The Dividend Value Discipline™
Market Commentary
2nd Quarter 2009

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Participants within **The Dividend Value Discipline™** made some solid progress over the quarter, with fully invested accounts posting year-to-date returns in the 15-19% range, versus an essentially break-even position at the end of Q1. That performance compares favourably with the TSX Composite Index's 15.4% return over the same period, especially when you consider that the program contains a significant amount of fixed income (cash and bonds) – 35-40% on average, as at June 30th. The fixed income component is a significant stabilization factor and it will also serve us well should we get a period of the "summer doldrums" where the market presents us with a few compelling value propositions, i.e. cash will be readily available for us to act.

Performance wise, no two accounts are exactly alike due to the ***"buys only"*** process and different start dates. Your individual results can be found on **The Progress Monitor**, which is included in your quarterly reporting package. Our objectives for the program remain unchanged – income every month, an acquisition process where we buy ***only*** those securities which become attractive on a "go forward" basis, and finally, absolute returns of 8%+ each and every year.

Strategy wise, over the last ninety days and into the foreseeable future, I continue to weigh the inflation/deflation debate. We continue to see inflation in those things the developing economies (China, India & Brazil) need, such as commodities, and deflation in those things that the developed world (North America, Europe & Japan) does not need more of, such as housing, cars and big ticket consumer items. Evidence out on June 26, 2009 further supports that view – our U.S. cousins have gone from spending more than they make to saving 15% of their household income, which is clearly deflationary. I suspect that Canadians are not as different as we would like to think. Certainly the Japanese continue to see deflation, as the month of May recorded a third successive decline in consumer prices, and at a rate not seen since 1971. Notwithstanding same, we continue to see robust prices in things like copper and oil. That duality has, in part, driven our investment decisions.

During the quarter we sold down those companies that we deemed to be most vulnerable to a sustained weak economy, in order to concentrate on consumer staple type businesses. Those commodity producing companies that we do own are very strong financially and should we get into a prolonged recession, we are confident they can weather the storm.

In the "sell the vulnerable" camp, over the past three months, we eliminated **Freehold Royalty Trust**, **CNH Global**, **Softchoice**, **Linamar**, and **Advantage Energy convertible debentures** from the program. In each case, at the time we sold, we believed that the risk of holding the stock through a "double dip" recession outweighed the upside opportunity.

In early May, we took profits in the **iShares Canadian Energy Index ETF**, a capitalization-weighted proxy on the Canadian oil and gas complex. Our thinking was that May is the seasonally high point in the year for energy stocks, the price of oil had rallied strongly, and the overall tone of the market seemed to be weakening.

By mid-May, with the market marching up like there was no recession going on, we started looking to more defensive positions, i.e. those things that we thought could do well in a weak economic environment. **Colgate Palmolive** had been on our radar for some time and it was relatively easy to make the value proposition, with toothpaste being a fairly recession-proof business, as well as the fact that the company actually benefits from a weakening U.S. dollar. Colgate Palmolive is extremely well managed, with a culture of promoting from within, and it also has a large insider ownership stake. Thus far, the market has confirmed our decision, and I hope it turns out to be one of those enduring great companies that we can hold on to for years to come.

Next were the purchases of **First Capital Realty** and **Overseas Shipholding Group** in late May. Our in-house analyst, Howard Ma, not only identified both candidates as being incredibly undervalued, he also pounded the table hard enough and long enough to get me to a buy decision.

Over 80% of First Capital Realty's revenues come from large, stable, retail businesses that serve everyday needs – businesses like Save-On-Foods, Loblaws, Safeway, Shoppers Drug Mart, London Drugs, Rexall, Toronto Dominion, HSBC, Royal Bank, Tim Horton's, Starbucks and Second Cup. Further stability is provided from the long term duration of its leases, which are currently averaging over 8 years. Financially, the firm is strong and well capitalized. We also appreciate the significant ownership stake and recent insider buying. The 7% dividend yield is merely the icing on the cake.

As far as Overseas Shipping Group is concerned, you really have to stretch your mind to call this defensive. Shipping oil across the world is not a defensive industry by any stretch. What made this investment so attractive was its stock price, relative to the underlying value of the company. Its strong financial position tells us that it can certainly weather a double dip recession.

Turning back to defence, in early June we took up a position in **Shaw Communications**, which we then added to later in the month. With more people staying at home, Shaw is benefiting from the move to digital set top boxes and pay per view services. Additionally, its high speed Internet business has one the highest penetration rates in North America. Unlike most of its competitors, Shaw is a customer focused organization and executes extremely well. Financially, it has shown consistent progress which has allowed the company to grow its dividend per share by an average rate of over 70% annually over the last four years. At the time of purchase, the dividend yield was around 4.5%, which is equivalent to roughly 6% interest income on a pre-tax basis.

Looking ahead, we are excited about the prospect of lower natural gas prices this summer. That may sound counter intuitive, but the longer gas prices stay down, the more industries will adopt it as their primary energy source. In North America we have identified massive shale gas deposits and now have the technology to cost effectively extract those deposits. There is lots of political appeal as well: we lessen our dependence on imported oil, and natural gas has 50% of oil's carbon footprint. So it's cheap, plentiful, cleaner, and in our backyard – I believe we are on the cusp of seeing natural gas as the fuel of the future. The prophets of doom will be out in full force on natural gas stocks this summer and we intend to accumulate more on that weakness.

Yours truly,

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Within the past 12 months, Raymond James Ltd. has undertaken an underwriting liability or has provided advice for a fee in regards to the securities of First Capital Realty.