Published for the friends and clients of
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January 2009 Newsletter

New Reality

We start 2009 in shock from 2008. Multiple U.S. bank failures, collapsed commodity prices, rising unemployment, GM and Chrysler taxpayer bailouts, and the worst stock market drop since 1937 has made 2008 a very uncomfortable year for investors.

During the last three months we have witnessed massive selling of stocks and corporate bonds, as hedge funds, banks and ordinary investors headed for the exits. In some cases this was instituted by margin calls. In other cases it was old fashioned panic as investors lost confidence in the financial system and couldn't stand to see their accounts go lower.

For the time being the market bottomed on November 21st.

	All Time High	Nov. 21/08 Low	% Drop	Jan. 2/09 Close	% Gain from Low
TSX	15,154	7,647	(49.5%)	9,234	20.7%
S&P 500	1,576	741	(53.0%)	931	25.6%

The most profitable investment class for 2008 would have been 30-year Canada bonds or U.S. treasuries. If you bought these one year ago you could have locked in a 30-year return of about 4.2% (Canada's). With 30-year Canada's now yielding 3.5% you would have earned the 4.2% plus about a 10% capital gain. At that time of rising inflation locking in a 30-year yield of 4.2% seemed a bit crazy so I thought that owning a diversified portfolio of secure Canadian financial stocks, REITs, corporate bonds, and hydro income trusts would be a better alternative.

Was I wrong!

Today's Investment Alternatives

Firstly, I'll mention the safest government guaranteed alternatives:

January 2 Close:

Canada T Bills	30-day	0.70%
	60-day	0.78%
	90-day	0.82%
	6-month	0.81%
	1-year	0.81%
Canada Bonds	2-year	1.15%
	5-year	1.83%
	10-year	2.83%
	30-year	3.55%

GICs*	1-year	3.05%
	2-year	3.75%
	3-year	3.95%
	4-year	4.00%
	5-year	4.10%

*Coast Capital Savings Credit Union annual pay

U.S. Rates

U.S. T Bills	1-month	0.02%
	3-month	0.08%
	6-month	0.27%
	12-month	0.375%

U.S. T Bonds	2-year	0.82%
	5-year	1.68%
	10-year	2.36%
	30-year	2.80%

All of these investments guarantee your capital if held to maturity. In the case of the longer (over one year) bonds, if interest rates go up the value of these will drop sharply.

The reality of these rates is that while they are "safe" they don't provide an acceptable return for most investors. As a result when people see signs that the economy has bottomed expect a stampede into corporate bonds and the stock market.

Corporate Bonds, Capital Trusts and Debentures

Corporate bonds currently carry huge spreads above Canada bonds. Should these companies survive we now have an excellent opportunity to lock in very attractive rates.

Examples are:

Issuer Bonds	Maturity	Yield to Maturity
Royal Bank F/F	June 2014	8.0%
Bell Canada	Feb 2017	7.2%
Shaw Communications	Mar 2017	7.6%
Telus	Mar 2017	7.0%
Great West Life F/F	June 2017	8.6%
TD Bank F/F	Dec 2017	8.3%
Suncor	May 2018	7.0%
Brookfield Power	Nov 2018	10.5%
Canada	2018	2.83%
Capital Trusts		
Royal Bank	June 2018	9.3%
TD Bank	Dec 2018	9.3%
Bank of Montreal	Dec 2018	9.6%

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

What we used to call blue chip "widows and orphans" stocks have been hammered and provide some interesting yields.

	All Time High	Jan 2/09 Price	% Drop	Yield
Royal Bank	$61.08	$36.95	(39.5%)	5.41%
TD Bank	$77.10	$44.09	(42.8%)	5.53%
Bank of Nova Scotia	$54.22	$33.28	(38.6%)	5.89%
Power Financial Corp.	$42.69	$24.33	(43.0%)	5.75%

These are the Canadian financial companies that have been the most unscathed in the last year. Clearly unscathed is a relative term. None of the big 5 Canadian banks have ever lowered a dividend, including during the great depression, World War II and the other numerous crises in the last 150 years.

Canadian Diversification

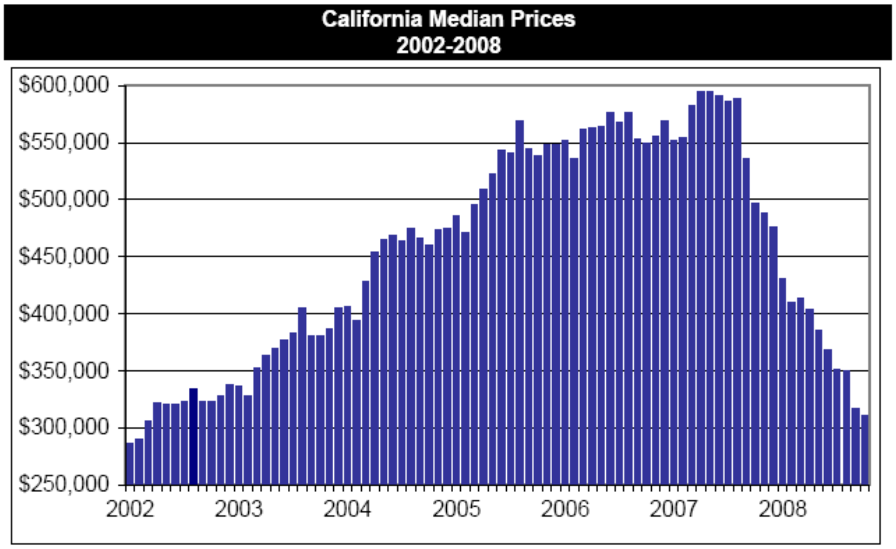
XIU is the symbol for the TSX 60 Index ETF. The management fee is only 0.17% and this is a cheap way to buy the Canadian large cap market. This will include the banks, insurance companies, oil and gas companies, golds, plus others including Potash and RIM. The yield is currently 3.45%.

Tax Free Savings Accounts (TFSA)

Every taxable Canadian adult with $5,000 of non-registered funds should open one of these accounts. This will provide a tax shelter for all of the income earned. Most investments are eligible for these, but in most cases interest bearing investments are the most suitable. I will try to contact everyone to set these up, but call if I've missed you.

Outlook for 2009

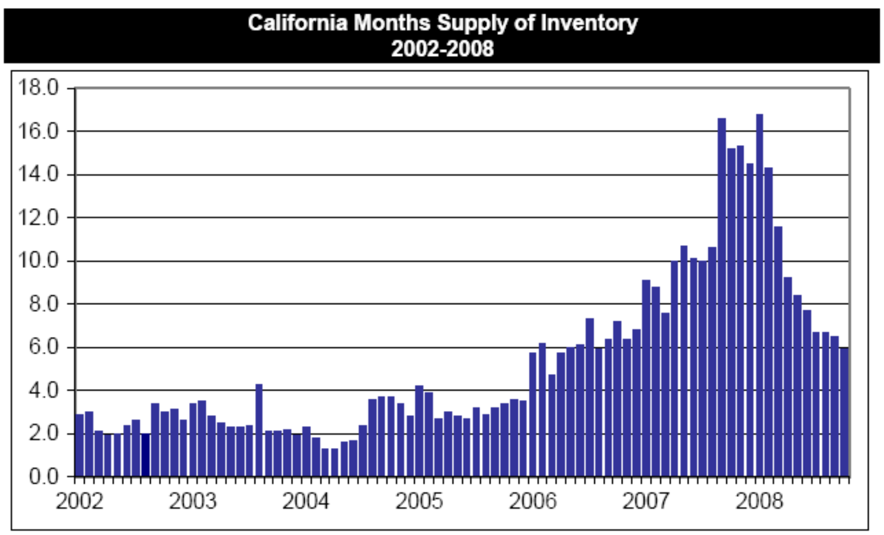
The U.S. market peaked 14 months ago, Canadian financial stocks peaked 19 months ago, REITs peaked 22 months ago and U.S. housing stocks peaked 41 months ago. There are very few people left on earth who don't believe we are in a recession or a depression. Cash on the sidelines, earning almost nothing, is at 20 year highs, ready to be invested when investors see light at the end of the tunnel. Warren Buffett has been buying and investors like Prem Watsa (Fairfax Financial) who made $2 billion shorting subprime mortgages recently invested $200 million in H&R REIT. Most shares have recovered from the November 21st low. While we may see more speed bumps along the way, I expect 2009 to be a good year for corporate bond and equity investors.



Source: California Association of Realtors and Raymond James & Associates, Inc.

California housing prices are down sharply...

Other California Housing Data



Source: California Association of Realtors and Raymond James & Associates, Inc.

…but inventory is starting to clear.

Thank you

Thank you again for your maturity and goodwill during these challenging times. This has made it much easier for me to try to provide the best guidance for each person. All the best for 2009.

Ian Douglas	Barbara Holmes	Lindy Edgett
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