



## To the Unitholders and Shareholders of Terra 2008 Mining & Energy Flow-Through Limited Partnership & Terra Resource Mutual Fund

We are pleased to present the June 30, 2009 quarterly update for the Terra 2008 Mining & Energy Flow-Through Limited Partnership (“Terra Flow-Through LP”) and Terra Small Cap Resource Fund (“Terra Mutual Fund”).

### Performance Overview

As of June 30, 2009, the unaudited net asset value of the Terra Flow-Through LP was \$61.24 per unit and the Terra Mutual Fund was \$5.84 per share (see pages 3 & 4).

Year to date the Terra Flow-Through LP has increased 11% and the Terra Mutual Fund has increased 17%. The net asset value for the Terra Flow-Through LP represents a 34% after-tax return for an investor taxed at a 46.41% marginal tax rate.

The Terra funds continue to perform well while reducing risk by maintaining **above average cash levels** as we move into the summer months. Oil and gold remain the largest single investments in our Terra Flow-Through LP at respectively 19% and 16% of the portfolio. Oil and gold also represent the largest investment holdings in the core portfolio for the Terra Mutual Fund. However, 40% of the mutual fund is temporarily invested in cash (down from 49%) so we retain flexibility to reinvest at better valuations.

### Commentary

Volatility continues to be a big factor in the market and has been beneficial to Terra. We have been very active with our portfolios for the past 3 months. The number of flow-through investments has been cut in half, with a corresponding increase in cash. Several holdings rose to levels beyond what we believed they were worth so we reduced these holdings.

Our cash balances serve two purposes:

- (1) to reduce risk in the interim in case this rally is short lived; and
- (2) to better position the funds to acquire additional firms at even better values which we believe will exist this Fall.

“Cash balances ... reduce risk ... and better position the funds... to acquire firms at better values..”

Volatility in the oil markets reached levels not seen since the mid 1980s and early 1990s and shows that markets continue to oscillate between fears of falling demand and falling supply. Regardless of what the short term reason is for the volatility, we

believe investors should be focused on the longer-term assessments of supply and demand.

“.... markets continue to oscillate between fears of falling demand and falling supply.”

On the demand side, the long-term trends for many resources show that there will be increasing difficulty in meeting that demand. One such trend in favour of growing demand is that world population is estimated to grow by 3 billion people by 2030. With this growth many nations will increase their standard of living resulting in even more resource consumption.

On the supply side, volatility in oil and other resources has increased uncertainty and caused firms to cut supply or suspend operations, reduce exploration efforts and therefore jeopardize future commodity supply. A June report by Cambridge Energy Research Associates has estimated that sharp reductions in investments and low oil prices could curb future supplies by almost *eight million barrels a day* (my emphasis) within the next five years.

Particularly hard hit are investments in unconventional resource sources such as wind, hydrogen etc. The decline in unconventional energy sources only adds more pressure to finding more “conventional” resources such as oil.

Of course there is an alternate view that supply can ramp up faster than demand. This view, however, assumes that there is a willingness to increase supply. The actions of many nations including Venezuela and Russia, as well as the OPEC cartel (which has managed to reduce production in recent months to match the drop in demand) shows that suppliers are more interested in maintaining higher pricing. The quick supply ramp-up view also assumes that the urbanization and industrialization of the emerging markets will not substantially impact commodity pricing – another view we do not subscribe to.

More commentary from our portfolio manager can be found on page 2.

Yours truly,  
John Jacobi  
President, Terra Fund Management Ltd.

## Portfolio Manager's Comments

### Terra 2008 Mining & Energy Flow-Through LP

The Terra 2008 Mining & Energy Flow-Through LP was up 11% for the quarter. The portfolio is currently invested 65.3% in cash. Mining investments account for 15.8% of the portfolio, of which 10.6% is in precious metals, 4.2% in base metals and 1% in uranium. Energy investments represent the balance of 18.9% of the portfolio, of which 16.1% is invested in oil and 2.8% in natural gas.

The majority of the Terra 2008 flow-through portfolio was invested in the midst of the financial crisis last Fall. The benefit to this was that we paid low prices for new flow-through issues. As well, the four-month hold restriction expired in the Spring just as the resource stocks were experiencing a mini recovery. We have used this rally to sell the non-core investments and reduce the size of our core holdings to a level where we do not have excessive risk in any one company. We now have the flexibility to let our investments appreciate over the coming months and in a few cases some might well become acquisition targets.

The summer is usually a slow period for the stock market in Canada and share prices have a habit of drifting lower on no news. It was important to do this housekeeping before the summer started. Now we are in a position to look at new flow-through opportunities in a more favorable market setting.

The LP's gold holdings continue to include SanGold (SGR-tsx) and Rubicon (RMX-tsx). This quarter we trimmed our uranium investment in JNR Resources (JNN-tsx). The larger cap oil investments in Petrobank (PBR-tsx) and Tristar Oil & Gas (TOG-tsx) are lower but we have plenty of time for a good recovery.

Our preference, as always, is for resource companies with an operating business or a late stage project, which we can invest in at a discount to its intrinsic value. The other key criteria remains management's ability to demonstrate the money will be correctly spent to qualify for the intended Canadian Exploration Expense.

The resource industry feels better today than it did a few months ago. However, many of the macro problems remain and the stock market valuations are susceptible to continuing weakness. Our flow-through investment strategy can use this weakness to our advantage as we continue to invest in undervalued assets as we proceed through this recession.

### Terra Small Cap Resource Mutual Fund

The Terra Small Cap Resource Fund rose 17% for the quarter. The portfolio is currently invested 40.3% in cash, which will be reinvested as opportunities present themselves. Energy investments represent 23.6% of the portfolio, of which 13.7% are Canadian large cap shares and 9.9% are Canadian small cap shares. Mining investments account for 19.5% of the portfolio, of which 13.4% is invested in gold and 6.1% is invested in base metals. The balance of 16.6% of the portfolio is invested in new yield investments, of which 7.4% are infrastructure trusts and 9.2% are resource company bonds.

We continue to hold core holdings in Encana (ECA-tsx), Imperial Oil (IMO-tsx), Canadian Natural Resources (CNQ-tsx), Goldcorp (G-tsx) and Agnico-Eagle (AEM-tsx).

Even though the financial credit crunch seems to be over we are now left with a lower level of global economic activity and a considerable amount of debt held by both governments and consumers in the Western world. What is most important for a resource investor is that it has become clearer that the developing countries of China, India and Brazil have been somewhat insulated from this crisis and their economies continue to grow.

We recently exited an environment where commodity prices were extremely high. Why? Because the financial crisis has affected credit and reduced demand. Although resource prices are lower this is in no way a collapse. Most base metals and oil are now trading at prices which reflect fair value.

Resource stock prices have been on a wild ride. Last Fall's selloff and this Spring's subsequent rebound have been more pronounced in base metals than in energy shares. The price decline into last November was more a result of the lack in liquidity, rather than due to a lack of demand. Stock prices declined until they reached a level where a buyer would purchase the stock. In many cases this price was at a steep discount to the value of the business. Because the crisis also coincided with the pre year-end tax loss selling, a price floor was established more quickly, which provided the support level for a recovery in share prices.

The strategy for Terra has been to remain cautious and add incremental investments where the business is relatively stable and we are able to pay an attractive valuation. For example, we have added Keyera Facilities Income Fund (KEY.UN-tsx), which is an industrial gas process company in Western Canada which we bought at a 12% yield.

Another key development over the past quarter is the return of financing activity for junior resource stocks. If a company does indeed have an attractive asset and the capital structure is transparent, the market will support such an equity issue. This has contributed to a recent run-up in stock prices. We have made two small investments in East Asia Minerals (EAS-tsx) and Claude Resources (CRJ-tsx), which have both benefited from this resurgent financing activity.

Natural gas remains the truly unloved sector of the resource world. The low North American natural gas price reflects both a hangover from newly developed shale plays and a collapse of industrial demand of approximately 15%. We believe the pieces are being put in place for a recovery of natural gas prices in 2010. We will remain invested in high quality, low cost producers but we might require a bit of patience while we wait for the upcoming rally.

Yours truly,  
Bill Harris  
Avenue Investment Management Inc.