”

- Markets spend more time in positive territory (bull) than negative (bear)
- Bull markets are, on average, longer and more intense, providing a more significant percentage change
- On average bear markets are briefer, and yet engender fear. It is during these periods that there are significant investment bargains to be found.
- Investor discipline during bear markets is critical.

See Chart “*Don't miss out*”

- Stay Focused – Don't let a bear market make you lose sight of long-term investment returns
- Stay Invested – Missing the best days of a bull market can drastically reduce your long-term returns
- Stay Diversified – A diversified portfolio is a key strategy to participate in bull markets across different sectors, industries and geographic regions

Inflation

Real equity returns and valuation multiples tend to be lower when inflation rates are higher. Bonds, especially longer term maturities, fair much worse. Commodities have proven to be resilient during inflationary periods, partly because a scarcity of raw materials is often the containing factor, thus inflationary for the global economy. The current surge in global growth, driven by emerging markets, is likely such a case. This would suggest that commodities will continue to be strong performers.

Inflation Factoids:

Today, these items cost **X** times as much as in 1950; **Y** times as much as in 1967 and **Z** times as much as in 1980:

Gasoline	16 times 1950; 12 times 1967; 3.3 times 1980
Crude Oil	49 times 1950; 45 times 1967; 3.6 times 1980
Gold	25 times 1950; 25 times 1967; 1.4 times 1980
Silver	21 times 1950; 9 times 1967; about the same as 1980
Homes	28 times 1950; 12 times 1967; 4.3 times 1980
Income	18 times 1950; 7 times 1967; 2.8 times 1980
S & P 500	77 times 1950; 15 times 1967; 12 times 1980
CPI*	9 times 1950; 7 times 1967; 2.6 times 1980

*CPI = Consumer Price Index – Government measure of inflation

Markets

The first six months of 2008 has been a period afflicted by volatile markets, record oil prices and global central bankers refocusing on inflation.

On a combined basis, the energy and materials sector account for just under half of the S&P/TSX index and this would largely explain why, on a year to date basis, the Canadian market (+6.0%) has been one of the few exceptions to the rule of declining global stock markets.

During this same time frame, the U.K. (-14.4%), FTSE Eurofirst (-21.0%), the S&P 500 (-12.5%) and MSCI World Equity (-12.0%) all suffered declines. The Reuters-Jeffreys CRB spot index has increased by 30.4% since the 1st of January, its strongest rise in 35 years. This is a measure of commodity prices.

The Bank Credit Analyst recently wrote "the oil bull market is developing into a major blow-off in prices which is both dangerous and electrifying". The danger lies in the fact that high energy prices threaten world growth and stability and often create negative sentiment towards the markets. Furthermore, like copper, zinc and uranium, this latest surge in oil prices has followed the financial roadmap carved out by investors and speculators alike, and has evolved into a financial mania. The debate surrounding potential manipulation of energy prices that was brought to the forefront with the May 20th testimonies in front of the Committee on Homeland Security, has added to the volatility. This, along with the decrease in subsidies for energy products by numerous emerging markets, including China and India, has led us to take a more conservative view of the energy markets.

Canada

Recession worries linger, especially for southern Ontario, as the Canadian economy continues to suffer from a weak export sector, lower investment as a result of tighter credit conditions and a slowing real estate market. Although we find the current sell off in banks interesting, we continue to have concerns and believe it prudent to remain under weight the sector with most accounts having no holdings.

Growth in Canada has moved to the West and East coasts as resources are now becoming the cornerstone of the Canadian economy. The continuing development of the oil sands increased spending on natural gas exploration and uranium and coal projects will all be major contributors to future growth. Meanwhile, regional job creation, national tax cuts and rising incomes have left the Canadian consumer in relatively good shape.

United States

Key indicators like housing, construction spending and service output levels have hit new lows. The bottom line is that at best, the United States economy has stalled and may even have actually contracted through the first six months of the year once the revisions are done. Any recovery will be modest and may be several quarters away. This year's policy actions have gone a long way to minimize the negatives. These include supporting the banking system with innovative tools, the fiscal stimulus package to support spending and reforms related to mortgage lending. While this is a near term benefit, it remains a long term negative as it addresses the superficial issues but largely ignores the structural issues that created the mess in the first place.

China/India/Asia

The drop in export growth should have only a small impact on China's economy, as domestic investment and consumption remain the primary engines of growth. Retail sales, the result of strong employment and wage growth and a high savings rate, continue to perform well not only in China, but in non-Japan Asia and Latin America as well.

India will probably be the least impacted economy from any global slowdown. Government spending as well as foreign investment, continue to fund a multitude of infrastructure projects.

Something to Ponder ...

Remember the old axiom, "As GM goes, so goes the nation." Well, let's hope that one is outdated. GM hasn't been making the right kind of cars -- no hybrids, no minis. Now GM is going to make the plug-in Volt. Will GM be too late? Will the Volt sell big-time? Will Americans continue to buy cars the way they did in the past? Guess we're going to find out. In the meantime, GM is now worth less than Marvel, which makes toy cars.