Quadrant
ASSET MANAGEMENT

QAM Update
April 2011

The QAM update that highlights recent developments that we think either affect the markets or are important to understanding them.

"No matter how serene today may be, tomorrow is always uncertain" - 2010 Warren Buffet letter to the Shareholders of Berkshire Hathaway Inc.

In the first few months of this year, the world experienced an incredible number of natural and geopolitical events, of which each event alone could have negatively impacted the capital markets.

The disaster in Japan brought with it incalculable human costs and the nuclear risks that are still being dealt with. Lives lost and human suffering as a consequence of the tsunami will mark the life of too many people for years, if not decades.

The uprisings in the Middle East are creating uncertainty in oil supply as well as concerns over the transition of power in those countries.

On top of all of this, we are coming out of a global crisis with many developed countries floundering in a sea of debt (and possible default), high unemployment and the housing market (in the U.S.) still depressed.

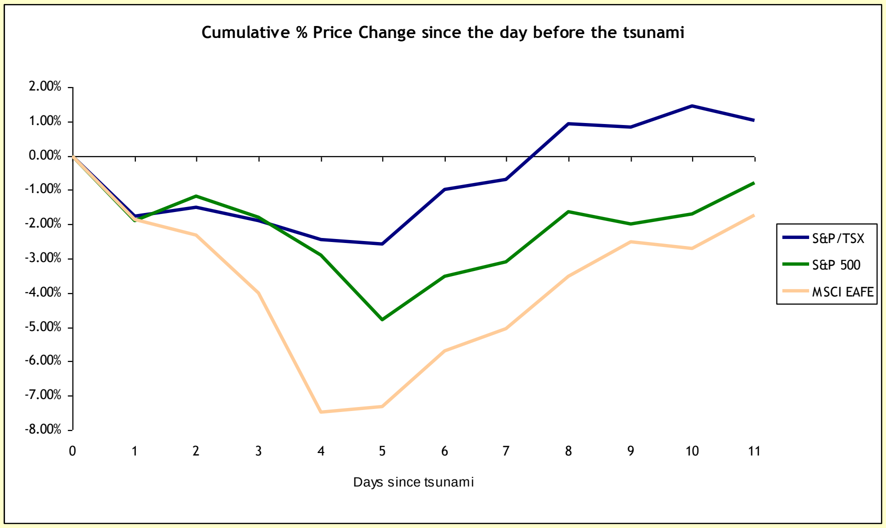
We, as money managers and advisors, have an obligation to our clients to monitor and consider, to the best of our knowledge and experience, what the financial impact of these types of events will bring for investors. Quadrant has looked at a myriad of fundamentals and observes that the capital markets, and in particular Corporate North America, are in pretty good shape.

In the days following the earthquake and tsunami in Japan we witnessed, predictably, the Media doing another very good job at confusing the general population and inciting the doctrine of fear. From an investor perspective we must remember that spread of irrational fear has been historically the single best reason to buy stocks, not sell them.

The economic reality is that more than $200 billion will be poured into the Japanese economy and that nation will rebuild itself. As investors, we deal with natural disasters every year. More often than not those disasters turn into an economic stimulus for the region and demand for goods for the global economy. Stock markets typically shrug off these negative events, recoup losses and move on.

This graph shows the reaction of major stock indices in the days following the tragic event in Japan on March 11, 2011.

We are not surprised by this chart. A few hours after the nuclear crisis in Japan became public we analyzed a graph that plotted the reaction of stock markets to previous accidents at nuclear plants: It follows the exact same pattern in all previous accidents. In fact, this is true for most recoveries from one-time events.



Q1 2011 Market Recap

Fixed Income

Fixed income produced negative returns in both Canadian and international fixed income markets. Canadian bonds, as represented by the DEX Universe bond index lost 0.3% while international bonds as represented the Citigroup World Government Bond index lost 2.1% (in Canadian dollars).

The outlook for bonds is problematic. The end of QE2 (quantitative easing) this summer will dry up the largest single source of demand for US Treasuries. PIMCO, the world's largest fixed income manager, officially abandoned U.S. Treasuries completely. Furthermore PIMCO started to “short” the US debt. The United States' massive deficit has caused Standard & Poor's Ratings Service to lower its long-term outlook to "negative" for the first time in history.

Quadrant and its managers continue to address the fixed income concerns through reducing duration and seeking opportunities to increase yield without significantly increasing risk.

Canadian Equities

Canadian large cap stocks outperformed small cap stocks during the quarter. The S&P/TSX rose 5.6% compared with the BMO Small Cap (Weighted) index which returned 3.7%. Top performing sectors in the S&P/TSX were Energy, Financials, Healthcare and Industrials. With a large valuation gap, apparently investors have begun to move to larger capitalization companies. Small caps usually lead in the early stages of a market recovery as they are more sensitive to the economy than larger more established companies. This bull market hasn’t been an exception.

US Equities

The S&P 500 index rose 5.9% during the quarter in US dollars. The index only returned 3% to Canadian investors as the Canadian dollar appreciated by 2.6% relative to the USD between January 1 and March 31, 2011. The Dow Jones Industrial Average, representing 30 large blue-chip stocks in the US, had slightly better performance, returning 6.4% (US) for the quarter.

From its March 9, 2009 low the S&P 500 is up a whopping 104.5% in US dollars.

Earnings continue to show growth, Price-to-Earnings ratios continue to be modest compared to historical standards and corporations are cash-rich (with close to $2.4 trillion in their balance sheet). Combined with a low U.S. dollar stimulating exports this bodes well for the U.S. stock market.

International Equities

Developed markets slightly outperformed emerging markets during the quarter. The MSCI EAFE index rose 0.6% while the MSCI Emerging Markets Index lost 0.7% (Canadian dollars).

Record food prices and surging oil prompted speculation that central banks in developing nations including Brazil, Russia, India and China will boost interest rates to fight inflation.

Despite the short term impact of these measures, the combination of China, India and Brazil have GDPs that are 4 times the size and impact on the global economy as compared to the 1990s. This growth, which will likely continue in the foreseeable future, will have more than offsetting positive impact over the medium to long term.

Market perspectives and portfolio positioning

We believe, and agree with most of our managers, that neither are equities over-priced nor do any of the valuation metrics we follow indicate any excessive overvaluation. There are sectors of the market that show some signs of frothiness. In particular the materials sector, which is a significant part of the S&P/TSX, appears expensive. In a defensive move our asset class managers have been underweighting the materials sector and they continue to do so. We are comfortable with this strategy. The “this time is different” voices supporting the bullish market in commodities trigger our conservative and mean-reverting instincts to be more alert.

We strongly advise investors to avoid attempting to time the markets based on major events, changing macro-economic indicators, media reports or natural political developments. Moving assets in and out of the markets based on these external events can increase the risk of affecting investors' long-term returns.