REVIEW & COMMENTARY
3RD QUARTER 2011

Remembrance

Our last quarterly commentary suggested that the US deficit ceiling impasse would be resolved, the Greek debt issue would be contained and the EU would construct a financial package that would protect the remaining troubled states and deal with the mounting financial strain on many of their financial institutions. To date, only one of these situations has been reconciled and the equity markets demonstrated their impatience by selling off dramatically in September. During the quarter, the pace of China's economic growth came into question hurling commodity prices lower. While the EU works toward a resolution, it is a complex process and any whiff of success or delay is met with significant movements in equity prices. This increased volatility, something we have discussed before, has one silver lining; market retreats (aka bear markets) are over in a fraction of the time compared to decades ago. While investors are bombarded with predictions of doom and gloom, many appear to be preparing for the worst. However, if there is a surprise this year, it may very well be that the US economy will do better than expected, China will not slow significantly and the equity markets may respond positively.

Recent statistics show that the global economies are not that bad. China recently announced GDP growth of 9.1%. Admittedly, it is down from the 9.5% reported in the prior quarter, however, this is quite good considering they are the second largest economy in the world. US GDP was revised modestly upward in the second quarter to 1.3%- again not enough to combat employment woes but certainly not recessionary. While the third quarter results for the US may be affected by the uncertainty throughout the EU, it still may be positive. Consumer sentiment can be a useful contrarian indicator. Recently, Bloomberg's Consumer Comfort Index reached its second lowest reading. The only time it was lower was in January 2009 when the US economy was actually in a recession. The Business Roundtable's survey of chief executive officers was the lowest it has been since back in 2009 as well. Equity mutual funds which endured $280 billion dollars of withdrawals between December 2007 and March 2009 (recent market lows) have yet to become net positive from March 2009 to present despite significant equity price gains. There is a lot of potential demand sitting on the sidelines waiting to get back into the market.

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What would make investors come back into the market? If we are correct and the US and Chinese economies do better than expected then this will be positive. While presently moving slowly, a resolution to the EU financial crisis would have a beneficial impact not only as Greek and other European countries' debts are re-valued but it will also require many European financial institutions to significantly strengthen their balance sheets as their counterparts in the US did over 2 years ago. Repatriation of US foreign earnings, under less punitive tax rates, may make many of the larger capitalized companies more attractive as these earnings could be put toward share repurchase, dividend increases or asset purchases. Our message remains the same- endure the volatility and stay with equities. Barring an unforeseen catalyst to the downside, investing in well capitalized dividend paying firms will become even more compelling compared to the low yielding fixed income alternatives which may remain low for some time.

Finally, we would also like to pay tribute to Jack Stodgell our Chairman and Partner who passed away August 24th, 2011 at the age of 86. For many within the investment business, he was an inspiration, a role model and a friend. As a true student of the financial markets for over 63 years, he provided sound advice and wisdom to his clients and partners alike. Jack worked tirelessly during his lifetime to serve his clients, his industry and his community and they all benefited from his intelligence, thoughtfulness and sense of humour. SIM's investment philosophy was reflective of the philosophy handed down to him from his father Simeon and one we have adhered to for decades and will continue to do so for decades to come.

Stodgell Investment Management Ltd.