

December 2009

Against a deflationary backdrop in the United States, and in the world, of faltering employment, of contracting bank loans, of failing banks, (to say nothing of the failings of ambitious Gulf States), and of slipping house prices (US), the authorities continue to push inflationary and expansionary measures.

Washington has priced money at near zero rates, has let the greenback slip, has piled on more spending – cash for appliances and more troops for Afghanistan, and has extended safety net measures for their banking system. Canada follows suit, more or less. Perhaps in our society, run by elected authorities, the idea of a period of rest and recovery, of savings and thrift, may not be entertained as normal.

The liberal measures have been so large down south as to move the growth in GDP into positive territory.

However, consumers and US corporations are acting sensibly. They are saving. They are liquidating their excessive debt. Household debt including mortgage debt and consumer credit contracted at an annualized rate of 2.6%, in the third quarter, the fifth consecutive decline on record. Business liabilities dropped at about the same rate. The negative changes in debt are a first in the post war period, a first since 1947. The savings spree and prudent pause slows the pace of business and demand.

To avoid the slowdown, we have the supportive actions by governments. We have intentional, international government policies counterbalancing growing fiscal prudence and necessary new frugality on the part of consumers. Our governments have implemented massive borrowings (up 20.6% annualized US) and spending schemes to mitigate the business downturn brought about by the new thrift.

Government spending is finite, as you know from the strictures placed on Iceland, Ireland, now Greece, and Dubai. We also are aware of the growing suspicion over the United Kingdom's policies and financial position. Government borrowing and spending for current consumption is no road to sustainable prosperity.

This observation plus the valuations placed by investors on equities in anticipation of a sustainable recovery still makes us wary of aggressive equity commitments. The S&P 500 Index trades at 86.2 times trailing earnings, a 2.0% dividend yield and at 2.5 times book value. These numbers are hardly bargain basement knowing the underlying book value has dropped by 15% in the past year, a result of write-offs exceeding earnings.

Equally, the bond markets have been strong and the appetite for new bond issues here and in the US appears almost insatiable. While QV did not take advantage of the acceleration in the more aggressive

Pooled Fund – Month End Unit Values[^]

Unit Values	Sep-09 [*]	Oct-09	Nov-09
Cdn Income Fund CI D	10.74	10.75	10.89
Cdn Balanced CI A	13.40	13.24	13.57
Cdn Equity Fund CI A	9.09	8.90	9.21
Cdn Small Cap CI A	18.77	18.97	19.32
Global Equity Fund CI A	8.07	8.00	8.04

[^] Fund NAVs reflect "full-fee" class * Post distribution

equities this year, we did participate fully in the bully bond markets and our asset mix is more oriented to bonds compared to our peers.

Recent bond issues have been snapped up with the gay abandon of initial public offerings of technology and media companies in 1999 or mineral issues in 2007.

At times what appears to be a secure course of fixed income investing, may carry the same risks we find in super-heated equity markets, which may lead you to the conclusion that QV is in a dilemma. And we would allow we are always in a dilemma, except we always err on the security of the better valuation, the lower risk and the more sustainable expectation.

The bond market has appreciated and enjoyed the benefits of zero rate policies, and may do so for some time if we listen to the central bank heads of Canada and the US. We will hold our bonds, but we will be calculating the long-term advantage to increasing the positions in some of the some of the better valued, dividend paying Canadian companies in the portfolio.

Total Return – Capital Gains plus Income (%)

To Nov 30 '09	1 Mo	3 Mo	1Yr	3 Yr	5 Yr	10 Yr
QV Pooled	%	%	%	%	%	%
Cdn. Income	1.4	2.0	8.9	5.9	5.6	5.5 [^]
Cdn. Balanced	2.5	3.8	14.1	3.2	6.4	10.3
Cdn. Equity [*]	3.5	5.6	11.9	0.2	8.6	15.8
Cdn. Small Cap	2.0	10.6	31.1	0.1	8.0	16.1
Global Equity	0.9	3.0	5.1	-	-	-

^{*}Historic equity returns from the Cdn. Balanced Fund

^{*} 7yr

Benchmarks:

	1.3	2.2	10.0	5.4	5.8	6.8
DEX Bond Univ.	1.3	2.2	10.0	5.4	5.8	6.8
Balanced Fund	2.9	3.7	16.8	2.3	6.9	6.7
S&P/TSX Comp	5.2	6.1	27.8	-0.7	7.6	6.5
BMO Small unwt'd	5.5	18.6	95.8	-2.7	3.8	7.2
MSCI World (SCA)	1.9	2.1	10.0	-9.9	-2.0	-4.6

- Pooled fund returns are gross of management and custodial fees. Returns over one year are annualized.

- The Balanced Fund Index reflects the total rates of return earned by the DEX 91-Day T-Bill Index (5%), the DEX Bond Universe (45%), the S&P/TSX Composite Index (40%), and the MSCI World Index (CS) (10%)