

The Ransby Report

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The Markets

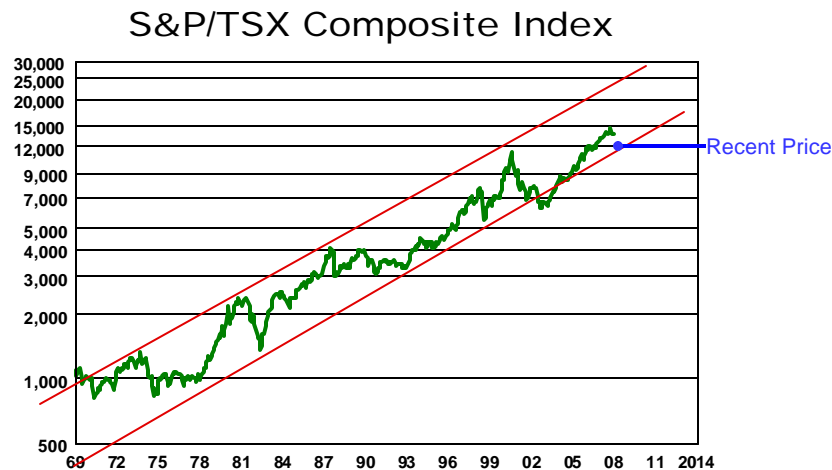
Since the beginning of the year, the equity markets globally have been severely battered as investors continue to be concerned with the financial and economic impact associated with the sub-prime credit crisis, especially in the United States. Despite assurances from central policy makers, many observers now expect the United States to slip into recession along with noticeable economic slowdowns in many other countries in the world. As a consequence of these concerns, global equity markets have fallen 10 per cent or more since year-end, one of the worst monthly performances in many years.

In order to bolster the United States economy and improve investor and consumer confidence, the Federal Reserve Board has just announced a 75 basis point cut in the fed funds rate as well as in its discount rate. The Bank of Canada also cut its key overnight rate, but only by 25 basis points. While these moves should not be looked on as a “quick-fix” because the credit problems will take some time to heal, they nonetheless should help to strengthen confidence on the part of investors. One of the biggest concerns of investors in recent weeks has been a view that the Federal Reserve Board in the United States has not understood the full extent of the credit problems, and has been too timid in its response. This just announced action should hopefully improve investor perception as well as begin to stabilize the economy.

What should investors do? We continue to view the long-term outlook as quite positive as we have discussed in the past. However, the markets, no doubt, will remain extremely volatile over the next few months. For this reason we strongly suggest that investors exercise discipline and patience, and keep focused on the positive long term picture.

A Perspective

From time-to-time we have presented an extremely long-term chart of the S&P/TSX Composite Index as one means of assessing market risk and potential upside. The chart, shown below, is semi-logarithmic; that is, similar percentage changes in price anywhere on the chart represent the same vertical distance. In other words, if the Index moves from 4000 to 6000 (or 50 per cent), the vertical distance would be the same as if the Index rose from 6000 to 9000 (also 50 per cent). In effect, the slope of any line on the chart represents the growth rate.



As you can see, the Index which is shown back to the 1960's, has been in this upwardly sloping channel virtually for the entire period. Coincidentally, the slope of this channel corresponds to a long-term return near 10.5 per cent, which is the long-term total return (including dividends reinvested) for the S&P/TSX. And keep in mind the "news" background during this lengthy period – booms, recessions, inflation fluctuating between 1 and 12 per cent, interest rates moving between 2 and 22 per cent, wars, political uncertainty etc. Despite all these "ups and "downs", equities still returned on average approximately 10.5 per cent.

Where are we today? With its recent weakness near 12,000, the S&P/TSX was nearing the bottom of the channel. This suggests first, that on an historical basis, the problems which the market is perceived to be facing today are becoming discounted even as stocks appear to be more risky. If stocks only trade near the bottom of the channel during the next few years, the total rate of return would still be close to 10.5 per cent. Remember that its upward slope together with dividends reinvested corresponds to that rate of return.

Secondly, if we wanted to be even more bullish longer-term, one only has to look at three previous periods on the chart; the '70's, '80's and '90's. During those periods stocks were the investment of choice, and the TSX, graphically, crossed the channel in a "north-easterly" direction over a period of several years. Because the movement of the TSX was much steeper across the channel, the rate of return for the Index was even greater – actually healthy double-digits. We continue to believe that such a move from the bottom to the top of the channel would be a reasonable expectation for the market over the next number of years.

Editor's Note

As indicated in the previous issue, this marks the final Ransby Report as I shall be retiring from GWLIM and Great-West Life in the near future. After more than four decades in the investment business, almost 34 years with GWLIM/GWL, and more than a decade producing The Ransby Report, I believe it is time to "hang up the spurs".

I have thoroughly enjoyed my investment career, and especially all the friendships and professional relationships which I have made through the years. I am particularly grateful for my long tenure at GWLIM/GWL, and for the colleagues, past and present, with whom I have been associated. Last, but not least, I want to thank all our advisors and clients for their business as well as for their interest in The Ransby Report. It has been a long and wonderful ride for which I am most grateful.

As for the future, I believe GWLIM is well positioned to generate excellent fund returns in the future. In place of The Ransby Report, GWLIM plans to launch a new investment publication which you should receive in the near future.

In closing, I again would like to thank you for your ongoing investments in our funds, and for your interest in The Ransby Report. All the best, and may your future returns surpass your expectations!

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