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MONTHLY MARKET COMMENTARY

INVESTMENT RESEARCH

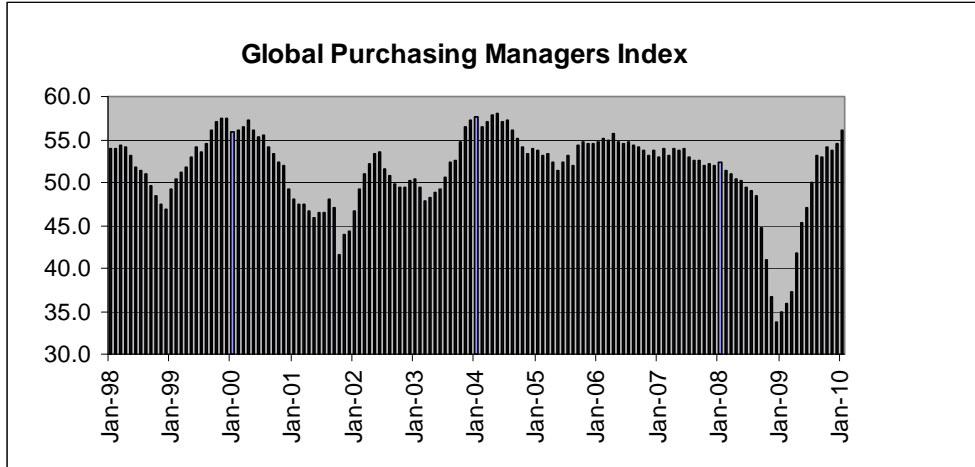
FEBRUARY 2010

January 2010 Review

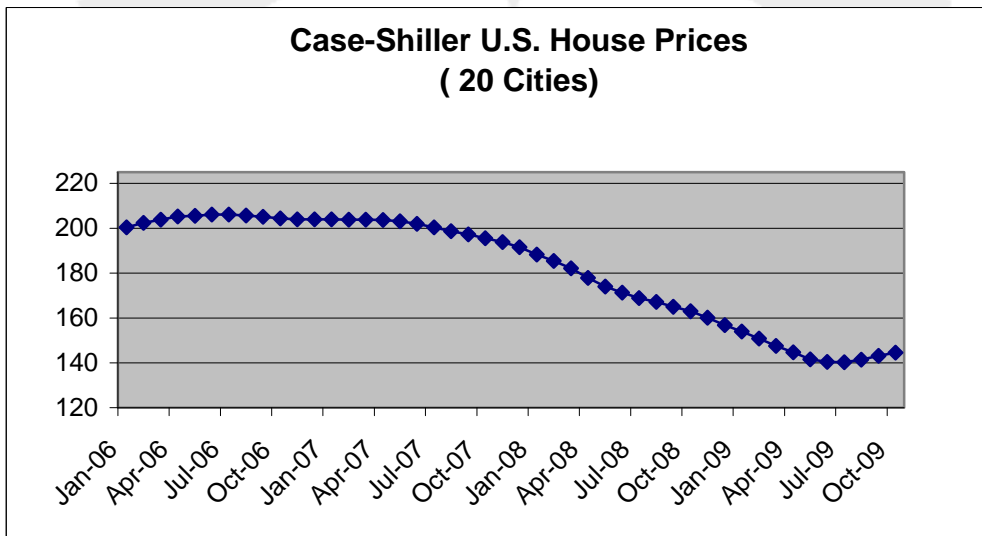
	January 31, 2010	December 31, 2009	% Change
TSX	11,094.3	11,746.1	(5.5)%
S&P 500	1,073.9	1,115.1	(3.7)%
DJII	10,067.3	10,428.0	(3.4)%
NASDAQ	2,147.3	2,269.1	(5.4)%
10 Yr. Cda Bonds	3.35 %	3.61%	26bp
10 Yr. US Bonds	3.58%	3.84%	26bp
90 Day Cda T-Bills	0.22%	0.24%	-2bp
90 Day US T-Bills	0.07%	0.05%	2bp
US\$ vs. Can\$	\$0.9342	\$0.9515	(1.8)%

From Hope to Growth:

Even the most bearish of economists will acknowledge economic growth has returned. Early in 2009, investors were in a state of hoping for growth. In the final months of the year, this hope became a reality as economic expansion, although tepid in many parts of the world, returned. Early economic data for 2010 shows the global economy further expanding. The graph on the following page highlights one widely followed index of economic activity, the Global Purchasing Managers Index. A reading above/below 50 indicates an expansion/contraction in the economy. The latest data point has a reading of 56.1.



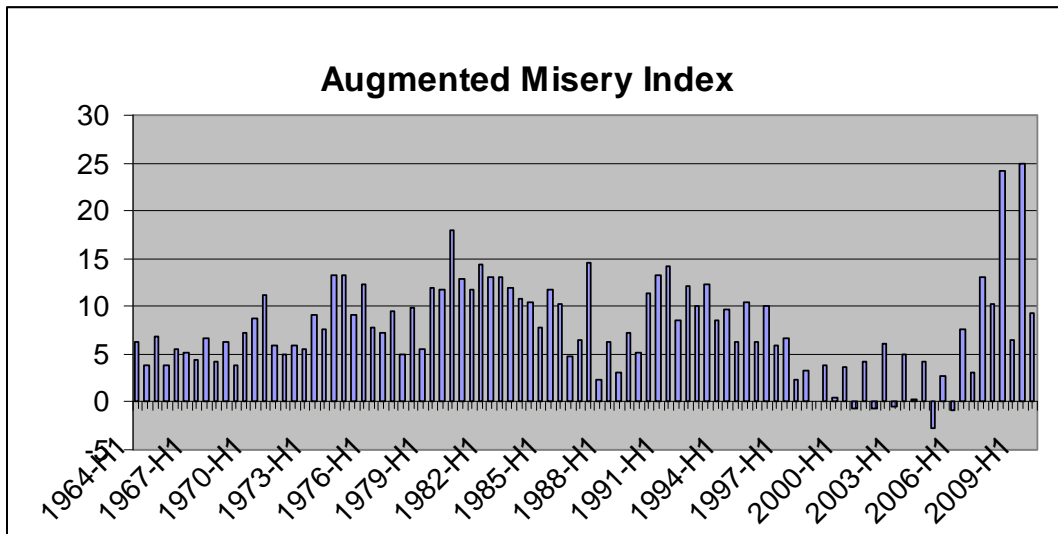
The economic “bears” have turned their attention to a possibility of a double dip recovery, whereby the economic improvement proves to be short-lived and falters later in the year. Although a possibility, it appears remote unless an external shock (e.g. a sudden increase in energy prices) or a policy mistake (i.e. an early removal of various government stimuli) happens. The prime reason we do not feel the economy will dip back into a recession is due to the “wealth effect”. The wealth of consumers has stabilized and shows signs of increasing. For example, we highlight in the graph below U.S. home prices which appear to have bottomed several months ago and now shows signs of an increase. The broad stock markets have rebounded significantly since early last year adding to household wealth. The wealth effect worked in reverse in 2007 and 2008 as consumers major assets fell in value, causing a retrenchment in spending and a major recession.



* The last data point reported is November 2009.

This increase in wealth has translated into better consumer sentiment readings, although not to the same levels before the start of the recession. One index we found to measure consumer sentiment is called the Misery Index. This was developed in the U.S. during the Carter administration and became popular during his presidential campaign in 1976. The index is the addition of the Consumer Price Index and the unemployment rate. The higher/lower the reading, the more/less “miserable” consumers feel and less/more likely to spend. An updated version has been developed adding one more variable; changes in housing prices using the above Case-Shiller Index. With housing such an important asset of a family, changes in housing prices according to the authors, is a better predictor of consumer sentiment and spending.

Below we illustrate this revised index starting in 1964 and ending in December 2009. The latest reading is 9.8. As one can see, there has been a significant change since the first half of 2009 when the index hit a record high of 25 (everyone was miserable), but ended the year at 9.8.



Source: Peterson Institute for International Economics-Hufbauer and Wong, January 2010

The authors conclude the following:

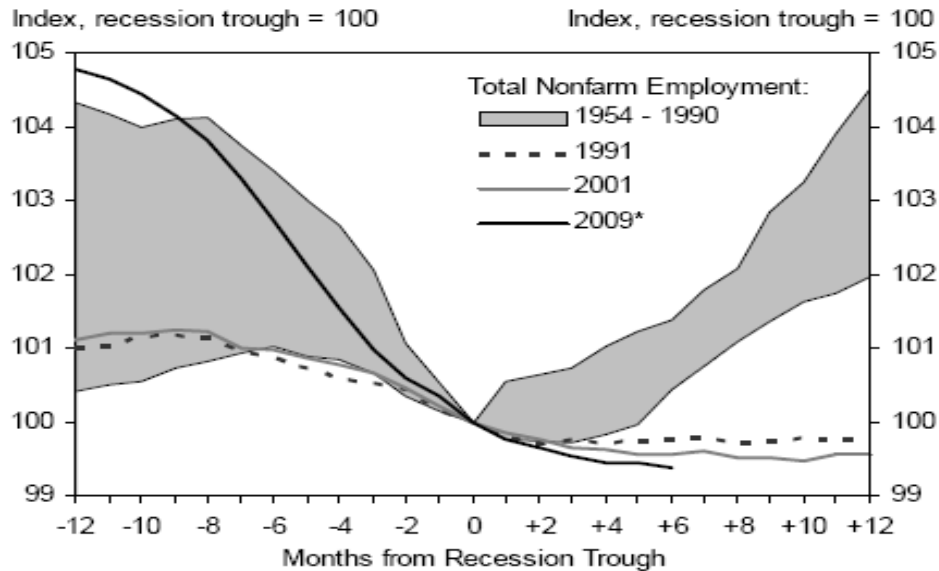
“What about 2010? The economy should continue along the recovery path, and unemployment rates should begin to drift down. The consumer price index may increase slightly, but housing prices should also enjoy a slow climb. These trends should improve consumer sentiment...”

What Worries Us?

1) **Interest Rates.** No one argues the current low interest rates will last, but it was a necessary condition to “ignite” an ailing economy. Lowering interest rates by central banks led to lower mortgage and consumer borrowing rates. In the case of mortgages, this has led to a revival of the housing market in Canada (to the extent some argue it has gone up too far and fast) and in the U.S. has stabilized a weak housing market. Central bankers are aware leaving interest rates at these levels for too long may lead to higher inflation and/or create another asset bubble, a situation they would definitely look to avoid. Unfortunately, raising interest rates too soon would jeopardize the recovering economy. A classic case of increasing interest rates too soon after a housing boom/bust was seen in Japan. Japanese central bankers believed after they experienced a real estate boom/bust and implemented many measures to restore their economy it was time to raise interest rates as the economy appeared to be gaining strength. Unfortunately, it was a mistake and the economy weakened again.

In addition to central banks increasing interest rates, bond investors may increase interest rates by selling their bond positions, if they felt inflation and/or budget deficits and accumulated debt by governments were not being seriously addressed.

2) **Trade Protectionism.** The consensus view is unemployment levels are close to peaking, but the trend downward will be slow. In other words, a jobless economic recovery is the most likely course. To date, the evidence points to this situation. We illustrate this point in the graph on the following page that shows job growth (expressed as an index) since the end of the recession versus previous recessions.



Source: Goldman Sachs- January 2010

Despite the recession being over there has not been job creation. The number continues to decline from the end of the recession and shows this jobless recovery to be the worst on record, pointing to a sub-par recovery in the economy. If this trend continues, there will be growing pressure on politicians to create jobs. One way is to reduce the amount of imports into a country by enacting or encouraging a Buy America or Buy Europe atmosphere. Less imports, in theory, displaces foreign made goods and jobs in favour of domestic made goods and jobs.

Lessons from the past have taught economists this activity leads to trade barriers and hostility among nations. In our view, one of the reasons for strong economic growth during the past fifty years is due to barriers being removed between nations and a movement towards globalization. It would be unfortunate if this trend is reversed. We do not feel this will happen in any meaningful way but we do acknowledge trade protectionism is a risk to our forecast.

One may question how a recession can be declared over when jobs are not being created or job losses continue. The Gross Domestic Product (GDP), the most common measure of economic expansion/recession, is defined as the total output (not job creation) expressed in dollars (excluding inflation) of all goods and services produced within a country. Economic expansions/recessions are normally expressed as percentage changes in the Gross Domestic Product. A recession is defined as being over when the economy stops contracting (i.e. the percentage change in GDP is zero) not when job losses are over. The end of the recession does not mean the level of economic activity has returned to pre-recessionary levels. Job growth normally takes several months after a recession is over, as businesses are reluctant to hire people until they feel confident business conditions are sustainable.

3) Risk Aversion: To run a successful and growing business one needs to accept an element of risk. To invest in the stock market also means accepting more risk than investing in interest bearing securities or leaving the money in cash, but the returns tend to compensate for this increased risk level. At times, investors are not risk averse enough and ignore signs of an over-heated stock market, while other times the opposite. Despite our base case that the stock market will continue to rise, albeit at a slower pace than in 2009 due to an improving economy, corporate profits and reasonable stock market valuations, the most difficult element to judge is the degree of risk aversion or sentiment investors have towards the stock market. One commonly used measure of risk aversion is the VIX Index or what is sometimes called the “Fear” Factor. The higher/lower the index indicates the greater/less fear among investors. The higher/lower the index the less/more likely the stock market will rise.

BUY - will represent opportunities that potentially offer in excess of a 20% return on investment within a 12-18 month period.
HOLD - will represent opportunities that offer between 5% and 20% potential return on investment within a 12-18 month period.
SELL - will represent opportunities that offer less than 5% return on investment within a 12-18 month period.

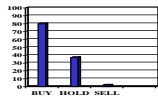
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MacDougall, MacDougall & MacTier Inc. employs two risk ratings with its research reports; Above Market Risk and Market Risk.

Above Market Risk denotes a company, which operates in an inherently speculative industry, or one that is more volatile than the market as measured by its beta. Above Market Risk may also indicate weakness in the company's balance sheet, low debt ratings, and the lack of a dividend, low liquidity or other deficiencies.

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■ Percentage of companies covered by MacDougall, MacDougall & MacTier Inc. Equity Research within each rating category.

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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