



# *Market & Investment Review*

## The Good, The Bad, and The Ugly

*Earning Your Trust.  
Building Your Wealth.*

Ray Joseph, CFP  
Vice President

Michael G. Flux, CFA, CFP, CIM  
Vice President

*Thursday, November 6, 2008*





# *Agenda*

- Who is Connor, Clark & Lunn Private Capital Ltd.?
- What happened to the markets?
- What did we do about it?
- What's our outlook?
- What's our strategy moving forward?



# *Connor, Clark & Lunn Private Capital Ltd.*

*“Experience”*

***Independence:*** Owned entirely by the partners of the firm – no conflicts!

***Focused:*** Our only business is managing investments

***Depth and stability:***

- In business since 1982
- Over \$36 billion under management
- Canadian firm, International organization



# *Connor, Clark & Lunn Financial Group Clients*

## Private Clients

*Over 1200 families across Canada*

## Financial Institutions

*Six chartered banks*

## Corporations

*Over 175 institutional clients*

## Aboriginal Clients & Communities

*Little Salmon Carmacks First Nation*

*Alexander First Nation*

## Government

*Canada Pension Plan*

## Foundations & Endowments

***Over 70 not-for-profit clients:***

*Col. Sanders Foundation*

*Toronto Public Library Foundation*

*Community Foundation of Orillia and Area*

*Hamilton Community Foundation*

*Canadian Cystic Fibrosis Foundation*

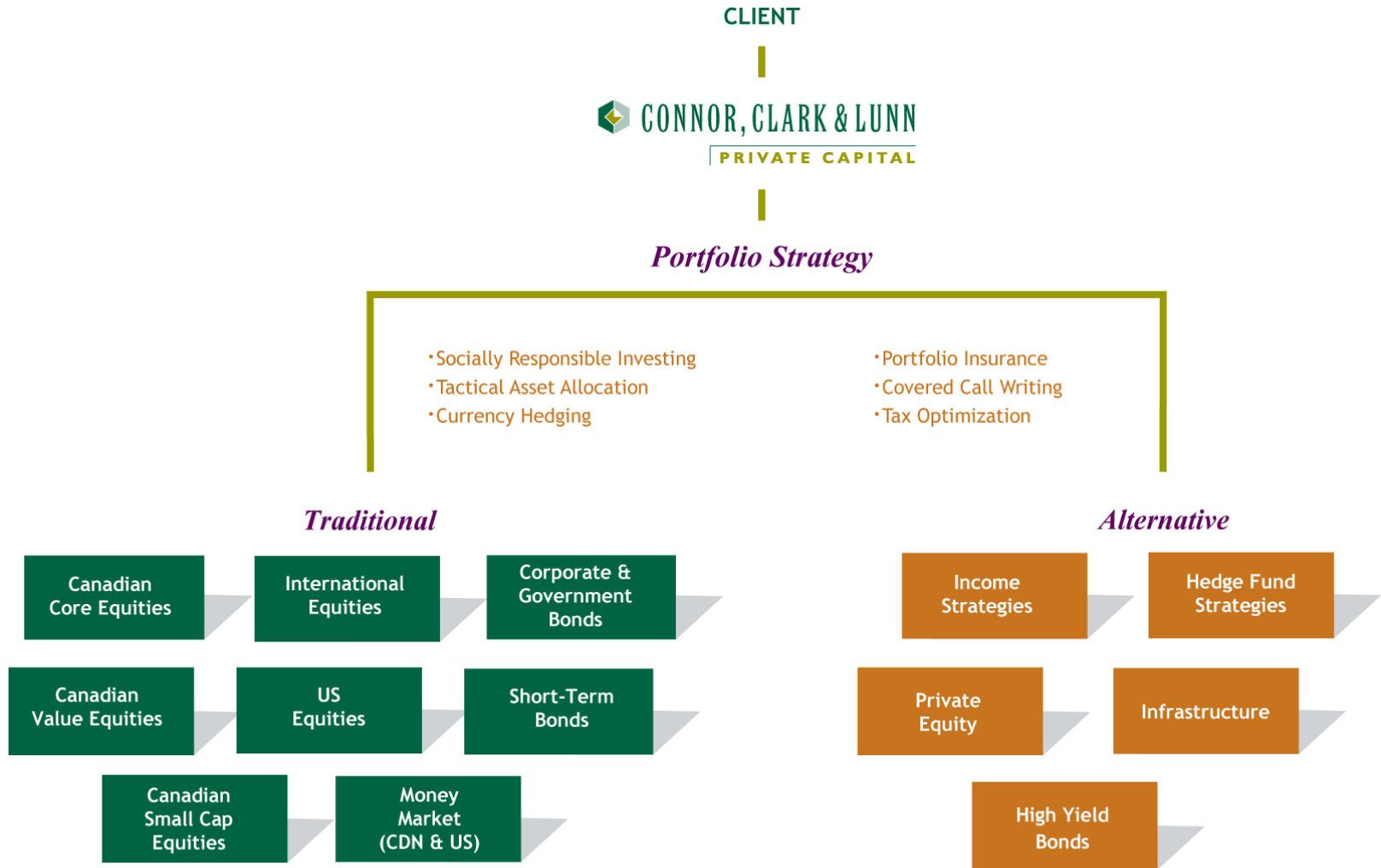
*Humber River Regional Hospital*

*Kingston General Hospital*



# Investment Teams and Alternatives

*As needs  
change &  
markets  
evolve,  
we respond*





# *What happened to the markets?*

## Financial Leverage:

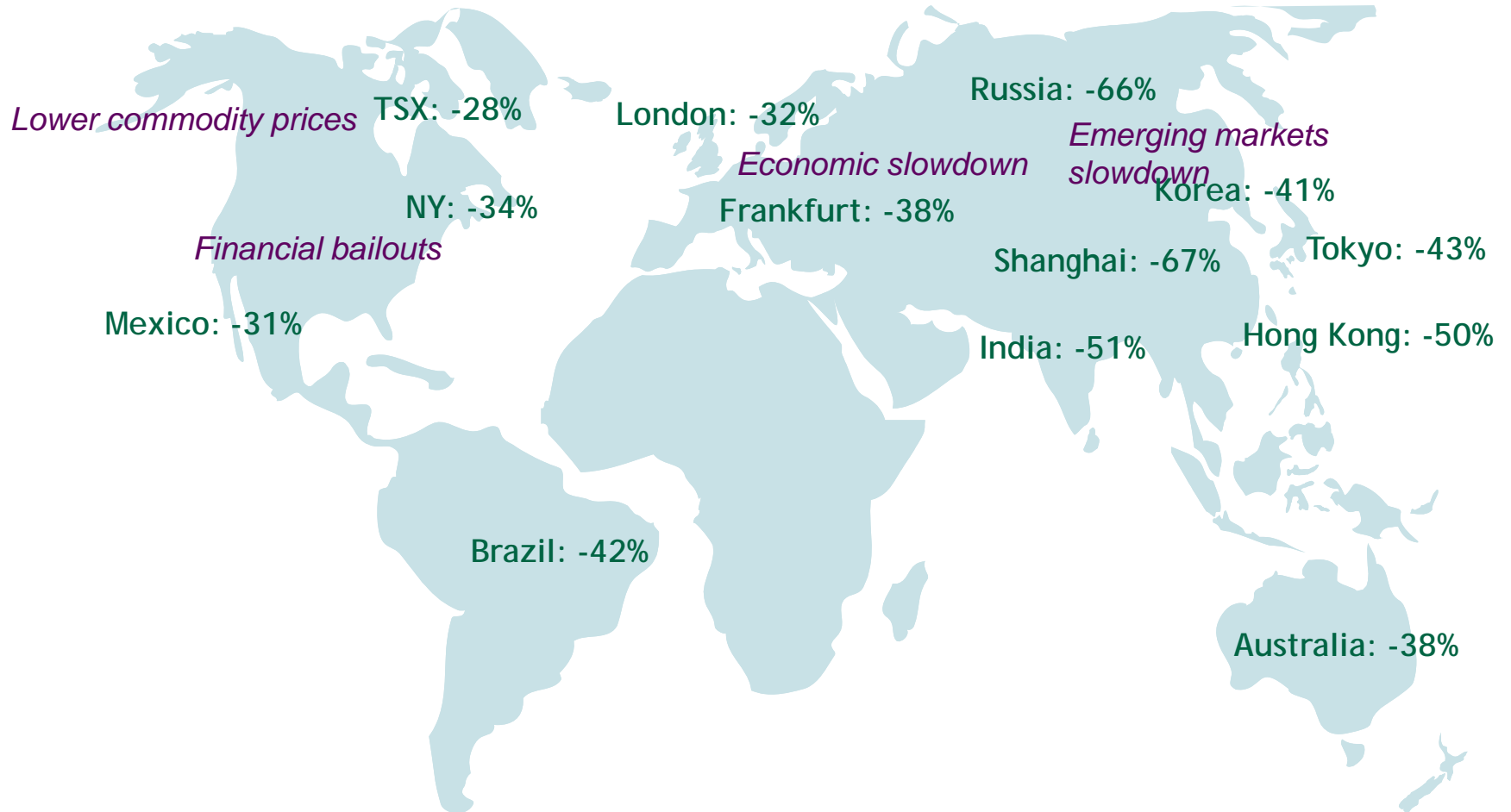
*“Using borrowed money in such a way that the positive or negative outcome is **magnified**”*

Negative outcome in 2008

- Massive de-leveraging
- Forced liquidations drive down stock market
- Bond prices also fall



# *What happened to the markets?*

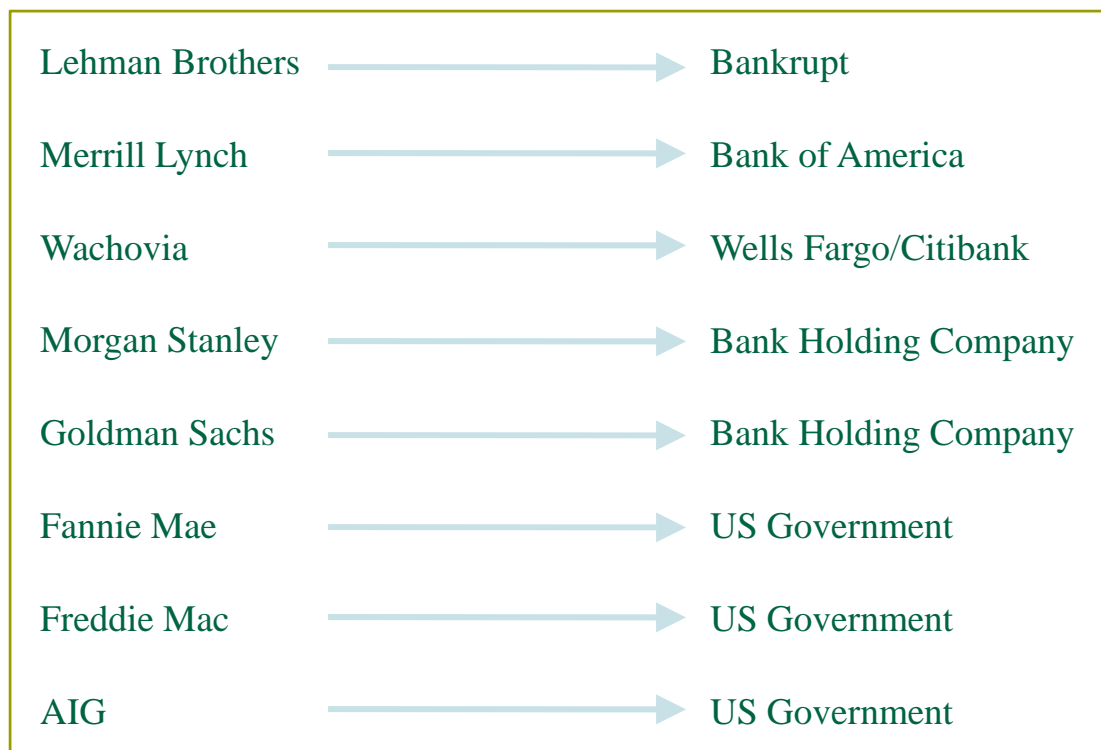


Returns are year-to-date at October 31, 2008 (in local currency terms)

*Global bear market in stocks*



## *What happened to the markets?*



- Leverage Ratios:

Investment Bank	Bank	Consumer
30:1	10:1	0.75:1

- US moving toward Canadian banking model



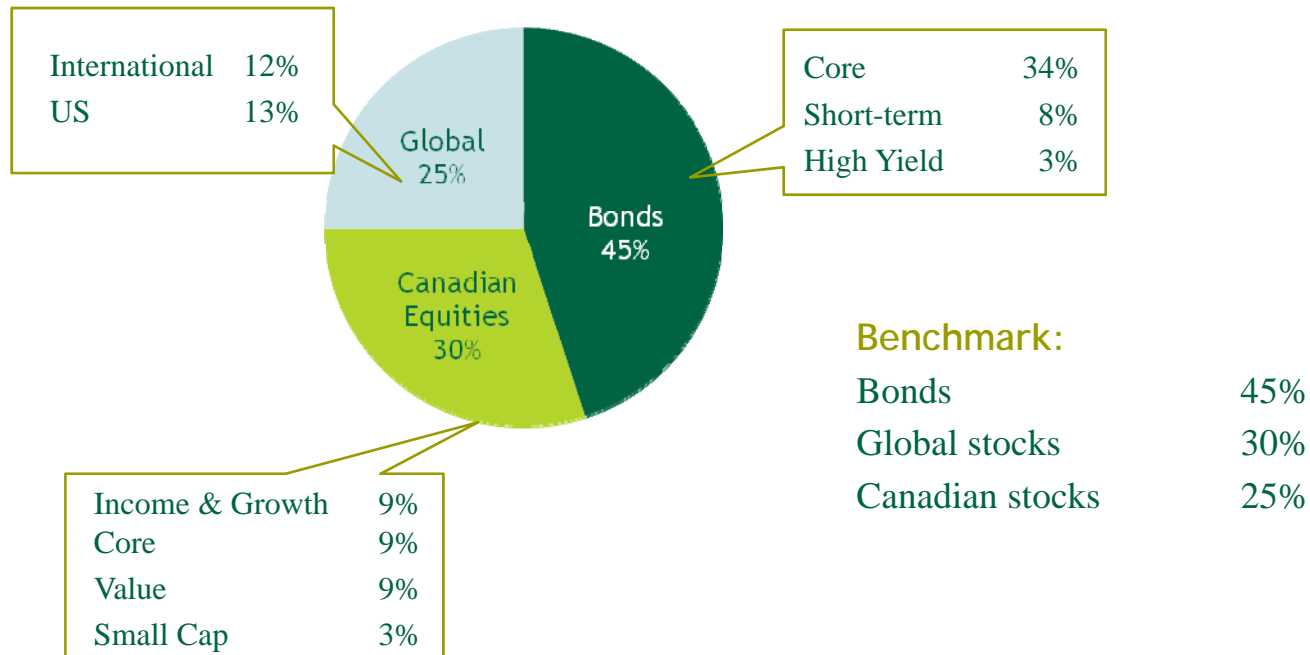
# What did we do about it?

## Prior to Downturn

- Reduced equities
- Reduced small caps
- Bought short-term bonds
- Increased income and dividend stocks

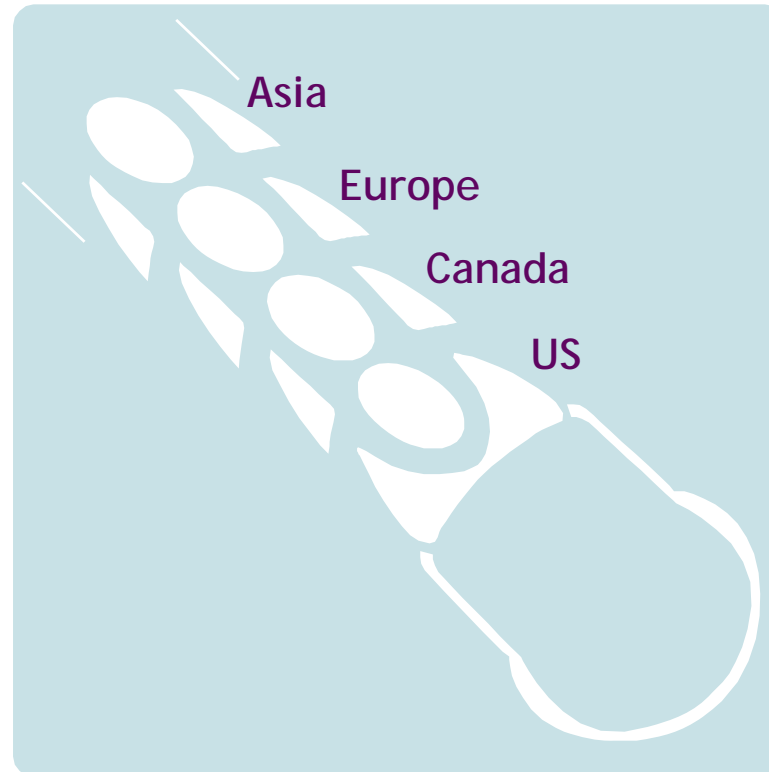
## During Downturn

- Did not rebalance portfolios as stocks dropped
- Focused on security selection
- Increased corporate bonds
- Added global small caps
- Reduced international stocks, bought US stocks





# *Outlook — heading into a global economic recession*

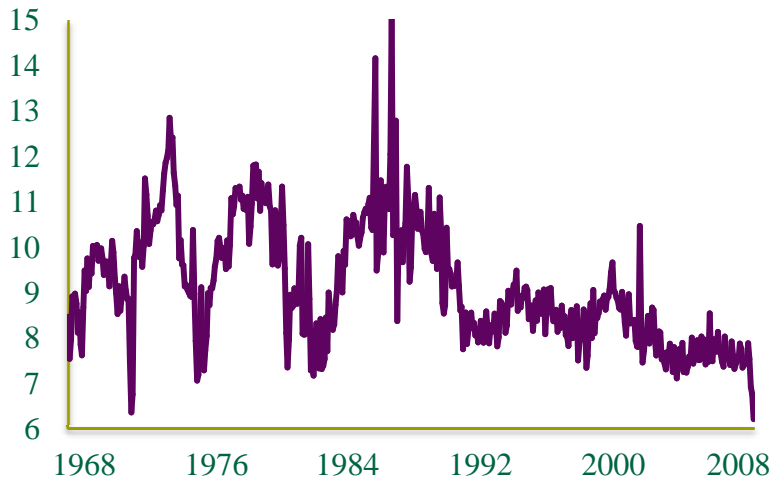


- US leading economic slowdown

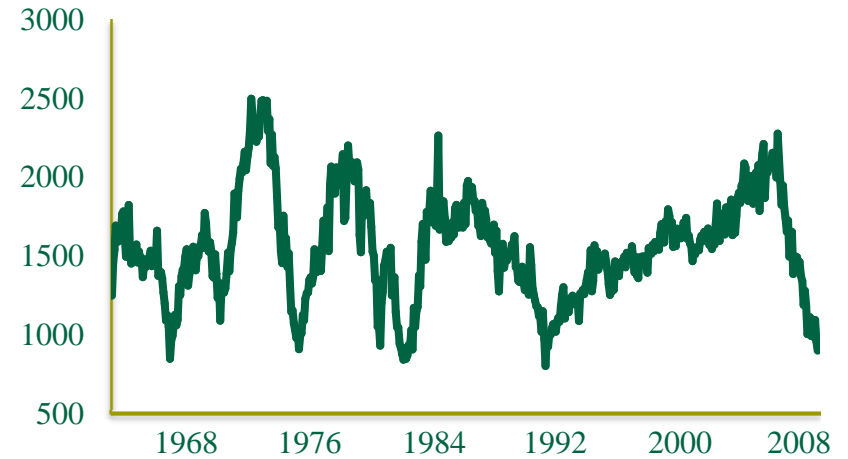


# Outlook — US at an economic bottom?

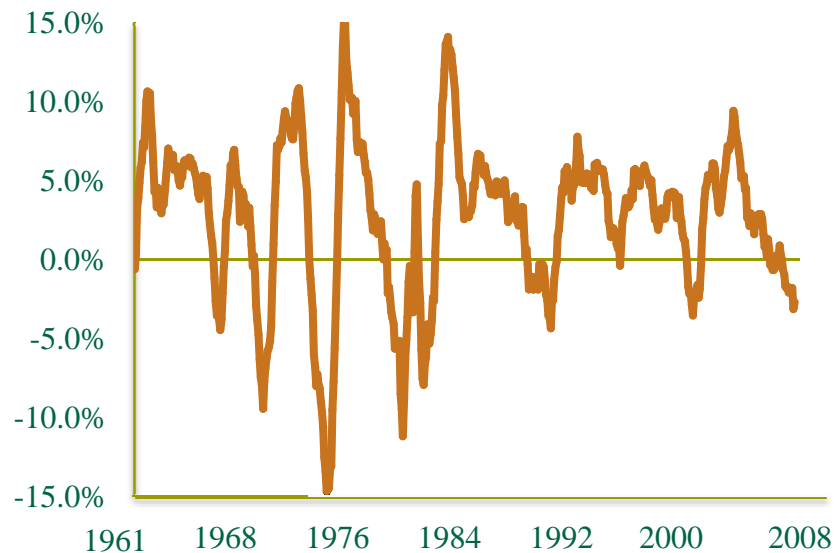
Retail Sales (US New Motor Vehicle)



Housing (US Housing Starts)



US Conference Board Leading Indicator Index (Year over Year Chg)



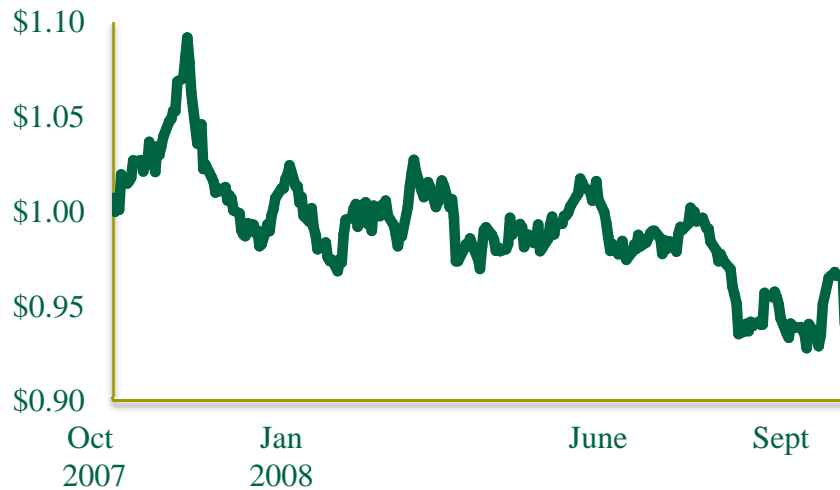
Source:  
Thomson Datastream



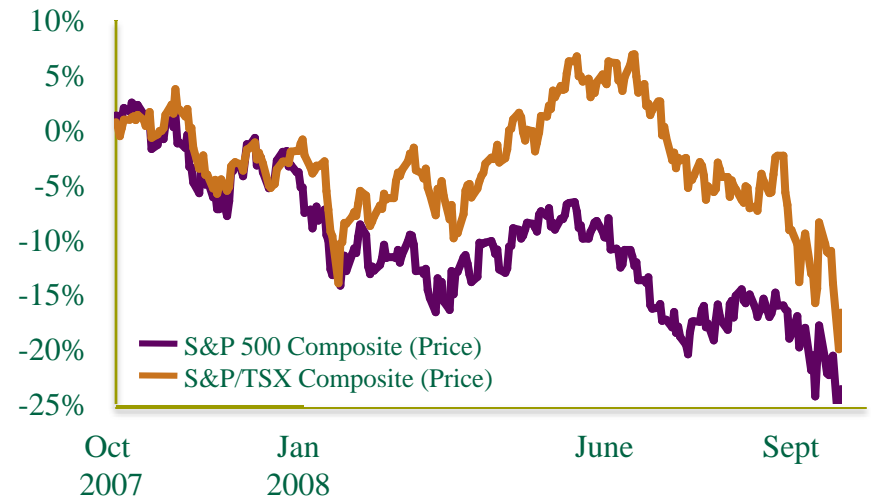
## *Outlook— moderate downturn for Canada*

- Tougher mortgage lending standards
- More solid banking system
- Government surpluses
- Canadian dollar stimulus
- Long-term energy projects

Exchange Rate CAD/USD



Canadian vs US Stocks



Source: Thomson Datastream



# Outlook — what needs to happen?

## Monetary

- Toxic debt out of banks
- Aggressive central bank easing
- Lower consumer/corporate loan rates

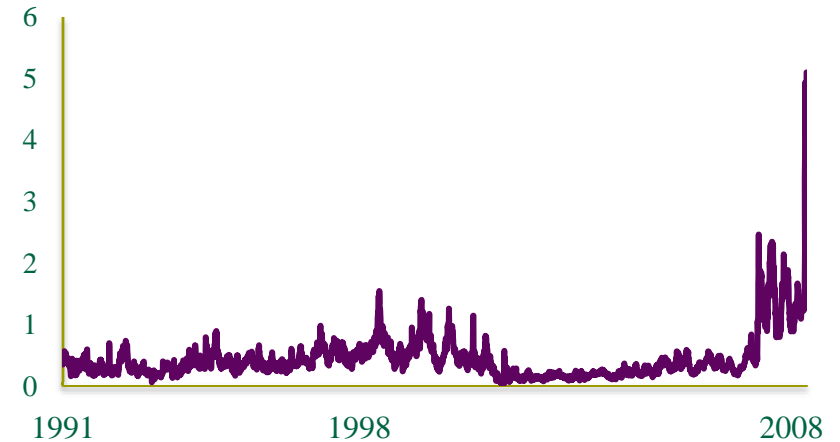
## Economic

- Stabilization of house prices
- Lower inflation
- Fiscal stimulus

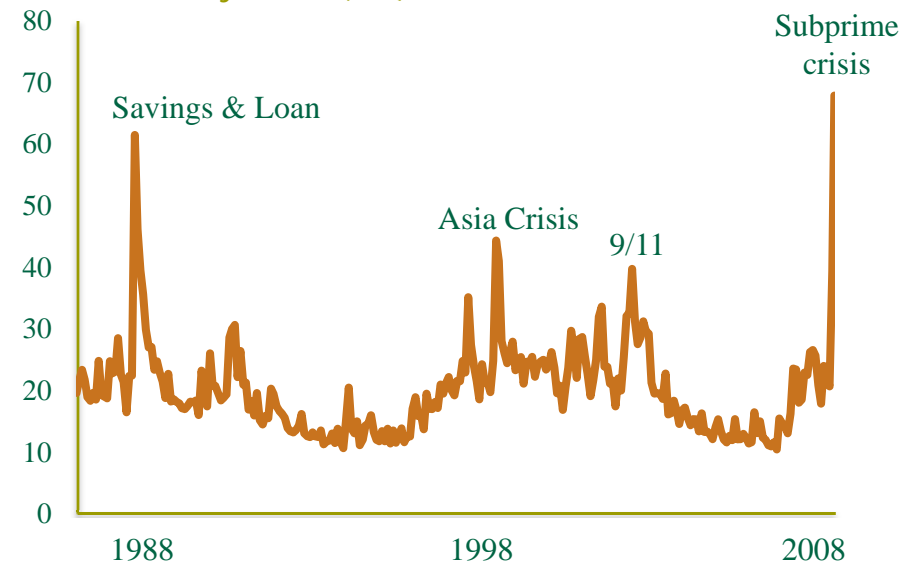
## Market

- Earnings predictability
- Investor confidence

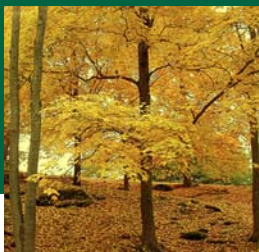
Spread 90 Day Euro vs. 90 Day T-Bills  
(interbank lending rate)



Stock Volatility Index (VIX)

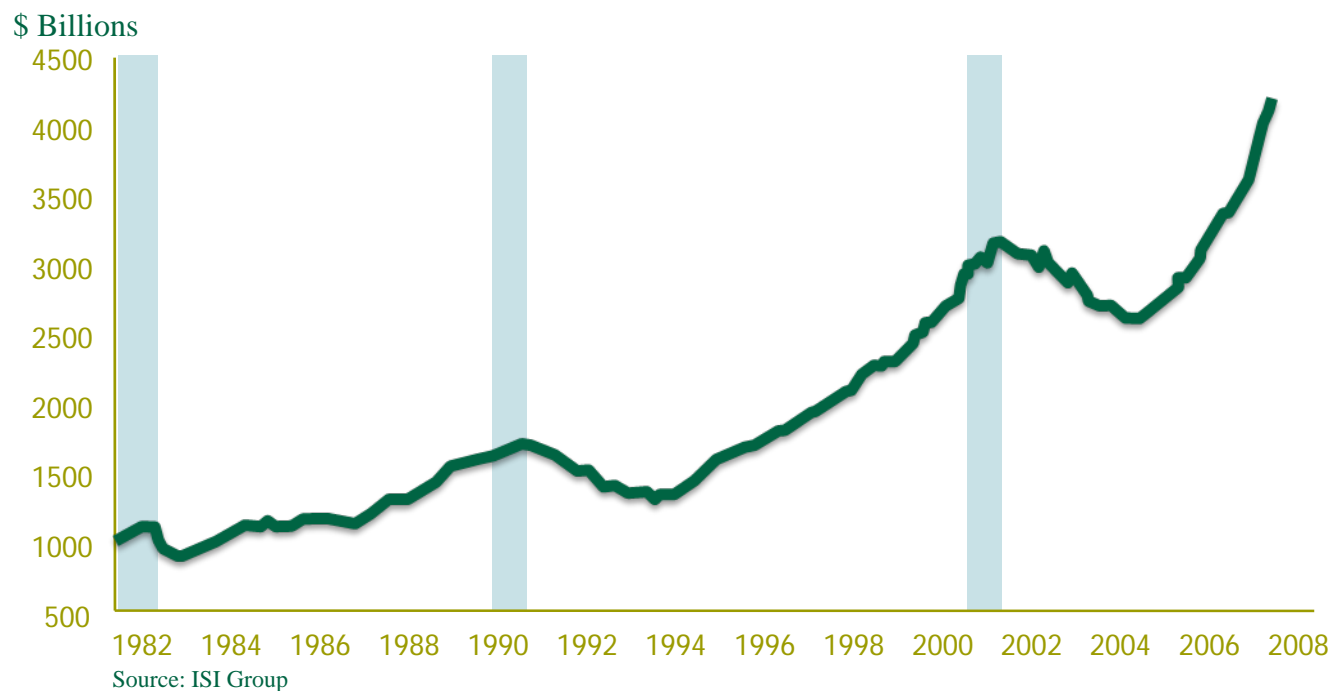


Source: Thomson Datastream



## *Market outlook — liquidity*

Individual and Institutional Cash  
Money Market Funds and Small Cash Deposits



*Up 25% over past year! — available for investment when confidence returns*



## *What's our strategy moving forward? — bonds*

- Maintain corporate exposure
- Reduce term when rates fall

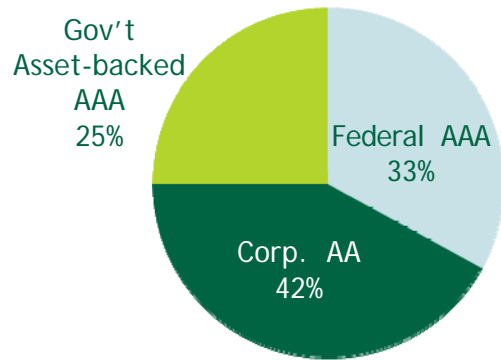
### Advantage of Corporate Bonds

<b>Term to Maturity</b>	<b>Gov't Canada</b>	<b>TD Bank</b>	<b>GMAC</b>
1 Year	2.0%	3.6%	22%
5 Years	2.8%	6.0%	
10 Years	3.0%	6.5%	



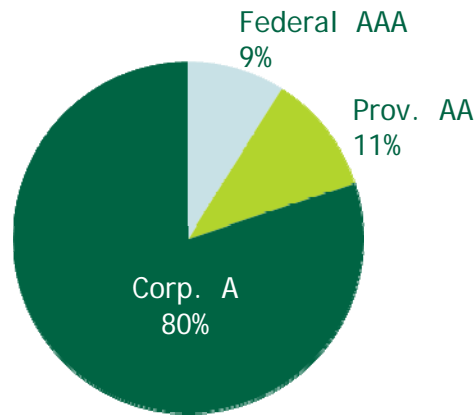
# What's our strategy moving forward? — bonds

## Short-Term



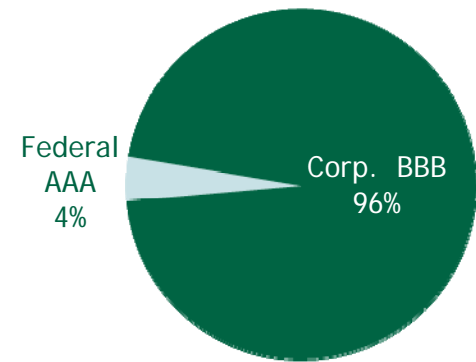
	CC&L	Index
Yield	4.7%	4.0%
Term to Maturity (years)	3	3
Quality	AAA	AA

## Core



	CC&L	Index
Yield	6.4%	4.5%
Term to Maturity (years)	10	9
Quality	AA	AA

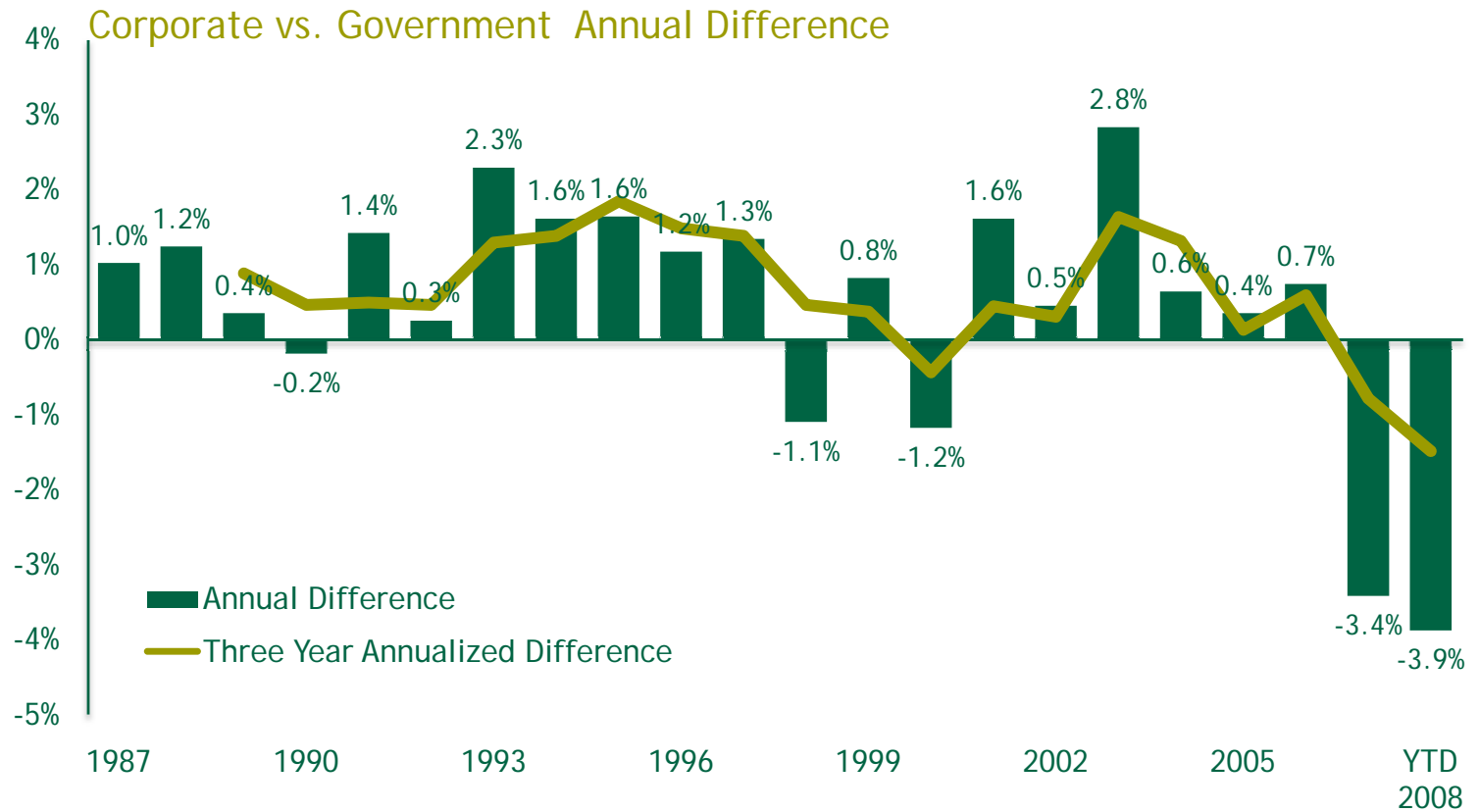
## High Yield



	CC&L
Yield	10.5%
Term to Maturity (years)	7
Quality	BBB+



## *Why hold corporate bonds?*

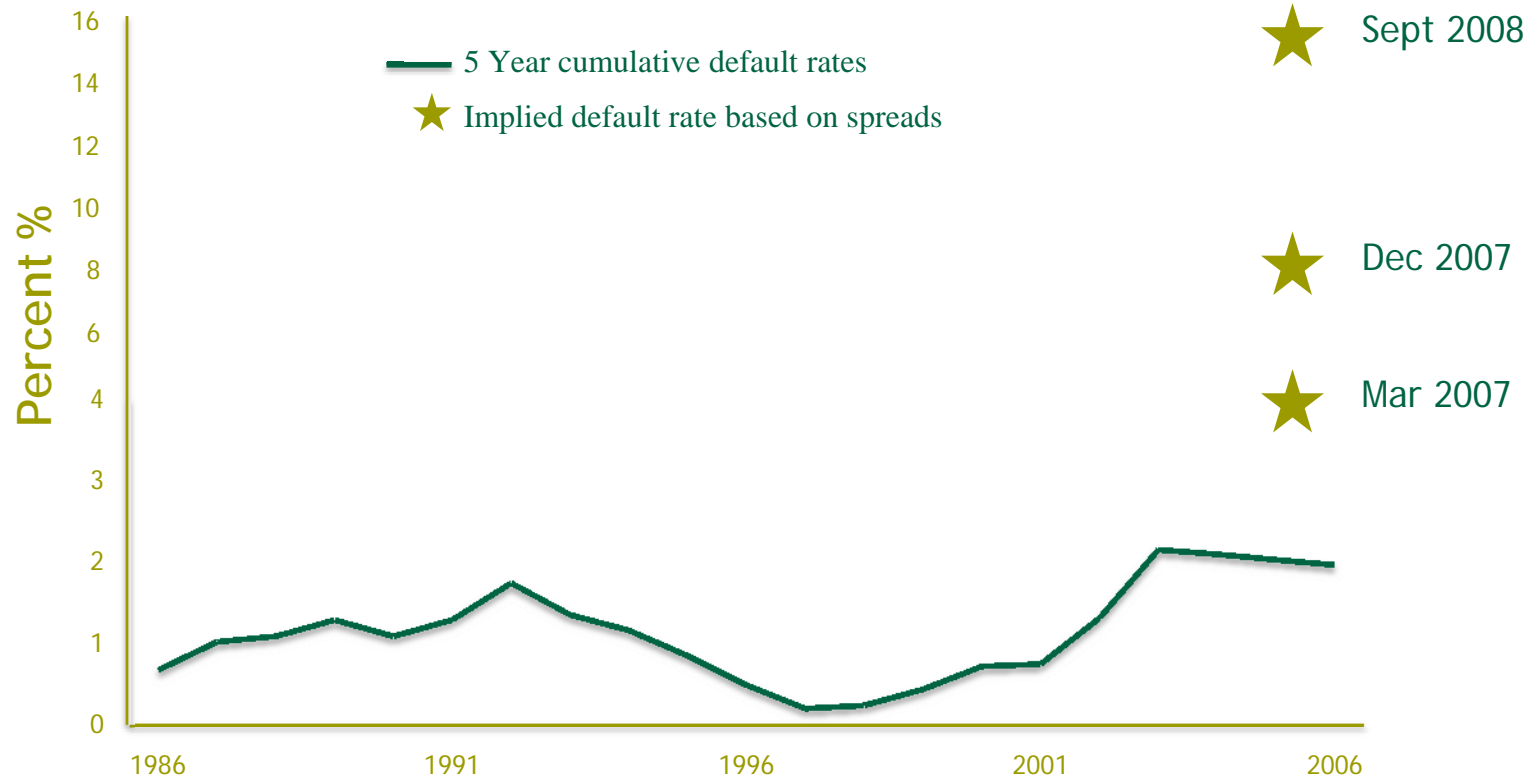


Source: Connor, Clark & Lunn Investment Management Ltd., Scotia Capital

*Has never been greater in 20 years*



## Compensation for Credit is Priced at Extremes



Source: Connor, Clark & Lunn Investment Management Ltd.

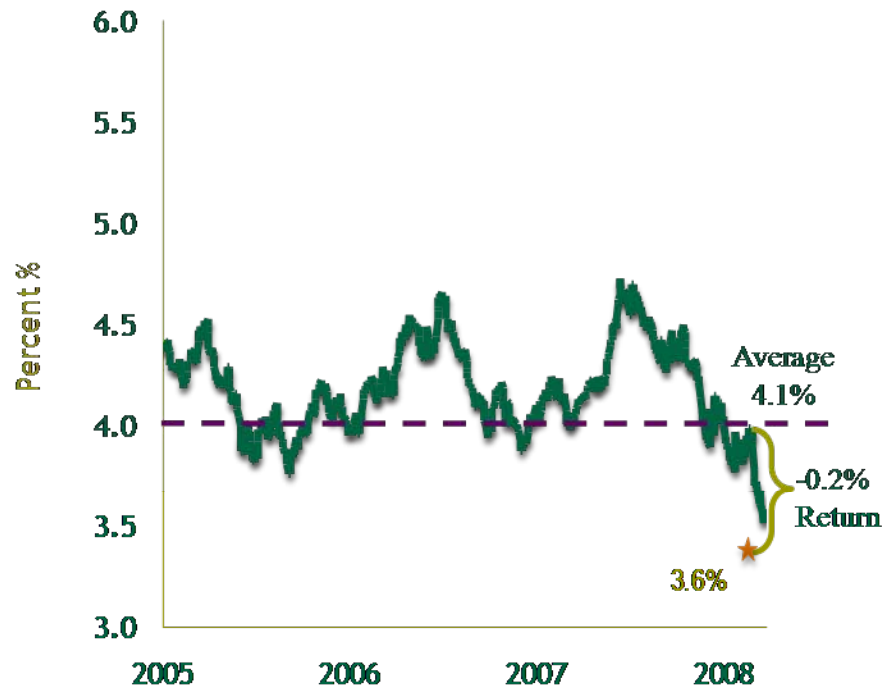
*Market implied default rates have soared – will we see 15% defaults?*



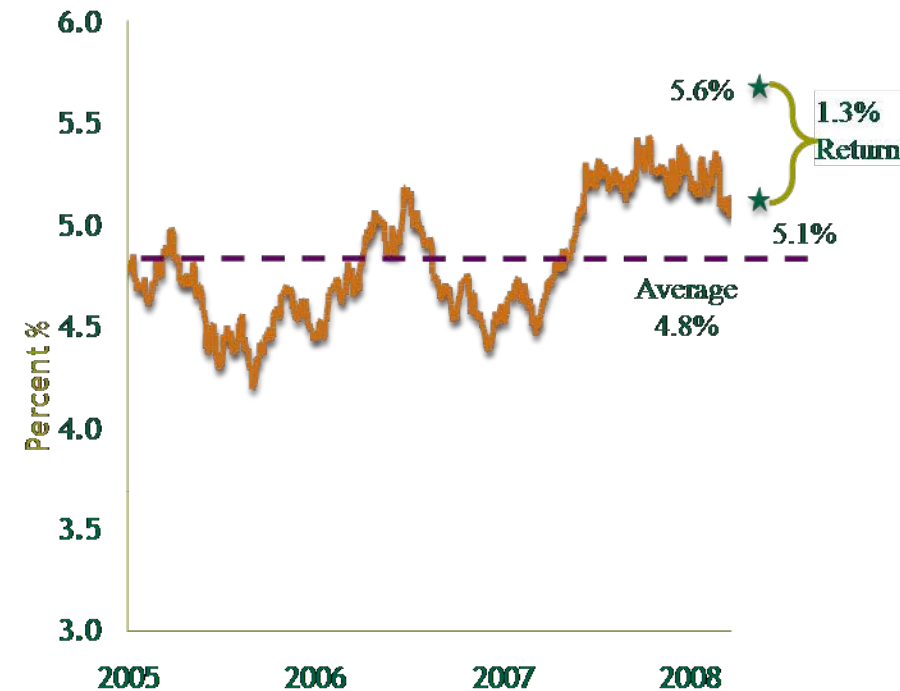
# The Cost of Safety is High

Which bond would you rather own?

Government 10-Year Interest Rate



AA Bank 10-Year Interest Rate



Source: Connor, Clark & Lunn Investment Management Ltd.

- Probability of negative government bond returns is quite high
- A 0.5% increase in rates leads to a 0.2% loss
- A similar 0.5% increase would generate a gain of 1.3%
- If spreads narrow by 0.5%, return +9.0%



# What's our strategy moving forward? — stocks

- Invest in best performers during early stages of financial/economic recovery

Financials

Canadian/US banks

Technology

Research In Motion/Microsoft

Consumer Discretionary

Canadian Tire/Home Depot/Toyota

- Buy companies with best valuations

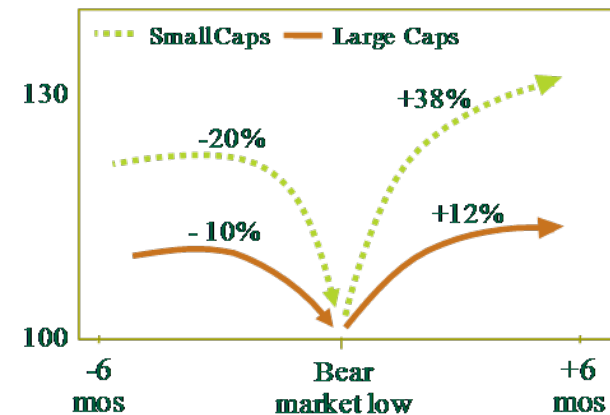
Suncor	Oct 05	Oct 08	P/E Multiples	
			Now	10-yr Avg
Stock price	\$38	\$26 (Oct 15)	Suncor 6.2x	17x
Price of oil	\$65	\$90	CIBC 7.6x	11x
Production	170,000 bls	350,000 bls	Research In Motion 12.1x	25x (5-yr avg)

- Canadian Banks

— Attractive dividend yields

- Small Cap stocks

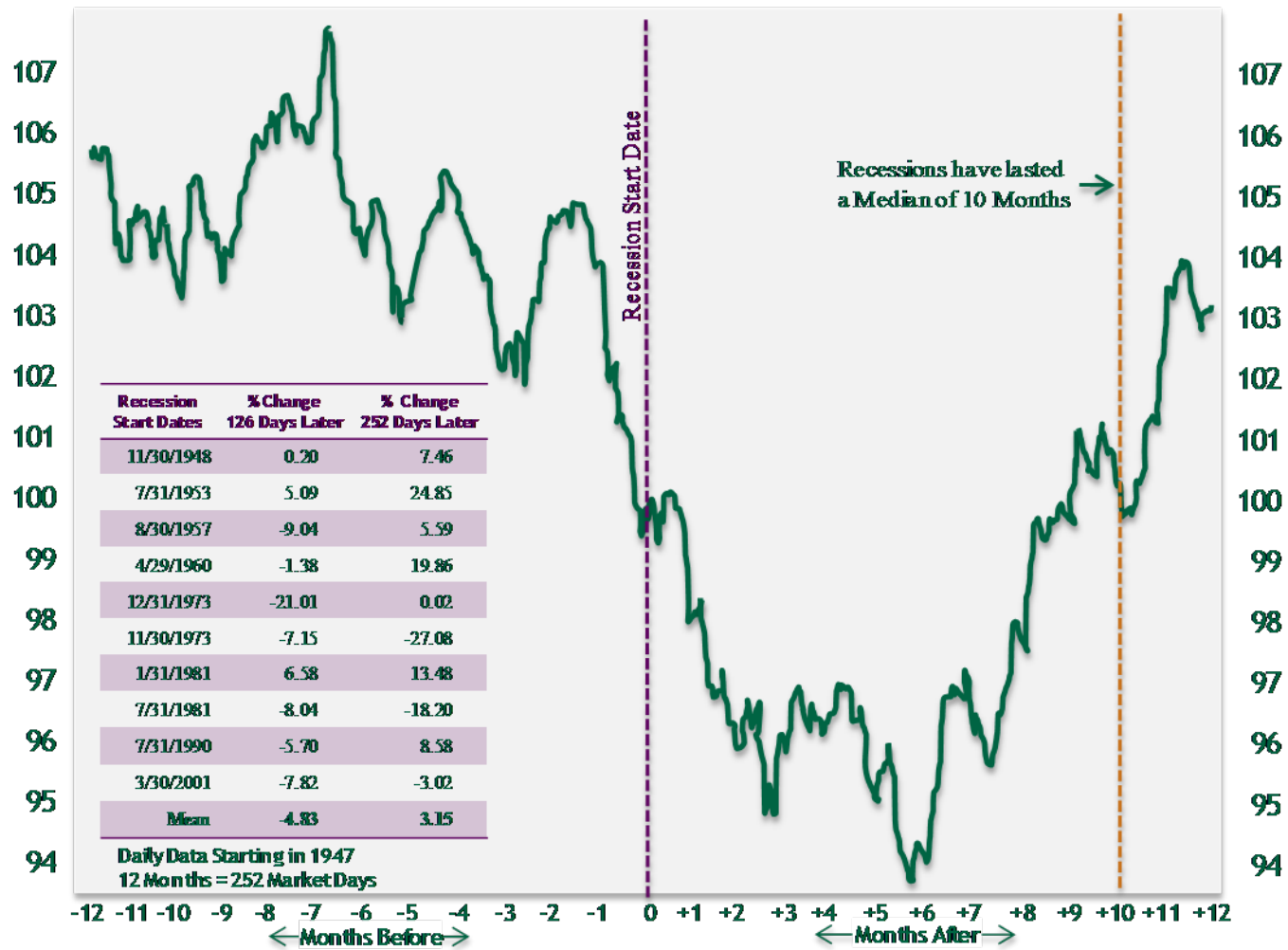
— Lead the way out of bear markets



Source: Ned Davis



# Market bottom?



Average S&P 500 during recession since 1949

Source: Ned Davis

*Stocks rally before end of recession*



# *How long will it take to recover market losses?*

## Approximate Years Needed to Recoup Losses

	Pre-Tax	After-Tax
1. Move to “all cash” position	7	11
2. Move to “conservative” position (25% stocks, 75% bonds)	4	6
3. Maintain balanced portfolio with average return	2	3
4. Maintain balanced portfolio with typical rebound in stocks during first year (30%)	1	2

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### **Assumptions:**

- Cash return 2.5%
- Conservative return 4.0%
- Balanced (55% stocks, 40% bonds, 5% cash) return 7.5%
- 40% tax rate



*“This too shall pass!”*



November 2<sup>nd</sup> 1987

DOW JONES = 2014.09

DOW JONES 10 years later = 7442.08

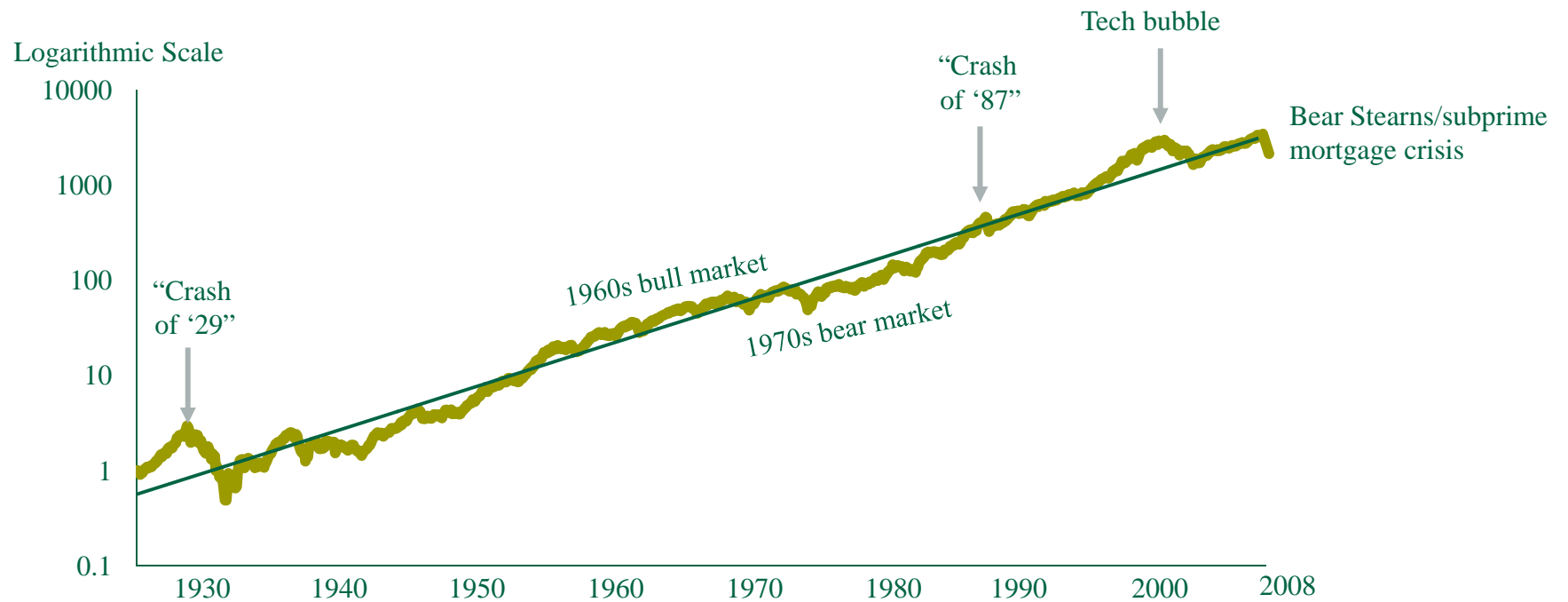
**\$1,000** invested in the Dow Jones on the day this issue hit the stands would have been worth **\$3,695** ten years later

**(more than tripling in 10 years)**

On October 19, 1987 the DJIA declined 508 points to 1,739 or 22.68%. Hong Kong - 45.8%, Australia - 41.8%, Spain - 31%, the UK - 26.4% and Canada - 22.5%. More interesting was that by December 31, 1987 the DJIA closed at 1,939. It took another two years before the market would close above its August 25, 1987 high of 2,722. But it did. Those that read tealeaves said that the potential causes for the decline include program trading, overvaluation, liquidity and market psychology.



# Longer-Term Outlook – stocks



Source: Datastream, Ibbotson

*Will latest crisis be another blip on long-term chart?*