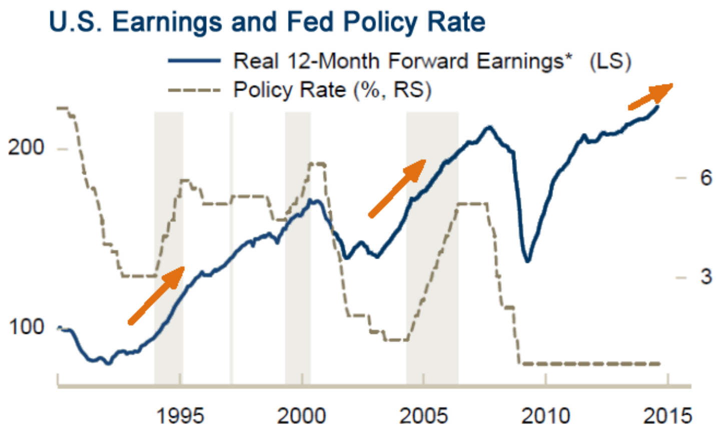
A Longer, Slower Growth Cycle

Governments have experimented with prolonged low interest rates and active bond purchases over the last few years as stimulative measures to avert a great depression, and subsequently to encourage growth. It may have worked. Global growth is present, but more muted than previous cycles with corporations holding less debt and more cash. Governments are working harder than ever to achieve balanced budgets and often enacting difficult austerity measures. Consumers and businesses are spending, but since 2008 many have seen debt and leverage in a different light.

The next part of the experiment is to see if the economy is strong enough on its own. Central bank stimulation is supposed to be reduced, something that most economists believe makes sense in the long-term.

Two things are important to note about this transition, compared to past transitions from a recovery period to sustained growth:

- **Earnings and stock markets historically rise** during the early years when stimulus is removed (a rate hike cycle begins).
- **Removal of stimulus is expected to be gradual and data dependent.** This means if the economy doesn't seem to be growing, then investors might expect stimulative measures to be re-initiated.



Source: Thomson Financial / IBES / MRB Partners Inc
* Deflated by U.S. CPI; rebased; source: Thomson Financial / IBES
Note: Shaded for periods of Fed tightening

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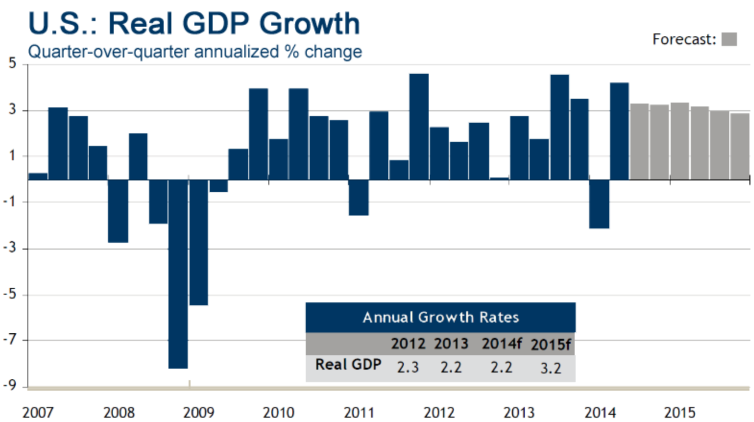
The U.S. economy is poised to outperform. It accounts for nearly half of global market capitalization, superior domestic economic growth, accommodative and increasingly effective monetary policy, and very strong corporate earnings. The U.S. is also the broadest, deepest, and most shareholder friendly equity market, which attracts investor support particularly from other markets in times of caution.

The U.S. economy grew by an impressive 4.2% annualized gain in the second quarter. The 2.1% drop in the first quarter is blamed on the unusually harsh winter slowing economic activity. Net year-to-date growth in the economy is positive, and forecast to be generally low but consistent.

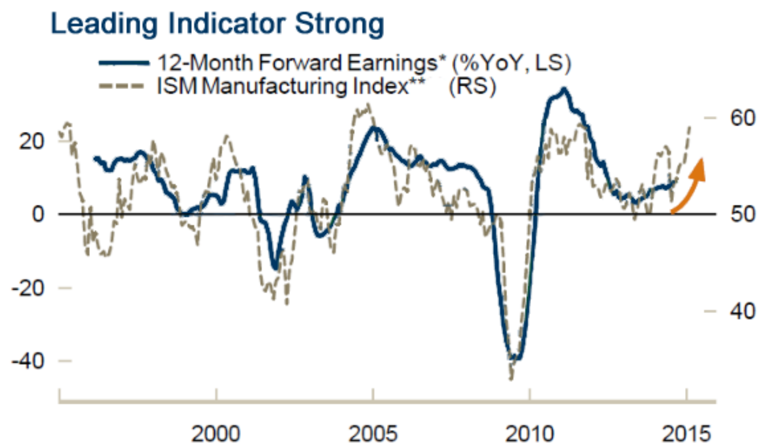
The ISM Manufacturing Index is considered one of the best leading indicators of economic strength. Graphed to the right, the ISM Manufacturing Index is advanced six months to show the strong predictive correlation between it and underlying corporate earnings. The August, 2014 measure of 59.0 represents a very optimistic reading on the health of the economy. At the same time, the U.S. job market has grown for the sixth consecutive month in August by more than 200,000 jobs.

Short-term rates should be rising because it is the U.S. Federal Reserve's publicly stated intention to raise them. Short-term rates are considered restrictive when they come close to the same yield available on longer-term rates. This "flatter" yield curve has been a good predictor of recessions. Currently, the shape of the yield curve is considered stimulative and seems several quarters or possibly years from being in a flat position.

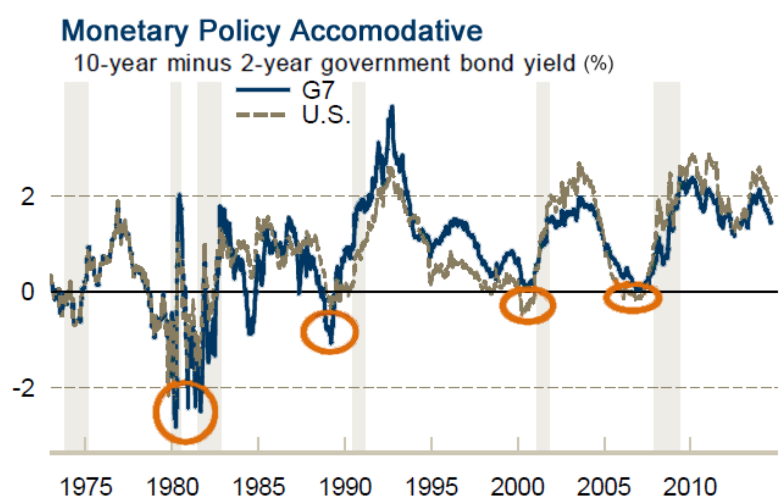
Increases in Fed funds rates have historically coincided with the outperformance U.S. equities leading up to the first hike. Investors are likely to believe the U.S. is best positioned to weather any impact from removing central bank stimulation. This period is often more turbulent and uncertain, with funds often flowing out of global equities and into U.S. ones. Once Fed hikes have been established, investors seem to rotate back into global markets, which then beat the U.S.



Source: Bureau of Economics Analysis, RBC Economics Research

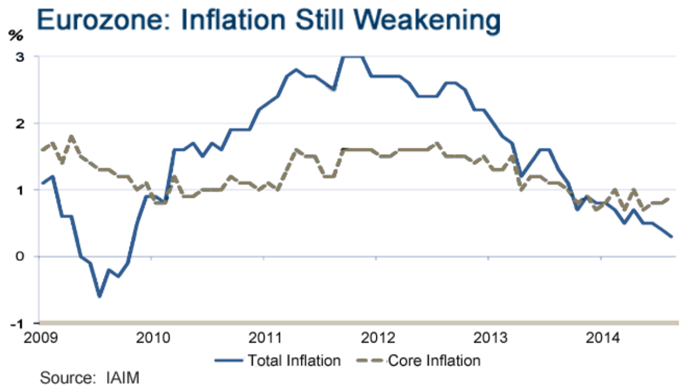


* Smoothed; source: Thomson Financial / IBES / MRB Partners Inc
** Advanced; smoothed; source: Institute for Supply Management / MRB Partners Inc
Note: ISM Manufacturing Index advanced 6 months



Source: MRB Partners Inc
Note: Shaded for NBER-designated U.S. recessions

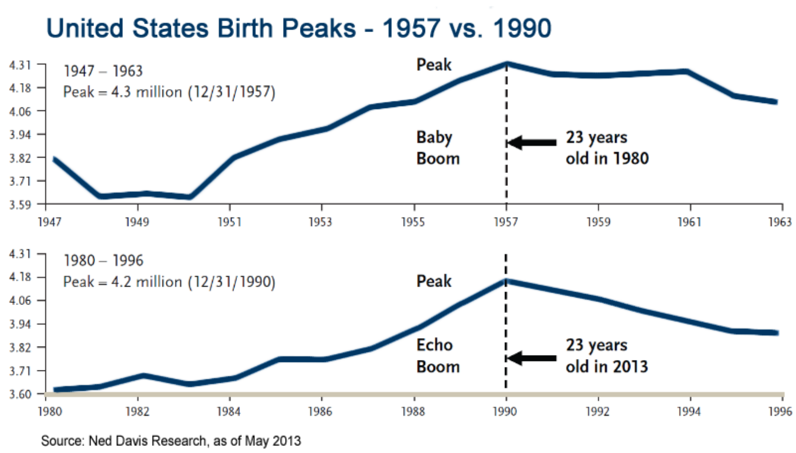
One major reason why growth is so uncertain in the U.S. is the weakness of other global markets. There was no European GDP growth in the second quarter, Germany's economy contracted, and Italy entered its third recession since 2008. The European Central Bank is still increasing stimulus as the latest data point of only 0.3% total inflation suggests that Europe may be heading straight into deflation. Note that the housing market and inflation have been relatively strong in the U.K. The Bank of England is expected to start hiking rates possibly before the U.S. Since the U.K. has far greater mortgage debt per household than in the U.S., they may move rates upward even more slowly.



The Japanese index fell back to lowest level in 10 years in response to the new April consumption tax. The impact of the sales tax hike in Japan was to decrease GDP by 6.8% in the second quarter (annualized rate).

Chinese data is also disappointing. Growth in Chinese GDP has been slowing over the past few years. In particular, housing prices, sales, and construction have recently slumped heavily. This has affected commodities like iron ore, whose price has dropped from U$140/ton at the beginning of the year to close to U$80/ton recently.

All of this adds up to a very choppy market and a wide variety of global economic situations.



Population drives consumption. The U.S. is one of the few developed markets that still boasts a reasonably strong population growth rate. Baby boomers were in their late 20's to early 40's during the period from 1980 to 2000. Spending is high during these ages typically and it coincided with a very healthy period in the stock market.

Over the next decade, the children of these baby boomers, called the "Echo Boom", are expected to reach that same high expenditure time of their lives. The number of births in the Echo Boom is similar to Baby Boom levels. This time, emerging market populations are likely to help consumption as well.

A correction is a reasonable expectation during the months leading up to the first Fed Funds rate hike. However, it is likely to be temporary and should be viewed as a buying opportunity. For long-term investors, this is not a period of time to wait on the sidelines until everything is resolved and markets are already higher. **Cautionary actions that are appropriate during this time of volatility** include owning U.S. securities to take advantage of currency appreciation and flight to quality during uncertainty; keeping fixed income exposure lower than average because of the negative effect of low interest rates combined with rising yields; favouring larger, more mature companies although the more cyclical industries are positioned best for growth in the current environment; and considering use of hedge funds that use shorting techniques to reduce risk and achieve returns independent of market fluctuations.

Security	Curr	6/30/2014 Value	Buys Date	Buys Price	Sells Date	Sells Price	9/30/2014 Value	3rd Quarter Dividends	Total Return
Top Performers									
Tim Hortons		58.37					88.19	0.320	52%
Open Text Corp		51.20			8/5/2014	59.58	61.95	0.173	20%
Ross Stores Inc	U	66.13					75.58	0.200	15%
National Bank of Canada		45.26					51.03	0.480	14%
Core Positions									
Apple Inc	U	92.93					100.75	0.470	9%
Great West Lifeco Inc		30.18	9/15/2014	32.81			32.21	0.308	6%
Royal Bank		76.28					80.05	0.710	6%
Biogen Idec Inc	U	315.31					330.81		5%
Constellation Software Inc		271.96					281.49	1.000	4%
Shaw Communications B		27.36					27.45	0.275	1%
BCE Inc		48.40					47.89	0.618	0%
Walton Westphalia		5.00					5.00		0%
Baxter International	U	72.30	9/4/2014	73.65			71.77	0.520	0%
Saputo Inc (split 2 for 1)		31.97					31.33	0.490	0%
Qualcom Inc	U		8/21/2014	77.00			74.77	0.420	-2%
Priceline.Com Inc	U	1,203.00	9/16/2014	1,177.00			1,158.58		-3%
Colgate Palmolive Co	U	68.18					65.22	0.360	-4%
North West Co Inc		23.65					22.38	0.290	-4%
Gamestop	U		9/23/2014	44.90			41.20		-8%
Weak Performers									
Mylan Inc	U	51.56					45.49	0.060	-12%
St. Jude Medical	U	69.25					60.13	0.270	-13%
Sandvine Corp		3.60					2.77		-23%
Labrador Iron Ore Royalty		30.68					21.85	0.500	-27%
Black Diamond Grp Ltd		34.32					23.82	0.235	-30%
Energy Positions									
Pason Systems		30.00					31.31	0.170	5%
Tamarack Valley Energy		6.44					6.59		2%
Whitecap Resources		16.47					16.03	0.182	-2%
Crew Energy		11.05					9.89		-10%
Alliance Resource Limited Partners	U		8/21/2014	48.89			42.84		-12%
Raging River Exploration		10.85	8/13/2014	10.00			9.17		-13%
Deethree Exploration	U	11.40					9.10		-20%
Bankers Petroleum		6.82					5.39		-21%
European Positions									
Ishares MSCI Belgium ETF	U	17.20					16.32		-5%
Ishares MSCI UK ETF	U	20.88					19.38		-7%
Ishares MSCI Germany ETF	U	31.28					28.06		-10%
Eliminated from Discipline Failure									
Valeant Pharmaceuticals		134.94			8/5/2014	121.50			-10%
Waddell & Reed Fncl Inc Cl A	U	62.59			8/5/2014	51.80		0.340	-17%

Source: Richardson GMP as at September 30, 2014

Analysis of Third Quarter Trading Activity

1. **Tim Horton's was the best position held, growing by over 50% in the quarter.** The merger with Burger King has put a floor on the share value at $88.50. The new entity has promising growth prospects. Each franchise will largely be left alone, but a consolidated purchasing department and head office, combined with other synergies, will likely keep earnings growing by driving costs downward. The valuation at the merger price is expensive. Shares are currently held really as a proxy for cash intended to be deployed likely in October.

2. **There were four themes that lost money over the quarter**:

   a. **The Russian conflict with Ukraine had a significant impact on energy**. Economic sanctions between Europe and Russia threaten already weak economies. Inventories of particularly North American natural gas had been depleted to low levels at the end of this year's particularly harsh winter. Unfortunately, gas inventories were able to recover to average levels over the summer, while global demand for oil slowed with economic weakness in Asia and Europe. I had thought in the spring that a new trend of sustained money flow into energy was being established, which I no longer think to be true – commodities had their quintupling last decade and may see muted growth going forward. However, seasonally energy stocks have proven to be strong between November and April and the current depressed environment is likely a buying opportunity.

   b. **The international positions held are currently exclusively in Europe**, in the stronger and more conservative countries. A combination of the uncertainties from the Russian/Ukrainian conflict and weak European economic data led these investments lower. Exposure to Europe will be held because of the very low valuations relative to U.S. stocks in particular, and the longer period of expected stimulation. I didn't want to sell investments in the U.K. during the Scottish referendum, but am likely to sell during any market strength in the next few months.

   c. **Valeant Pharmaceutical was a difficult stock to part with after doubling to tripling in most portfolios, particularly at a price much lower than its peak and more recent purchases.** I have enjoyed the success of this company's consolidation model in the health industry. For over six months now, Valeant has engaged in a very nasty battle to acquire Allergan. In early August it seemed that the shares were ready to break down and I sold. Recently, the companies dropped law suits against each other and might be starting to work together. The shares recovered somewhat. Looks like I needed six months of patience and not just five. This company currently doesn't fit in my investment model because daily news drama has completely overshadowed earnings.

   d. **There were a few particularly bad individual performers.** What these stocks had in common was that they are making a reasonable amount of earnings, however in all cases the earnings slowed from what was previously expected. I had assessed the earnings to still be strong enough to warrant owning the company, but underestimated how much investors can punish stocks when growth slows. Labrador Iron Ore was a little different. I've held it over fifteen years and have never seen the royalty fund drop like it did in a matter of a days in September. Underlying iron prices did fall, but they don't really affect the 80 more years of iron royalties the company's lands are likely to produce. Individually, these companies are being assessed closely right now.

3. **Over the quarter, hedge funds were included in several portfolios.** These securities tend to have performance that is uncorrelated to stock and fixed income markets. Their risk level measured by volatility is often less than one-third of average stock markets. They are often designed to achieve a consistent return regardless of market conditions. Ultimately they tend to be one of the best assets during market declines.

4. **After several quarters of strong equity performance, the third quarter results keep me humble.** I do see market declines in the current environment as more of an opportunity than a trend. I hope I am able to take advantage of current weakness to deliver strong results in the continued growth cycle I see ahead.

Save the date! - Exploring Alternative Investments Seminar

I am pleased to host Andrew McCreath, President and CEO of Forge First Asset Management Inc. as well as Andrew Milne, Vice-President and Partner of Picton Mahoney in a very important discussion about investing in hedge funds.

Alternative investments can offer an opportunity to take advantage of investment strategies that exist beyond traditional stocks and bonds.

We invite you to join us for an informative lunch presentation and learn about:

- Challenges in today's investment environment
- What hedge funds are and how they reduce risk
- What hedge managers are doing today in their funds to earn returns for their clients
- How these products may compliment a traditional investment portfolio

FULL EVENT DETAILS – CLICK HERE

Date:	**Wednesday, October 8th, 2014**
Time:	**11:30am – 1:00pm**
Location:	**Eighth Avenue Place Conference Room – 4th Floor** **Suite 400, 525 8th Avenue SW (map)**
RSVP:	**Rita Penno by telephone 403.355.6034 or** rita.penno@richardsongmp.com

FORGE FIRST ASSET MANAGEMENT INC

PICTON MAHONEY Asset Management

Lunch and refreshments will be provided.

Please pass this invitation to anyone who may benefit from attending.

Regards,

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