



Palos Weekly Commentary

Investment Themes



U.S. Equities Decline on Profit Growth Concerns

U.S. equities closed lower for the week. Lower-than-expected growth in consumer spending coupled with forecasted weakness in profit growth in the consumer discretionary and technology sectors led the market decline. Furthermore, the growing risk of dividend cuts by large money market banks resulting from shrinking asset quality added to existing negative pressures on the equity markets.



Oil Rises on Gasoline Inventory Decline and Weakening U.S. Dollar.

Crude oil closed higher for the week due to rapidly shrinking gasoline inventories and refinery shutdowns. Furthermore, declining refinery utilization rates led traders to speculate that demand could increase for the commodity in the near term. The bulk of the increased demand would come from economies that subsidize refiners as margins are becoming increasingly thinner. Finally, the declining U.S. dollar was the final catalyst that helped push crude oil prices higher, as foreign investors flocked to the commodity to take advantage of currency differentials.



Spreads Rise Slightly as Concerns over U.S. Economy Persists

Credit spreads continued to widen during the week as concerns over the credit crisis still persist. Anxieties over default rates,

inflationary pressures, the fate of U.S. financial institutions, asset write-downs and lower profits are pushing corporate bond yields higher.



U.S. Treasuries Decline on Inflation Concerns

U.S. Treasury notes closed lower for the week as rising oil prices spur inflation concerns, resulting in rising Treasury yields. Furthermore, Treasury markets reacted negatively to TIPS spread implied inflation. Speculators are expecting an inflation rate of 2.35 percent. As a result, term structure differentials widened further as 10-Year long term rates rose more than 2-Year short rates.



Canadian Equities Fuel Demand for Loonie

The Canadian dollar closed higher for the week as rising Canadian equity markets increased demand for the currency. Foreign investors are increasingly interested in Canadian equities. Many large resource companies are offering attractive yields and favorable growth prospects. Furthermore, there is growing awareness that Canada is becoming gradually more independent of its U.S. neighbour. Accordingly, investment prospects are viewed more freely and objectively and, in turn, adding further support to the Loonie



Investment Themes

- **Equity Markets:**
U.S. Equities Decline on Profit Growth Concerns
- **Energy Markets:**
Oil Rises on Gasoline Inventory Decline and Weakening U.S. Dollar.
- **Credit Spreads:**
Spreads Rise Slightly as Concerns over U.S. Economy Persists
- **US Treasury:**
U.S. Treasuries Decline on Inflation Concerns
- **Canadian Dollar:**
Canadian Equities Fuel Demand for Loonie

Comment Corner

Although, the FRB is playing a crucial role in stabilizing the money markets by liquefying the financial sector and lowering target rates, it seems as if the free markets may have lost its self-healing capabilities; *an ancillary boost to the markets has come from political pressure demanding government intervention.* History shows that subsidised and regulated systems, while great at averting catastrophes, usually do not efficiently allocate resources. Accordingly, the expected long term decrease, by many seasoned scholars, in employment growth, productivity gains and leverage borrowing should negatively affect business conditions. It may take more time for the economy to turn the corner and get it back to par than *is generally believed.* Widening credit spreads, tightened lending standards, rising bank capital inadequacy and increasing risk aversion could, under the aforementioned long term trends, potentially prolong the period of sub-performing profitability and economic activity. In this connection, Palos actively recommends INCOME GENERATING FUNDS as an investment that can help dissipate the visible uncertainty and volatility of the economy. *Thus investors get 'paid' while they wait for the markets to recover.*

Figure 1: Performance

Funds	Value	Weekly Returns	Year-To-Date Returns
Palos Income Trust Fund LP	CAD\$ 11.32	3.45%	-1.61%
Palos Equity Income Fund - RRSP	CAD\$ 10.24	2.65%	2.45%
Palos International Equity Income Fund PLC - CAD	CAD\$ 8.63	0.82%	-1.15%
Palos International Equity Income Fund PLC - EUR	EUR€ 7.75	-0.26%	-10.05%
Palos International Equity Income Fund PLC - USD	USD\$ 9.83	-1.50%	-4.10%
CTI Palos Equity Fund LP	CAD\$ 11.90	3.77%	-1.38%
CTI Palos Equity Fund - RRSP	CAD\$ 10.04	3.33%	0.39%
CTI Palos Bond Fund LP	CAD\$ 10.57	0.19%	3.16%
CTI Palos Bond Fund - RRSP	CAD\$ 9.97	0.06%	-0.28%
Gauthier Palos Global Macro Fund LP	CAD\$ 8.75	-1.46%	-4.13%
MVest Opportunity Fund LLC	N.A.	N.A.	N.A.
Palos Capital Pool LP	N.A.	N.A.	N.A.

Figure 2: Benchmarks, Interest Rates & Commodities

Benchmarks, Interest Rates & Commodities	Value	Weekly Change	Year-To-Date Change
S&P 500 Total Return Index	1,315.22	-1.04%	-9.96%
S&P TSX Composite Total Return Index	13,233.79	3.75%	-3.70%
S&P TSX Capped Income Trust Total Return Index	147.98	5.55%	5.14%
MSCI All Countries World Total Return Index - CAD	576.27	2.24%	-11.45%
DEX Universe Bond Total Return Index	N.A.	N.A.	N.A.
US Government 10-Year Yield	3.44%	0.11%	-0.63%
Canadian Government 10-Year Yield	3.45%	0.00%	-0.57%
Crude Oil Spot	USD\$ 104.95	USD\$ 3.11	USD\$ 8.97
Gold Spot	USD\$ 930.60	-USD\$ 44.40	USD\$ 92.60
US Government 10-Year/Moody's BAA Corporate Yield Spread	353 bps	4 bps	89 bps
USD/CAD Exchange Rate Spot	0.9781USD/1.00CAD	0.0011USD/1.00CAD	-0.0407USD/1.00CAD

Sincerely,

Charles Marleau

Tommy Nguyen

Minh Nguyen

Robert Sands Jr.

