

Fall - 2006



September 30, 2006

Dear Clients,

The third quarter marked the beginning of a major cyclical move out of the resource sector and into consumer staples, biopharma and technology. US growth rates are slowing down primarily because of the significant decline in real estate activity. High gasoline prices have motivated consumers to look for more fuel efficient transportation and away from the Big 3's gas guzzling SUV's. The drop-off in consumer spending for big ticket items – ie: cars and houses – will be felt throughout the US economy and probably, the world.

The growth “slowdown” is having a dramatic effect on the price of resources, namely oil and gas, and industrial commodities. The physical supply and demand equation and price adjustments are being amplified by the huge amounts of speculative capital that have flowed into the commodity markets. As the economists would say, the price “signals” are being confused and amplified by the sheer size of the speculative capital flows. The demise of Amaranth Advisors, LLC hedge fund is “prima facie” evidence of the effect speculators can have on commodity prices and markets.

By maintaining larger cash reserves and a very small weighting in energy, we have been able to avoid most of the decline in the TSX index, off 3% in the quarter ending September 30th. Making money has proved to be more difficult. The NASDAQ market has revived but with large, daily swings, it has been difficult to stay invested.

My US focus has been on the biopharma and health care products. Most analysts suggest that any future “blockbuster” drugs will migrate from the biotech sector. Picking the winners out of a large field is not easy. The vagaries of the Federal Drug Administration (FDA), in the US make investing in this sector a political as well as an investment decision.

I have continued to avoid the traditional bond markets as the yield on Government of Canada 10 year bonds approached a paltry 4%. With inflation at 2-2.5% only a wide-eyed optimist would be buying bonds at these levels.

The portfolio has grown rapidly to approach the \$50million mark. Getting the asset mix right is a difficult decision, accomplishing this with the added unpredictability of weekly cash inflows makes the task that much more difficult.

My first task has been to make the portfolio as “bullet-proof” as possible. Comparing the portfolio’s first 6 months performance to the TSX index, it appears that we have been successful. Growing the portfolio’s Net Asset Value (NAV) in such a volatile market has proven to be more difficult. By sticking with quality names and keeping the resource sector exposure to a minimum the portfolio is well placed to grow in the 4th quarter of 2006.

Sincerely,

Stephen D. Barlow