

Why a weak US economy matters.

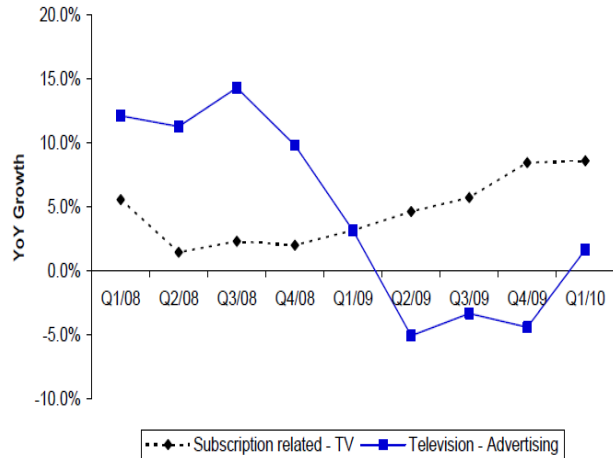
Canada has fared relatively well in this extremely difficult economic environment. Canada did not have to rescue any Canadian Banks like in the US, nor did the Federal Government have to come up with an insane number of programs (e.g. cash for appliances, and TARP) to keep the economy alive.

The US market has a significant effect on our economy. As Canadians know, we export a multitude of products into the US, but we must also remember many of our financial institutions operate in the US. The health of Canadian financial institutions is important since a reduction in credit availability hurts businesses in Canada, especially the small and mid sized businesses. TD Bank, Bank of Montreal, and the Royal Bank all have significant operations in the US. Each has exposure to US consumers and US commercial real estate. Consumers in the US have been plagued by unemployment and rising costs such as gasoline.

Statistics show US debt service payments as a percentage of personal disposable income have been coming down. This can be explained by individuals reducing their debt (saving more), but it is also from individuals having their debt payments reduced through debt restructuring programs and default. US commercial real estate delinquency rates have sky rocketed. Foresight Analytics, a California based real estate Analytics Company, estimates the Q4 2009 delinquency rate is 9.5% up from 5.5% a year ago and under 3% three years ago. We believe these difficulties in the US will hamper the willingness of these three large Canadian financial institutions to lend. Therefore, we still believe credit will be tight and those companies with ample liquidity will continue to perform well.

Inside the Fund

Astral Media Inc. (ACM.A) reported earnings this week for its first quarter of Fiscal 2010. The company is the country's largest broadcaster of English and French specialty and pay television channels. Astral also is the largest radio broadcaster with 82 radio stations in 8 provinces and 8000 advertising faces in Quebec and Ontario. Astral can be used as a barometer for the economy because much of their revenue is generated from advertising. The remainder of their revenue is derived from customer subscription to their channels. Ian Greenberg, Astral's CEO over the last 14 years, indicated advertisers are "more interested in discussing possible promotions. We're [Astral] getting much more incoming calls, they're receptive to new ideas, much more than they were six months ago." As displayed in the following table, Astral has finally seen a positive increase in advertising revenue after 3 quarters of negative growth.



Source: Scotia Capital

We added Astral to the Fund in July 2008, after a sell off from the start of 2008. We bought Astral even though we were starting to witness a decline in the economy and corresponding advertising revenue, and added further on price weakness due to the strength of this franchise.

The Greenberg's, who founded Astral 45 years ago and still hold a substantial amount of stock, have been disciplined. They continue to focus on their core businesses and try to leverage off this platform to introduce new specialty and pay channels and acquire assets when necessary. Astral has been clear they will not buy assets that do not fit into their strategy; therefore, we aren't worried they will buy the assets within the insolvent CanWest.

The franchise is very strong with a national advertising platform allowing companies such as wireless phone providers to make one call to access markets across the country. We like to buy a business such as this because of its entrenched market share and strong competitive positioning.

Astral acquired Standard Radio and its 52 radio stations in 2007 to strengthen their platform. With this deal, they added a substantial amount of debt, but they committed to reduce this debt level slowly each quarter. The strong cash flow this quarter and over the last two years has allowed them to do exactly that. Astral has also begun discussing share buybacks, dividend increases as well as debt repayment.

Astral has proven that even in very difficult markets they will stick to their strategy. In 2009, they paid back over \$100 million in debt, launched a new TV channel, HBO Canada, and continued to expand their number of radio stations. We continue to hold Astral as a top ten weight in the Fund