RBC Dominion Securities

Money
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The Newsletter for the Informed Investor – www.rbcds.com/vito.finucci

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The big Picture

Thirteen Trillion Reasons

I love the United States. Growing up I spent some summers in my formative teen years near Boston. I am a big fan of their history, their political process, their extraordinary technological achievements, of how a "nobody" can become a billionaire there, and despite the constant criticism, of all the good things they have done worldwide throughout history. But the biggest achievement for America may be its economic success. There is a sense that there is nothing that the U.S.A cannot achieve when it puts its mind to it.

The U.S. economy in 2006 had a Gross Domestic Product (GDP) of about $13.2 trillion. Read that number again. It says $13.2 trillion. That is about 28% of all goods and services produced in the world for that year, and that figure is larger than the combined GDPs of the next four countries – Japan, Germany, China and the United Kingdom. In spite of the current "globalization" taking place, U.S. industrial production was $2.1 trillion, equal to that of Japan, China and Germany's combined. The point is, ladies and gents, the U.S. economy is staggeringly enormous. It is a Goliath economy.

So when I hear and read how the current subprime mortgage crisis is going to cause the U.S. economy to collapse, I am a cynic. Why? Because since I started in this business in the late 1980s, this is at least the sixth time a "crisis" has hit the financial markets that was going to take forever to sort out: The 1987 Crash was the steepest stock market drop since 1929. The 1990-1992 Crunch (and recession) was the worst banking industry troubles since the 1930s culminating in the Savings and Loan Crisis. The 1997-1998 Emerging Markets Turmoil saw global currency collapse, and at the time was considered the worst global financial crisis in 50 years. The 2000 Tech Bust, where most global markets dropped 50%, by many measures the worst bear market since the Great Depression. September 2001 and 9-11 which hit the heart of the U.S. financial system. Who saw this coming? And now… the 2007 subprime mess, shaping up as the worst decline in housing prices since the 1930s. Nevertheless, despite these "doomsday" scenarios, the world economy has grown each and every year, with an average annual gain of 3.7%, with no down years!

But I digress.

So while the housing slump has spread and is causing an economic slowdown, perhaps even a mild recession, I can think of Thirteen Trillion reasons why yet again this is not the end of the world. Despite all the political rhetoric we are currently inundated with south of the border, the current housing crisis most likely could not have been prevented in its entirety. It is the type of

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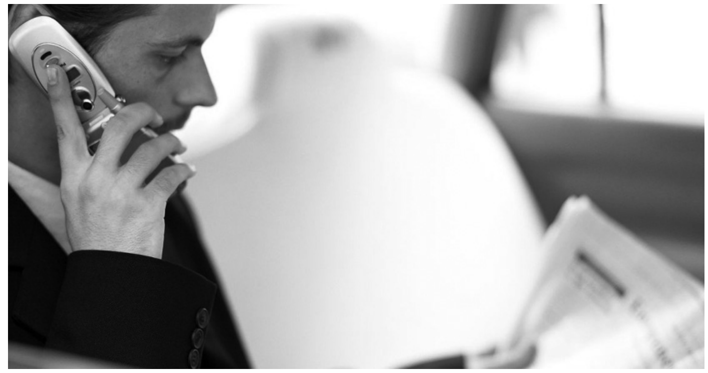
speculative excess we see periodically. We saw it in the dot-com bubble in the late 1990s and in the S&L crisis in the late 1980s, early 1990s. It's the natural excess of capitalistic markets.

Does a healthy global economy need these financial crises periodically as part of the cleansing process? It might be a touchy question but may be part of the new global reality. Global growth today is being driven in a large part by the free flow of capital. It is increasingly easier for people and companies around the world to raise money through any of a number of credit channels which include public and private equity, junk bonds, venture capital, bank loans and yes even…subprime mortgages. Access to relatively cheap capital fuels spending and growth but also opens up the possibility of what we are seeing today, dangerous lending and borrowing practices.

Let me present another scenario. If I told you at the beginning of 2007, that oil prices would surge close to $100, other commodity prices would surge as well, interest rates would rise, that housing would meltdown, there'd be endless losses at big bank's, recession fears, higher inflation, the weakest U.S. dollar in 30 years… and despite all that the Dow Jones and TSX would finish 2007 "only" 6.7% below all-time highs, I don't think any of you reading this would have believed me. I know they say Wall Street likes to climb a wall of worry, but this is like Mount Everest.

The financials have weighed heavily on North American markets the last six months. Investors are worried about the gears of commerce grinding to a complete halt. It is hard to imagine the U.S. economy moving forward if the financials continue to be an anchor, so this may take a few more months to sort out. One thing is for sure… we exited 2007 under a dense cloud of worry and concern.



It's the kind of stuff that isn't resolved in days, weeks or even a couple of months. The lessons of 2007 begin with "cheap money has consequences". But the aggressive action we will see going forward by central banks to pump liquidity into the system via lower interest rates and the printing of cash will also have numerous positive affects. The current crisis has also attracted over $40 billion of investments by the so-called sovereign wealth funds (countries) into names like Citigroup, Merrill Lynch, Morgan Stanley and UBS.

There have been 32 economic cycles between 1854 and 2001, with the average lasting 4.6 years. The 10 business cycles from 1945 to 2001 lasted an average of 5.6 years. Even if we believe the media and agree the economy slipped into a recession in November of 2007 that would have ended a six-year business cycle *(source: Wikipedia)*.

I've been accused many times of being eternally optimistic. Time has proved me correct. This crisis too, shall pass. As we head into a U.S. election, and with global interest rates set to fall (more than people expect), I believe the glass is half full and the U.S. will lead the charge, because they always have and for thirteen trillion other reasons.

NOTES (or things that make you go, huh?)

World Fertility Rates 1995-2000

Industrialized		Non-Industrialized	
Spain	1.19	China	1.80
Italy	1.21	India	3.45
Russia	1.25	Saudi Arabia	5.09
Canada	1.56	Pakistan	5.48
UK	1.70	Nigeria	5.92
USA	2.05	Yemen	7.30

(Source – United Nations 2002 Population Report)

Recent French elections called into question lack of French millionaires living in France. The far left-of-centre philosophy in France has simply forced them to live elsewhere like Switzerland, Belgium, London, etc…to escape French wealth taxes. In the past two decades, 35,000 French have moved to London alone.

(Gartman Report)

Pinching Pennies? On July 12th, 2005 Edmond Knowles of Alabama broke the world's record of largest-ever single cash-in of pennies, totaling 1,308,459 (or $13,084.59). Mr. Knowles, 62, owned Ed's Service Station since 1986 and collected pennies in a jug since 1962 to supplement his social security but by the end used a 55 gallon drum!

(Wall Street Strategies July 12, 2005)

QUOTES

"Don't worry about avoiding temptation. As you grow older it will avoid you."
Winston Churchill

"That which is not good for the beehive cannot be good for the bees."
Marcus Aurelius

"Be the change you want to see in the world."
Mahatma Gandhi

"Live in each season as it passes, breathe the air, drink the drink, taste the fruit, and resign yourself to the influences of each."
Henry David Thoreau

"We should spend as much time in thanking God for his benefits as we do asking Him for them."
Saint Vincent de Paul

Portfolio Corner Summary

(As of close January 21, 2008)

. . . For investors thinking 18-24 months or longer.

This quarter's recommendations:

Canadian Banks – Royal Bank (RY $46.00), **Toronto Dominion Bank** (TD $61.85), **Bank of Montreal** (BMO $51.70)

Commodities – Petro Canada (TSX – PCA $47.00), **First Quantum** (TSX – FM $69.50)

USA – Big Banks – Citigroup (C $24.45), **Bank America** (BAC $36.00), **Wachovia** (WB $30.80), **Wells Fargo** (WFC $25.50), **US Bancorp** (USB $30.20)

Techs – Intel (INTC $19.00), **International Business Machines** (IBM $103.00), **Netsuite** (N $27.75)

Other – Corning (GLW $22.00), **Bank of Ireland** (IRE $55.50)

All are 18-24 month holds, list is longer, but too long to name all of them.

Portfolio Review

As is our tradition, we like to look back and see how our calls did. While many hit decent highs (in brackets), Q4 made for a tough year.

Date Recommended	Name	Price Then	Price Now (High)	Total Return (with dividends)
October 2006	Altria + Kraft Spinoff	$76.55	$76.00	43.00%
	March Networks Inc.	$18.82	$10.21 ($27.00)	(45.75%)
January 2007	Boston Scientific Corp.	$16.90	$11.63	(31.00%)
	Sandisk Corp.	$41.75	$33.30 ($60.00)	(20.00%)
	General Electric Co.	$37.50	$36.90 ($42.00)	2.00%
	Yahoo Inc.	$25.60	$23.90 ($34.00)	(6.60%)
	EBay Inc.	$30.00	$33.19 ($40.00)	10.60%
	Ford Motor Company	$ 7.50	$ 6.75 ($ 9.00)	(10.00%)
	CGI Group Inc.	$ 8.10	$11.00	35.80%
April 2007	Loblaw Companies Ltd.	$46.30	$34.23 ($55.00)	(25.00%)
	Wi-Lan Inc.	$ 6.58	$ 2.56	(61.00%)
July 2007	Neo Materials Technologies	$ 3.90	$ 5.02	28.70%
	Motorola Inc.	$17.80	$16.04 ($20.00)	(8.70%)
October 2007	The Gap Inc.	$17.84	$21.28	21.00 %
	Sandvine Corp.	$ 6.00	$ 3.82 ($7.30)	(36.00%)

Around the globe

Canada (SELECTIVE BUY)

- ❖ Has ridden commodity boom for a while now.
- ❖ High dollar hurting exporters and manufacturers.
- ❖ Since start of 2007, C$ appreciated 14.07% vs. US dollar
- ❖ Up 8% for 2007.
- ❖ Balance sheets remain strong overall.
- ❖ TSX at upper end of valuation band vs. global markets.

U.S.A. (STRONG BUY)

- ❖ GDP estimates have been falling as recession risk increases.
- ❖ Fed expected to continue cutting interest rates.
- ❖ Presidential election in November
- ❖ Bottom for U.S. dollar in 2008?
- ❖ Still many questions on credit crunch/subprime lending woes.

Europe (HOLD)

- ❖ In 2007, Euro up 10% vs. U.S. dollar
- ❖ Relatively high interest rates in UK have cooled housing.
- ❖ ECB maintains hawkish tone in face of financial crisis as inflation has edged up to 3% in November and biggest gain since 2001.

Asia (HOLD/BUY)

- ❖ Japan has been weak sister in these economies and short rates remain at 0.5% since last February.
- ❖ Emergence of China and effect on the entire region cannot be ignored but Chinese government taking steps to curb growth.
- ❖ Summer Olympics in Beijing in 2008 will add catalyst but may also signal a peak?

Latin America (AVOID)

- ❖ Overall, economic growth has been solid, supported by hard commodities like oil, mining, gold, etc…but political instability is a risk
- ❖ Slowing U.S. and global growth may be a wake-up call and expose bad economic policies.

A special welcome to all new clients who have joined us.

Thank you especially to clients who have mentioned our name to people they know. As a sign of gratitude, four times a year we'll randomly select a client who has introduced our services to a friend for special acknowledgement via a nice dinner at one of the finer restaurants in London.

Congrats, Charlie H.

Our winner this quarter!

PLEASE DON'T KEEP A SECRET FROM US!

We are very happy and proud of the clients we serve in our practice and we are always open to serve more clients just like you. Should you be talking to someone who is unhappy with their current advisor, we would be grateful if you passed on our number 519-675-2011 or 1-800-265-5911. Thanks for keeping us in mind.