# FIRST QUARTER LETTER 2008

The first quarter of 2008 proved to be another very challenging one for investors worldwide. Regardless of which benchmark is used to measure relative performance, the results were similar: S&P500 -9.9%, Dow Industrials -7.6%, NASDAQ -14.1%, MSCI Europe -14.5%, MSCI Far East -9.7%, MCSI World -9.0%. The TSX index was down 3.5% but that was skewed by the high weighting of volatile gold, materials and energy stocks in the index. The average return of our unconstrained all-equity portfolios was -7.9% during the period, while our balanced portfolios fared much better.

We felt that the stock market declines could have been much worse given the severity of the global credit crisis. Central banks moved quickly to provide liquidity, and overnight rates were drastically slashed in the US in response to a real estate crisis which is still far from over. The Bank of Canada followed suit, taking a proactive approach in pre-empting any economic slowdown that might filter in from the south, and more importantly is trying to stem the harm done to our exporters caused by the appreciation of the Canadian dollar, which would have worsened had interest rate differentials with the US widened further.

We anticipate that the market will continue to trade sideways for another quarter or so while the financial institutions worldwide get their houses in order. Although there are further write-offs coming, the forward looking stock market has discounted a reasonable worse case scenario. For some time now, we have been advocating low weightings in the US dollar, financials and long bonds, while sticking to our tried and true style of value investing in smaller, profitable domestic companies where we as managers have a clear competitive advantage. Nevertheless, the share prices of some of these companies have declined significantly from their peaks due to indiscriminate selling by panicky investors, broker margin calls, or the liquidity needs of institutional investors such as mutual and hedge funds facing redemptions. Few, if any, of our investments have declined in value due to poor results or diminished prospects, and we have the utmost confidence in our portfolio investments. In fact, many of the companies we have invested in have released record profits during the quarter such as Glacier Communications, Stella-Jones, MTY Foods, Logistec, Neo Materials, Astral Media, Gemcom, Viterra, Shopper's Drug Mart, Tim Horton's and Shaw Communications, and they should continue to do so in the future.

Unfortunately, investors in international funds have suffered long term damage, as the value of many companies in the financial service sector, the most heavily weighted sector in global stock market indices, has been permanently impaired. Also, high multiple sectors have been “repriced” downwards to reflect a lower tolerance for risk and profit-taking in overbought markets. On the contrary, many of our companies trade at modest multiples which are below their respective rates of profit growth, or trade well below their private market value, and thus represent attractive investments. Paradoxically, investors have driven yields on “safe heaven” securities, such as cash and short term government bonds, to such extreme overbought levels that these are now generating negative real rates of return after inflation and taxes. This means that investors are losing money on cash and cash-equivalents, and the opportunity cost is rising of not investing in equities, many of which are paying historically high dividend yields. We believe that now is an ideal time to invest in well managed and profitable companies, and those who take advantage of this during periods of market weakness will be rewarded with superior long-term returns.

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