1999 Second Quarter
Value Contrarian Canadian Equity

Dear Investors,

> "I don't say we are in a new era because I have experienced too many alleged new eras in my lifetime that have come and gone."
>
> **Allan Greenspan**
> **May 1999**

> "It has been the common feature of all speculative episodes in the last three centuries that some came forward to proclaim a new era."
>
> **John Kenneth Galbraith**
> **Harvard University**

Today, one is hearing increasing talk of a "new paradigm". Both Mr. Greenspan and Dr. Galbraith wisely understand that there are no "new eras" when dealing with the age-old activity of speculation, manias, and asset price inflation. There are, however, new "technological eras" that serve to dramatically change the world we work and live in. And these new "technological eras" do present numerous investment opportunities.

It is important to realize that "new eras" don't prevent stock prices from rising to levels far beyond any rational assessment of their value. New eras don't prevent investors from acting irrationally.

Unfortunately, the longer speculative activity occurs during a so-called "new era", the more it discredits those professionals and analysts who argue for caution. (Remember invincible Japan at its peak in 1989).

The internet represents a huge business opportunity and will radically change how information is distributed globally. Unfortunately, much of what is happening now is hype.

Aside from a few "blue chip" internet plays (i.e.: Cisco, AOL, Nortel), very few internet related companies are actually profitable. Just as we have seen speculative booms in radio (1920's), gold-oil (late 1970's), personal computers (1980's), etc., we are now witnessing a speculative run-up in internet stocks.

One of two things will happen to the current field of internet issues. Either their businesses will evolve to profit levels such that their share prices can be justified based on fundamentals; or their business plans will not produce sustained profitability in which case their share prices will eventually collapse.

Our response to all the internet related equity activity is to do what we have always done. At some point in the future (usually during recessions), we will have ample opportunity to participate in internet related issues at more favourable prices. This also reminds us of the virtues of patience. While we did not participate in the initial cellular boom of the late 1980's, our patience was eventually rewarded during the 1990 recession when we were able to buy into the industry at reasonable valuation levels.

Second Quarter Performance

Your fund ended the second quarter of 1999 with a net asset value of $1,428.08 per unit, an increase of $11.60 from the December 31, 1998 asset value of $1,416.48.

Rising long-term interest rates during the first half of 1999 adversely affected our performance. Of the 14 TSE sectors, the financial service sector (-7.9%) was second to last, just ahead of gold and silver (-18.3%). We nonetheless continue to feel comfortable with our core holdings in the banking and insurance sector due to their very reasonable valuations and ability to earn ROE's (return on equity) in the mid to upper teens.

Due to their rapid rise in value, our two Japanese investments now constitute 11.8% of the fund's total assets. So far this year, the Nikkei has quietly seized the mantle of the world's second best performing major stock market index. Japan is in the very early stages of its business cycle. While there are still doubts about whether the country has entered a truly sustainable recovery, the time to sell will be when Japan experiences a US-style boom.

It is important to note that a few dozen high P/E, ultra-high market-cap players (i.e., Nortel, Lucent) tend to skew reported stock market multiples. Hence, the Dow and the S&P trade at unprecedented earnings multiples.

But drill down into the strata of small and mid-cap companies, and good values can still be found. In particular, we are finding some "best buys" amongst companies with temporary earnings disappointments. Nonetheless, investors seem wary of buying what is cheap and selling what is expensive, preferring instead to buy expensive and "ride the tide".

Many institutional investors are willing to ignore high stock valuations as long as the stock meets quarterly earnings expectations and does not "disappoint". The penalty for disappointment is usually an immediate and significant price decline. However, it is important to remember that all portfolios experience earnings disappointments at one time or another. Unless, of course, your crystal ball is a better model than ours.

We have no idea how long this irrational behaviour will last. We believe that the companies in the Value Contrarian portfolio have excellent long-term appreciation potential while exposing investors to tolerable levels of business risk.

Outlook

There is a volatile "seesaw" battle taking place in the financial markets today. On the one side, robust corporate profit growth generates optimism that pushes stock prices up. On the other side, persistent "bubble" musings and interest rate actions by Mr. Greenspan cause stock prices to sag.

This "war" between earnings optimism and gloom on rates will continue for the remainder of the year, or until investors sense that interest rates are peaking. The abundance of pricey, big-cap stocks in the major indexes also magnifies this trend of volatility.

With respect to the Canadian market, we highly doubt that commodity prices will slide back to the depressed levels of last year. Oil prices, for example, have risen from $10.00 a barrel to a recent $20.00. This surge in commodity prices bodes well for the Canadian stock market. While the current market environment is extremely challenging in light of rising interest rates, we are still optimistic regarding your Fund's long term prospects.

Respectfully yours,

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