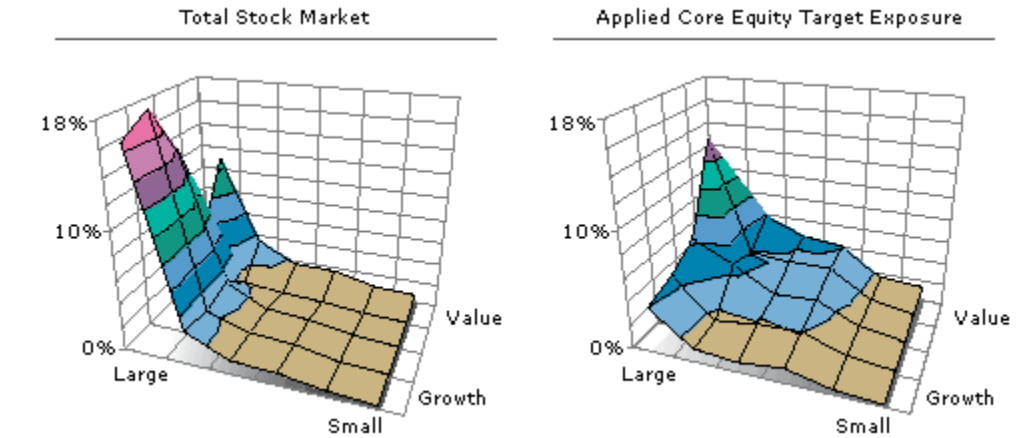


Quarterly Commentary: Second Quarter 2008



Courtesy of Dimensional Fund Advisors

Staying calm as stocks align themselves in the investment universe

An advertisement that appeared recently in *Barron's* got me thinking about the process I use to manage your investments. The headline read, “**Manage Risk. Deliver Returns. Repeat**” and repeated itself five times half way down the page. I liked the measured, mechanical approach to the ad. The two charts above illustrate my disciplined, unwavering portfolio management approach amidst a universe of over 9,000 stocks that are included in your Canadian, U.S. and International holdings.

The second quarter of 2008 saw commodity and oil stocks soar as financials slipped from favour. Does this mean that now might be the time to move away from oil and commodities and back into financials? What about manufacturing? No one knows where stocks will align themselves in the vast investing universe at the end of the next quarter. And I have no inclination to guess.

In the left hand chart above, the US stock market is represented with market capitalizations of all US stocks. The axis on the bottom shows large companies on the left and small companies on the right. The axis on the right side places value, or inexpensive companies, on top and growth, or expensive companies, on the bottom. Over 3,000 US companies are represented on this graph. Large growth stocks such as Cisco Systems and Microsoft would be in the top left corner. And Kraft Foods is nesting in the top middle “spike” along with other large value stocks. On the right side at the top of the brown section is Winnebago Industries along with other small value companies. Lastly in the bottom right corner are i2 Technologies and other small growth companies.

The point is to show you how these US stocks are constantly floating through the universe as their prices change, oblivious to forecasts of where they will appear on the grid in the next quarter. I accept that it is futile to place bets on stock moves. I therefore base my approach on enhanced index investing, which takes into account the movement of the economy and stock markets at large. This is then reflected in prices of specific stocks within the universe.

The graph on the right “Applied Core Equity Target Exposure” is the result of fifty years of research by the world’s leading financial economists. Dimensional Fund Advisors currently has the best execution of this strategy, which is a dynamic and efficient approach. A key aspect is an overweighting of value and growth companies relative to the comparable stock market, in this case the US, because these companies have higher *expected* returns. My goal is to maximize the potential for strong returns with an acceptable level of risk while keeping costs low.

I have spent a large portion of my career gaining a full understanding of the benefits enhanced index investing can bring to my clients and have tremendous confidence in this investment process. I remain a specialist who relies on

enhanced index investing to reward my clients, rather than one of the many generalists working within this country's investment industry.

My lunch with Ken French

Imagine being held in such high esteem that institutions routinely send private jets into the wooded New Hampshire haven of Dartmouth College to pick you up and take you to speaking engagements where experts line up to gain your insights.

Such is the lot of Ken French. French, a Dartmouth finance professor who is most famous for his work on asset based pricing with Eugene Fama, a finance professor at the University of Chicago. French and Fama are also heads of research at Dimensional Fund Advisors in Santa Monica, California. These two brilliant gentlemen have published more ground-breaking papers in finance than *anyone* ever!

French was in Toronto recently to speak at the Rotman School of Management at the University of Toronto, where institutional investors from around the world gathered to hear his views. I had the opportunity to join French and six other financial advisors for a two-hour lunch, which proved to be a highlight of my career that spans nearly three decades. He had strong opinions and offered useful input into several portfolio investment ideas I shared with him over lunch. Whether in the woods of New Hampshire or in the big city, French confirms that hard work and brilliance know no boundaries.

French is a director at Dimensional Fund Advisors in Santa Monica, California where he also works as Consultant and Head of Investment Policy.

Tread carefully through the wealth management forests

Technology has been a huge enabler for the financial services industry. Investment options that were once reserved for large institutions are now accessible to most affluent investors, in degrees. These investors often see their wealth grow as they have more time to do other things besides monitoring their portfolios.

With choices, however, come decisions and increased costs. And relatively few investors are trained to understand how mounting costs driven by the complexity of investment products can potentially erode their investment returns. By the time the investor helps pay for development, distribution and marketing of the product (and assumes a fair share of the risk it presents), some offerings just don't pan out as initially thought. In strong markets, some investors are not as likely to demand to look under the hood for a full accounting before they put down a payment and drive the vehicle off the lot. As investment products become more difficult to understand and less transparent, investors need to fully understand what they are getting ... **and for how much**. No one is paying them a salary or a commission for taking on the risk inherent in new products.

I wrote some time ago about Warren Buffett's reference to the "helpers", those professionals who strive to add value to an investor's experience but often succeed only in driving up management costs in fees for services the client does not understand, although the helpers may provide them in good faith. Performance is essential, but it is important to understand the cost to potentially realize it.

What you missed.....

The credit crisis and the huge fall of investments directly effected by it. Why do I mention this? I think it is instructive to review **what you did not own in your portfolio**. To quote the Globe and Mail's Report on Business from July 22, 2008 "Canada's federal government workers and pensioners have been hit hard by the credit crisis, which forced the money manager that runs their retirement fund to book \$920-million of losses on holdings of asset-backed commercial paper and other exotic investments." You did not own **any** of this wild stuff in your portfolio. It was way too complicated and risky for the modest *potential* returns offered.

I wish you an enjoyable, safe summer. Please contact me should you have any comments or questions about your investment portfolio.

Yours sincerely,

David R. Bruce
Portfolio Manager
416.945.4850