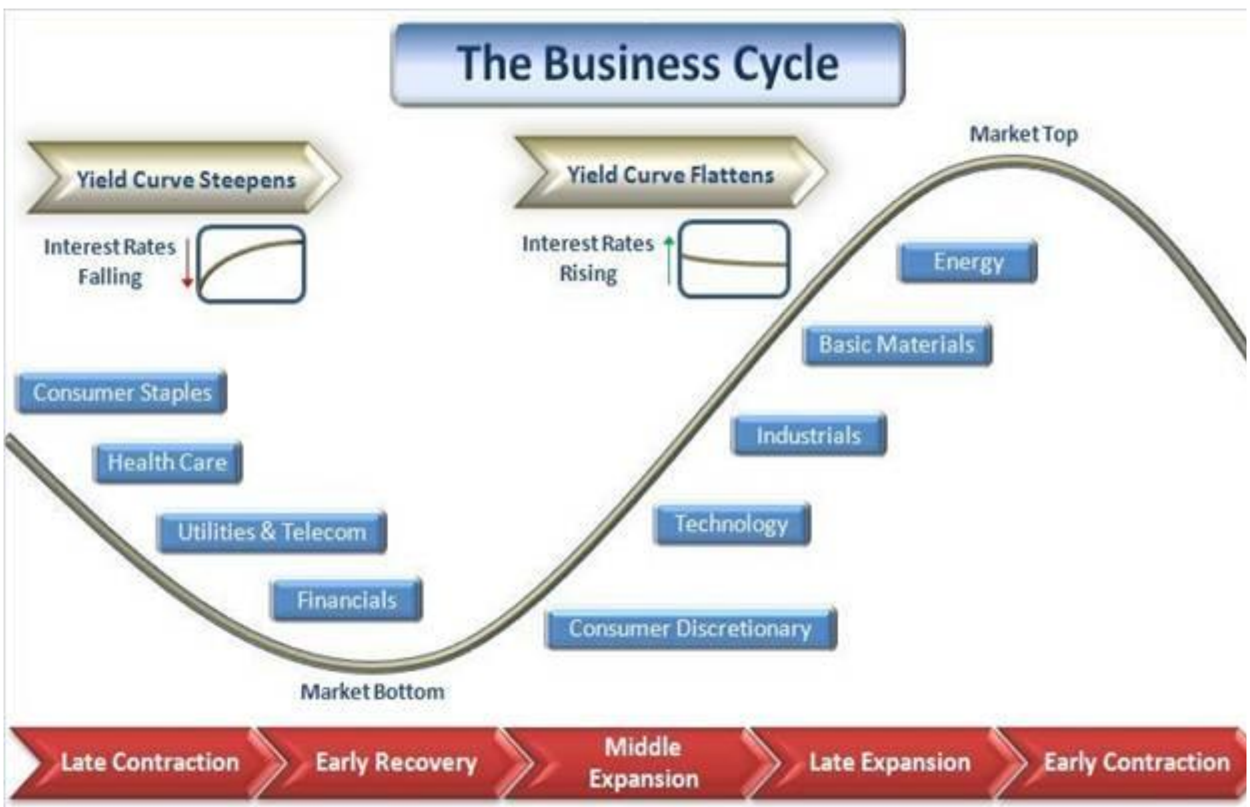
General Comments

Timing the financial markets has become more important since 1998. Viewing a chart of the S&P 500 Index for the last 130 years (a good average of how US stocks have performed) looks like a picture of a staircase, with each growth period between 16 and 22 years, and each flat period about the same - two decades. Market technicians sometimes call these periods **secular bull markets**, where there is a backdrop of sustained growth for a long period; or **secular bear markets** where there is no nominal growth at all from beginning to end. With the Canadian S&P/TSX and the US S&P 500 at roughly the same levels they were in 1998, it seems like investors are 12-14 years into a secular bear market.

Within a roughly two-decade long secular market, business cycles still seem clear. The secular period seems to be made up of four or five business cycles, each of which is approximately 4 years long. In the secular bear markets where no long-term gain happens, the business cycle highs and lows appear to have greater amplitude, while in strong bull markets like the 1980's and 1990's, the recessionary periods of cycles were often short in duration and/or small in magnitude. North American economies seem to be past the peak of the third business cycle and may face one or two more before the possibility of a longer term secular growth cycle (likely eventually driven by large Asian populations finally significantly experiencing improvements in per capital average income levels). **Investors may have to spend more effort timing investments for the next 6-8 years than they may have thought prudent based on a 1980-2000 investment experience.**



Objective ways of determining where the economy and stock market are in the business cycle include:

- Understanding of the types of sectors investors buy at each part of the business cycle, and objectively measuring what sectors are actually being bought currently.
- Understanding of the shape and movement of the yield curve, and how governments influence interest rates at various points in the yield curve during different stages of the business cycle.

From January to April of 2011, money started flowing into the most defensive sectors like consumer staples (food & pharmacies), health, utilities and telecom. **From April to August, 2011, money flows can be seen moving out of the more aggressive, economically sensitive sectors** like Energy and Materials. Charts of the Canadian S&P/TSX clearly peaked in April of 2011 and the flow of investor's capital into less risky businesses over 2011 confirms this peak.

The current interest rate yield curve in Canada is fairly steep; short-term interest rates are much lower than mid- to longer-term interest rates (by about 2-3%). This is a stimulative shape for the yield curve, representing Bank of Canada policy (and the US Federal Reserve) of trying to promote growth in economic activity by making capital inexpensive. A steep yield curve develops during the recessionary part of the business cycle. But like the flow of capital into defensive stocks, it has not recently become steep, but has been steep for many months now. In Canada, there started to be upward movement in short-term rates, and largely from US policy enactments like Operation Twist, long-term rates have remained close to the same levels or have slightly dropped depending on the measurement points.

Both the flow of investments into defensive sectors and the shape and movement of the yield curve suggest that both the Canadian and US economies are likely in the late stages of the recessionary part of the business cycle. The good news is that a market bottom is right around the corner. The bad news is that confirmation of a trough (such as short-term rates starting to rise, or capital flowing heavily into consumer discretionary and financial stocks) has not been established. Since the stock market is already nine months into a recession (already at the long-term average of a recession over many prior cycles), it is likely close to ending. Investors have to start thinking about being open to increasing their exposure to equities when the market does bottom, but recognize that it is still too early to do that in a significant way. Overall, a defensive stance is probably still more prudent until more evidence of a bottom in the market emerges.

I expect 2012 to be a "bottoming year" in stock markets. Last year, investors worried about the US entering another recession, the eurozone breaking up, and China crashing from lack of developed market demand. Investors were far too pessimistic on all three issues pricing in dramatically worst cases, which don't seem to have happened. Political news around the globe about debt and sovereign issues is shocking and bleak – that is what sells newspapers. Quietly, many companies are making record profits with huge hoards of cash available on their balance sheets - not that exciting for the media, but the raw materials for an eventual surge in stock prices.

Corporate bonds with 3-8 years in term to maturity, paying 4-7% yields appear the most attractive on a risk/reward basis to me for 2012. With the US Federal reserve on hold until 2014, essentially promising to keep interest rates low, bonds seem to have little risk of interest rates rising. Short-term bonds pay very little and are likely to mature with interest rates available that are still very low. It may take five or more years before rates are meaningfully higher, and investors who neglect owning longer-term bonds or cling to below-inflation returns from government bonds and GICs may be leaving mid-single-digit, and generally low-risk returns, out of their portfolios.

Managed Account Transactions During January

Managed accounts are discretionary accounts in which I can proactively make trades in a client's best interest based on a written Investment Policy Statement and an intimate understanding of their financial goals. Conflicts of interest from commission are eliminated since all trades are free. Logistical difficulties in contacting clients and obtaining authority for changes they would likely want are eliminated and all parties gain time not spent on discussing small details of individual securities. Instead, time can be focused on wealth planning and discussing what the client feels is important and wants to discuss.

The comments below represent changes I have already made for managed clients, but also represent a good source of ideas for those that manage their own portfolio and rely on me for implementation, ideas, and a source of professional feedback.

Summary: *Markets started the year strong. Early in the month, there were a few additions to stock portfolios, but on net, more money was taken out of the stock market. The current level of the market is likely close to a short-term top and although downward fluctuations in 2012 may end up being shallow, several positions that had substantial short-term rallies were reduced. Changes took place in a variety of sectors, but there were no changes generally in stocks of a defensive nature.*

New Positions Added:

Tupperware Brands: This company has a market capitalization of close to $4 billion with $2.6 billion of annual sales. Only 13% of sales are in Canada and the United States, while sales have grown to 27% of total in Latin America. The stock trades at an inexpensive 12x next year's consensus earnings estimate, with that estimate being slightly below the earnings guidance of U$5.00 to U$5.10 per share recently provided by the company. Shares were purchased in managed accounts at U$56.30 in January and the stock already has moved to close at $62.84 on January 31st. I expect to write covered calls on the stock as it nears my short-term target of U$65 to U$70.

Existing Positions Added To:

Canadian Energy Services & Technology: The core business of the company is to design and implement drilling fluid systems for oil and natural gas producers. The company is still in a very strong growth mode with an increase in revenues of 56% on a year-over-year basis at the end of the third quarter. Earnings have doubled over the past five years, and despite this growth focus, the company maintains a lucrative 4.8% dividend. Reduction in demand for natural gas service business seems to be more than offset with strength in demand for oil related services.

Ishares MSCI Germany Index: The German economy is benefiting from a strong manufacturing base, a stable government with close to a balanced budget, and a very low financing rate while some other eurozone countries are experiencing significant increases in the interest rates payable on their bonds. Managed clients have no exposure to Europe at all except to this, the strongest component of the European economy. As an exchange traded fund, covered calls can be written against shares owned to provide additional income above the current dividend of 3.1% that the index pays.

Platinum Metals Group: Originally bought in 2009 in anticipation of environmental approval for their platinum mine to be built in South Africa, shares originally doubled at which point some profits were taken. Speculation mounted that the company was ripe for being taken over as George Soros bought a significant position in 2010. Unfortunately a takeover has yet to happen and with the company facing three long years of building the mine, the shares have languished. In December, tax loss selling drove the shares down precipitously, but into January many of these same shareholders are likely buying their positions back. The stock has rebounded to the $1.10 level and may find its way back to some resistance in the $1.60 to $1.70 zone at which point shares in managed accounts will be reduced.

Positions Entirely Sold:

Stantec: As an industrial sector company that provides engineering and construction expertise primarily with infrastructure projects, it is not particularly a great time in the business cycle for this stock. Shares fell from close to $30 last spring to $22 lows by the fall, based on the change in sentiment about economic growth. Shares of Stantec rebounded to the $27 level in January, which was approximately the level most shares were originally acquired, allowing a reasonable exit point. Further, the stock has deteriorated on my quantitative ranking system.

Reduced Positions:

Bank of Nova Scotia: January covered calls had previously been written that set a target price of $54 for shares of the company. On the third Friday of the month when those options expired, the stock traded one penny above that strike price. This was enough for the owners of the calls to assign my managed client's Bank of Nova Scotia positions (effectively managed clients sold, or assigned, their stock at $54). At month end, the shares dropped back to $51.53 and should they fall closer to a $48-$49 price level they will be considered for re-acquisition.

Keyera Corp: Keyera was originally purchased in 2009 around the $17 level and has risen past $50, where this January, positions were finally trimmed. Rankings on my quantitative discipline have finally deteriorated somewhat, but only enough to trim positions; not enough to eliminate the lucrative 4.3% dividend-paying stock. With facilities and marketing tied to the natural gas business there is risk of a business slowdown warranting a reduction in holdings of the security.

Labrador Iron Ore Royalty Corp: This stock is the second-longest held stock, owned since 1996 when the original instalment receipt was purchased, and has been added to client accounts ever since. The stock has been fantastically profitable over that long period. Between very high distributions and stock appreciation, investors likely made ten times their original investment. It was also the largest position held in accounts in January. The stock price peaked in April as most base metal stocks did, but recovered nearly to those peak levels in January at which point reducing exposure seemed prudent. The company may go into a trading range as uncertainties over economic growth persist in 2012, but has much lower risk than other base metals companies because its revenues are from royalties from production of Iron Ore Company of Canada on their lands. It is still one of the larger positions held in accounts.

Covered Calls Written:

Alamos Gold Apr $20
Intel Apr $28 (the Jan $26 contract was repurchased as the stock had appreciated just slightly past this strike price)
Rogers Communications Mar $40 (only partly completed)

Flow-Through Shares

Investment in flow-through shares allows investors to write-off approximately the entire value of their investment against current year's income. The types of investments that allow investors to experience this benefit are usually investments in the energy and metals sectors in Canada. There are many flow-through vehicles available now and for the next few weeks. Three of my favourites include:

- **Qwest 2012 Oil & Gas Flow Through LP**: Don Short focuses on investment in junior oil companies and still feels it is too early to pick up natural gas bargains. Last year he was one of the few that was very positive on oil and turned out to be right. The underlying energy stocks Don picks tend to be among my favourites.
- **Stone 2012 Flow-Through LP**: This flow-through turned up on my buy list this year because it was one of the only ones that made money in 2011, a difficult year for resource managers. The fund is smaller and possibly more nimble and has a diversified selection of oil, natural gas, base metals and gold.
- **CMP 2012 Resource Limited Partnership**: This issue is likely going to be fully subscribed and close very soon. The Goodman family and Dynamic are the largest recipients of flow-through capital

investment most years by a large margin. CMP is likely to be roughly balanced between energy and materials sectors. The manager posted incredible performance in 2009 and 2010 but like most resource baskets in 2011, it lost money that year. CMP is one of the larger flow-throughs and has a long and successful track record.

Please let me know if you would like to buy any flow-through in 2012 or like more information about them.

Website

Richardson GMP plans to launch a new and dramatically improved website on February 6th. I hope to substantially develop my personal sections of this site and use it in conjunction with my weekly communications. I'll let you know more as it becomes available.

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