LONDON CAPITAL MANAGEMENT

Monthly investment commentary

March 2009

FEBRUARY'S HIGHLIGHTS

- Global economies continued to weaken and Canada was no exception. Canada's fourth quarter annualized GDP shrank by 3.4% (q/q). The U.S. fourth quarter annualized GDP declined by 6.2% - the weakest since the first quarter of 1982.
- Gold prices continued to rise, ending February at $937.70/oz.
- The Bank of Canada reduced its central bank rate to an all time low of 0.5% in an effort to spur on economic growth.
- Major world markets have now officially halved their returns from peak to trough with declines of 50% or more.

The stock markets continued their Olympic luge run in February - downhill, fast, and record setting (see Table 1).

Table 1– Summary of major market developments

Market returns*	February	YTD
S&P/TSX	-6.6%	-9.6%
S&P500 (US$)	-11.0%	-18.6%
S&P500 (C$)	-8.7%	-15.3%
NASDAQ	-6.7%	-12.6%
Russell 2000	-12.3%	-22.1%
FTSE 100 (U.K.)	-7.7%	-13.6%
NIKKEI 225 (Japan)	-5.3%	-14.6%
EAFE (C$)	-7.4%	-16.2%
EAFE (local currency)	-7.9%	-13.7%
Canadian Bond Market	0.7%	-0.3%
World Bond Market (US $)	0.3%	-1.3%

*local currency (unless specified); price only

It's been a troubling start to 2009 for global stock markets. After having traded within a range for several months, many world markets revisited their November 2008 lows. An ongoing barrage of grim data throughout the first months of 2009 continued to erode investor confidence and caused a retreat from the markets.

For the Canadian S&P/TSX only the Materials sector, helped by the fertilizer and diversified metal companies, managed to avoid losses in February. The Financial sector, across both the U.S. and Canada, continued to weaken despite Canadian banks largely posting better than expected earnings.

CANADA HOLDING UP WELL – RELATIVELY SPEAKING

While news of Canada's fourth quarter decline in annualized GDP (down 3.4%) was disappointing, it continues to be an outlier among other G7 nations who continue to post much larger declines (e.g. in the fourth quarter, U.S. annualized GDP was down 6.2%, while Japan's GDP was down 12.7% in the fourth quarter). Likewise, with all the negative headlines surrounding U.S. and global banks, it's easy to forget that Canadian banks continue to be the envy of the world. While it is true that Canadian bank profits were decidedly weaker in the fourth quarter, it's important to note that all of the major Canadian banks still posted a profit! Posting a profit in the current environment is no small feat.

Table 2 - Sector level results for the Canadian market

S&P/TSX sector returns*	February	YTD
S&P/TSX	-6.6%	-9.6%
Energy	-4.6%	-8.6%
Materials	0.0%	0.2%
Industrials	-9.7%	-16.8%
Consumer discretionary	-4.0%	-11.4%
Consumer staples	-3.8%	-5.2%
Health care	-2.4%	10.4%
Financials	-11.0%	-17.3%
Information technology	-22.2%	0.8%
Telecom services	-5.2%	-8.1%
Utilities	-3.1%	-5.1%

*price only

MADDENING MONTH FOR MARKETS

While the overall cause for market declines continues to be the uncertainty and pessimism surrounding the U.S. and global economy, there were a few noteworthy events that have made recent weeks full of frustration, disappointment and surprise for investors – in short, making it a maddening month for investors.

We saw corporate giants like General Electric cut their dividends for the first time in 30 years, and American International Group (AIG) report historic losses. Throughout the month we also saw more evidence that the economic weakness is hitting Main Street in Canada and the U.S., as employment figures and corporate earnings continued to weaken across the board. But what seemed to frustrate investors most during the month was the long-awaited details of how the Obama administration planned to fix the financial system. Despite the $750 billion (U.S.) commitment to pump cash into the banking system, it lacked the detail the market was looking for in determining exactly how they intended to value those assets they planned to take off the banks' balance sheets.

Despite many of these events taking place in the U.S., the lack of confidence and the effects of declining wealth are being felt on equity markets around the world.

AS INEVITABLE AS SPRING FOLLOWING WINTER

The market declines and extreme volatility have tested the mettle of even the most battle-hardened investors, and the headlines continue to trumpet only the most depressing of news. This has left many investors asking 'when is it going to end?', or in other words, 'when are we going to see the market bottom'?

The bottoming process is the stage at which markets have hit their lowest point and the start of a market recovery can begin. Sometimes these are marked by a quick, sustained recovery and other times (as it appears now) it can take months of equity markets trading within a range and retesting lows before markets find the bottom.

Markets find their bottom not when investors feel excited about a potential bull market to follow, but rather when they feel worry, doubt and concern about the situation at hand. In other words, market bottoms feel terrible! And despite historical evidence that equity markets are more likely to rise and have above average returns over the next five to ten years after a weak period (see chart A), fear causes many investors to not take full advantage of these upswings.

We cannot predict the exact timing that will mark the absolute end to the recent market declines, but experience tells us it is most likely to happen when investors feel their worst – and right now, we know investor sentiment is at multi-year lows. We also know that at some point the tides will turn and markets will start to recover - it's as inevitable as spring following winter. The question is, how will you be invested when that change happens?

CHART A