

Charting a Course with Cautious Optimism



Gareth Watson, CFA - Director, Portfolio Advisory Group

Geoff Ho, CFA – Director, Portfolio Advisory Group



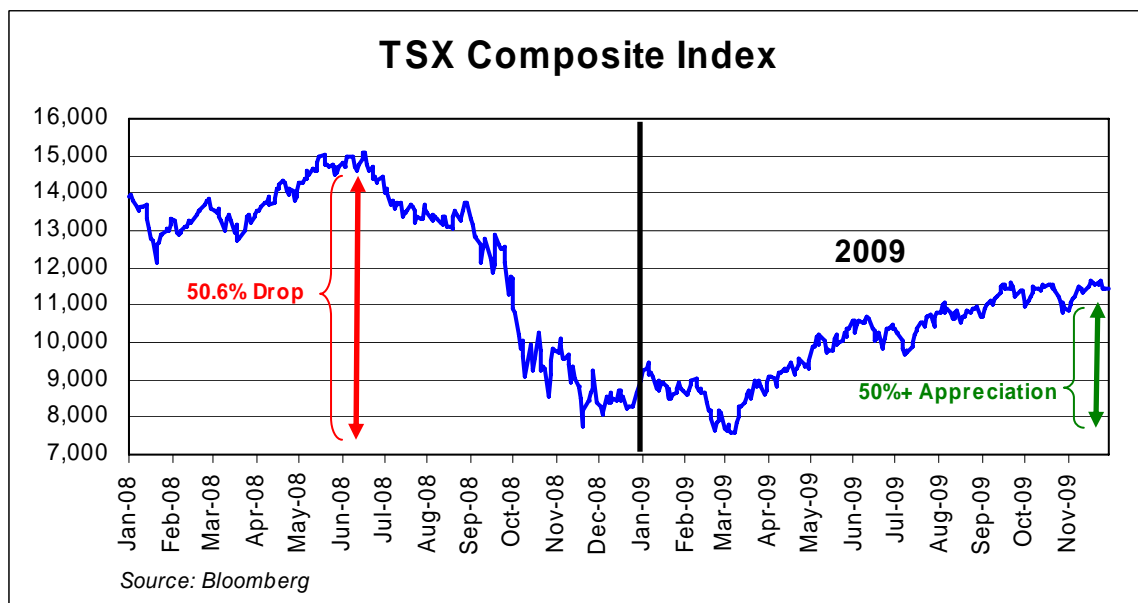
Wednesday December 9, 2009

Contents

	Page
2009 – A Review	3
The Present	5
The Economic Argument	9
So What Now?	14
Economic Outlook	15
Where is the Canadian Dollar Headed in 2010	15
Canadian Equity Market Outlook	17
Financials	17
Energy	18
Materials	19
Technology	21
Consumer Discretionary	21
Industrials	21
Defensives	22
Individual Stocks to Highlight	23
Overall Conclusion	24

2009 – A Review

What a difference a year makes. At this time last year we had just witnessed the beginning of one of the worst financial collapses in 80 years. The flow of capital within the financial system ground to a halt, recessions globally accelerated and investors were left with disappointing returns amongst several asset classes including equities. Alas, here we are in December of 2009 and most investors would agree that the state of the markets is not as bad as it once was. While no major stock market has managed to regain all of last years' losses, most indices have shown signs of improvement as some losses have been recaptured. As you can see in the chart below, the TSX index has been on a dramatically volatile course since 2008. The TSX fell by 35% in 2008 and from the peak of June 2008 to the trough of March 2009 the Composite index actually lost half of its value! But since the March lows, the TSX appreciated for a number of reasons which we will discuss in this report. In our Outlook 2009 report from last year we made several predictions. We thought the TSX Index would post positive returns in 2009, albeit single digit returns; we thought the U.S. dollar would depreciate; we thought that commodity prices would regain lost ground towards the end of the year; and we thought defensive industries would still provide investors with dividend stability and growth. As we look back on 2009, we feel as though we can claim that our predictions proved true for the most part; however, we were pleasantly surprised at how quickly some of those predictions came to fruition.



Were we right that the TSX would appreciate? Yes. But did we expect returns between 20% to 30% and expect those returns so quickly? No. One of the main reasons why we underestimated the resiliency of the Toronto market was the speed at which the U.S. dollar depreciated. While we expected depreciation, we did not expect it to happen as quickly as it did in the first half of 2009. The U.S. dollar had been a “go to” currency for risk averse investors in 2008, but once speculation of a U.S. and global economic trough began to pick up in March, investors couldn’t leave the U.S. dollar fast enough. The result of this weakness was that commodity prices climbed and since the TSX is weighted 47% to commodities it should come as no surprise that equity investors were ready to jump back on the Canadian bandwagon.

2010 Outlook

Another factor that helped the Canadian market outperform related to successful monetary and fiscal policies used throughout the financial crisis and economic recession. The magnitude and speed of the response via various stimulus packages helped to establish some financial stability, albeit still fragile, over the past several months. When signs of economic stability and even modest improvement started to emerge, investors increased their risk tolerance and were more than happy to go after cyclical investments. Commodity related economies such as Canada and Australia were the beneficiaries of this interest. We expected commodity prices to rebound in the second half of the year, but since economic optimism returned to the market sooner than we expected, our original prediction proved to be conservative. But considering the year we had in 2008, we'd much rather be wrong for being too conservative than too aggressive.

And while cyclical (economically sensitive) stocks clearly outperformed defensive (less economically sensitive) stocks in 2009, we were pleased to see strong, blue chip companies within defensive industries continue their impressive record of not only maintaining, but increasing dividends. While defensive stocks may not have provided investors with the highest overall returns in 2009, from an income perspective they did provide consistency.

One theme worth noting from 2009 is that we feel fundamental analysis was less relevant than it has been in the past. Simply put, there were a number of factors affecting the market in 2009 that left us scratching our heads and noting "that doesn't make sense". For example, why were oil prices increasing when demand was declining and inventories were rising? Why were investors assuming a robust economic recovery was inevitable when consumers were saving instead of spending? And just because the absolute worst of the credit crisis was over, why did some investors act as if risk had disappeared altogether? While we recognize that markets are forward looking and that an economic recovery was inevitable, we also believe that other speculative and technical factors were at play in 2009 that made fundamental analysis less relevant in predicting future market direction. Without a doubt money flows influenced market returns, especially in commodity markets which are relatively small in size. While we like to think that the global equity market is large, it is completely dwarfed by the size and magnitude of both the fixed income and foreign exchange markets. And the equity market is larger than the commodity markets, so when you have billions of dollars chasing a smaller commodities market, it is inevitable that these speculative money flows will bias commodity prices higher. This fact is particularly true as purchases of commodities are no longer done just to meet physical demand (i.e. industrial use), but for investment purposes as well. The amount of choice investors have today to invest in various asset classes is staggering compared to even 5 years ago. The expansion of such choice has led to money flowing into asset classes that haven't seen such money flows before; therefore, we are seeing increased volatility in those asset classes as well.

Overall 2009 was what we would call a pleasant surprise. We will certainly not complain about the returns that were posted as we were more than happy to have some of our predictions prove too conservative.

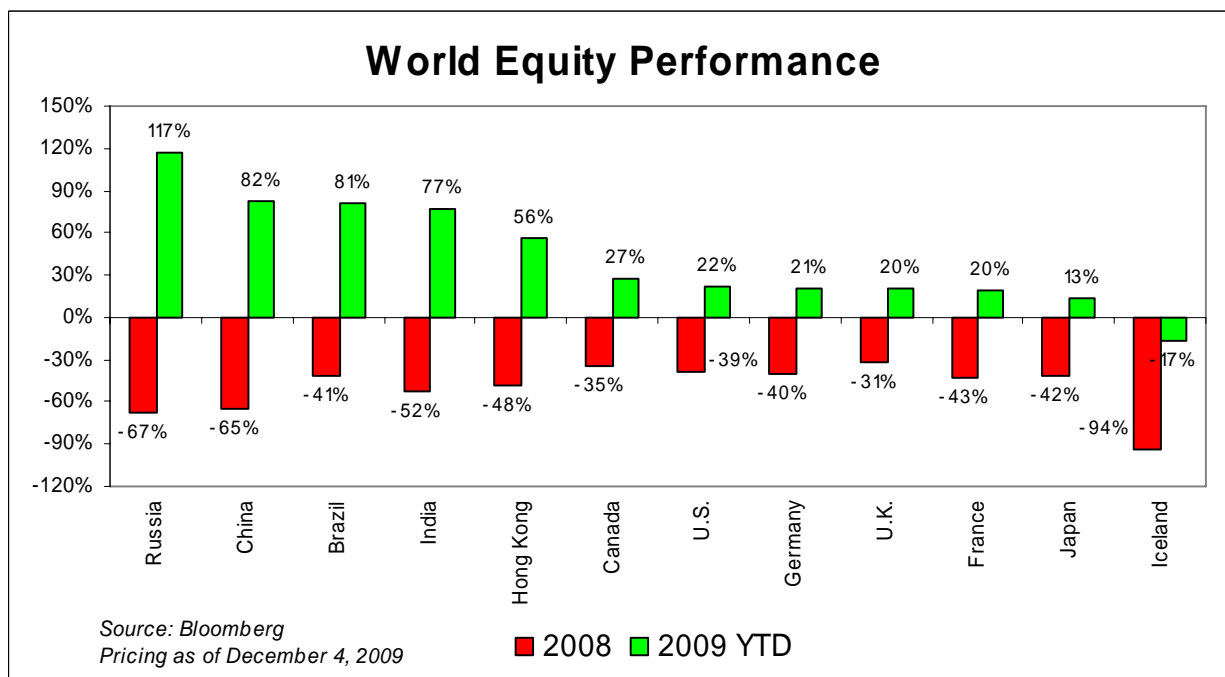
The Present

Even though investors feel better about 2009 than they did about 2008, it's important to step back and take an honest and hard look at where we actually stand when it comes to the stock market, the credit crisis, the economy, monetary policy, fiscal policy, the currency market, and Canada's standing amongst its peers. In these areas of discussion we make the following conclusions:

- Equity markets worldwide have rebounded nicely off their lows
- The absolute worst of the credit crisis is likely behind us, but problems will persist for years
- Government and central bank intervention appear to have averted a depression
- Interest rates are at all time lows and will remain there for months
- The recession technically ended in the third quarter for North America, but the recovery could be sluggish
- U.S. dollar weakness has pushed commodity prices higher and speculators have returned to markets they briefly abandoned
- Canada emerged as a winner during a difficult time

Equity markets worldwide have rebounded nicely off their lows:

As you can see in the chart below, 2009 was much kinder to equity markets than 2008 as all of the world's major exchanges have posted gains. Markets which posted the worst returns last year posted the best returns in 2009. This is evidence that we tend to over buy markets on the way up and over sell them on the way down. It also reflects the expectations and risk-reward tradeoff that exists with emerging market economies such as Brazil, Russia, India, and China (otherwise known as the BRIC countries). Investors were anxious to leave the emerging markets when the recession hit, but when signs of economic recovery began to emerge in 2009 they were the first markets investors embraced. We also highlight that Canada not only posted one of the smaller losses amongst industrialized nations in 2008, it also led gains within this group in 2009 thanks to its commodity based economy and responsible financial management.



The absolute worst of the credit crisis is likely behind us, but problems will persist for years:

Is the credit crisis over? Absolutely not. Any investor that believes the credit crisis started when Lehman Brothers filed for bankruptcy would be incorrect. Believe it or not, the origins of the credit crisis can be sourced all the way back to the earlier part of this decade when U.S. banks started to underwrite subprime mortgages. It wasn't until mid-2007 that homeowners began defaulting on these mortgages and the U.S. housing market went into freefall. So it wasn't bank failures that led to the credit crisis, it was the U.S. real estate market that put us in the credit turmoil that still persists today. What originated as a real estate crisis morphed into a corporate credit crisis after Bear Stearns, Lehman Brothers, Freddie Mac, Fannie Mae and AIG all went bankrupt. It was this shock that accelerated and accentuated the economic recession since it's hard to provide capital and liquidity to your economy when your banks have no money to lend. From September 2008 to February 2009 it was exceptionally difficult for any corporation to raise money, especially at terms they found acceptable. This was the worst of the credit crisis as the flow of money within the global financial system had dried up and governments/central banks were forced to intervene and provide that liquidity. Since March, with stock market conditions improving, companies have found it increasingly easier to raise capital but the accentuation of the economic recession has done little to improve the balance sheets of individual consumers, especially those in the United States that have lost their homes, their jobs and can't get a dime of credit from their bank. The corporate credit crisis exacerbated today's current consumer credit crisis. Therefore, not only is the credit crisis not over, it's going to take years before credit conditions get "back to normal". While the absolute worst may be over with the corporate credit crisis, we still have a lot of work to do.

Government and central bank intervention appear to have averted a depression:

While anyone can debate the policies that were used or the dollar amounts spent, it is quite clear that government and central bank intervention from September 2008 onwards averted a depression. How do we know? Because we're not in a depression now and it would appear that most of the world's economies are showing signs of growth instead of contraction. There is no exact science to determine how much of an effect interest rate policy, fiscal stimulus, bailout packages, or central bank liquidity injections had on market and economic activity, but at some point in time during 2009 they began to work for the better.

Interest rates are at all time lows and will remain there for months:

One of the policies used by central banks to minimize the damage was the reduction of interest rates. This policy has left rates at all time lows in some of the world's largest countries/regions. The rate cuts were not as effective as they might have been in previous recessions as many financial institutions simply did not have the cash to lend at such low rates, but now that the global economy appears to be improving and money is flowing more freely, rate cuts will have a more meaningful impact. Considering that the U.S. consumer has been slow to recover from the recent downturn, it's unlikely that U.S. interest rates will increase in the immediate future. The same can be said for Canadian interest rates, but our higher dollar may be a more important factor prohibiting higher borrowing costs. With that said, all investors and consumers must be aware of the fact that interest rates here and in the U.K., Europe and Japan have nowhere to go but up. So while low rates provide cheap borrowing at present, those costs will inevitably increase. Believe it or not, rate increases are not necessarily a negative event. This may sound like a bizarre statement to make, but remember that interest rates are used to stimulate the economy when it slows or contracts. Conversely, rates are also used to slow a growing economy, thereby keeping it from overheating. From our perspective, when central banks eventually decide to raise rates, we view this as a positive signal that likely signifies that the economy has gained traction and that growth has fully resumed.

Various Central Bank Interest Rate Cuts since 2008

	Rate as of Jan 1/08	Rate as of Dec 1/09		Difference
Bank of Canada	4.25%	0.25%	↓	400 bps
U.S. Federal Reserve	4.25%	0.25%	↓	400 bps
Bank of England	5.50%	0.50%	↓	500 bps
European Central Bank	4.00%	1.00%	↓	300 bps
Bank of Japan	0.50%	0.10%	↓	40 bps

Source: Bloomberg

The recession technically ended in the third quarter for North America, but the recovery could be sluggish:

Recent data out of the United States and Canada indicate that both economies expanded in the third quarter of 2009, thus “technically” putting an end to their respective recessions. But we use the word “technically” because the end of the recession is no guarantee that everything is fine. Unemployment will continue to be a problem as will the ability of U.S. consumers to increase their spending. Canadians may not face the same problems as Americans as we did not have a real estate crisis that eliminated home equity and spending power; nor did the average Canadian encumber themselves with excessive debt. But we care about the state of the U.S. economy as the U.S. is still our largest trading partner by far. If the U.S. is hurting then it’s hard for Canada to recover at the same time. Further along in this report we will provide you with data that suggests U.S. consumer spending continues to be under pressure and may stay restricted for some time to come.

U.S. dollar weakness has pushed commodity prices higher and speculators have returned to markets they briefly abandoned:

It wasn’t that long ago that we saw a great deal of speculation in the commodity markets. Many investors will remember the days of US\$140+ per barrel of oil and how oil prices were actually climbing when the U.S. economy started to contract. How could this be? While we would like to think that fundamentals drive commodity prices, speculation is also a contributing factor. We believe that speculators returned to the commodity markets earlier this year after a brief disappearance following the collapse of so many hedge funds in 2008. This became all too evident to us when supplies were increasing, yet so were prices. Markets are supposed to be forward looking, so pushing commodity prices higher when the fundamentals suggest otherwise may be a precursor to future demand increases, or it could be simple price manipulation to make a quick dollar. Either way, speculation will always be a part of the commodity markets due to their relatively small size and will always lower the predictive ability of fundamental analysis.

With all this said, there was another significant factor at play in moving commodity prices and that was the downward direction of the U.S. dollar. Simply put, if most commodities are valued in U.S. dollars and the value of that dollar declines then theoretically you need less of that dollar to buy the same quantity of any given commodity. As such, commodity prices increase when the U.S. dollar weakens and vice versa. When risk tolerance started to change in March and investors decided to move out of the U.S. dollar, commodity prices appreciated. This U.S. dollar weakness only accelerated in the second half of 2009 as investors were even more risk tolerant and concerned about the outlook for the U.S. economy and its growing debt levels. We certainly

can't attribute all of the strength in 2009 to currency translation, but it was a significant factor. While many investors believe that investing in Canada was a play on the economic recovery, we'd argue it was more a play on U.S. dollar weakness through the equity market.

Canada emerged as a winner during a difficult time:

Investors will wonder how we can make such a statement when we are in the midst of creating the largest deficit in Canadian history. While it is true that we will have a record deficit in the current fiscal year, it is not fair to make a comparison between today's deficit and deficits of the past in absolute terms. Instead, it is useful to compare the size of our deficit or debt to the size of our economy (GDP). As an example, it is expected that our debt to GDP ratio in Canada will likely range somewhere between 25% and 35% over the next three years. However, this compares to our last growing deficit in 1992 when our debt to GDP ratio was 64.1% and our peak debt to GDP ratio in 1996 of 68.4%. While our spending has increased during our recent recession, the debt raised to finance it is manageable.

In addition to our debt levels, we have also been better at keeping our fiscal books in order at both the Federal and Provincial level. Canada's federal deficit is expected to reach about \$55 billion this year which would equate to about \$1700 per Canadian. Contrast that with the U.S. where a projected deficit of \$1.5 trillion would equate to \$4870 for every American. Deficit spending is needed during a recession to stimulate the economy as governments need to spend when consumers are unwilling to do so. Indirectly, governments spend our money for us through our tax dollars, but if there isn't enough money to go around then issuing debt is necessary. Not only is our Federal government in better shape, but our provinces are doing relatively better than what we're seeing in some U.S. states. While we recognize that the situation in Ontario has only worsened with time, we can be happy that we're not California which almost went bankrupt earlier in 2009.

Finally, in addition to our better fiscal bill of health, Canadians can take pride that our financial system withstood the worst shock since the Great Depression 80 years ago. Our financial institutions were forced to write down some investments, but the dollar figures involved in this country paled in comparison to what we saw in Europe and the United States. The conservative nature of our banks and oversight by regulators at the Office of the Superintendent for Financial Institutions (OSFI) established a structure and mentality within our financial industry that steered us away from taking excessive risk. While the recession in Canada has impacted the finances of all Canadians, the credit crisis experienced in this country still left people with equity in their homes and some form of accessibility to credit. This contrasts to the United States where home equity has been destroyed and access to capital has been difficult to achieve. Canada used to be criticized for being too conservative in the past; however, in hindsight most Canadians are happy that we endured such criticism as Canada has been recognized for having the best financial system in the world for the past two years.

The Economic Argument

In the discussion that follows we will try and provide you with a process in which you can evaluate the global economic recovery and thus reach your own conclusion as to what may or may not happen in the equity markets in the next 12 to 24 months.

Before we provide you with such an argument, we must make one point particularly clear. While it is true that countries such as China have provided a great deal of strength to the global economy this decade, we do not believe we can have a full economic recovery without the U.S. economy on side as it is still the largest economy on the planet. More importantly, we must have the western world growing in addition to the emerging markets as it is the consumption of North America, western Europe and Japan that helps support emerging markets. Admittedly, domestic investment has helped these emerging economies tremendously, but international trade is a component that can't be ignored. So while China steals the headlines for its impressive growth profile, it is still only one piece of the larger economic puzzle.

With that established and while we are not trying to oversimplify a complex issue, our argument is that there are two parts of an economic recovery – the Producer recovery and the Consumer recovery. As such we believe we cannot have a sustainable economic recovery and sustainable equity market gains unless both the Producer and Consumer participate.

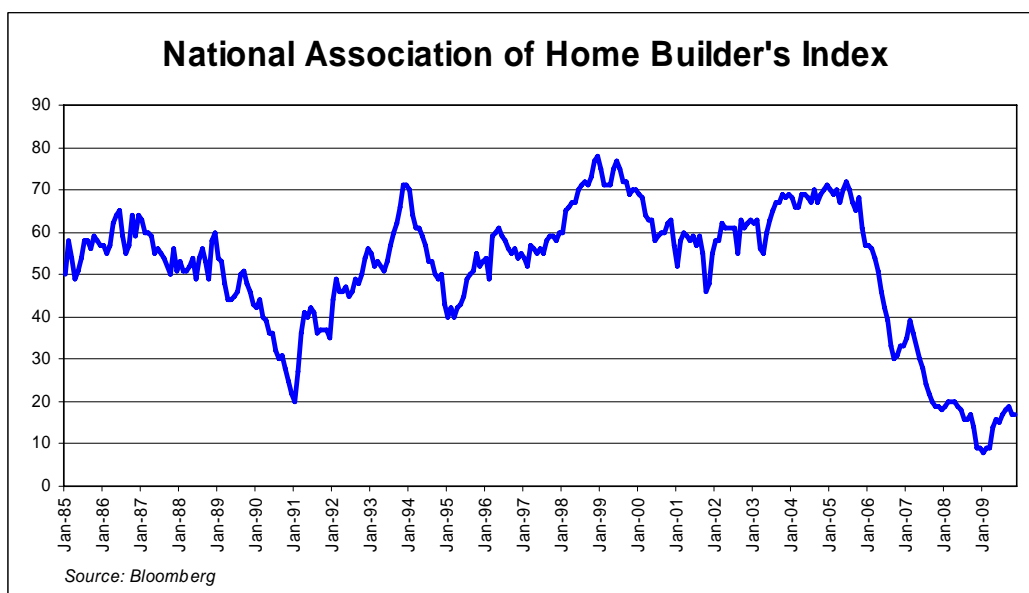
By Producer we're referring to those businesses and countries that "make stuff". They are the creators of goods and services that actively trade on a global scale. It should come as no surprise that over the past few decades, with increased globalization and a shift to low cost producing nations that the emerging markets are now responsible for a lot of the goods and services that the western world consumes. Therefore, it should come as no surprise that countries like China and India have seen a pick up in economic activity before the western world because they have to "make stuff" before we can "consume stuff". Recent economic statistics would reinforce this view as the Chinese economy slowed only for a short period of time. We are even seeing producer related activity in the United States improve as metrics such as the ISM Manufacturing Index and ISM Non-Manufacturing Index have hovered near the 50.0 level thus indicating economic expansion. However, with this pick up in activity we must ask ourselves whether or not we have seen an actual and sustainable pick up in consumer demand or whether this increased activity is a result of businesses restocking inventory in the hope that individuals will increase their consumption rate after last year's retrenchment. While the debate over this question still continues, what is clear is that Producers are "making stuff" again and therefore buying commodities and other input materials which has put upward pressure on commodity prices and helped the TSX Index.

Is the recent pick up in economic activity here to stay on a more sustainable basis? The wildcard to this question lies with the Consumer. In the discussion that follows we will focus on the U.S. Consumer due to his/her influence on U.S. economic growth. While it is true that recent producer metrics have been better than expected, we cannot say the same for consumer metrics such as consumer confidence, retail sales and U.S. home prices. As such, investors are not convinced that the recovery will be quick and robust. Simply put, if the Consumer does not have the capacity to increase his/her rate of consumption then it's going to be very difficult for the economic recovery to accelerate. By capacity we mean the ability of the Consumer to spend the money they have and to get access to capital they need. When individual wealth declines, the capacity to consume declines with it.

We include home prices in this discussion as they are one of the best indicators of individual wealth. Chances are the largest asset you own is your home and the value of your home is a reflection of your own personal wealth and your ability to secure further financing if required. While we have not faced a real estate crisis in Canada, we cannot say the same for the United States where home prices in some regions of that country fell at one point by over 50%. Think for a moment how you would react if I told you that your home was only half of what you thought it was worth? If you bought a home for \$500,000 and it was worth \$250,000 today would you be rushing out to buy a car? Likely not, especially if you have a mortgage of \$400,000 on that house which means that your mortgage is worth more than your home and that you have negative equity in the most expensive asset you own. Such a situation is unfortunately not uncommon in the U.S. In fact some projections indicate that by mid 2010, over 30% of mortgages south of the border could be under water (home price worth less than the mortgage). In previous recessions, Americans have not necessarily seen a collapse of the housing market at the same time, so they've been able to borrow and consume their way back to economic expansion. However, considering the state of the financial system in the United States and the fact that so many Americans have absolutely no equity in their homes whatsoever, banks are simply unwilling to lend money to consumers because they have no assets to act as collateral. This inability to obtain financing reduces their capacity to consume no matter how much they want to buy. This is why we place such high importance on home prices going forward because they will be vital in the wealth restoration process for Americans. While home prices will recover one day, the question remains how long it will take for that recovery to take place? Considering that there is so much supply in the U.S. housing market at present, we suggest it will take longer than some investors think and thus the rate of consumption will not increase materially in the near future. We've also seen the end result of the infamous "subprime" mortgages in the United States, but we're due to see more mortgage resets amongst Alt-A and Option Arm mortgages over the next couple of years which could cause more foreclosures, could increase housing supply and thus keep housing prices depressed.

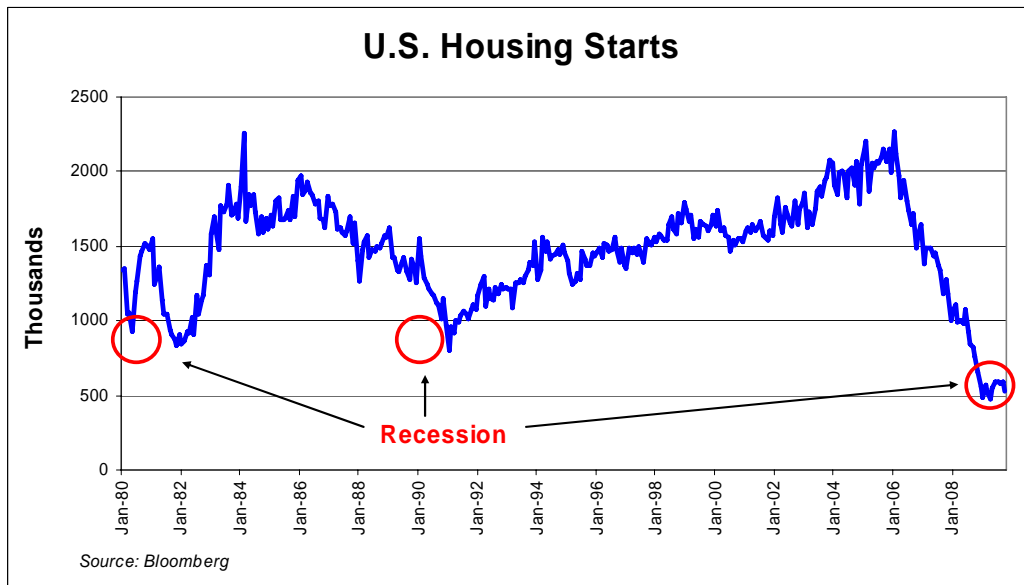
To provide more colour on the poor housing situation in the United States, we provide the following charts.

The National Association of Homebuilders Index is essentially a sentiment index that depicts sales expectations. A level of 100 is good, and 0 is bad. While this index has bounced slightly in 2009, it is still sending us an overwhelming message that expectations remain depressed going forward.

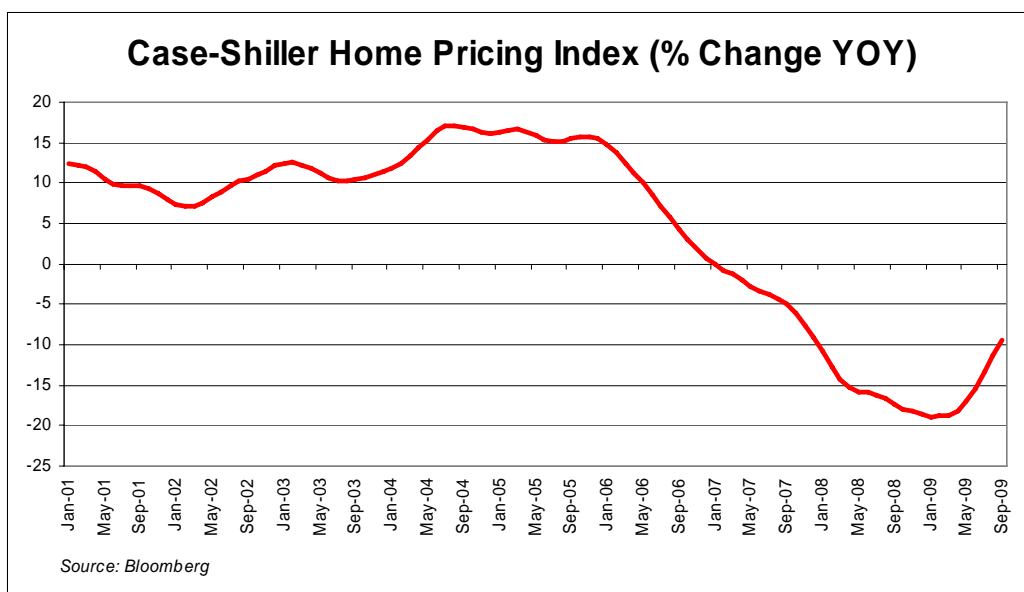


2010 Outlook

Usually when an economy is strong, the number of homes built increases and vice versa. As you can see in the chart that follows, not only have U.S. Housing Starts reached the lowest levels in 30 years, they are currently stuck in the 500,000 to 600,000 range. While this is a bad indicator in the short term as fewer homes are being built, it can also be viewed as a good thing for the long term as it indicates that homebuilders are waiting for excess supply in the resale market to decline before building new homes and adding to supply concerns.

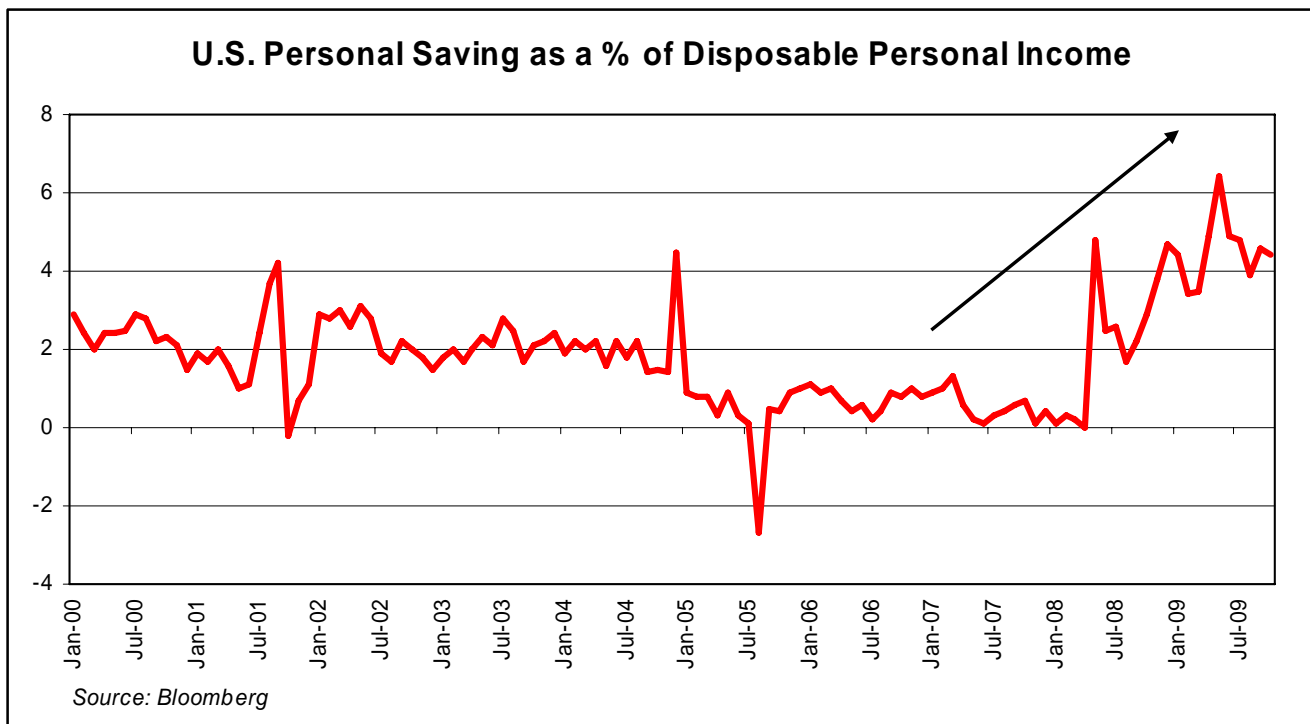


Finally, the Case-Shiller Home Price Index which measures the year over year changes in average home prices within the 20 largest real estate markets in the United States. While recent data has been encouraging as home prices have been declining at a lower rate, they're still declining year over year. On a month over month basis, data would suggest that U.S. home prices are actually starting to rise again, but at such a marginal rate that we don't believe it will have an impact on consumer behaviour in the very near future.

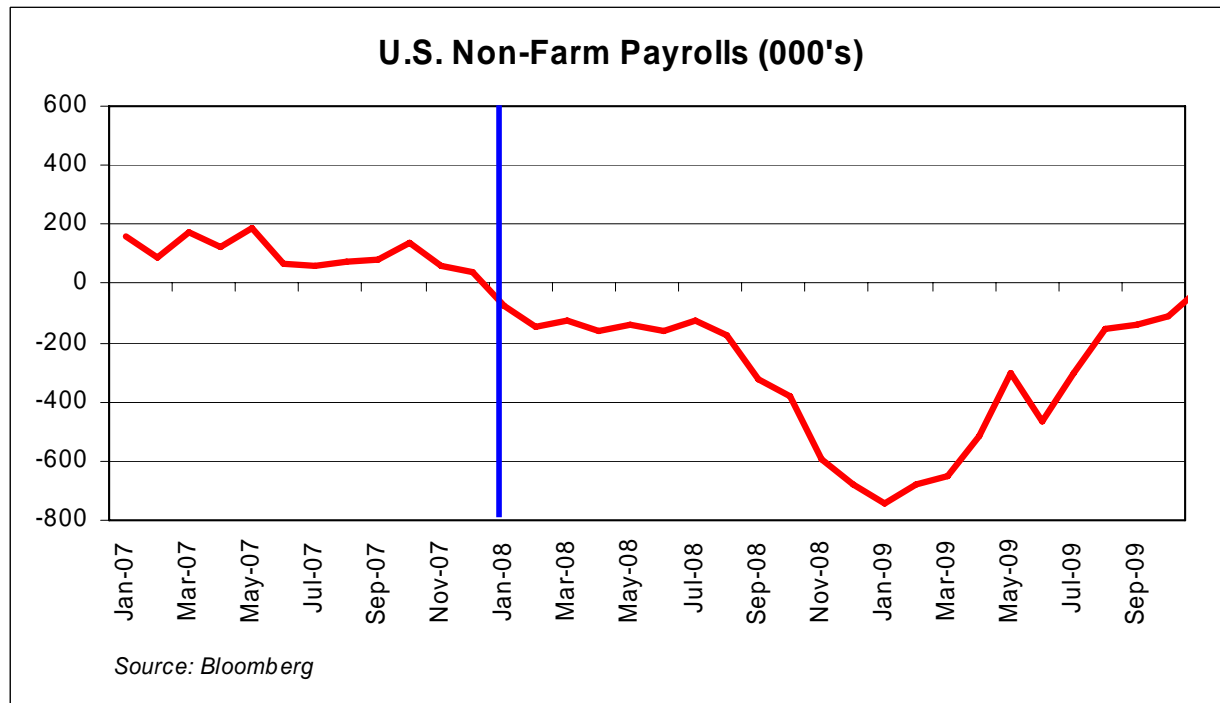


In some of our reports over the past year we have continuously emphasized that since about 70% of aggregate demand in the United States comes from domestic consumption, the U.S. consumer is going to have to be a significant participant in any economic recovery. However, in addition to the effects of housing noted above we are seeing other consumer related metrics suggest that an economic recovery could be sluggish.

While Americans tend to be known for their spending habits, recent data would suggest that U.S. consumers are actually starting to save again. In the chart that follows you will see that the amount of personal income that is now being saved has increased since mid-2008 and the savings rate for Americans is at the highest it's been all decade. While such saving will have a positive influence for U.S. consumers over the long term as they rebuild their own balance sheets, it does little to help the U.S. economy in the short term as Americans are choosing to save rather than spend.



The employment picture in the United States also does not bode well for a quick near term rebound in spending. The unemployment rate is in double digits and while fewer jobs have been lost over the past few months, they are still being lost which means that fewer Americans have more disposable income to spend. While we recognize that employment statistics can be a lagging indicator, we must not ignore their importance when it comes to the ability of the general public to not only spend, but increase their consumption to pre-recession levels. We have not seen job growth in the United States since late 2007 and while such growth will return in 2010, it may not grow fast enough to change consumer behaviour in the immediate future.



After reading this section of our report, some of you may conclude that we are bullish on production and bearish on consumption. Believe it or not we actually disagree with that conclusion as there are big “ifs” that accompany such a statement. We are bullish on what we’ve seen on the production side of the equation as long as it is a result of a sustainable global pick up in consumer demand. Are you making “Product A” because consumers actually want more of “Product A”, or are you producing it because the effects of the recession have slowly dwindled inventories of “Product A” to the point that businesses need more production just to be sustainable? Remember, we never bring our rate of consumption to zero in a recession, we merely reduce it. So do we need more of “Product A” because our rates of consumption have increased or because we’ve used up all available supply at our current rate of consumption?

Most of our discussion about the consumption side of the equation has focused on the risks that currently exist with the Consumer. But don’t get us wrong, we’re not saying the Consumer can’t recover, we’re just saying that he/she still face a number of hurdles which need to be overcome before a permanent change in consumer behavior happens for the better. We hope such a change does happen, but it is our job to inform you not only of the benefits of investing in the market but of the risks that exist as well. As far as we’re concerned, more risk exists amongst Consumers than it does amongst Producers, so we cannot decide conclusively that Consumers are back on board and that a robust and sustainable recovery is imminent. We want a solid recovery just like anyone else does, but it is vitally important for every investor to remember that “risk” has not disappeared just because stock markets rebounded. Risk is always present even in good times, but when we’ve just come out of the worst financial failure in 80 years, we feel it’s our responsibility to remind investors about risk and to make sure it’s handled in the most appropriate way.

So What Now?

Now that you've read our argument and we've given you many different factors to think about, the next question that may come to mind considering all this information is "so what now?" We believe there are 3 scenarios that could play out in 2010: the "V" shaped recovery, the "W" shaped recovery (the double dip recession), or the "Goldilocks" scenario (sorry if we're making you think back to your bed time stories).

V-Shaped Recovery

A V-shaped recovery naturally resembles the letter "V" in the alphabet and these bullish investors believe the market will recover as quickly as it fell. These investors believe that regardless of unemployment and lower real estate prices, Consumers have already started to line up and spend once again (perhaps not the case according to U.S. holiday sales forecasts). For this to be true, the recession had little impact on the lower and middle class and access to credit is rapidly improving. Evidence would suggest this is not the case. However, if we do start to see rising employment, higher than expected retail sales and material improvements in the U.S. real estate prices over the next couple of months, these investors could actually be correct and the rally we've seen thus far could be sustainable. In such a case Financials, Energy and Materials stocks will continue to rally while Defensive industries will remain depressed due to sector rotation. Naturally the opposite is true if the bulls are wrong in that cyclical stocks could give back some of their recent gains.

W-Shaped Recovery (double dip recession)

A W-shaped recovery naturally resembles the letter "W" in the alphabet and these bearish investors believe that while Producers may be back producing, Consumers are in no mood to start consuming again. High unemployment, low credit availability and negative home equity have reduced their desire to spend. These investors also believe that Consumers are trying to live within their means and may have made some permanent spending habit changes during this process. If the Consumer stays away and Producer inventories are replenished, then economic activity could stop once again until the Consumer inevitably increases spending down the road. Creating jobs and materially higher home prices will not happen in the next couple of months. If the bears are correct then you will likely see a material pull back in cyclical stocks over the next 6 months while money could rotate back into defensive industries that offer stability, and in most cases, a decent yield.

The "Goldilocks" Scenario (not too cold, not too hot, it's just right!)

While there is no letter to describe what these investors expect to happen, they find the middle ground in that they recognize Producers have ramped up economic activity but don't feel the Consumer will stay away for an extended period of time. While the Consumer may not return to pre-recession spending levels in 2010, we could see increases in spending as we progress over the next 12 months. However, such increases could be slow and gradual resulting in a sluggish economic rebound as opposed to rapid rebounds we've seen coming out of previous recessions. If these investors are correct then commodity stocks have likely rallied too quickly in 2009 and could be victims of short term profit taking as we go into 2010. Financials will also come under some pressure, but Canadian financials should hold up well compared to their international peers. Some money flows will find their way back to defensive industries, but not on a permanent basis as investors will be patient until it appears as though the Consumer has returned to the market. While it's easy to take the middle road, we tend to share the views of the Goldilocks scenario which we believe acknowledges both the positive developments of 2009, but also the risks that still remain in the global financial system and economic recovery.

Economic Outlook

The economic outlook for 2010 from Scotia Economics is much better than what was forecast for 2009 since most of the world's economies that were in recession should see economic expansion over the next 12 months. We should also see further expansion from countries such as China and India which were strong enough in 2009 to avoid economic contraction. As you can see below, our economists are forecasting that overnight interest rates in Canada and the U.S. will start to increase once again in the third quarter of 2010, finishing the year up 100 basis points at 1.25%. They also believe the upward trend for the Canadian dollar will continue as parity should be reached on a more sustainable basis by the second quarter.

Scotia Economics Forecasts as of December 1, 2009

Real GDP (% change)	2008	2009f	2010f	2011f	
Canada	0.4	-2.6	2.7	2.8	
United States	0.4	-2.5	3.3	2.5	
Japan	-0.7	-5.3	1.3	0.9	
United Kingdom	0.7	-4.5	1.2	1.1	
Euro Zone	0.8	-3.8	1.3	1.1	
China	9.0	8.3	9.5	9.0	
India	6.7	6.8	7.0	6.5	
Brazil	5.1	0.5	5.0	5.0	
	Q4/2009	Q1/2010	Q2/2010	Q3/2010	Q4/2010
Bank of Canada Rate	0.25	0.25	0.25	0.75	1.25
Federal Reserve Rate	0.25	0.25	0.25	0.75	1.25
Canadian Dollar (USD/CAD)	\$1.04	\$1.02	\$1.00	\$0.98	\$0.97
Canadian Dollar (CAD/USD)	\$0.96	\$0.98	\$1.00	\$1.02	\$1.03

Source: Scotia Capital Economics

Where is the Canadian Dollar Headed in 2010?

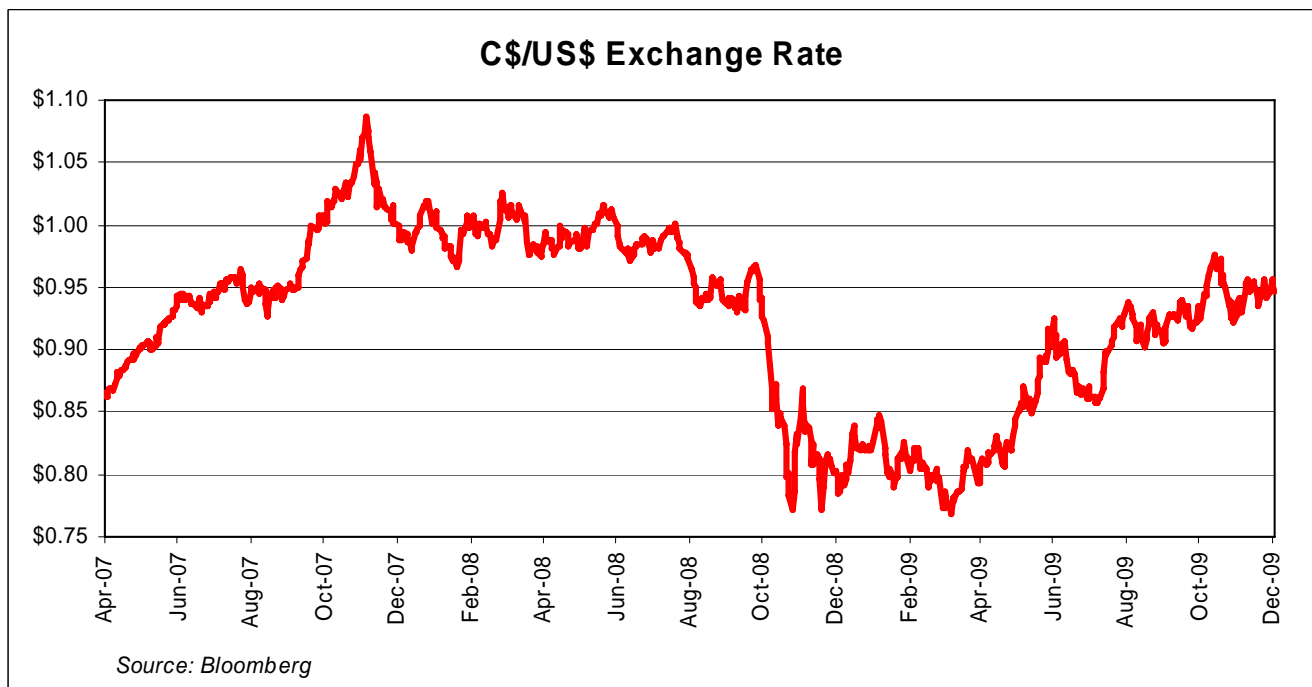
The simple answer is "higher". There are a few factors that contributed to Canadian dollar strength in 2009 that should continue in 2010.

1. **U.S. dollar weakness:** We remind investors that currency movements are dependent on relative views between two countries. Investors have been moving away from the U.S. dollar as they do not like what they see from an economic and fiscal standpoint. This movement has strengthened the Canadian dollar, not because Canada is so much stronger, but because the U.S. has been relatively weaker.

2010 Outlook

- Commodities:** Where we can make an argument for Canadian dollar strength is in the realm of resources as we are perceived to live in a commodity based economy. But the strength in commodities is in part a function of U.S. dollar weakness in the first place. Where Canadian strength comes into play is if global demand for resources continues to increase as commodity prices appreciate for fundamental reasons rather than currency translation.
- Better Fiscal Outlook:** As already discussed earlier in this report, while we are currently accumulating the largest deficit in Canadian history, Canada's debt levels are still manageable when compared to what we're seeing in the United States. As long as Canada keeps its books in check, it should provide further stability, if not further strength for the Loonie going forward.

Considering that the United States has a long way to go to get its fiscal house back in order and Americans still have a long way to go to get their own personal balance sheets back in order, we expect the three themes above will continue to be relevant in 2010.



Canadian Equity Market Outlook

In order to properly examine where the TSX may lead us in 2010, we must first understand its composition. As of November 30, 2009, the TSX was weighted to the following sectors point of the economy. We also show each sector's contribution to 2009 returns during the first 11 months of the year.

S&P/TSX Index Breakdown by Sector

	Weighting in the TSX Index	Point Contribution to the TSX Index Jan 1 to Nov 30	
S&P/TSX		2459.50	
Financials	30.5%	887.19	36.1%
Energy	27.1%	658.74	26.8%
Materials	20.3%	726.29	29.5%
Industrials	5.5%	72.88	3.0%
Telecommunications	4.4%	-45.10	-1.8%
Consumer Discretionary	4.3%	65.59	2.7%
Technology	3.2%	66.91	2.7%
Consumer Staples	2.7%	9.22	0.4%
Utilities	1.5%	-0.49	0.0%
Health Care	0.5%	18.27	0.7%

Source: Scotia Capital, Bloomberg

It should come as no surprise that with the recovery in Financials, Energy and Materials that these three sectors continue to make up a substantial portion of the TSX Index. For that reason most of our forward looking commentary will focus on these sectors, but we will touch on others as we look forward to 2010.

Financials

Banks

Following their fiscal year end earnings reports in December, the Canadian banks yet again provided evidence that they were in better financial position than their international peers, that dividend policies were not in jeopardy, that risk was managed more appropriately in Canada, and that Canadian banks were profitable in a difficult economic and financial environment. The Canadian banks continue to execute well and their financial strength has only improved. In fact, one could easily argue that capital levels at the Canadian banks are too high and that shareholders are not earning enough return for the extra capital that has been raised over the past 12 months. It is for this reason that we believe the banks may make acquisitions over the coming year or return some of that capital to shareholders in the form of share buybacks or even dividend increases. Yes, that's correct, dividend increases. While some investors fretted at the prospect of dividend cuts last February, we cannot rule out the possibility that shareholders could see a return to dividend increases over the next year if the banks can't find a more efficient use for their capital. While the operating environment for the banks still remains challenging as the world emerges from recession and while credit concerns still linger, their diversified

revenue streams have provided stability and should continue to do so for the foreseeable future. It's also quite possible that we may have seen the peak in loan loss provisions for the current cycle and if this is true then Canadian banks can only benefit as earnings leverage will increase. While it is conceivable that the Canadian banks could fluctuate in price over the coming quarters as high expectations have already been built into their share prices, we are bullish on the Canadian banks and encourage investors to maintain their banks holdings as long as their weightings within their portfolio are appropriate. While investors should not expect a repeat of 2009 share price performance in 2010 as the market has already rewarded Canadian banks for their operating outperformance, they still remain in a position to grow earnings. If this is the case and we keep valuation multiples constant then we should see capital appreciation for the Canadian banks over the next year.

Life Insurance Companies

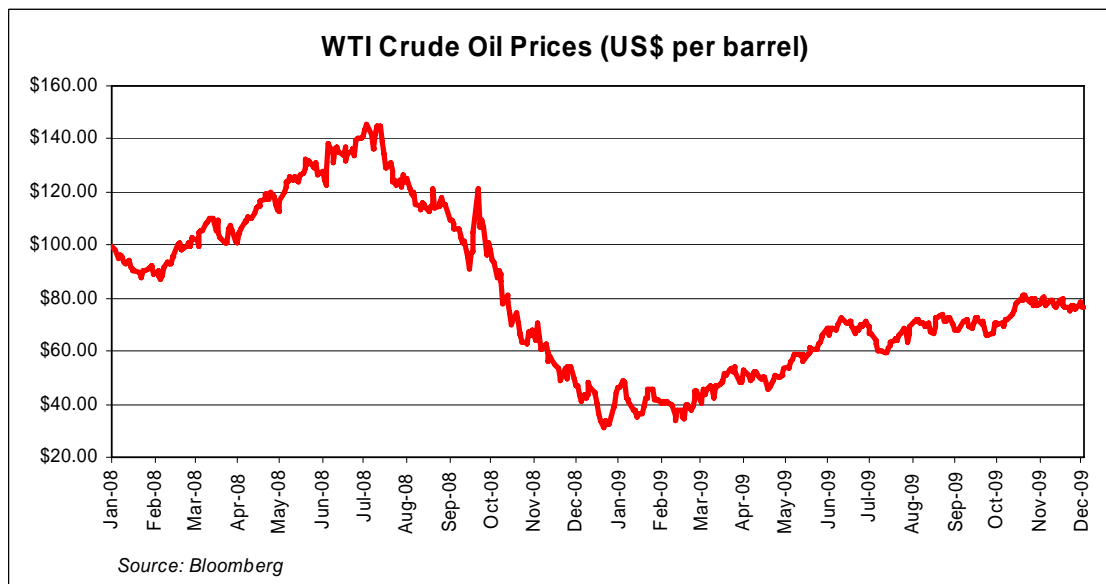
On the other side of the financial equation are life insurance companies such as Manulife Financial, Sun Life Financial and Great-West Lifeco. These companies have not been treated as well as the Canadian banks over the past year as depressed equity and turbulent credit markets resulted in many writedowns. Furthermore, investors were not amused by the surprising dividend cut and massive equity issues out of Manulife. However, following such a difficult year for this industry, are these companies bad investments? A few months ago, we would have said no as the market appeared so distracted by offsetting credit losses and recent equity gains that it may have lost sight of the underlying insurance business which is holding up reasonably well in a difficult environment. But the most recent \$2.5 billion equity issue out of Manulife has caused us concern as we cannot be certain there are not more structural issues impacting the finances of these companies. Admittedly our concern lies mostly with Manulife as Great-West Lifeco's share price performance and earnings for that matter have held in quite nicely relative to its peers. But if there are some concerns at Manulife then we would expect all life insurance companies to experience these problems to differing degrees. The much longer term outlook for a Manulife or Sun Life does look better if equity and fixed income markets continue to recover and expansion plans into other markets are efficiently executed. Such transformational growth will take time to achieve, but it would appear as though the seeds for growth are being sown as they try and diversify away from the more mature North American market. So again, are life insurance companies a bad investment? We would still answer that question with a no, but we will readily admit that we would much rather own a Canadian bank at this stage as they offer better transparency in our view and a better earnings track record. Great-West Lifeco would be our preferred name amongst the big three life insurance companies at this time.

Energy

Crude Oil

Throughout 2009 we expressed some reservation about the speed at which oil prices appreciated from a fundamental perspective. While prices have not pulled back to a great extent, they haven't appreciated much either during the second half of the year even with further U.S. dollar weakness. Perhaps this is a recognition that oil prices were too high, but investors were too reluctant to sell in case the rally continued. What is obvious is that speculators have returned to the market and that financial investing is possibly outweighing physical purchases. We still believe that inventory levels are too high and that demand is not strong enough yet to justify where oil prices trade today; however, as previously mentioned, markets are forward looking so perhaps speculators are telling us we have some good economic times to look forward to over the next 6 months. In the short term, barring any unexpected major supply disruptions, economic uncertainty and high inventory levels

will likely limit near term gains in the price of oil. However, we are of the view that if a pullback were to occur or if we consolidate at current levels until signs of an economic recovery strengthen, such a scenario would present an excellent long-term buying opportunity. This would allow investors to capitalize on the seasonally stronger spring period for energy stocks as well as the bullish longer-term supply fundamentals that are extremely supportive of the underlying commodity price. We strongly believe that under-exploration over the past few years as a result of budget constraints, increasing reliance on unconventional resources that tend to be more costly to produce, and the eventual uptick in the global economy all lend to the notion of higher crude prices over the longer term.



Natural Gas

Natural gas prices look even worse on a near term basis than oil prices as inventories continue to rise. Increasing supply will continue to be a dominating theme for the commodity. Aside from high inventory levels, the onslaught of liquid natural gas (LNG) supply and the emergence of shale gas will prove to be major headwinds for natural gas prices going forward. However, at some point natural gas prices will revert back to their marginal cost of production which will help normalize them over the long term. With this in mind there may be an opportunity for long term investors; however, we think those long term opportunities are greater with investments in crude oil at this time. As such, we recommend that investors looking to play the Energy sector buy equities that are more weighted to crude oil production over natural gas.

Materials

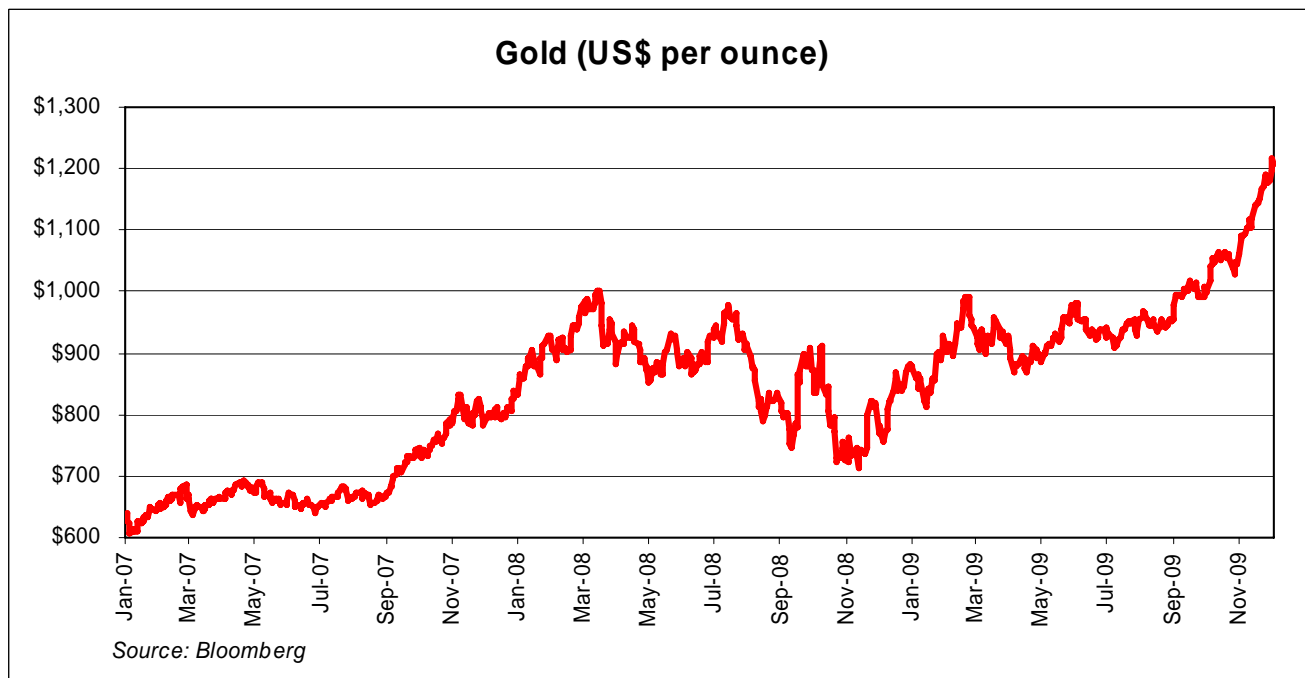
Base Metals

Base metal equities have behaved in a similar fashion to energy equities in that they're both sensitive to the global economic recovery; therefore, most of what we've argued above for oil is similar to what we'll argue here for base metals. While base metal prices have appreciated over the past year thanks to increased demand, U.S. dollar weakness and speculative premiums, fundamentally speaking we are not convinced that supply/demand fundamentals are strong enough to justify such increases in the short term until we see an

increase in U.S. consumer spending which has yet to materialize. In fact it's interesting to note that as prices for aluminum, copper and zinc increased during the second half of 2009, so too did their inventory levels at the London Metals Exchange. Either prices will have to come down if inventory levels continue to rise or consumption will have to increase to draw down those inventories and justify current pricing. With our short term caution we also recognize that it is possible to see additional strength in this sector over the next 6 months if the economic recovery is greater and faster than expected. The emerging markets are starting to show signs of life again and they will be the first to pick up their demand of raw materials, but the western world will eventually have to follow. Longer term, the supply concerns we raise above for oil could become prevalent for base metals as well. It is for this reason that our short term concern becomes more constructive for longer term investors if the economic recovery accelerates.

Precious Metals

We have been bullish on gold since the beginning of 2007 and emphasized gold as an investment opportunity in our 2009 Outlook due to our expectation that the U.S. dollar would weaken further. Considering that we've just hit an all time high for gold prices, we feel our comments from last year have been vindicated. U.S. dollar weakness was our justification for owning gold in 2009 and that view is unchanged going into 2010. In addition, we note that increased investment demand has put upward pressure on gold prices and that will not change until the U.S. dollar strengthens. One day the U.S. dollar will eventually rebound more sustainably, but we do not believe that time is now. While we are not the gold bugs that believe prices are going to US\$4000 an ounce, we do believe that there is support for average gold prices around the US\$1100 level in 2010. Admittedly, gold prices could easily retreat below this level in the first few months of the year due to seasonality or due to a short term spike in the U.S. dollar if the economy improves more than expected. However, the time for US\$1000 + gold prices is not over just yet! Our views on gold can be repeated for silver as U.S. dollar weakness has been a driving factor for that precious metal. Therefore, we believe that support for silver prices should also continue into 2010.



Fertilizers

When an investor puts money into fertilizer stocks, they must understand that there are many short term factors that can impact grain prices and thus fertilizer equity prices. Weather is the most influential amongst them, so it's always wise to have a long term investment horizon when purchasing stocks in this sector. Not much has changed in the past twelve months when it comes to our outlook for fertilizers as we continue to believe the supply/demand fundamentals for food on this planet help support fertilizer stocks over the long term even though many bumps in the road are likely along the way. Just like other commodity related stocks we've discussed thus far, the short term performance for fertilizer equities remains uncertain; however, in the absence of a double dip recession, we feel that fertilizer stock prices should be higher one year from now.

Technology

While most investors look south of the border for technology stocks as we have very little choice amongst large capitalization names in this country, we continue to recommend Canadian industry champion Research in Motion (RIM) for long term shareholders. The company's recent earnings were not as strong as the market might have liked them to be as selling prices for the company's devices declined; however, we believe this concern is more cyclical in nature as no new devices were launched during the quarter. Aside from the average selling price disappointment, we still saw good earnings and solid subscriber additions. While competition is always going to remain fierce within the cell phone/smart phone market, we believe RIM is well positioned both strategically and financially for the long run.

Consumer Discretionary

This sector is made up primarily of retailing and consumer goods stocks with the exception of food stores and drug stores. It is only logical to assume that if the economy improves then consumption increases and the Consumer Discretionary sector benefits. And while we don't deny that the market has been pricing in these expectations, we still remain concerned about the outlook for the U.S. consumer. However, we also recognize that Canadians have not been impacted to the same extent as Americans since we did not have a real estate crisis wiping away billions in consumer equity. As such, considering that the Canadian economy came out of recession in the third quarter of 2009 we are no longer discouraging investors from looking at this sector. While the economic recovery could be sluggish, we feel the Canadian economy will have enough momentum over the next 12 months to get consumers spending more and profits rising for Consumer Discretionary names.

Industrials

If we are no longer hesitant about Consumer Discretionary stocks then we are no longer hesitant about most Industrials. In fact since most of the pick up in the global economy has come from developing nations it's only logical to feel more bullish on industrial stocks in Canada than Consumer Discretionary. If goods are being produced overseas and resource demand is increasing then the engineering services, railroad, and industrial equipment sectors are likely going to see an increase in business which should translate into increased profitability. We would certainly encourage investors in these sectors to maintain their exposure if not increase it over the course of the next year if they are underweight. If the Canadian economy is firmly back on track

then it might even be time to start rethinking airline and auto part stocks; however, we recognize there is more risk in purchasing these stocks due to lower domestic demand and a stronger Canadian dollar.

Defensives

As a reminder, defensive stocks/equities are those that perform well even when the economy does not. Such examples are Consumer Staples (drug stores and food stores), Utilities, Pipelines and Telecommunications. You still use the services and products provided by these industries even if we're in a recession. You know from previous comments that we're expecting a more gradual recovery in the Canadian and global economies going forward. As such, we continue to recommend that investors maintain defensive positions in a well balanced and diversified portfolio because the financial and economic headwinds we face are not going to disappear entirely in the immediate future. Furthermore, many defensive companies in Canada also have strong balance sheets, good management teams and offer a sustainable and high relative dividend yield. However, we must make investors aware of the fact that since the global economy started to show more signs of improvement, we witnessed "sector rotation" as investors that bought defensive stocks in 2008 started to sell them and buy more economically sensitive cyclical stocks to position their portfolios for an economic recovery. Such a move can provide temporary weakness for defensives, but just because their share prices may fall does not mean they are bad companies and in most cases we see value investors step in and buy them if share prices fall too far. So while we recommend investors maintain exposure to these sectors of the market, we do not recommend that investors overweight defensive industries as sector rotation will have an ongoing influence in the market for the next 6 to 12 months. It's also important to realize that even while investors may be flocking to cyclical areas of the economy, it is also unwise to eliminate your exposure to defensives altogether, especially if you're looking for dividend income. If you have a diversified portfolio you will always have both defensive and cyclical stocks as holdings, but as we progress through an economic cycle it's likely the relative weightings of these sectors will change to reflect the outlook for the economy.

Consumer Staples

In Canada there are really only two types of companies that make up the Consumer Staples sector and those are drug stores and food stores. For 2010 we still favour drug stores over food stores as we believe the industry fundamentals are still more attractive for the drug store industry and the competitive position of Shoppers Drug Mart in particular. Shoppers Drug Mart is Canada's only national publicly traded drug store and has continued to produce consistent earnings growth and cash flow over a number of years which should allow it to outperform in 2010.

Utilities & Pipelines

Companies in this sector tend to have regulated assets and therefore consistent revenue streams and dividend growth track records over the past few decades. This type of consistency is what investors like to see whether the economy is expanding or contracting. While sector rotation will likely keep some investors away from this sector if economic indicators improve, utilities could easily be the first sector that investors turn to if economic growth stalls or the rate of acceleration does not meet market expectations. No matter what the economic environment, we still believe that utilities and pipelines should be components of a well diversified portfolio.

Telecommunications

To be blunt, we believe the Telecommunications sector was mistreated in 2009 not only due to sector rotation, but also due to an overreaction to competitive threats. It is no secret that new entrants are trying to get their businesses up and running in this industry to compete against the major incumbents including Rogers Communications, TELUS, and BCE Inc. However, as of December 2009 these companies have yet to officially start operating or even gain full approval to do so from the CRTC. The longer this process drags on, the better for the incumbents. We also question how much business these new entrants will actually steal in the wireless market. Without a doubt they will take some market share as they have nowhere to go but up when it comes to counting new subscribers, but do not underestimate the competitive position of the incumbents due to service bundling and their ability to compete on price. Let's also not forget that companies like Rogers, TELUS and BCE are cash flow generating machines and as such offer investors stable and growing dividends. As mentioned above, defensive stocks are usually oversold when investors rotate into cyclical stocks thus creating value opportunities. We believe this was the case towards the end of 2009 and that the market is starting to pay attention to this sector once again. While we recognize that cyclical stocks could still outperform telecommunications stocks in 2010, we still think investors will see positive returns from this sector going forward.

Individual Stocks to Highlight

Last year, considering the state of the markets, we provided investors with two lists of stocks to watch. The first list identified stocks to consider if the economy continued to struggle and the second list identified stocks to consider if positioning your portfolio for an economic recovery. Since the worst of the economic struggles are likely over in 2009, we will provide you with two different lists this year:

Stocks we Feel should be Consistent Performers in a Balanced Portfolio

Barrick Gold
Canadian National Railway
Enbridge
Great-West Lifeco
Research in Motion
Rogers Communications
Royal Bank
Shoppers Drug Mart
Suncor
Thomson Reuters

Stocks that could add some Extra Return if Fundamentals Improve/Strengthen

Bank of Montreal
Brookfield Asset Management
Canadian Natural Resources
Crescent Point Energy
Finning International
IAMGOLD
Potash Corporation
Silver Wheaton
SNC Lavalin
Thompson Creek Metals

While these lists are not exhaustive, our intention here is to highlight higher quality names with relatively strong balance sheets, good management teams and a decent track record of past performance. We are not saying these companies will be the top performers of the year, but we do believe they should be considered depending on what you're trying to achieve and we recommend you contact your ScotiaMcLeod Wealth Advisor for further insight. We believe our sector commentary from earlier in this report will help explain why you see these particular names in their respective lists.

Overall Conclusion

There is no denying the fact that the rebound for the TSX Index has been impressive. Needless to say, our expectations have been exceeded due a weaker-than-expected U.S. dollar, a credit market that improved much faster than anticipated and emerging markets which literally refused to participate in the global recession. While we certainly do not expect the same rate of appreciation for the TSX index in 2010, we are bullish for the Canadian stock market over the long term and believe this country will be a great place to invest as the global economy accelerates this year and beyond.

2010 Outlook

The author(s) of the report own(s) securities of the following companies: **Bank of Nova Scotia, Rogers Communications Inc., Research In Motion Limited, Potash Corporation of Saskatchewan, Inc.,**

The supervisors of the Portfolio Advisory Group own securities of the following companies:

Bank of Nova Scotia, Manulife Financial Corporation, TELUS Corporation, BCE Inc., Canadian National Railway Company,

Scotia Capital Restriction -- U.S. (American) **Bank of Nova Scotia**

The Fundamental Research Analyst/Associate, in his/her own account or in a related account, owns securities of the following issuer(s) under his/her coverage: **Bank of Montreal, Bank of Nova Scotia, Canadian Imperial Bank of Commerce, Manulife Financial Corporation, Royal Bank of Canada, Sun Life Financial Inc., Toronto-Dominion Bank**

The Head of Equity Research/Supervisory Analyst, in his/her own account or in a related account, owns securities of the following issuer(s): **Bank of Montreal, Bank of Nova Scotia, BCE Inc., Canadian Imperial Bank of Commerce, Canadian National Railway Company, Canadian Natural Resources Limited, Crescent Point Energy Corp., Enbridge Inc., Great-West Lifeco Inc., Manulife Financial Corporation, Research In Motion Limited, Rogers Communications Inc., Royal Bank of Canada, Shoppers Drug Mart Corporation, Sun Life Financial Inc., Suncor Energy Inc., Talisman Energy Inc., TELUS Corporation, Thomson Reuters Corporation, Toronto-Dominion Bank, Finning International Inc.**

The Portfolio Strategist/Associate, in his/her own account or in a related account, owns securities of the following issuer(s): **National Bank, Sun Life Financial Inc., Toronto-Dominion Bank**

The issuer paid a portion of the travel-related expenses incurred by the Fundamental Research Analyst/Associate to visit material operations of the following issuer(s): **Barrick Gold Corporation, IAMGOLD Corporation, Silver Wheaton Corp., Finning International Inc.**

Scotia Capital Restriction **Bank of Nova Scotia**

Scotia Capital Inc. and its affiliates collectively beneficially own in excess of 1% of one or more classes of the issued and outstanding equity securities of the following issuer(s): **Bank of Montreal, BCE Inc., Canadian Imperial Bank of Commerce, Enbridge Inc., Great-West Lifeco Inc., Manulife Financial Corporation, National Bank, Rogers Communications Inc., Royal Bank of Canada, Sun Life Financial Inc., TELUS Corporation, Thomson Reuters Corporation, Toronto-Dominion Bank, Finning International Inc.**

The Bank of Nova Scotia ("the Bank") is the parent company of Scotia Capital Inc. ("SCI"). This Report includes comparative information regarding a substantial number of competitors of the Bank where such comparable information is known or ascertainable by SCI and in equal prominence to the information in respect of the Bank. **Bank of Nova Scotia**

The Fundamental Research Analyst/Associate has visited material operations of the following issuer(s): **Barrick Gold Corporation, BCE Inc., Canadian National Railway Company, IAMGOLD Corporation, Potash Corporation of Saskatchewan, Inc., Research In Motion Limited, Rogers Communications Inc., Shoppers Drug Mart Corporation, Silver Wheaton Corp., TELUS Corporation, Thomson Reuters Corporation**

Within the last 12 months, Scotia Capital Inc. has undertaken an underwriting liability with respect to equity securities of, or has provided advice for a fee with respect to, the following issuer(s): **Bank of Montreal, Bank of Nova Scotia, Barrick Gold Corporation, Canadian Imperial Bank of Commerce, Canadian National Railway Company, Crescent Point Energy Corp., Enbridge Inc., Great-West Lifeco Inc., IAMGOLD Corporation, Manulife Financial Corporation, National Bank, Potash Corporation of Saskatchewan, Inc., Rogers Communications Inc., Royal Bank of Canada, Shoppers Drug Mart Corporation, Silver Wheaton Corp., Sun Life Financial Inc., Talisman Energy Inc., TELUS Corporation, Thomson Reuters Corporation, Toronto-Dominion Bank**

Scotia Capital is a member of the Canadian Investor Protection Fund (CIPF). ScotiaMcLeod is a division of Scotia Capital Inc. (-SCI-). This report has been prepared by SCI on behalf of the Investment Executive. Opinions, estimates and projections contained herein are our own as of the date hereof and are subject to change without notice. The information and opinions contained herein have been compiled or arrived at from sources believed reliable but no representation or warranty, express or implied, is made as to their accuracy or completeness. Neither SCI nor its affiliates accept liability whatsoever for any loss arising from any use of this report or its contents. This report is not, and is not to be construed as, an offer to sell or solicitation of an offer to buy any securities and/or commodity futures contracts. SCI, its affiliates and/or their respective officers, directors or employees may from time to time acquire, hold or sell securities and/or commodities and/or commodity futures contracts mentioned herein as principal or agent. SCI and/or its affiliates may have acted as financial advisor and/or underwriter for certain of the corporations mentioned herein and may have received and may receive remuneration for same.

The content may have been based, at least in part, on material provided by Credit Suisse First Boston Corporation ("CSFB"), our correspondent research service. CSFB has given ScotiaMcLeod general permission to use its research reports as source materials, but has not reviewed or approved this report, nor has it been informed of its publication. CSFB may from time to time have long or short positions in, effect transactions in, and make markets in securities referred to herein. CSFB may from time to time perform investment banking or other services for, or solicit investment banking or other business from, any company mentioned in this report.

This research and all the information opinions and conclusions contained in it are protected by copyright. This report may not be reproduced in whole or in part, or referred to in any manner whatsoever, nor may the information, opinions, and conclusions contained in it be referred to without in each case the prior express consent of SCI. SCI is a wholly owned subsidiary of a Canadian chartered bank. SCI is a member of The Securities and Futures Authority Limited E&O.E. U.S. Residents: Scotia Capital (U.S.A) Inc. (-SCUSAI-), a wholly owned subsidiary of SCI, accepts responsibility for the contents herein, subject to the terms and limitations set out above. Any U.S. person wishing further information or to effect transactions in any security discussed herein should contact SCUSAI at 212-225-6500.

Bank	Symbol	Scotia Capital Recommendation	Risk Rating	1 Yr Target
Bank of Montreal	BMO	1-Sector Outperform	Low	\$65.00
Bank of Nova Scotia	BNS	2-Sector Perform	Low	\$55.00
CIBC	CM	3-Sector Underperform	Low	\$75.00
National Bank	NA	2-Sector Perform	Low	\$75.00
Royal Bank	RY	1-Sector Outperform	Low	\$75.00
Toronto-Dominion Bank	TD	2-Sector Perform	Low	\$80.00