

Third Quarter 2011

CLIENT UPDATE

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Volatility over the past few months has certainly been gut-wrenching. In August, stock markets around the world more or less crashed. After churning in a choppy and violent trading range for most of September, stocks swooned to new lows on October 4, only to reverse course sharply in the final half hour of trading. Nine days later, the S&P 500 rallied 14%¹, a record month with a backdrop predominated with bad news.

Markets have always been known to be manic depressive, but over the past few months it just seems that emotion has completely taken over the market. On any given day the stock markets around the world can swing several percent based on a rumor, a flimsy blog or some statement by a central banker.

The cycle goes something like this; fear of "return of capital", is replaced by the fear of an "inadequate return" on capital, then replaced by a fear of missing the upside "growth potential" of capital, over and over and over again.

"Men, it has been said, think in herds; it will be seen that they go mad in herds, while they only recover their senses slowly and one by one"

- Charles Mackay, *Extraordinary Popular Delusions and the Madness of Crowds*

As crazy as this kind of trading activity is, it was to be expected. Public opinion is no substitute for thought and I continue to consult world experts so I can provide you with rational thought during uncertain times. Please call to discuss, or refer to my most recent client letters, also available on luckfinancialgroup.com, with specific reference to my expectations for volatility following a period ***of creative destruction, the ensuing reconstruction*** and a rough ride due to this being the most ***non-linear recovery*** ever recorded.

Six months ago we advised clients to be patient, like a baseball player waiting for the perfect pitch. Despite all the activity, the market is basically unchanged in 2011, in fact the S&P 500 is at the same level it was on December 1998! Interest rates are much lower and valuations are much cheaper today than they were thirteen years ago. Perseverance, patience and discipline will payoff, and it is time to think about swinging the bat.

Continuation of investment themes:

- With interest rates close to zero, short term bonds and cash earn nothing. They provide a very false sense of security – in real terms, inflation adjusted, most fixed income investments are actually losing propositions over the mid to longer term. As a cash substitute, consider our CDIC

¹ Calculated using the Low Price for October 4, 2011 and Close Price on October 14, 2011.
<https://ca.finance.yahoo.com/quote/%5EGSPC/history?p=%5EGSPC>

insured 1.2% yielding high interest savings account, or our 2.8% yielding short term income account.

- Even with a backdrop of economic weakness and more political uncertainty, equity markets continue to be dominated by rising dividends and share buybacks, provide investment returns in the absence of economic growth.
- With fixed income portfolios, avoid longer dated government issues and safeguard against inflation. Diversify into high quality corporate issues that reward investors with higher yields and comparatively less risk.
- As a fixed income alternative, high yield, blue chip equity is the low-hanging fruit recommended to generate predictable returns and a high degree of inflation protected income ahead of any economic recovery. Canadian banks and utilities still provide yields of 4% to 5%. With yields so low, both individuals and institutions require safe income, and high yields can support (and appreciate) their prices.
- Going against the grain, patience and contrarian thinking will finally reward investors. History has proven that you can't do well by investing in what is popular; in fact, history has proven that the most popular investments have the most risk and least potential for return. An all time record \$1.25 Trillion has migrated from equity to bonds since 2007. The last time we saw such extremes was 1998, money poured into tech stocks like Nortel, and we know how well that worked out.

As always, feel free to call and speak with me or any member of our team with questions that you would like answered, or for clarification on any of the points I've discussed. We appreciate the trust and confidence that you've placed in us which allows our relationship to work. Please contact us to arrange a convenient time to discuss your investments and update your overall financial plan.

Allow us to exceed your expectations in delivering the *Peace of Mind Experience*.

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P.S. Update: I am very pleased to report that our team is growing!

* Rhonda Middleton is currently off on a maternity leave, returning mid 2012. September 7th, 2011, Rhonda gave birth to baby boy, 9 ½ pound Carsen Middleton. Mom, dad and baby are all healthy and doing well. Covering for Rhonda and doing an excellent job in relief, is **Stephanie Senteris**. Please join me in congratulating Rhonda, and welcoming Stephanie to the Luck Financial Group.

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