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Published for the friends and clients of
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April 2009 Newsletter

Excitement and Confusion

The first quarter of 2009 has provided us with more extreme volatility. The year started well until January 6th, when the 24% recovery rally that began on November 21st of 2008 failed and the TSX slid 21% until March 6th, coinciding with a 12-year low for U.S. stock markets. A few positive words from America's bank CEOs then triggered the current rally.

While we continue to see bad economic news, a number of previously bearish investors have become optimistic during the last 6 months of carnage. Warren Buffett made his famous bullish call in October, after being negative for years. Prem Watsa, CEO of Fairfax Financial, famous for making a $2.5 billion profit shorting subprime loans has also become a stock buyer. Li Ka Shing, buyer of the Expo 86 waterfront land in 1987 and Renaissance Energy in 1999 has also become bullish. While no one has a perfect track record, self-made billionaires have more credibility than most when it comes to economic forecasting.

	All Time High	Mar 6/09 Low	% From High	Mar 31/09 Close	% From High
S&P 500	1,576	666	(58%)	798	(49%)
TSX Composite	15,154	7478	(51%)	8720	(42%)

Guaranteed Investments

March 31st Close:

Canada T Bills	30 day	0.35%
	60 day	0.36%
	90 day	0.37%
	180 day	0.47%
	one year	0.58%
Canada Bonds	2 year	1.07%
	5 year	1.74%
	10 year	2.78%
	30 year	3.58%
GICs	1 year	2.05%
	2 year	2.35%
	3 year	2.80%
	4 year	3.05%
	5 year	3.30%

U.S. Rates

U.S. T Bills	1 month	0.12%
	3 month	0.20%
	6 month	0.41%
	12 month	0.53%
U.S. T Bonds	2 year	0.80%
	5 year	1.66%
	10 year	2.66%
	30 year	3.53%

Clearly the zero risk options, while safe, are not producing reasonable returns today.

I personally believe that Canada bonds over one year in term are very risky. If inflation returns and rates rise, a 10 year bond currently yielding 2.78% will drop sharply in price.

Corporate Bonds, Capital Trusts and Debentures

Examples are:

Issuer Bonds	Maturity	Jan. 2 Yield to Maturity	March 31 Yield to Maturity
Royal Bank F/F	June 2014	8.0%	7.00%
Bell Canada	Feb 2017	7.2%	6.00%
Shaw Communications	Mar 2017	7.6%	6.93%
Telus	Mar 2017	7.0%	6.11%
Great West Life F/F	June 2017	8.6%	9.17%
TD Bank F/F	Dec 2017	8.3%	8.30%
Suncor	May 2018	7.0%	6.52%
Canada	2018	2.83%	2.78%
Capital Trusts			
Royal Bank	June 2018	9.3%	8.13%
TD Bank	Dec 2018	9.3%	7.58%
Bank of Montreal	Dec 2018	9.6%	8.22%

Note that the yields for most of these bonds are LOWER than on January 2. This is because the bonds have appreciated in value, providing recent buyers with capital gains as well as the income. I believe that a diversified corporate bond portfolio is much better value than Canada bonds at today's prices.

Please check with me prior to purchasing any of these. These all have different credit ratings and the fixed floaters (F/F) all have different maturity terms. If our banks become Lehman Brothers stories these will suffer. Corporate bonds are usually sellable prior to maturity, but are generally not as liquid as stocks or government bonds. However, if the credit markets return to normal in a few years this could be a once in a decade opportunity to lock in decent returns with relatively moderate risk (in a diversified portfolio).

Equity with Income

The following income producing stocks were in my January newsletter:

	Jan 2/09 Price	Mar 6/09 Low	Mar 31/09 Price	Current Yield
Royal Bank	$36.95	$25.52	$36.78	5.43%
TD Bank	$44.09	$32.37	$43.46	5.61%
Bank of Nova Scotia	$33.28	$23.99	$31.07	6.30%
Power Financial Corp.	$24.33	$14.66	$20.58	6.80%

While these are down only slightly now, they were much lower at the March 6th bottom, making the last quarter a challenging time to hold blue chip financial companies. While making no predictions for the next 6 months, I suspect these will be meaningfully higher in 18 months.

Taking Losses

One of the most challenging aspects of investing is when to cut our losses on the "dogs" in our portfolios. We don't want to "buy high" and "sell low," but we also don't want to ride lost causes down to nothing or next to nothing. For example, Nortel, Air Canada, Ballard Power, and GM have provided nothing but grief and just kept going down once they started their slide.

Today is as good a time as any to get rid of "lost causes," as the highest quality companies are also beat up and the current economic climate can accelerate the demise of flawed business models.

Picking total losers from beaten down stocks that can recover is tricky, but this is what to look for:

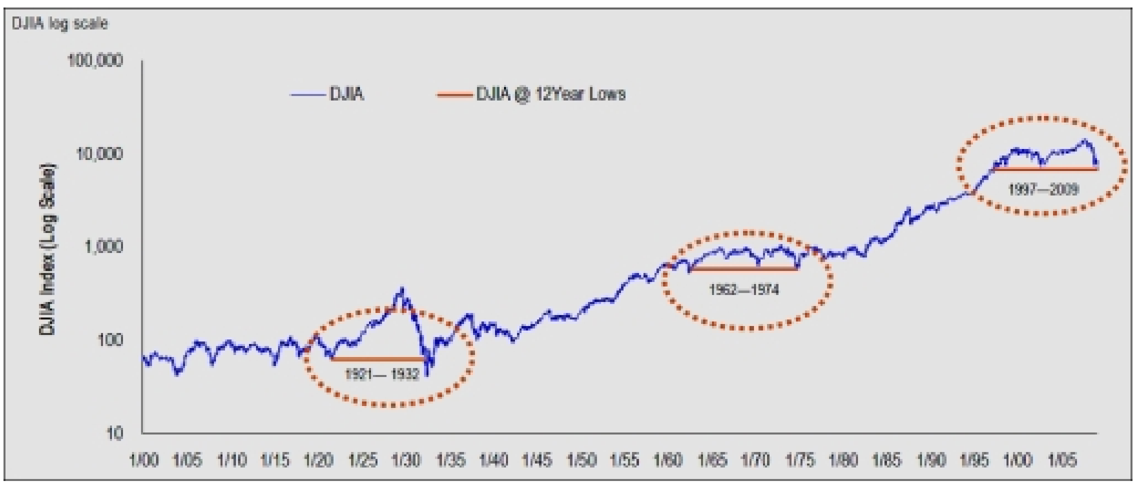
1) The stock is underperforming the market and others in its sector.
2) The company has too much debt, is losing money, or has expensive legacy costs (U.S. autos, Air Canada).
3) The company's competitive advantages have been overcome by technology or other social changes (Ballard Power, newsprint makers, Yellow Pages).
4) Management has been "ethically challenged," lining their pockets at the expense of shareholders.

Attractive recovery candidates typically have dropped due to temporary falling demand and prices for their services. For example when commodity prices and the economy recovers we can expect to see gains in beaten down stocks (H&R REIT, Trinidad, NewAlta, Canadian banks).

One advantage of purging your account of the nastiest stocks is that once you don't have to see these dogs on your statement every month you are less likely to throw in the towel and sell your best stocks on an inopportune down day.

Long-Term Picture

The chart below goes back over 100 years. During this time we had three 10 year plus periods when the Down Jones Industrial Average made nothing; 1921 to 1932, 1964 to 1974, and 1997 to 2009. Following 1932 and 1974, markets recovered and hit new highs. While there are no surefire indicators to predict markets, historically long periods of lousy markets are followed by long periods of good markets.

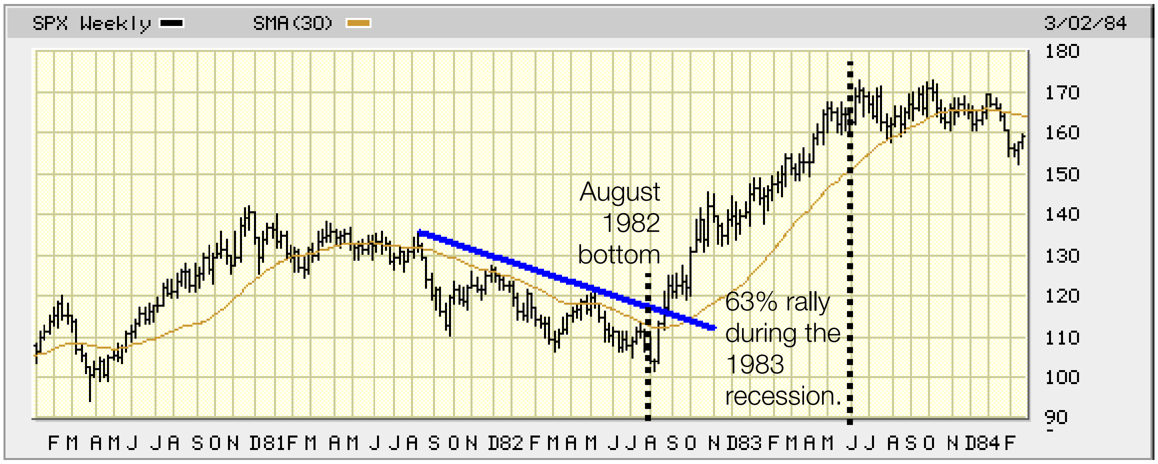


Short-Term Picture

While the market has picked up nicely from its March 6th low (up 16.6% for the TSX) the market has not yet flashed a technical buy signal. U.S. home sales and manufacturing new orders numbers have come in better than expected and credit spreads on bonds have also improved, but unemployment numbers have been terrible. In the short term the jury is still out on whether we are in a bear market rally or a new bull market. If you wait to see good economic news before becoming optimistic on the market you will likely miss the recovery.

For example, world stock markets bottomed in August of 1982, while the Nanaimo economy didn't show much signs of recovery until 1985. 1983 was a fabulous stock market year, long before the local economy recovered.

1982 Bull Market Start



Now

Favorite Corporate Bond

Currently RioCan REIT 3 year bonds yield over 7%. These have a BBB credit rating and RioCan has a solid business and a good balance sheet. These are particularly attractive for RRSPs and RRIFs.

Favorite Preferred Shares

Recently Canadian banks have been issuing 5 year preferred shares with 6.25% dividend yields. These have been coming to the market regularly. These look like great value compared with Canada bonds or GICs. If this sounds like your cup of tea, call and I can put you on a list for the next issue, or find some trading on the market.

Favorite Equity

The XIU is an exchange traded fund for the TSX 60 index. It is currently made up of about 28% energy shares, 28% financials, 19% materials (mining, gold, etc.) and the balance would be other large Canadian companies. This is a great way to participate in the Canadian market for its eventual recovery.

Summary

Today is a good time to get rid of some "dogs" in your portfolios. Depending on your risk tolerance and current asset allocation, the proceeds could go to cash, corporate bonds and preferreds or equities. If you can hear some of these dogs "howling" in your portfolio, give me a call and we can discuss which holdings should be kept for potential recovery and which should be sold.

Most of you, particularly if you own bank shares, will see an improvement on your March statements. Our winter won't last forever, and neither will this bear market.

Ian Douglas	Barbara Holmes	Lindy Edgett
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