SECOND QUARTER LETTER 2008

After a brief rebound in April, world stock markets continued to decline on the back of recession fears and the continuing massive write-downs at global banks, brokers and insurance companies. Additionally, the world is plagued by plunging real estate prices, eroding consumer confidence, the rising spectre of stagflation, a toxic combination of increasing commodity prices (particularly energy and food) and slower growth. In fact, as the prices of oil, gas and food rise, the consumer has less funds available for other purchases, which in turn places more pressure on the economy. American consumers have also been discouraged by the fact that they have lost much of the equity previously held in the value of their homes.

The Dow Jones has declined 14.4% year-to-date, representing the worst first six month performance since 1970. The S&P 500 and the NASDAQ are down 12.8% and 13.6% respectively. European markets have faired even worse with the MSCI Europe down 18.9% this year. Most emerging markets have also corrected sharply, led by China's Shanghai Index which is down an eye-popping 49.6%. Closer to home, Canada's TSX was still positive as of June 30 due primarily to energy and materials. However, at the time of this writing the TSX is also well into negative territory.

Our portfolios drifted slightly lower during the quarter but continued to out-perform most of the relevant benchmarks. In fact, we had more than our share of winners during the quarter which helped mitigate the broader decline, including Canadian Oil Sands +32%, Denison Mines +38%, Dover Industries +27%, Gemcom +26%, and Neo Materials +15%.

The merits of our style of emphasizing value investing are certainly being tested these days. To put it all into perspective, the two leading value investors of the U.S. and Canada respectively, Warren Buffet and Irwin Michaels, are both down about 30% during the past year. Of course, this is not the first time value investing has fallen out of favor. During the .com boom of the late 90's value stocks were much more neglected than they are today. Nevertheless, our strategy remains intact, as we totally agree with something we read recently from CIBC: "*… there is one characteristic value gurus proclaim is a prerequisite for this style to work: patience. As happened before, while value investing can fall out of favor, when it returns, it comes back with a vengeance*".

Our view is that world markets are in for some sustained turbulence as the domino effect spreads from the US subprime fall-out to prime mortgages, credit card debt, car loans, commercial real estate and corporate lending, in combination with a bias towards tightening monetary policy by central banks to counteract inflationary pressures. Certain commodity prices have run-up due to legitimate supply and demand imbalances as well as speculation that prices will rise further, and as a hedge to inflation and a declining US dollar. Those who thought that emerging market economies had decoupled from the US consumer are beginning to realize that this may not quite be the case, and that raging fuel and food prices are also having a negative impact on other countries such as China.

While Canada is certainly not immune to these macro headwinds, we are lucky enough to have plenty of vital resources (food, water, energy, metals, fertilizer), and this should at least keep the western part of our economy buoyant and Canada a favored place to invest in for decades to come. Many of our less well known core holdings continue to benefit from western based activities, including Glacier Media (community newspapers and trade magazines), Vicwest (agricultural and energy storage products), and Viterra (grain handling). Others continue to grow from infrastructure spending such as Stella Jones (rail ties and utility poles), Velan (nuclear and petrochemical valves), and Logistec (cargo handling and water pipe repair), or from the proliferation of new technologies worldwide such as Neo Materials (high performance engineered materials), Mosaid/Wi-Lan (semi-conductor and wireless patent licensing) and Nstein (digital content management).

Finally, in regards to how to deal with one's investment portfolio in turbulent times, we refer again to one of the greatest investors ever, Warren Buffett: "*Occasional outbreaks of those two super-contagious diseases, fear and greed, will forever occur in the investment community. The timing of these epidemics is equally unpredictable, both as to duration and degree. Therefore we never try to anticipate the arrival or departure of either. We simply attempt to be fearful when others are greedy and to be greedy only when others are fearful".*

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