



Winter Edition  
2008

## PROVEN INSIGHT

“Cautious  
Optimism”



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## Skate to where the puck will be, not where it is now.

Wayne Gretzky is regarded by most as the best hockey player of all time, he was asked, at a press interview what made him so good, to which he immediately replied **“I try to skate to where I think the puck is going to be. I frequently have to discipline myself to skate not to where the puck is but to stay focused on where the puck is going to be”**. Wayne Gretzky was not the fastest or biggest player, nor did he have the best shot but he excelled above everyone else because of his ability to foresee where the play was going to be, not where it was. I like to use the same strategy for investing.

By applying a “where is the puck going to be” strategy we can look beyond today’s news to what lies ahead for equities. Believe it or not, a bleak economic outlook can be positive for stocks. Recession fears are on the rise, more and more credit issues are coming to light, uncertainty and panic selling rein supreme. When investors panic, it tends to result in bad decisions. Like most things in life, careful calculated decisions, result in better results. Investors should note that stocks have consistently bottomed 4-6 months ahead of the end of a recessions/economic slow down. If one expects the economy to improve by fall 2008 the “low” in equities should be this month or next. Buying now would allow for 3 quarters of a slowdown/recession – this is the same length as the actual recessions in 1990 – 2001. **In short, if you expect another 4 to 6 months of negative economic data, you should be considering buying quality companies at today’s prices.**

Going against the grain or taking a contrarian position is not easy but some of the greatest investing fortunes have been built on this strategy. Hedge fund manager John Paulson’s racked up a massive return for his fund last year betting on the housing market credit crunch. He began this strategy in 2005 when the market was the hottest and he was very much alone on the hill with this ideology. His fund earned \$15 Billion last year and Mr. Paulson took home a paycheck of \$3 Billion, the largest single year paycheck in Wall Street history to date.

**I am presently a selective buyer of equities and well valued index-units for my clients. I focus on high-quality companies which are trading at a discount. These positions should provide an excellent avenue to participate in a likely 3rd or 4th quarter recovery in equities.**



## Software for a Soft Economy

According to a research report by (National Bank Financial) Technology analyst Richard Tse, the Software & IT sector makes a great home during an economic slowdown. **In a study of the past 20 years we have experienced an economic slowdown in 11 out of 20. In 8 out of those 11 “down” years the, Software & IT group outperformed the broad S&P500, and outperformed the Nasdaq in all 11 of those years.** Mr. Tse believes the sector represents a strong play during slowdowns due the typical recurring revenue stream in the form of maintenance and (long-term) outsourcing contracts.

*History is no definitive indicator of the future performance of a sector or market; however a consistent trend tends to provide some good framework for investment decisions.*

## Why YOU Should own Commodities

As my clients know, I invest with a long-term outlook and focus on “trends” and do my best not to get caught up in the daily fray of panic selling and newsfeeds. Perhaps one of the biggest trends at the moment is that of Commodities, which by all accounts is in a SECULAR BULL CYCLE. A good measure of the rise in natural resource prices is to measure it against a broad equity market. When one compares the Commodity Research Bureau Index which is a measure of natural resource prices and the S&P500, over the past 12 years, most of the 80’s and 90’s were dominated by non-resources equities (S&P500), whereas in 2000 a shift towards out performance in natural resource equities emerged. One can expect volatility and corrections along the way but historically bull markets in commodities run 14-21 years. **Given that the bull market in commodities started in 2000 we should have at least another 6 or so years more of this upward trend.**

**I like to balance out my investment ideas with one part history and one part common sense.**

Its one thing to say we are in a secular bull trend in commodities but you have to understand why from a practical point of view. For all the complex forecasts and reports one can read, it all boils down to a rather simple supply/demand equation. A rapidly growing middle-class in China, India, and other emerging regions is driving the demand side equation and we have stagnating supply side. Even a more moderate growth profile would still result in large demand.

**While I view natural resources as a finite resources I’m not in the camp that suggests we are running out of oil and other commodities, however what’s being found now will take years to bring “on-line” to meet additional demand, and most of the new finds require more costly extraction methods.** We can expect to see volatility and corrections along the way, but, based on the above, natural resource prices over the long-term likely have only one place to go. Up.

In the specific case of GOLD you have two factors at play. The first is rising demand for actual jewelry (growing emerging markets) and the second is a greater focus on gold as an investment, this has been spurred along by the advent of the various ETF’s and gold funds which allow one to profit from the rise in gold prices without having to hold actual gold bars.

## Rough Road? Drive a Hummer

GE is as “blue-chip” as they come and trading at bargain prices. A major weight on GE’s stock price has been that half of GE’s earnings come from its lending and investing. What investors are not seeing is that GE has no exposure to troubled assets like collateralized debt, in fact this may be a time for GE’s to capitalize on the credit issues. **GE’s new CEO was recently quoted as saying “These are classically times where our financial services business does very well. This is a great time to be triple “A” rated”.** The old saying that “it takes money to make money” is



very true and GE has cheap cost of funds and ready access to them, a major bonus when credit ratings are falling. In addition GE's share price will benefit as investor move towards quality when markets are rough, GE is the Hummer of stocks and provides a comfortable ride during rough markets, in addition its growing earnings at 12% per year and pays a 3.57% dividend. **The average 12-month target price for GE is US \$43.80. Combined with its dividend, that equates to a potential 12-month return of around 29% over today's price (01-16-08) of \$34.79....not bad for a blue-chip!**

## Trend to Watch: Agribusiness

As mentioned earlier I like to skate to where the puck will be, not where it is now. The price of energy and materials tends to take center stage with headlines but what is often overlooked is something that's right in front of us. FOOD.

*"The Agribusiness sector will be, in my opinion, one of the best performing sectors over the next few years as spending on everything from equipment to fertilizer is increased in order to ramp up farm production to meet growing demand."*

The rapid growth of a new middle class in emerging regions creates a huge demand for meat and dairy products, in addition there is also heavy demand for crops from the biofuels industry. All of this creates a major build up of demand on the global food supply. You can already see this happening with the rise in raw food prices, which rose 22% this past year. In the center of this issue is corn; which is the main staple of the Ethanol industry and has seen prices rise 44% over the past 15 months. A good indication that this sector is going to be in focus this year is the recent flurry of IPO's for Agribusiness Funds and Income Trusts. My clients participated in the IPO of "The Global Agribusiness Income Trust", one of the top "AGRI" offerings to hit the market. It has already risen 5% (not including income distributions), in contrast the S&PTX index has fallen 6% over the same period.

## Are all your Eggs in One Basket?

Common mistake investors and many Investment Advisors make is to assume you are properly diversified as you hold a number of stocks or mutual funds. For example most Canadian Equity mutual funds hold relatively the same holdings, or at best different companies but in the same popular sectors.

*"Well you might hold a few different funds with different mandates you're probably not properly diversified. Proper diversification by company, sector, as well as region is the key to reducing risk and maximizing long term gains."*

I would be happy to provide you with a detailed analysis of your current holdings broken down by sector, region, risk quality, as well as correlation between each other. I will then recommend what changes would have to be made to better diversify your holdings. **To learn if your portfolio is properly diversified please feel free to contact me and I would be happy to provide this to you on a complimentary basis.**

## Smart Giving

### Donating \$100k of Securities with a cost base of \$50,000

(\$100,000 - \$43,000 tax credit assuming a top tax rate = \$57,000).

### Selling the securities and donating cash

(\$100,000 - \$43,000 tax credit + \$10,750 in capital gains tax payable= \$67,750)

\*Note these calculations are based on a BC resident in the top tax bracket who has already donated the basic \$200 amount in that year.

**The 2006 budget removed the capital gains tax on securities donated to a registered Canadian charity and the 2007 budget extended this rule to Private Charitable Foundations.** This change couldn't have come at a better time for charities or investors given the strong growth in the resource sector over the past few years, leaving investors sitting on big gains (and eventually a tax liability).

A client recently wanted to donate a gift of \$100k to a charity, by looking at his portfolio we decided to donate \$100k of a gold stock he held with a cost base of roughly half. **By donating \$100k of stock he was able to donate this amount for a cost of \$57,000, had he sold the stock and donated the cash it would have cost him \$67,750.....so he saved \$10,750 in the process.**



## Did you know that you can donate shares held in your RRSP to a registered Canadian charity?

A donor is entitled to a tax credit at the highest marginal tax level so this strategy is only of benefit to someone in a lower tax bracket, however it can be useful to a high tax bracket individual if the donation is made from the RRSP of a lower income spouse.

Take for example a fictitious client, Susan Smart, who is retired with the bulk of her assets in an RRSP, she receives a yearly income of \$25,000 from her investments, this puts her in a 21% tax bracket. Assuming she has already donated \$200 worth of donations during the year, and then makes a special donation of \$1000 from her RRSP, she would pay \$210 in tax on the withdrawn funds but would get a tax receipt for \$1000 which is worth 40% or \$400. So by donating the \$1000 from her RRSP she effectively withdraws the funds tax free and get an additional \$190 (\$400 - \$210) of tax credits to use to off-set other income.

**Donating stock is a great way to help society as well as your bottom line.** I have always believed that it's important to give back to society so charitable giving has been a major focus of my business. I also make it a large part of my personal life by working with a number of non-profit organizations, most notably the Vancouver Friends For Life Society where I have held a Board seat for the past 4 years. **If you have questions about the ins and out of charitable giving involving securities or if you are a Foundation or non-profit organization which would like to learn more about this strategy, and how it can benefit your fund development, I can provide you with expertise in this area.**



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As a steward of my client's wealth, I balance risk/reward and endeavor to deliver the **best returns for the least amount of assumed risk.** I provide clients with **personalized investment management, objective advice** and a high level of **personal service.**

To learn more about how I might be able to help **grow and protect** your wealth please feel free to contact me at your convenience.

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