

A Certain Kind of Attitude

— JASON VINCENT, PFP, TEP, CHIEF OPERATING OFFICER AND VICE PRESIDENT, MULTI-FAMILY OFFICE

Institutional investors, such as pension funds, foundations and endowments, use sophisticated investment strategies to improve long-term results. These strategies generally involve the use of a select group of investment managers chosen with specific objectives such as style, geographic focus and asset class in mind. In addition, institutional investors focus on core and alternative investments.

Similar to institutional investors, we employ all of these tangible investment tools in managing our clients' very individual portfolios. However, there's another equally important facet to successful institutional investing and that's a matter of attitude. Here's what we mean.

Emotion is a key element that can often influence individual investment results. We believe effectively implementing an investment strategy means replacing emotion with discipline and pragmatic decision making. We remove emotion from our programs by adhering to your investment policy that identifies permissible investments and prescribes corresponding allocation guidelines for asset classes and alternative investments.

We also establish appropriate performance benchmarks with measurable criteria. This sets the stage for both transparency and accountability. It provides us with a means of evaluating managers and ensuring underlying investments are meeting long-term objectives.

An institutional attitude is also reflected in how you choose to live with your long-term investment strategy. For instance, do you respond in a knee-jerk fashion to market volatility, consequently damaging a strategically sound long-term plan?

In general terms, we see volatility as providing opportunity. Extensive due diligence on any investment is fundamental to this viewpoint. For example, the recent significant depreciation of gas and broader energy stocks is opening select doors for future gains.

More specifically, when a security, asset class or manager is underperforming, individual investors will often respond with a sell order. Once again, presuming the proper due diligence has been done and the thesis remains intact, institutional investors demonstrate greater patience. This capability is based on a critical understanding of the need for rebalancing a portfolio on an ongoing basis and the value of active investment management.

We regularly rebalance portfolios back to strategic asset allocation targets. Without such steps, portfolios can drift away from the strategic plan and become increasingly concentrated. We've seen this occur as some investors' portfolios have become heavily weighted in the Resource and Financial Services sectors. Unfortunately, the pronounced risk associated with such concentration becomes apparent only when the market moves in the "wrong" direction and performance suffers significantly.

Part of the rebalancing process involves our role as active managers. Some investment managers take a passive, long-term buy and hold position while others, on the opposite end of the spectrum, generate an excessive turnover of stocks. As active managers, we start by working with our market outlook and within a client's strategic policy framework. These two factors are the foundation for proactively managing the asset mix of a portfolio, which in turn produces disciplined and measured security selections.

Given human nature, it's easy to understand how emotion can wreak havoc with one's decision making. However, working with your advisor in applying both the attitude and technical fundamentals of institutional investing can create a distinct emotional and financial advantage, particularly in such volatile times. ■



MATCO FINANCIAL INC.

We are a wealth management office that believes a comprehensive approach to living well with money simply makes sense.

The result is strategies that help you shape what comes next, now and for generations. Strategies that integrate the investment portfolios, trust, estate and tax plans developed exclusively for you. Strategies that can be implemented seamlessly by our group or in concert with your advisors. Finally, consolidated reporting that gives you a comprehensive view of your wealth—raising hidden weaknesses and new opportunities.

This is what we do.

As a private company, we have a personal stake in your success. We believe the most valued relationships are built one-on-one over time. We believe you judge risks and opportunities as much by the people involved as by the numbers on the page.

This is who we are.



Matco Financial Inc.

Making Progress in Questionable Times

— **BILL K. DICKIE, CFA, PRESIDENT AND PORTFOLIO MANAGER**

— **JERRY OLYNUK, LLB, CFP, CFA, VICE PRESIDENT AND PORTFOLIO MANAGER**

In life or business, periods of transition can be challenging. The same holds true for shifts in the markets and economies. Over the past 12 months, we've seen financial markets switch from the smooth sailing of the past several years to current choppy conditions. We expect volatility to prevail until answers to key questions, such as those listed below, emerge and provide clearer direction for investors:

- What's next for the U.S. economy? The U.S. Federal Reserve Board (the Fed) has picked its battle and that's to avoid recession. As soon as the Fed cut interest rates, wholesale and consumer prices jumped in the United States, based on high food and energy costs. However, both the Fed and Washington policymakers are taking a novel approach to dealing with this conundrum. By acknowledging the residual strength in the U.S. economy and focusing on a rate relief plan for homeowners, while increasing liquidity for financial institutions, U.S. officials are signalling a greater sense of urgency to avoiding a major recession.
- Where to from here for the greenback and the loonie? The aggressive upward price movement of the loonie in the fourth quarter put some braking action on the Canadian economy, giving the Bank of Canada room to cut rates by a quarter per cent. As the loonie settles back near parity, we expect the currency to trade in a moderate range as global economic demand, not central bank intervention, will drive our economy in 2008. The greenback's weakness has put the United States in much the same position as Canada in the '90s, forcing Americans to refocus on value-added exports, budgetary restraint and domestic consumption. We don't foresee a recovery in the value of the U.S. dollar until such fiscal imbalances are alleviated.
- How powerful is the new third engine? The global economy is working in uncharted territory as Asia takes its place beside traditional economic powers such as the United States and Europe. Asia's ongoing momentum is already keeping the wind in the sails of economies such as Canada's. The tremendous accumulation of capital in the Middle East and Asia due to the manufacturing-commodity boom is now reversing itself, as foreign companies and governments extend loans to, or purchase, struggling entities such as Financials.
- How do we invest in a truly interconnected world? Throughout 2007, we saw examples that demonstrated how linked markets and economies have become. For instance, look at the worldwide ripple effects of interest rate increases in New Zealand and China earlier in 2007; the far-reaching tentacles of the subprime mortgage issue; and the high correlation rates among markets such as the United States, Europe and Asia. The latter trend is causing new challenges for investors. On the surface, finding room to diversify appears more problematic these days given the trend for U.S., Asian and European markets to move in sync. Here in Canada, three sectors—Energy, Materials and Financial Services—comprise 74% of the market, making it a fairly narrow playing field.



Yet, mine down further and there's considerable divergence among sectors both at home and abroad. In Canada, for instance, Information Technology, which represents 5% of the S&P/TSX Composite Index, was up 48.1% for 2007 while the Financial Services sector, which stands at 30% of the Index, was down approximately 4.6%. Does that mean jumping on technology? Not necessarily, because the story behind that 48% performance is dominated by one company, Research In Motion Limited.

Instead, we're taking full advantage of our multi-manager platform to coordinate our exposure by sector while maintaining traditional diversification across markets, asset classes and manager styles.

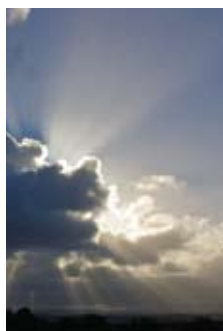
Taking Action

We've maintained our asset mix to address the way things are now, but as importantly, with a longer-term view in mind. You'll see:

- We continue to prefer equities over fixed income due to inflation concerns.
- We remain committed to U.S. equities. Despite the year-end turmoil, we foresee a recovery for U.S. equities in 2008. We intend to take advantage of the current weakness by switching Canadian dollar denominated holdings to U.S. dollar denominated holdings. Going forward, we expect American productivity will be at the heart of the recovery in U.S. stocks.
- We've increased our commitment to International equities on expectations that a U.S. slowdown will have a mild impact on Asian and European companies.
- We continue to overweight Canada. This is based on our view that, without a dramatic interruption, the demand for energy and materials from India and China will be ongoing.

OUR CURRENT INVESTMENT STRATEGY (for the period January 1, 2008 to March 31, 2008)

ASSET CLASS	STRATEGY (LONG-TERM)	TACTIC (SHORT-TERM)	ACTIVE BALANCED PORTFOLIO
Cash	Neutral	Unchanged	0%
Fixed Income	Underweight	Increasing	36%
Canadian Equity	Overweight	Decreasing	36.75%
U.S. Equity	Neutral	Unchanged	12.50%
International Equity	Overweight	Unchanged	14.75%



Reviewing Q4 performance, the Canadian dollar surpassing the \$1.10(U.S.) mark and growing signs of a U.S. recession challenged our market themes and tactics. Our underweight position in Fixed Income undermined performance results for the period as this asset class generated greater returns than International and U.S. equity markets, factoring in the strength of the Canadian dollar. While the Canadian equity market was off 1.9% for the quarter, we're pleased with the stability that our investment in QV Investors Large Cap stocks added to our portfolios. As well, the Bissett All Canadian Focus Fund continued to deliver solid returns through its significant weighting in Materials. Over the past year, the Fund outperformed the overall market by a wide margin.

Looking Ahead

We expect our core managers to continue their underweight views about the Financial Services sector in light of continuing uncertainty in credit markets. Given the ongoing strength in commodities and concerns about inflation, we remain underweight in fixed income. Going forward, we believe four key areas will drive the markets: Oil, Materials, Gold and Agriculture. We've had very good exposure to the first three through the MFi Energy Fund, the Bissett All Canadian Focus Fund and C.F.G. Heward Investment Management, respectively. We're currently exploring avenues that would give us optimal exposure to Agriculture.

We believe this period of transition requires a shift in focus from broader market themes to value-added sector investment decisions. We'll continue to make such calls on an active, ongoing basis until the U.S. economy shows signs of stability. ■

Searching for a Bottom

— MATCO FINANCIAL INC.

Though \$100(U.S.) per barrel oil garnered all the publicity in November, natural gas rose to \$8 per thousand cubic feet and outperformed oil for the month. However, hope for a sustained recovery faded as natural gas finished the year flat. The accompanying drop in business sentiment and asset valuations to all-time lows at year-end left prospective investors wondering whether or not the sector had truly hit bottom. If so, is now the time to invest? We believe there are a number of supply and demand issues in the United States—the primary market for Canadian natural gas producers—that need to be worked through before we see solid footing for the uphill climb. For instance, a December 2007 report by Ross Smith Energy Group identified several factors contributing to depressed gas prices, all of which reflect excess supplies south of the border:¹

- The level of working gas in continental United States storage hit a record at the start of the current heating season, beating the five-year average by 9%.
- “Liquefied natural gas imports to the United States are projected to be up 40% for 2007. This pace is expected to slacken a bit next year, but nonetheless remain robust due to expanding global liquefaction capacity.”
- “Net withdrawals from storage through the first four weeks of the heating season were about double last year’s anemic pace. Nonetheless, with limited fuel switching opportunities and abundant gas in storage, Henry Hub prices remain firmly grounded while West Texas Intermediate continues its high-wire act.”
- Drilling in the United States continues at a hectic pace. The gas-directed share of drilling effort has been about 80% or higher for the past nine years.

Here at home, changes announced under the Alberta Royalty Review mean that companies will likely delay to 2009 those prospective gas projects that were favourably affected by the new regime, further reducing drilling activity.

Under these conditions, balance sheet strength will be the key to survival for Canadian natural gas producers. Our holdings in the MFi Energy Fund reflect this view. Companies such as EnCana and Canadian Natural Resources Ltd. have already adjusted capital spending or made major acquisitions outside Alberta to deal with uncertain gas prices. Our intermediate players such as Bonavista Energy Trust Ltd. and Duvernay Oil Corp. are in a good position to make strategic acquisitions of properties and competitors. While the distributions of gas-weighted trusts are under pressure, we have positioned Daylight Resources Trust Ltd. and Progress Energy Trust as potential merger and acquisition candidates in the Fund due to their attractive net asset valuations. Whether or not the sector truly has hit bottom, focusing on relative valuations is a prudent first step. We believe upward progress for Canadian natural gas producers will depend upon a fundamental recovery in North American gas prices. ■



¹ “Not-So-Great Expectations,” *The Energy Investment Handbook: The Natural Edge*, Ross Smith Energy Group, December 2007.

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