

QUARTERLY COMMENT
Second Quarter 2010

MACRO ENVIRONMENT

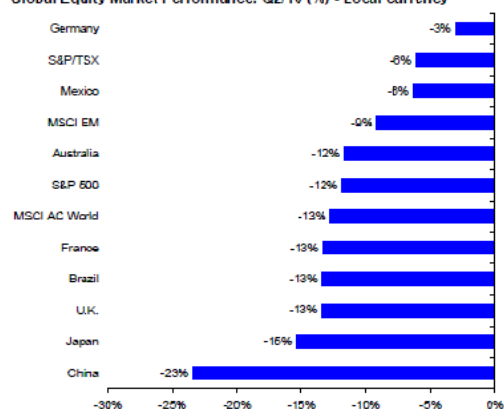
Capital market volatility increased in the second quarter of 2010 as investors reacted nervously to sovereign debt concerns in the Euro region and the potential risk those developments pose for the global economic recovery.

While the Canadian equity market (measured by the S&P/TSX index) was down approximately 6% during the quarter, it held up well compared to most other major global markets. The S&P500 index, a proxy for the US market, was 12% lower, or approximately 8% in Canadian dollar terms, the UK market was off 13%, Japan was down 16% and China was 23% lower at June 30 compared to March 31.

Investor attention and concern focused on the potential for debt defaults in the PIIGS countries (Portugal, Ireland, Italy, Greece and Spain). The related debt restructuring and austerity measures that are under way in those countries could potentially slow or reverse the global economic recovery that has been underway since mid 2009.

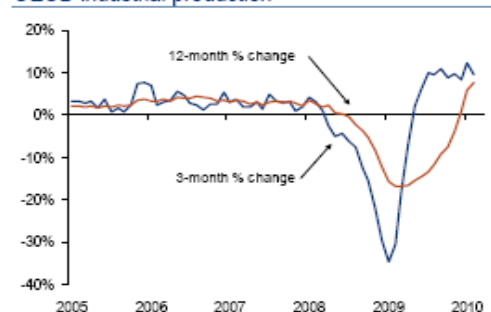
At the same time, while the debt issues of some members of the Euro region have been much publicized, it is worth noting that the global economy continued to recover as demonstrated by industrial production within the OECD (developed economies), which has rebounded sharply since early 2009.

Global Equity Market Performance: Q2/10 (%) - Local currency



Source: Morgan Stanley

OECD industrial production



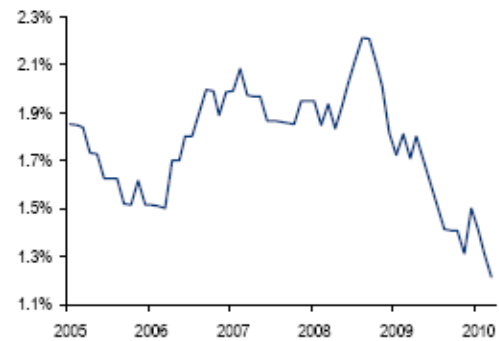
Source: OECD, BoFA Merrill Lynch Global Research

Economic growth projections for Canada for all of 2010 remain at 3% - 4%, suggesting solid economic performance driven by a homebuilding recovery, and relatively robust retail consumption supported by a stronger job market and low interest rates.

While inflation remained subdued, the Bank of Canada took the initiative to increase the bank rate by 0.25% on June 1 to 0.75%, reflecting its vigilance in keeping growth and inflation under control. Canada continues to be viewed very favourably by our global peers largely because of our relatively strong banking system, stable political climate and sound fiscal discipline which have served us well through the economic turbulence of the past 12 – 24 months. We have also benefitted from a strong global resource sector for most of the past decade which has provided an additional tailwind. In measuring market sentiment, The Royal Bank of Canada recently published data showing that approximately 67% of Canadians believe the overall outlook for the economy is good. Canada continues to hold attractive investment opportunities for global investors.

In the US, the Federal Reserve continued to hold rates at effectively zero, suggesting that the American recovery is still in an early, somewhat fragile state. However, the US consumer is gaining more confidence as evidenced by the widely followed University of Michigan survey of consumer sentiment, which recently rose to its highest level since June 2008. In addition, despite the difficulties in the Euro region for US trade, the American economy is expected to benefit from buoyant economic growth in Asia, Latin America and Canada by increasing exports accordingly. At the time of writing, growth remains widely expected in the US economy in 2010.

OECD* core CPI (12-month % change, ann.)



Source: OECD, BoFA Merrill Lynch Global Research

*OECD total excluding high inflation countries

The recently held G8/G20 meetings in Canada highlighted the divergent circumstances and issues facing the various group members. However, there was general consensus on some issues. Reflecting the balance between growth and fiscal consolidation, advanced economies committed to fiscal plans that will at least halve deficits by 2013 and stabilize or reduce government debt-to-GDP ratios by 2016. The G20 also expressed support for the idea that the financial sector should make a fair and substantial contribution toward paying for the burdens associated with government interventions, when they occur to repair the financial system. Canada, along with other nations, opposed a bank levy, suggesting instead new capital rules to prevent another global financial crisis. A plan to overhaul bank capital and liquidity rules is expected to be finalized by November 2010, with implementation at the individual bank level by the end of 2012. These measures should help further stabilize the global banking system.

Existing home sales (Thousands, annualized, SA)



Source: National Association of Realtors, BofA Merrill Lynch Global Research

While there are fears of a double-dip recession, history shows that such events are rare. The global economy is expected to continue to recover, although the sovereign debt crisis in the Euro region, and the related austerity measures that were recently announced, represent some risk to recovery.

INVESTMENT STRATEGY

In terms of Canadian fixed income, interest rates are expected to remain low as inflation at home remains subdued. Globally, the threat is more biased towards deflation and a lower rate environment. We continue to maintain a broadly laddered bond portfolio with emphasis on Government of Canada bonds and high quality provincial and corporate bonds.

Looking at our model equity portfolio, we sold our position in Aflac during the quarter. Aflac is a US-based insurance company with a strong business model. However, Aflac experienced significant volatility because of its bond portfolio, which held direct investments in both Greek bonds and certain European banks which in turn held Greek and other PIIGS-related debt. We became uncomfortable with the increasing risk profile of this company and deemed it prudent to sell relatively early in the unfolding Euro debt crisis.

During the quarter, our model stocks featuring particularly strong balance sheets and yield were the strongest performers. These holdings, which are often considered prime destinations during “flights to safety” by other capital market participants, include BCE, Thomson Reuters and Enbridge. Some of our healthcare-oriented holdings lagged in the quarter, including Teva Pharmaceuticals and Becton Dickinson (medical devices). This primarily reflected capital market uncertainty with regards to the long-term impact of the US Administration’s recently enacted healthcare reform package on healthcare companies.

The BP-leased Deepwater Horizon rig sank on April 22nd unleashing the worst environmental disaster to afflict US shores. The catastrophe highlights the risks involved in deepwater drilling. Canadian oil producers and pipelines, such as TransCanada Corp., one of our model holdings, may become the unintended beneficiaries of future regulation to limit offshore drilling. TransCanada is leading a project for a proposed 2,151 mile pipeline, which would transport crude from Alberta to refineries in Texas.

At Coleford, we have always believed that dividends are an important part of investment returns and therefore a critical consideration in assessing the merits of potential stock ownership. History supports this view. Dividend income represented 43% of the total return provided by US equities between 1926 and 2009. Dividends, and more specifically regular increases in dividends, provide investors with a very good indication of how effectively

companies manage their capital. We prefer companies that regularly return cash to investors through rising dividends and will remain steadfast in our conviction.

In terms of the Coleford equity portfolio, approximately 50% of our holdings have increased their dividends in the last 12 months.

Dividends have accounted for over 40% of total returns over the long term

	S&P 500: Contribution of Dividends to Annual Total Return 1926-2009			As A Share of Total Return	
	Total Return	Income Return	Price Appreciation	Dividend	Price
				Income	Appreciation
1926-39	5.1%	5.2%	(0.2%)	na	na
1940's	9.2%	6.0%	3.0%	67%	33%
1950's	19.4%	5.1%	13.6%	27%	73%
1960's	7.8%	3.3%	4.4%	43%	57%
1970's	5.9%	4.2%	1.6%	72%	28%
1980's	17.5%	4.4%	12.6%	26%	74%
1990's	18.2%	2.5%	15.3%	14%	86%
2000-2009	(0.9%)	1.8%	(2.7%)	na	na
2009	26.5%	2.4%	23.5%	9%	91%
2003-2009	5.5%	2.0%	3.4%	37%	63%
1926-2009	9.8%	4.1%	5.5%	43%	57%

Source: FactSet, Bernstein analysis

Despite recent economic challenges, corporate balance sheets have generally improved, leaving companies with the flexibility to reinvest in their businesses, make selective acquisitions or increase dividends. In fact, US corporations have been building cash reserves at levels not seen since the 1960s. How and when these companies start deploying cash could influence the pace of the recovery. It must be noted that this cash will have to be deployed at some point as holding excessive amounts suppresses corporate returns.

Net Debt to Market Cap: Large Caps Ex Financials
Through April 2010



Source: FactSet, Bernstein analysis

Capital markets could remain somewhat volatile over the summer months as the global economy works through its recovery phase. As we reflect on recent volatility, we are reminded of the words of a well-respected investor who said: "The key to making money in stocks is not to be scared out of them."

We believe this period continues to provide us with opportunities to add to some existing equity holdings and pursue new ideas that we are currently reviewing.

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