



MONTHLY MARKET COMMENTARY

INVESTMENT RESEARCH

JANUARY 2010

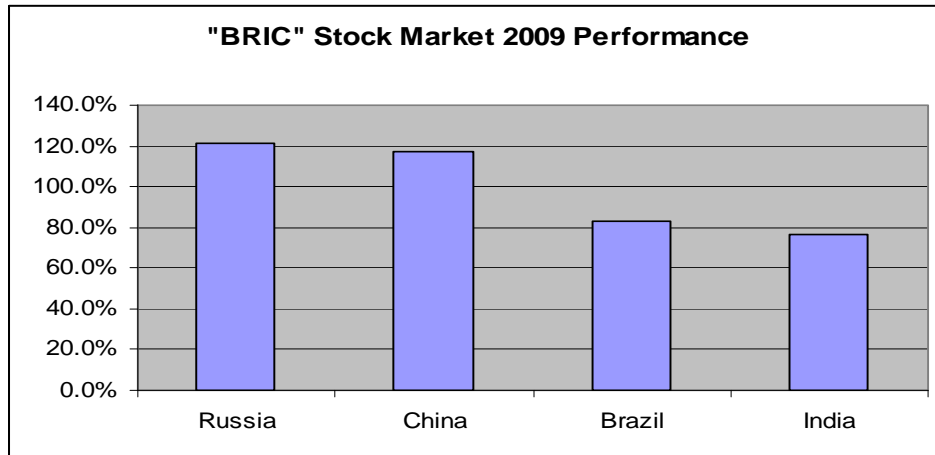
December 2009 Review

	December 31, 2009	December 31, 2008	% Change
TSX	11,746.1	8,987.7	30.7%
S&P 500	1,115.1	903.4	23.4%
DJII	10,428.0	8,776.4	18.8%
NASDAQ	2,269.1	1,577.0	43.9%
10 Yr. Cda Bonds	3.61%	2.69%	92bp
10 Yr. US Bonds	3.84%	2.21%	163bp
90 Day Cda T-Bills	0.24%	0.91%	-67bp
90 Day US T-Bills	0.05%	0.08%	-3bp
US\$ vs. Can\$	\$0.9515	\$0.8200	16.0%

2009

A rollercoaster ride is the best way to describe 2009. We started the year with a great deal of anxiety and uncertainty over the economy and financial markets, but ended the year with a sense of relief and general optimism towards the future. Unlike 2008, 2009 was a very successful year for those investors willing to accept some risk in their portfolios. In 2008, government bonds and cash were the best performing asset classes with positive returns while other asset classes recorded negative returns. In 2009, cash & government bonds had the poorest returns. We feel 2008 was an anomaly for investors, as the concept of risk and return became detached i.e., investors tend to be rewarded (return) over time for taking on some risk. As one can see from the table above, government bonds suffered a capital loss as Canadian ten-year bond rates rose in 2009 from 2.69% to 3.61%, while U.S. ten-year bond rates rose from 2.21% to 3.84%. Bond prices move inversely with bond yields (a higher/lower bond yield implies a lower/higher price).

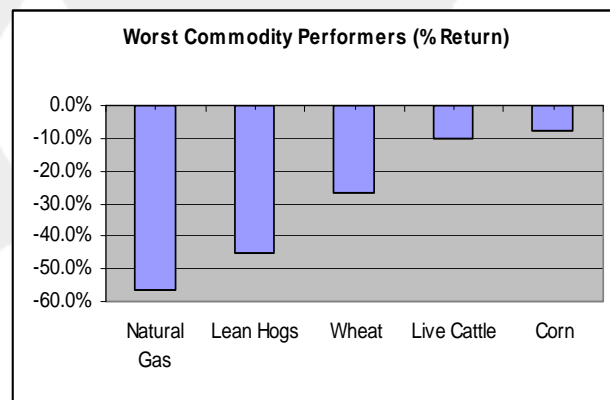
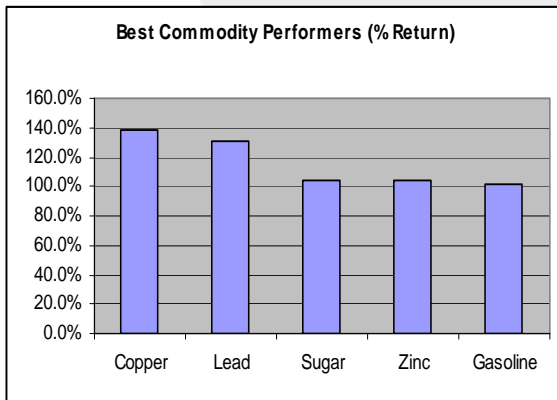
North American stock indices did well as the TSX was up close to 31%, the S&P 500 Index rose 23.4%, while NASDAQ rose 43.9%, with the latter two expressed in local currency. For those investors who were willing to assume even more risk in 2009, the BRIC (Brazil, Russia, India and China) and other emerging countries stock markets did particularly well as we illustrate on the following page.



Source: Bloomberg. Russia is the MICEX Index, China is the Shenzhen Index, Brazil is the Bovespa Index and India is the Sensex 30 Index. All returns expressed in local currencies.

We could not find any of the global stock market indices showing negative returns for 2009. The lowest performer we found is the TOPIX Index (Japan) with a return of 5.6%.

In addition to equities, the commodity sector also did well in 2009 as illustrated below, although the performance was more mixed. One of the reasons we highlight this asset class is we continue to believe it will attract investment dollars and grow in importance in portfolios. We are reminded of the early 1980s when real estate gradually became an accepted asset class for institutional portfolios, despite early naysayers. Today, real estate is an accepted asset class. We feel commodities will become an "accepted" asset class in addition to fixed income, equities and real estate in the coming years.



Source: Bloomberg

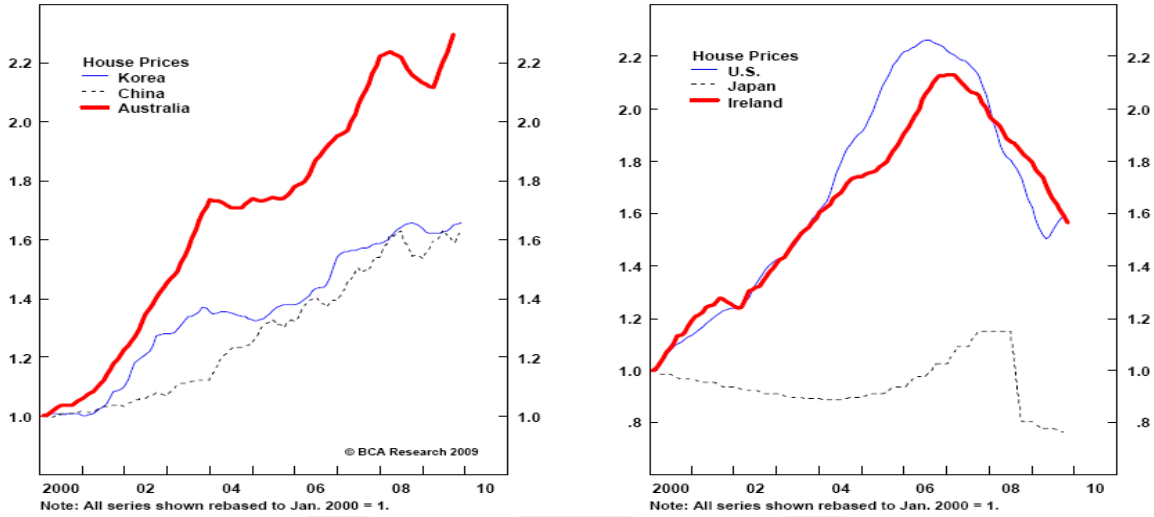
2010

Economy: Our view for 2010 is the world will continue to recover from a very deep recession and financial crisis and although there are many challenges facing the global economy, (large deficits, high unemployment rates are but two examples) the challenges, in our view, will not be as difficult as the financial crisis we have just emerged from.

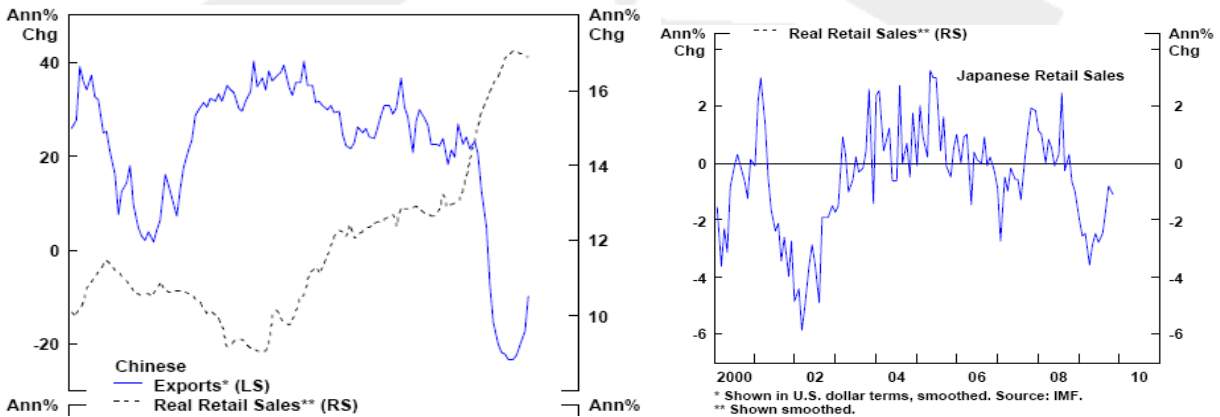
The global economy is on the mend and better times lie ahead. The economic recovery looks to be an uneven one with the developing/emerging economies leading the way. One lesson we are reminded of again and again is that world economic growth is no longer solely dependant on North America/Europe/Japan.

Although trading among nations is the “glue” that binds us as a global community, many of the emerging countries that have traditionally relied on this for their economic growth have shown a remarkable ability to detach from this. In particular, we illustrate this point with the graphs below, as we show how well house prices and retail sales have done in the traditional exporting Asian countries (ex Japan) versus the developed (North America and Europe) countries.

HOUSE PRICES

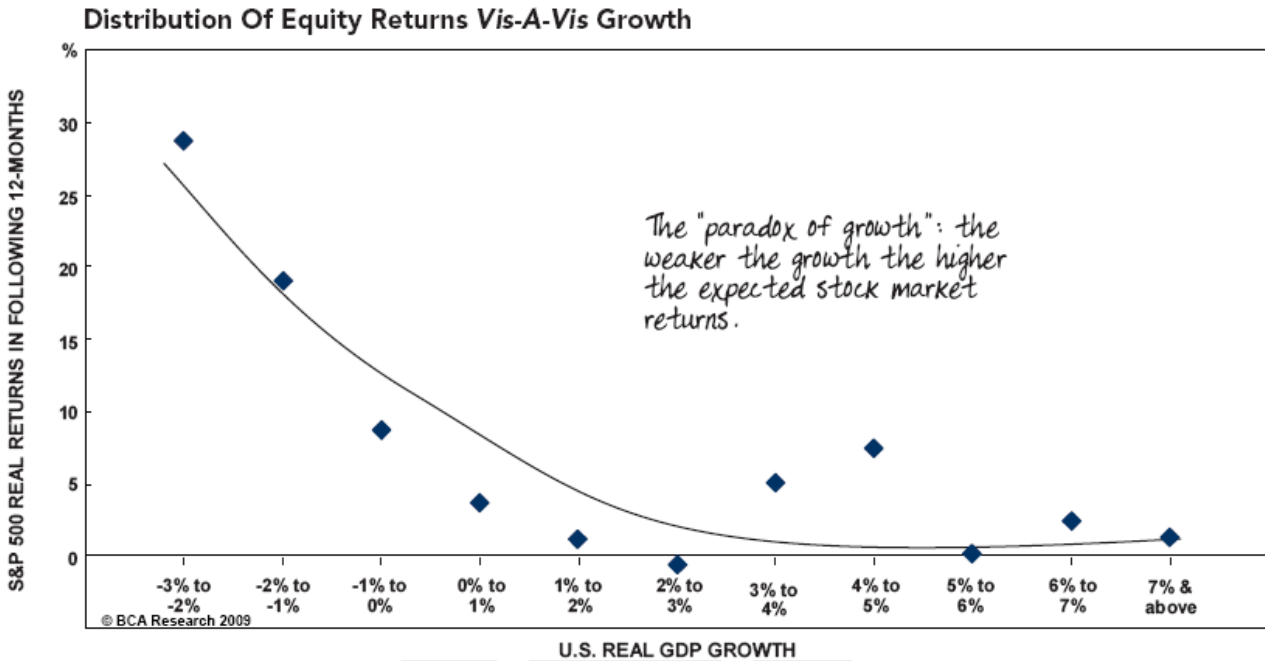


RETAIL SALES (CHINA LEFT, JAPAN RIGHT)



Source: BCA

Outlook for the Stock Market: All signs point (high indebtedness in developed world consumers, fragile banking system) to a recovery in the economy which will likely be below historic averages. One may feel this implies that returns from the stock market will not be good; this is not necessarily the case. We illustrate this point in the following graph.

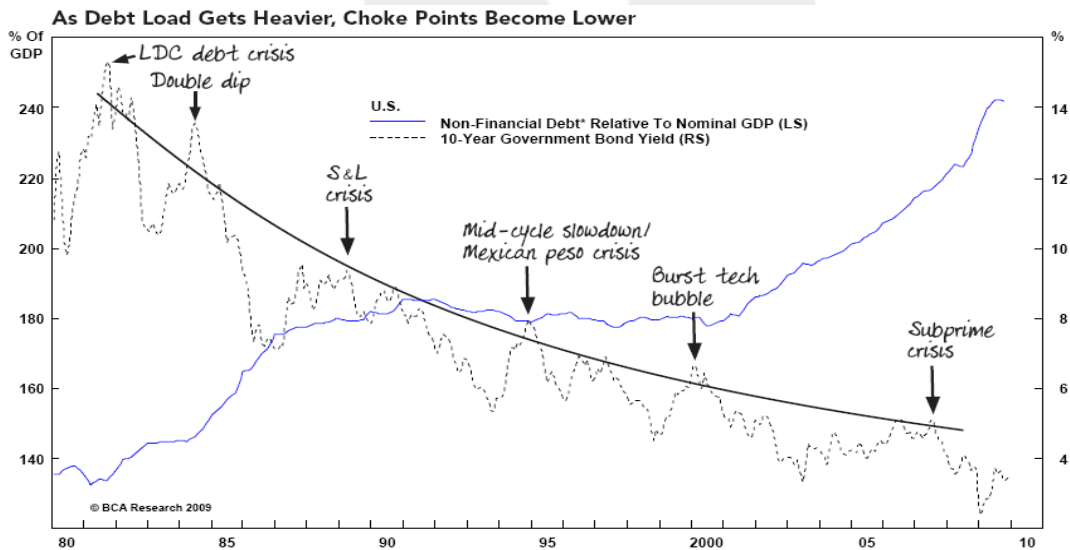
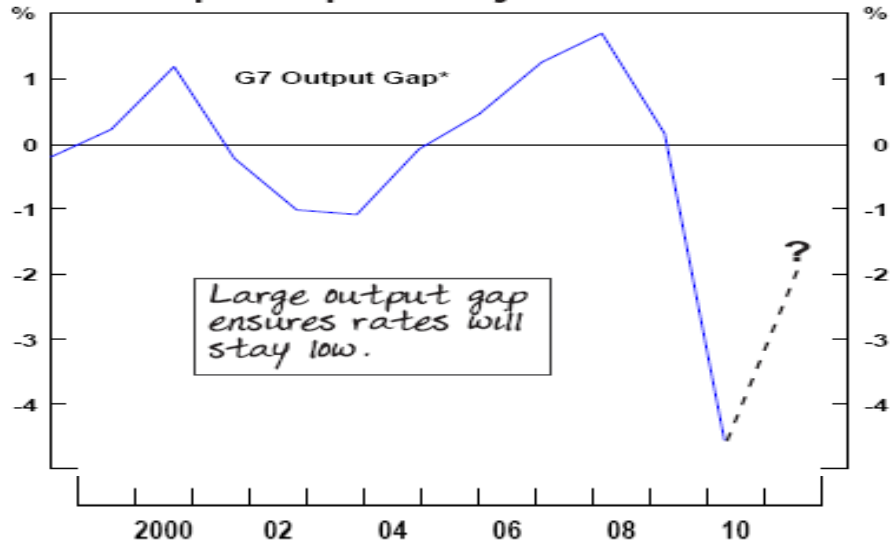


Source: Bank Credit Analyst (BCA)

As one can see, the best returns (the Y axis which excludes inflation) from equity markets are when economic growth (the X axis) is either negative or low. Stock market returns become less as economic growth becomes stronger. *Bank Credit Analyst* uses the term to describe this situation as the “paradox of growth”. One would naturally assume stock market returns are very good when the economy is doing well. The reason for this paradox is due to interest rates and inflation. As the economy grows, interest rates and inflationary pressures tend to rise, prompting central bankers to increase interest rates. With a fast growing economy, interest rates and inflation tend to rise rapidly, which has the effect of putting downward pressure on the stock market. Conversely, with a slow economy, interest rates and inflationary pressures tend to rise much slower, improving stock market returns. Interest rates act as an alternative investment (e.g. Guaranteed Investment Certificates) to the stock market. Low/high interest rates act as an incentive/disincentive to invest in the stock market.

Themes for 2010:

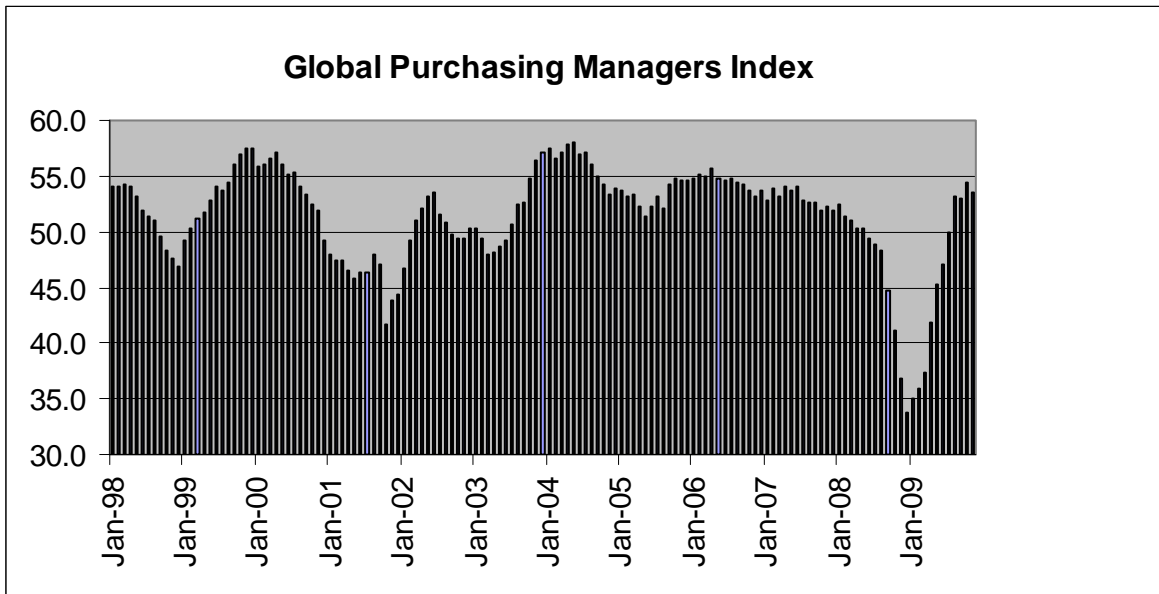
A) Low Interest Rates: Administered (set by the central banks) interest rates in Canada and the U.S. are close to zero. In Canada, the Bank of Canada has stated these low interest rates will stay in existence at least until the second half of 2010, while for the U.S. they have used the term “an extended period of time” to describe their current low interest rate policy. There are two reasons we feel interest rates will remain low by historical standards; 1) The output gap is the difference between the demand for an economy’s goods and services relative to the supply of goods and services available. The larger the gap, the less likely inflation and interest rates will rise. The graph on the following page illustrates this gap. Even if demand were to strongly rebound (not our forecast), the output gap is still large. To our understanding, this output gap is at a thirty-year high. There appears to be very little need to materially increase interest rates to fend off inflation. 2) Interest rates still appear to be on a secular downtrend starting from the 1980s. The second graph (right axis, dark line) illustrates this point. As the developed economies of North America and Europe have progressively taken on more debt (left axis, light solid line) they become more vulnerable to the effects of rising interest rates. It is difficult to imagine a significant rise being sustainable as the demand for credit (e.g. mortgages) will quickly drop off causing interest rates to fall again.



Source: Bank Credit Analyst

Given our view that interest rates will remain low, we advise investors to seek relatively high and stable dividend paying equities (any company which has kept its dividend intact is unlikely to reduce it in 2010).

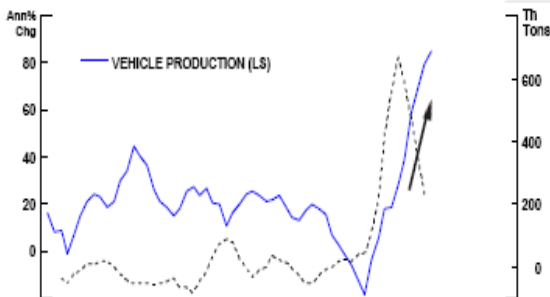
B) An Improving Economy: As mentioned above, the global economy is on the mend. The graph on the following page highlights what business managers are saying (doing) in terms of their business. When asked if they plan to buy, more or less the majority answer is more. The Global Purchasing Manager's Index asks this question and a response above 50% (more yes than no) indicates businesses plan to spend more. The depth of this downturn was seen in the first quarter of 2009 when less than 35% of the respondents replied yes.



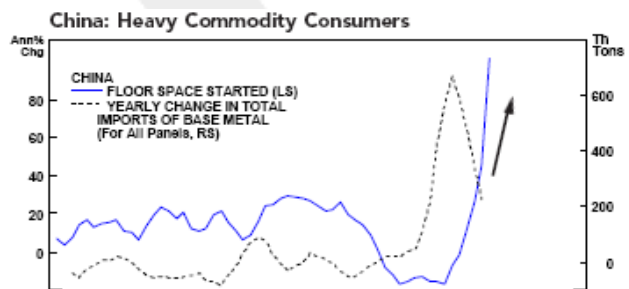
Source: J.P. Morgan

The developing countries have shown a remarkable resilience to the financial crisis. China, in particular, has shown a strong rebound in their economy and the Chinese consumer has been spending. The left graph (solid line) is China's automobile production, while the dotted line in the same graph is the growth rate of imported base metals. The right graph illustrates China's commercial construction measured in terms of floor space.

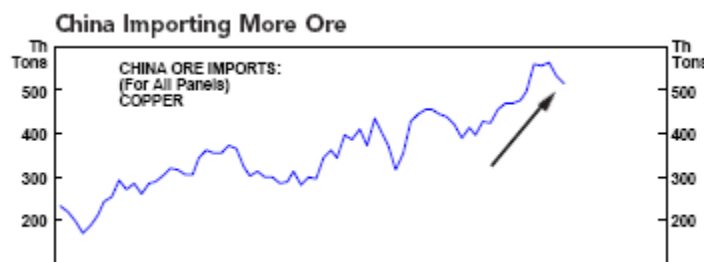
Chinese Vehicle Production



Chinese Commercial Construction



Chinese Copper Imports



Given our outlook for an expanding global economy we continue to feel individual portfolios should have industrial and commodity based companies.

Ian Nakamoto
Director of Research

Important Disclosures

<u>Company</u>	<u>Ticker</u>	<u>Disclosures</u>
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Glossary of Terms:

EPS	Earnings per Share
P/E	Price to Earnings Ratio
EBITDA	Earnings before Interest, Taxes, Depreciation and Amortization
Market Cap	Total Shares Outstanding multiplied by Shares Price
Enterprise Value	Fully Diluted Shares Outstanding
PEG	P/E Multiple Divided by Growth Rate
ADR	American Depository Receipt
WACC	Weighted Average Cost of Capital
Risk Free Rate	10 Year Treasury bond
Yield	Dividend divided by Share Price
ASP	Average Price
DSOs	Days Sales Outstanding
Capex	Capital Expenditures
CPU	Cost per Unit
EVA	Economic value Added
EV / EBITDA	Enterprise Value / Earnings before Interest, Taxes, Depreciation and Amortization
DCF	Discounted Cash Flow
Holts DCF	Holts Discounted Cash Flow
DYT	Dividend Yield Target
Yield	Yield
BSOPM	Black Scholes Options Pricing Model
BETA	Quantitative measure of the volatility of a stock, mutual fund, or portfolio, relative to the overall market
MF	Mutual Fund

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Montreal 514-394-3000

Quebec 418-656-1212

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