RBC Dominion Securities

# Money
NEVER SLEEPS

The Newsletter for the Informed Investor – http://dir.rbcinvestments.com/vito.finucci April 2007

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## The big Picture

## A BROKEN RECORD – "SWEET"

Since the calendar year turned to 2007 my mantra has remained the same: I think financial markets will do quite well in 2007 and for most of 2008, albeit with some increased volatility. The irony is, I said the same thing for most of 2006, and in the end, it turned out to be a decent year as measured by most global indices. And now 2007 is looking a lot like 2006. My story remains the same: solid corporate earnings combined with the best balance sheets in years, along with benign inflation, on top of a still buoyant (and buying!) consumer, to go with a slower (but not collapsing!) economy which will lead to lower interest rates, all of which combines going into a US election which historically has been the best of times.

I am really starting to sound like a broken record.

In 2006, the S&P 500 was up 15.8%, the TSX approx. 13%, and the world 20% (including dividends). Ten-year bonds were approx. 4% and cash slightly less. The same forces that made 2006 successful are still there today, most are mentioned above.

However I still detect that while investors are not content with 4% GIC returns, they remain very wary and risk averse. Many still cling to the skeptical sentiment they learned to embrace from 2000 to 2003. But the "smart" money continues to drive cash-based stock buybacks and takeovers and mergers by private equity players with deep pockets.

And need I remind everyone there has not been a negative third year of a President's term since 1939, and only two single-digit positive years. Third years tend to be as my teenage sons say "Sweeeet", just a question of how "Sweeeet".

Corporate earnings and interest rates ultimately drive the markets. The former remain good, not outstanding, but that's OK. A few years ago in this newsletter I wrote how in the post 2000-2001 market meltdown, post Sarbanes-Oxley and Enron, how CEO's would now ratchet expectations lower and keep comments about the future less optimistic. Well these days management seems to walk on eggshells. Their jobs are perennially at risk so they make moves to appease Wall Street and investors rather than coming up with grand designs or risky growth strategies that would bring big dividends in the future. Because every quarterly earning release has become so important in this impatient world we live in, many companies only focus on the near term and don't seem positioned with real innovations that would separate them from the pack. There simply isn't time to build. Investors are too impatient. Perhaps if earnings were released every six months instead of every three, there would be less sense of immediacy and perhaps the quarterly swings and

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**Big Picture** | *Continued from Page 1*

volatility would smooth out.

On top of that, mature North American markets can't match up to the sizzling economics of India and China, and others like Vietnam, which have great sex appeal for investors looking for the hot hand and quick buck. China's GDP grew 10.7% in 2006 and is just within a hair of passing Germany for the third largest economy on the planet. Their central bank has a $1.0 Trillion cash horde to boot. But despite all that hype, the Chinese equity market represents less than 1.5% of the total global market, even less than Canada! This is a great time for China, but the inevitable growing pains are around the corner. I will only say Shangri-La doesn't last forever. I won't even try to predict when, but we will see the results when they are in the throes of their first big recession.

The recent 10% one day meltdown in the Shanghai market brought volatility to our world for a few days, but since then no news from our media. Wonder why? Well, since then the Shanghai market has reversed and exploded to a new record high on the upside, our markets, which joined in on the downside, haven't had the corresponding move upwards.

Shanghai wasn't the only "surprise" this past quarter. Much was made about the sub prime loan mortgage market meltdown. From what I read, this market represents 15% of the total mortgage market, which upon itself is a big number, but assuming 15% of those loans go into default, it would translate into 1.0% of the total loan market. While this is not a good thing, it will not prove disastrous for the US economy. One just has to recall that this is the same economy that withstood exogenous shocks from events like 9-11 and hurricane Katrina, and came through with flying colours. What is likely to occur from all of this is that lending standards will be tightened by banks, meaning a good part of the population will not be able to afford a home.

Despite these issues, the US economy is in better shape than one might suppose from reading headlines. The death of the consumer has been predicted as long as I can remember. Yes auto sales are tough, yes housing is slowing, but those will both lead to interest rate cuts by the US Federal Reserve sometime this year. Valuations are reasonable and liquidity is hugely positive. There remains a lot of cash on the sidelines looking for a home.

It's not the kind of stuff that gets a lot of press, but I've been impressed by how the market finds a way to close higher in recent weeks. For all the talk of inflation, higher oil prices, the slumping housing market and every other kind of woe, retail stocks have fared very well over the past six years. As a proxy for consumers, the S&P 500 retail index is close to an all time high.

In past issues I've been advising to focus on the financials, health care and tech sectors. The financials (who benefit from lower rates) have been solid, tech has been perking up (and I think it will be one of the best sectors for the next 2-3 years) and health care has been treading water overall.

It's been like a broken record but I remain very positive for 2007-2008.

## Sign of an Oil Peak?

If you had $449 billion dollars to spend buying companies today…

| | |
|---|---|
| You could by: | Exxon |
| Or you could buy: | Agere Systems<br>Micron Tech<br>Microsoft<br>Sun Micro<br>Gateway Computers<br>Dell Computer<br>Unisys<br>Intel Corp.<br>EDS<br>Lexmark |

… and still have $4 Billion to put in the bank

*(Source: Brandes Investment Partners)*

# Portfolio Corner Summary (as of close April 6, 2007)

**This Quarter's Recommendations:**

**Loblaw Companies** (TSX – L $46.30) – Has been beaten up by the markets due to struggle to improve operations. With the entry of Wal-Mart into overlapping markets, it has spooked many but it is reportedly worth $40 based on real estate holdings alone. Has recently withdrawn from many non-profitable ventures (like merchandising) and if management can show any signs of their former growth it can get big upside. Hold 18-24 months, Moderate Risk. (12 month range – Hi $57.83, Lo $44.92)

**Wi Lan Inc.** (TSX – WIN $6.58) – Former high-flying tech name (hit $94.00 in March 2000) is a developer and licensee of intellectual property mainly for wireless platforms and local area networks (Wi-Fi). Has decent balance sheet and with new management seems to have turned it around. Very Aggressive play for 12-18 months. Target $9 – $10+ (12 month range – Hi $7.97, Lo $0.62).

## NOTES

The last 10 years, the entire economy combined produced 80 million new members of the middle class. Beginning in 2007, the economies of India and China will produce 40 million per year. (CNBC 4-2-2007)

| The UK vs Iran: | UK | Iran |
|---|---|---|
| Population | 60.6 million | 68.7 million |
| GDP | 2,341 billion (USD) | 610 billion (USD) |
| Unemployment Rate | 2.9% | 15% |
| Population under poverty | 17% | 40% |

*(The Gartman letter March 28, 2007)*

We have all read and heard how hot the real estate market has been. Ready for some reality? House values have risen 264% over 25 years, but other routes would have been richer:

| | |
|---|---|
| Gold | 1.90% annualized |
| Real Estate | 5.30% |
| S&P | 7.84% |
| TSX | 13.17% |

*(Source: National Post January 25, 2007)*

## Quotes

"Old age is like climbing a mountain. You climb from ledge to ledge. The higher you get, the more tired and breathless you become – but your views become more extensive."
*Ingrid Bergman*

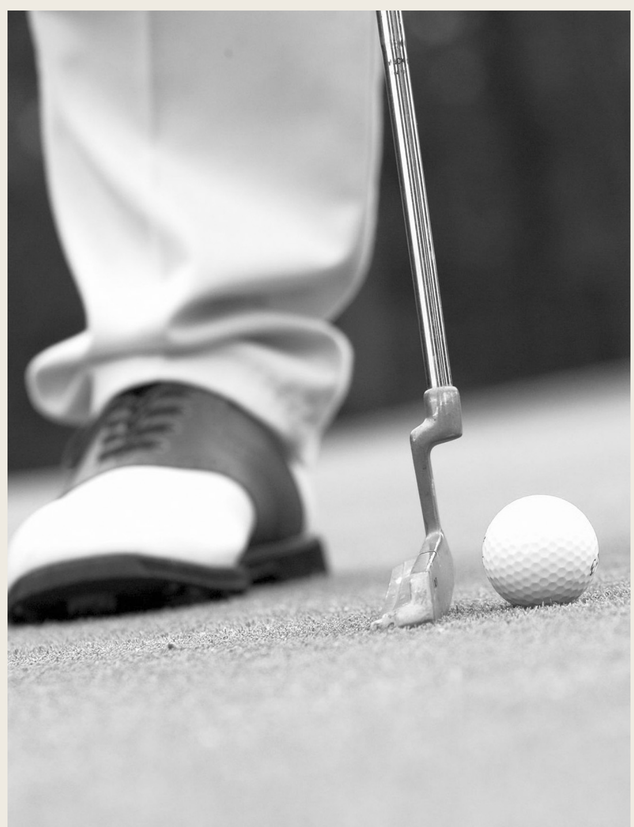
"My experience of the world is that things left to themselves don't get right." *Thomas H. Huxley*

"One-fifth of the people are against everything all the time."
*Robert Kennedy*

"Those who make peaceful revolution impossible make violent revolution inevitable." *John F. Kennedy*

## Little Picture

June 25th – Sunningdale Golf and Country Club will be the venue for the 18th annual Children's Golf Classic of which I have been the major sponsor for the past 15 years. Last year as a reminder, we raised $180,000 of which 100% goes to our local Children's Hospital of Western Ontario here in London. This year, Canada's top golf champion, Mike Weir, the 2003 Masters champ will be joining us to help the cause. If you or your organization would like to help us help the sick kids get better, please let us know. All cash donations over $10 will get tax receipts and all products or services in kind are welcome. And barring that, you can all do me a favour and pray for sunshine! Will give you all an update in the next issue of "Money Never Sleeps".



# Around the globe

**Canada (SELECTIVE BUY)**
- ❖ 2007 Growth expected of approx.1.75% with 2.0% inflation.
- ❖ Has had "two-speed" economy for some time.
- ❖ Strong currency hurting exporters and auto sector restructuring in question.
- ❖ Only G7 nation with budget surpluses (9 years in a row now).

**U.S.A. (STRONG BUY)**
- ❖ 2007 Growth expected of approx. 3% with 2.25% inflation.
- ❖ US Dollar remains weak but economy remains buoyant despite weaker auto and housing sales – soft landing?
- ❖ Lower rates later in 2007?

**Europe (BUY)**
- ❖ European growth quickening as German economy gains momentum.
- ❖ Eurozone on target for 3.6% GDP growth in 2007 with subdued CPI.
- ❖ Tighter central bank.

**Asia (HOLD)**
- ❖ In Japan gains have helped, China remains robust, Hong Kong solid, Viet Nam resurgence.
- ❖ Higher oil prices have hurt, as all are importers.
- ❖ Overall steady as she goes.

**Latin America (AVOID)**
- ❖ Politics remain too left leaning for my liking. Never make for good economics.

# Looking ahead

**April**
- ❖ Has been best Dow month averaging 1.8% since 1950 – Could be spring, could be first quarter earnings.
- ❖ Last year up before a tough May.
- ❖ First trading day of April up 9 of the last 12.

**May**
- ❖ Last year tough correction of 6-8% on most markets took place in May.
- ❖ Recent record 17 up, 6 down, average gain of 1.8% (3rd best)
- ❖ Friday before Mother's day up 9 of the last 12.

**June**
- ❖ Recent record: 14 up, 9 down with average gain of .7% (ranks 8th)
- ❖ Last few June's had end of quarter "portfolio window dressing", down 13 of the last 19
- ❖ First trading day up 8 of the last 9 years.

*(Source: 2007 Stock Traders Almanac)*

**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, Ashley M.**

Our winner this quarter!