OB REPORT

JUNE 2012

INSIDE THIS ISSUE

It's Not As Bad As You Think

> "IT WAS AN OUTSTANDING TIME TO BUY STOCKS THE LAST TIME WALL STREET STRATEGISTS WERE AS NEGATIVE AS THEY ARE TODAY."

INVESTORS ARE NERVOUS. Europe is in a recession and politicians in Greece are threatening to exit the Eurozone. China, the engine of global growth in recent years, is slowing down. And, with weakness indicated in the latest U.S. employment report, people are wondering if the recovery in the world's biggest economy will come off the rails.

Although stock investors have recouped much of their losses from the financial crisis, the major North American equity benchmarks are nonetheless still below their levels from five years ago. Moreover, individual investors are not getting much encouragement from the experts. According to Bespoke Investment Group, Wall Street strategists are the most negative they have been on stocks since March 2009.

Investors are understandably wondering if equity investing is worth the hassle.

In our opinion, stocks remain a highly desirable asset class that most people need in order to achieve their retirement goals.

Ironically, the experts' lack of enthusiasm towards stocks is actually a good thing, as negative sentiment sets the stage for better returns. After all, stock prices and future returns are inversely related. It was an outstanding time to buy stocks the last time Wall Street strategists were as negative as they are today.

Still, it is easy to get the impression that the sky is falling by listening to the fear mongering on the nightly news or by watching the performance of the Canadian benchmark stock index, the S&P/TSX Composite. As of May 15, 2012, it is down more than 20 per cent from its high in April 2011. Understandably, investors with index-like portfolios are glum, with the benchmark making zero headway over the last two years. However, the performance of the overall index paints a deceiving picture; beneath the surface there is good news and an upbeat story to tell.

The Canadian benchmark index is dominated by energy, material, and financial stocks, which are among the worst performing sectors in recent years. Sectors with less influence on the benchmark index have been doing quite well. For example, the Canadian Telecom, Consumer Staples and Utilities sectors have produced total returns of more than 30 per cent over the last two years. South of the border, the picture is even brighter. The S&P 500 has produced a total return of 19 per cent over the same period, with nine of the ten major industry groups generating double-digit returns.

MANY SECTORS PERFORMING WELL
2-YEAR TOTAL RETURN BY SECTOR[1] (MEASURED IN CANADIAN DOLLARS)

Sector	Canada	United States
Telecom	34%	41%
Consumer Discretionary	6%	33%
Consumer Staples	35%	29%
Utilities	31%	26%
Info Tech	-62%	25%
Health Care	149%	25%
Energy	-3%	18%
Materials	-19%	14%
Industrials	19%	13%
Financials	6%	-6%
Index	**0%**	**19%**

[1] Based on S&P/TSX Index and S&P 500 Index; as of May 15, 2012.

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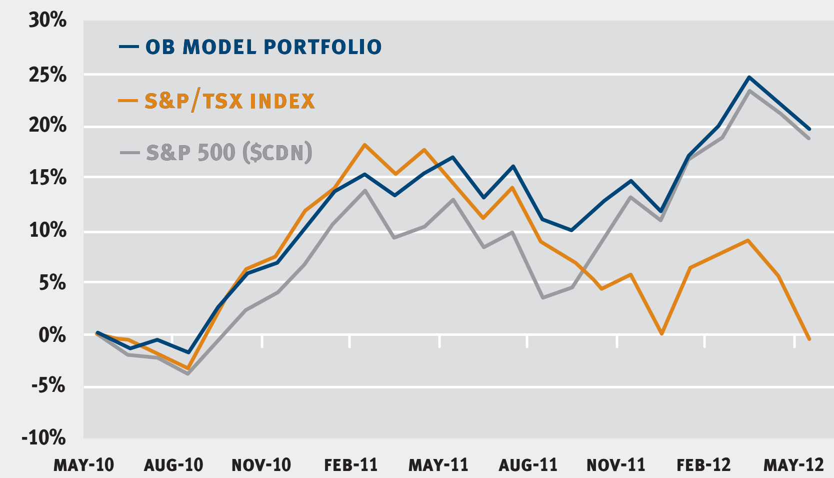
It's Not As Bad As You Think

Enhanced Client Account Documentation

We have enhanced our client account documentation to better understand your investment needs and objectives and to improve our overall service. If your account documentation has not already been updated, your Investment Advisor or Portfolio Manager will be in contact with you to assist you in completing these forms.

We encourage you to review the materials contained in the "Client Agreement and Notices" section of our website (odlumbrown.com), which form part of our new client account documentation program.

THINKING DIFFERENTLY PAYS OFF
TOTAL RETURN: MAY 2010 – MAY 2012*



* Returns are measured from the middle of the month.

The Odlum Brown Model Portfolio is also faring quite well. It is more diversified than the S&P/TSX Composite Index and its exposure to less cyclical sectors has contributed to its relatively good performance. Owning foreign stocks, principally high quality U.S. multinational companies, has also helped. Over the past two years, the Model has achieved a total return of 20 per cent.

With the underlying intrinsic value of many of the businesses on our recommended list rising faster than their respective stock prices in recent years, we believe that the stocks we favour have pent-up potential. We also believe that the economic outlook is better than generally perceived.

We are particularly confident that the U.S. economic recovery will remain on track. While some of the recent economic data points have been a little weak, we do not expect the sluggishness to persist. Indeed, we believe the weakness in the European and Asian economies will have a positive influence on America's consumer-driven economy. The near-record low interest rates and the recent moderation in commodity prices drive our optimism, as both trends will help U.S. businesses and consumers.

A few months ago, pundits warned that rising gasoline prices threatened to act like a tax on consumers and undermine the economic recovery. Now that gasoline prices are falling alongside oil and other commodities, as China's economy slows, few see the benefit to the consumer and the overall economy. That is not logical.

OB MODEL PORTFOLIO ON TOP
2-YEAR TOTAL RETURN BY MARKET[1] (MEASURED IN CANADIAN DOLLARS)

OB Model Portfolio	20%
U.K.	19%
U.S.	19%
Korea	9%
Germany	6%
Hong Kong	2%
Canada	0%
Japan	-1%
Russia	-1%
China	-4%
France	-7%
India	-20%
Brazil	-22%
Italy	-27%

[1] As of May 15, 2012.

The troubles in Europe are driving down interest rates in North America, as investors seek shelter in the relative safety of U.S. and Canadian bonds. For example, the average 30-year fixed rate mortgage in the United States is 3.75 per cent today, down from more than 4.5 per cent a year ago. The decline has helped to create record home affordability and drive an improvement in the outlook for the important U.S. housing sector. Indeed, since the Canadian stock market peaked last year, the S&P 500 Homebuilding Sub Industry Index has led the U.S. stock market higher, with a return of more than 55 per cent (in Canadian dollars).

The most telling trend is in junk bond yields. Unlike the case during the financial crisis in 2008 and 2009, borrowing costs for non-investment grade corporations are falling, as illustrated in the chart to the right. This suggests that bond investors are not worried about the economic outlook. Today, the average yield on a 'B' rated Industrial bond is about 6.5 per cent, whereas it was close to 16 per cent at the height of the financial crisis when investors were deeply concerned about the outlook and the ability of such companies to repay their debts.

Europe is also getting a lot of negative media attention, but that is not a reason to abandon high quality stocks that are generally performing well.

It is no surprise that the European economy is weak, as this is what happens when austerity is forced upon economies with private sectors that are retrenching. Fortunately, the authorities, and the European Central Bank (ECB) in particular, stand ready to inject monetary stimulus when necessary. Most importantly, the European banks have access to ample funding to ensure that a banking crisis is unlikely. By providing significant liquidity to the banking system, the ECB has greatly mitigated the downside risks to the overall European economy.

Talk of Greece leaving the Eurozone makes for a sensational news story and no doubt undermines investor confidence. However, the country is not large enough to matter in the grand scheme of things. The big German, French and British banks have already written off the lion's share of their Greek debt, so the major contagion risk from Greece has already been greatly reduced. Similarly, the big and important foreign banks have been gradually reducing their exposure to the other troubled southern European countries.

While we do not expect the European economy to bounce back quickly, we also do not expect the situation to deteriorate significantly. Moreover, it is not all bad news in Europe. Stronger countries like Germany are proving to be resilient, likely due to low interest rates and the positive influence the weak Euro is having on exports.

BOND INVESTORS DON'T DOUBT U.S. RECOVERY

The economic slowdown that is underway in China is clearly not good news for Canada's resource-geared stock market; however, it does have a positive influence on many businesses and consumers, as it has taken the edge off of commodity prices. Investors who have diversified appropriately into less cyclical sectors and higher quality foreign stocks should continue to benefit from the moderation in commodity prices.

Overall, we think the Canadian economy will muddle through, achieving growth that is reasonable but less than what the U.S. economy will deliver. Weakness in commodity prices will exert a negative influence on Canada's economy, but much of that should be offset by an export boost from a re-acceleration in the U.S. economy.

We have always argued that the economic recovery will be long and gradual, punctuated with fits and starts, and fears of deflation and inflation. We believe the recent slow patch and fears of deflation will be followed by better growth and renewed optimism, as has already happened several times during the recovery.

Last year, the combination of rising commodity prices, higher interest rates, and the natural disasters in Japan undermined the economic recovery. Such is not the case this year. Interest rates are extremely low, inflationary pressures have abated, and Japan is rebuilding.

We have little doubt that investors who focus on owning shares of high quality businesses will do well over time.

MURRAY LEITH, BCOMM, CFA
VICE PRESIDENT AND DIRECTOR,
INVESTMENT RESEARCH

MJT Odlum Brown Classic – PGA of BC Junior Championship
July 3 – 5, 2012
Surrey, BC

Odlum Brown lends its support for the seventh year as Tournament Partner of the 10th annual MJT Odlum Brown Classic – PGA of BC Junior Championship. The tournament, which draws top golfers from across the province, is endorsed by the British Columbia Golf Association and eligible top finishers receive exemptions into the BC Bantam, Juvenile and Junior Championships.

The MJT Odlum Brown Classic – PGA of BC Junior Championship takes place at Northview Golf and Country Club (6857 – 168th Street) in Surrey.

For more information, visit maplejt.com

The Odlum Brown Model Portfolio was established on December 15, 1994 with a hypothetical investment of $250,000. The Model provides a basis with which to measure the quality of our advice. It also facilitates an understanding of how we believe individual security recommendations could be used within the context of a client portfolio. Trades are made using the closing price on the day a change is announced. Performance figures do not include any allowance for fees. Past performance is not indicative of future performance.

ODLUM BROWN FINANCIAL SERVICES LIMITED

Not All Accounts Are Created Equal: Death and Taxes

THIS MONTH, WE HIGHLIGHT SOME income tax implications that can arise from holding non-registered, registered, and tax-free savings accounts at the time of death. As individual circumstances may vary, the information provided below is for general information purposes only.

NON-REGISTERED ACCOUNTS

General Rule: *Deemed Disposition at Fair Market Value*

- Any resulting taxable capital gains (50 per cent of capital gains) are added to income in the year of death.
- Any resulting capital losses must first be deducted against capital gains reported in the year of death. Remaining net capital losses may then be used to reduce taxable capital gains and/or other income in the current and previous years, subject to a number of rules and limitations.

Exception: *Spousal Rollover*

- When the deceased's capital property passes to their spouse[1] under the terms of a will or by virtue of the asset being owned jointly with right of survivorship, the transfer, by default, takes place at cost, effectively deferring any capital gains or losses. This is known as a "rollover."
- The executor may choose to elect for the transfer on a property-by-property basis to take place at fair market value if it is desirable to trigger capital gains or losses at that time.

REGISTERED ACCOUNTS (RRSPs & RRIFs)

General Rule: *Income Inclusion at Fair Market Value*

- The fair market value of all registered accounts on the date of death is added to the deceased's income on his or her final income tax return.

Exceptions: *Rollover to Spouse or Dependent Child*

- If the named beneficiary of the account is a spouse, the value of the RRSP at death qualifies as a "refund of premiums" and is taxable to the surviving spouse. The spouse could choose to transfer some or the entire amount directly to his or her RRSP or RRIF and claim an offsetting deduction.
- Specific rollover provisions exist for beneficiaries who are financially dependent children or grandchildren under the age of 18.
- A rollover to a registered disability savings plan (RDSP) for a financially dependent infirm child or grandchild is also available.

TAX-FREE SAVINGS ACCOUNTS (TFSAs)

General Rule: *Tax-Free*

- The death of a TFSA holder does not trigger any immediate income tax consequences.

Other TFSA Considerations

- If the TFSA holder's spouse is named as the "successor holder" in the TFSA contract, the spouse will become the new account holder and keep the tax exempt status of the TFSA without affecting their own contribution room.
- If the surviving spouse is named as the beneficiary, the proceeds can be used to make a tax-free contribution[2] to the spouse's TFSA without affecting their contribution room.
- If the beneficiary is someone other than a spouse, payments will only be taxable to the extent that they include income or capital gains earned after the holder's death.

Not all accounts are treated equally when it comes to income tax – in life and after death. To learn more about the potential tax implications that could affect your accounts, or for more information about the products and services offered by Odlum Brown Financial Services Limited, contact us through your Odlum Brown Investment Advisor or Portfolio Manager.

1 All references to "spouse" in this document also apply to common-law partners.

2 The contribution must be made before the end of the year following the holder's death and designated as an exempt contribution on the survivor's income tax return.

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FINANCIAL AND TAX PLANNER,
ODLUM BROWN FINANCIAL SERVICES LIMITED

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