Jul-Aug

CastleMoore Investment News

Uniquely Superior Portfolio Management

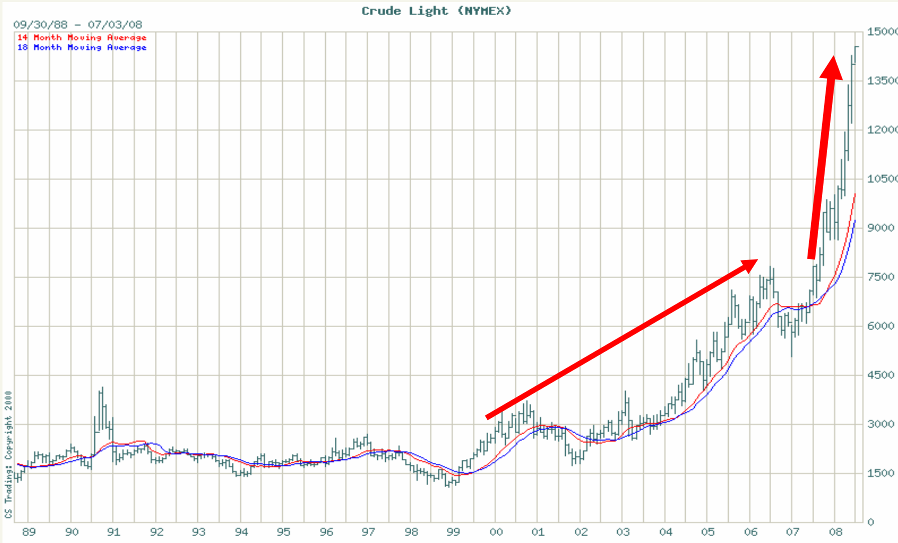
Boiling Oil

By

Ken Norquay CMT, Partner

Rookie stock broker: "How far up will it go?" Grizzled veteran broker: "Farther than you think!"

This chart shows us the price action of crude oil in US$ for the past 10 years. In the last year, summer 2007 to June 30, 2008, the rate of increase has been increasing. Technical analysts call this "going parabolic." The price of oil is going straight up!



Up, up and away: Oil broke out big in 2004, but can its parabolic nature last?

Whenever the price of anything goes parabolic, we know we are near the end of the up trend. It signifies that many speculators are piling in, driving the price up "farther than you think!"

As you read this article, try to get a "feel" for what it's like at/near a parabolic top of a market cycle. Here's what you might notice: 1.The financial press is aggressively covering the story 2. Many new investors are entering the market, speculating it will go higher 3. Many analysts are forecasting much higher prices 4. Everyone is an expert – everyone has an opinion – even the shoe shine boy.

How does all this feel? Is it exciting? Depressing? How does that feeling affect your investing judgement?

This is a list of common mistakes people make when investments go parabolic. 1. Over concentration: they put too many eggs in that one exciting basket. 2. Over confidence: because the profits are made so fast, we become unrealistically sure of ourselves. [Or over reliant on some advisor.] 3.Failing to sell when the up trend reverses.

How does it end? Parabolic rises usually end with a dramatic and sudden reversal, dropping even faster than they went up. Technicians call this a 'spike reversal." It is very difficult to make money once the spike sets in.

Quiz: in the past year, there have been two dramatic spike reversals. What were they? (See Chart Page 5)

What can we learn from all this? How should we handle ourselves when some investment we own goes parabolic? This is our attitude at CastleMoore: 1. We like to participate in parabolic rises. We look for potential parabolic rises and try to position ourselves in those sectors and industries. We do this by focusing our buy list on those areas of the stock market that are out performing the averages.

2. We try to sell as close as possible to the top. Sometimes we sell a bit too early and miss out on some of the run up. [For example, we sold our oil and gas stocks in June] Other times we sell out a bit too late and give back some of the profit we made. [For example, we sold our gold stocks in early May] Our attention is on selling.

3. We study investment research material on both sides: bullish and bearish. This helps us stay neutral. We don't believe either argument. We do believe that the market is going up "farther than we thought." And we do believe that the reversal will be sudden and dramatic.

When the investment world heats up, try to stay cool.

- Ken

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The Seeds of a Company, CastleMoore

By
Robert "Hap" Sneddon
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CastleMoore was created out of a hypothesis and sustained through facts that there was a need for a new approach to managing money. Having worked in the traditional client-broker relationship for the top firm on the street through the 90's and the early century I understood what the status quo was and how to do a good job of it. In March of 2000 much changed.

As I rode the chairlift on the slopes of Whistler I phoned back to my office to check-in. My assistant explained to me that the NASDAQ was under some big selling pressures, big enough to instantly bring to the forefront of my mind the historical market research I had been doing.

A generational or "secular" bull market ended in 2000

Sometimes to be a good advisor you must have a cautious conservative nature, but this was more than that. Markets, even secular (generational) ones, don't go up forever. I had been keen on understanding what impact aging baby boomers would have on security prices. As someone who was a gen-Xer, that small demographic group squished between boomers and their kids, the "echo" generation, I knew there could be some tidal changes coming to global markets, and in particular, the Western ones. Changes like these would affect my clients, they would affect me. Its well and good to ponder theories but you need evidence for confirmation, and then a game plan if you intend to act.

March 2000 revealed the beginning of the changes to come. Equity markets had been stellar for a generation. Since 1982 you truly didn't need an advisor if you had a dart-throwing monkey and a board with only the most average of mutual finds on it. Every investor gets one, maybe two, of these type of markets in a lifetime. Such markets make all participants geniuses. The first crack showed in the tech sector. Eventually prices for all industries and all indices were headed south by the time September 11th happened. Incidentally, the terrorist attacks were not any type of catalyst. They were only an accelerant that drove prices to a bottom.

Since 1982 growth in equities was driven by two main factors: the growth of the personal computer and the effect of a large swath of the public investing for retirement. Like many things in nature, human behaviour is constantly changing, but also empirically susceptible to patterns. Why humans often repeat the same behaviour I don't know. Historical data matched against contemporary action points to a very high probability

Nowhereville: The Dow Jones 1970-1982

we are in the midst of markets that will reveal similar investment returns produced by the Dow Jones between 1967-1982. That is to say limited.

We don't know what the markets' course will look like. Nor do we for sure if the US will be a proxy for all non-US markets. Fundamentally speaking Canadian-based investors will have unique response options to global geopolitical and economic drivers. For example, we invest using a different currency, have a resource-heavy market and have much better national balance sheet than the US. Emerging economies have their own unique economic conditions too, the most obvious being the push to modernise and the creation of domestic demand.

An adaptive micro or regional strategy is essential to future investment success. Understanding the broad market environment within which any contra situation may exist is necessary. If you look at the market data from a long term perspective it is easy today to ob-

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"Buy, Hold...And Know When To Sell"

Prepared by Dan Popescu

Created in MetaStock from Equis International

2

100 Year Look: Alternating 17 year periods of growth and contraction/stagnation. Will the pattern hold?

serve the potential challenges we face. In the analysis of the markets between 2000-2002, as it began and was as it was unfolding, are the seeds of CastleMoore.

Markets cycle in many time frames from minutes to decades. The above chart chronicles the DJIA from 1900 to the present. The black arrows show periods of growth; the red periods of consolidation or stagnation. They occur in approximately 17 year alternating intervals. The most recent period (orange) began in 2000/01.

During the tech-based run of the 90's I began to pay much more attention to understanding where we might be in grand, historical terms. The confirmation of such large, secular movements takes time. The best analogy is to a massive ocean liner changing course. When they turn it takes some time and is usually not acute. But when they reach that new course they persist on that bearing for a very, very long while.

I wanted to start a new, dynamic company that would be able to adapt to market conditions and deliver cost-effective portfolio growth while also protecting assets But I did not want to leave my stock brokerage career based on one phone call from a ski hill. Like the ship turning, it took some time to let the data present itself and for an action plan (CastleMoore) to be put in place.

- Hap

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My Choice of Careers (Part II)

By
Sheldon Liberman
Portfolio Manager

In my last column (and there are a few choice words waiting for those who suggested it *should* be my last column) I put forth some perspective on being CastleMoore's Portfolio Manager. Now I would like to mention why that label is not entirely accurate.

First of all, I am one of two Portfolio Managers at the firm, with Robert (Hap) Sneddon being the other.

Secondly, portfolio management alone does not completely cover my job description. I am also CastleMoore's Chief Compliance Officer (as well as having served as the model for CastleMoore's logo, but we'll save one that for another day).

Being a professional in a highly-regulated business is pretty straight forward: everything is either prohibited or compulsory. That might be a bit of an exaggeration but the point to be made is that anytime you hold the public trust certain standards must be created and upheld, lest the industry crumble beneath the weight of all the suspicion cast upon it.

My responsibility is to insure that these standards are not only met, but exceeded as far as possible. In other words, to say no. That why I'm considered a no-it-all.

In truth, this part of my job is made easier by two factors. First, I am deeply involved in the study of Jewish Business Ethics, which, trust me, trumps anything the securities regular can come with; and second, Fair Dealing with clients, which is at the core of any set of Compliance Policies, is already such a high priority among members of CastleMoore's team that Compliance directives not only are not resisted but actually sought out.

Part of the service is to insure such things as priority of clients over employees—as well equality amongst clients—in trade execution, that all investment decisions have a reasonable basis, that the firm maintains adequate capital, and that the firm is insured against the highly unlikely event of fraud or similar misbehavior. In short, it is to make sure that no client has reason to complain, and that the odd one who does not have his or her name "accidentally" added to the monthly report we send to the securities regulator on suspected criminal activity. There are stories…

We take our "studies" seriously

What makes it all work is communication. Each employee must know what is expected of him or her with regards to Standards of Professional Conduct. It's something we never take for granted at our shop; mistakes are frequently the result of miscommunication. Articulation has become especially important to me since the one time I had a conversation with that French-speaking salesman. I thought my French was better than it in fact was, and by the time the dealing was done I found myself the proud owner of a 1977 Plymouth Volare, 12 books on the subject of stamp collecting, and a small village in Africa.

Though we often use humor to take the edge off what can be a very stressful occupation, know that safety in all aspects of the investment process is as important to us as it is to the securities regulator. The latter is always ready and willing to exact a pound of flesh from anyone who breaches its standards. Therefore, the next time you interview a potential Portfolio Manager you should ask yourself, "Hmm… does this person seem too thin?"

Jobs I've had (or tried to get)…

I've always loved spy pictures. I wanted to go into intelligence but, unfortunately, none of it went into me.

I got a job in the frozen meat business, but they gave me the cold shoulder.

Then I went to work for a moving company, but I was told to vacate the premises.

I got a seasonal job as a department store Santa. Even there I was given the ol' heave ho,ho,ho.

The manager for FedEX asked me if I could start to work in Atlanta the next morning. I told him I absolutely positively couldn't get myself there overnight.

-Shel

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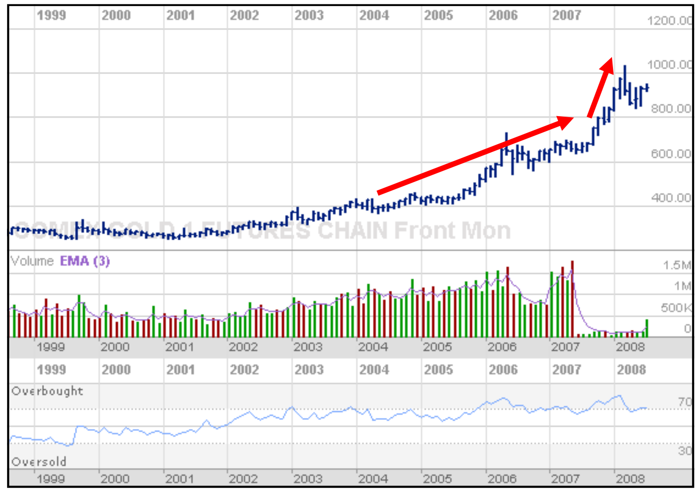
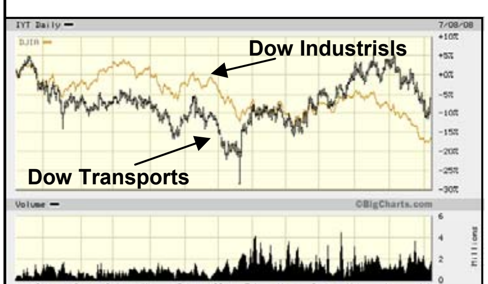
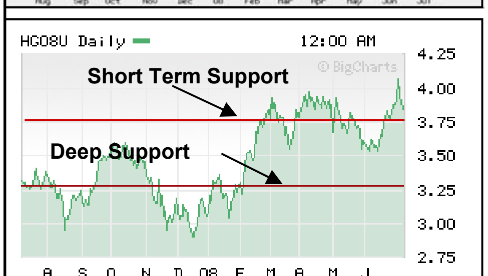
The Chart Page



The CDN/US dollar price relationship broke out of a long trading range between the 62.5 and 70 cents in mid 2003. The spike top occurred in November 2007. Today, the thesis is for a continued trading range between $1.02 and $0.90. .

Gold broke out of a long trading range in mid 2003 as well. The spike top in gold occurred in March 2008. Spike tops in and of themselves do not mean a security is entering a period of decline or bear market. It can simply be a substantive correction a in longer bull trend.





Canaries in the Coal Mine — Life In the Markets

Because of continued market volatility and speculation this section, initially introduced as a "one-off", will carry on indefinitely in our attempts to monitor key signals about the nature of security prices and the economy they reflect. These little birdies and others to come tell us what's going on in the deep.

BONDS/PREFERRED SHARES: This relationship has continued to deteriorate since the May-June newsletter. At that time the spread was 15% out performance in bonds favour. Now it has climbed to almost 23%! The preferred we used is a Royal Bank one, so a good name. It's a perpetual fixed rate preferred. The yield-to-call (issuer initiated) is a whopping 19.34%. We are closely looking for opportunities to lock in decent yields, but we are also careful of what we wish for. Investors are still clearly worried about getting paid.

DOW THEORY: If you pay attention to your investments or the markets closely you don't need me to tell you the US market has really performed poorly lately, especially since June. What is positive is that the Transports remain above the Industrials. If we get oil futures falling it may bode well for both, and we think this is the reason why the relationship is healthy, despite both falling.

COPPER PRICES: You wouldn't know most equity markets (Canada and Brazil being the major exceptions) have been trending down with big momentum if you only looked at copper. Since May it launched past $4.00/lb, indicating that it demand is still quite robust. Copper prices tells us about economic activity which in turn is reflected in the stock markets. Stock markets reflect economic activity 6 months in the future. Copper prices may be supported by infrastructure build out in India and Asia regardless of what happens to global equity prices.

-Hap