May 8th, 2012

Portfolio Strategy

May 2012 Update

Equities Slip in April, S&P/TSX Financials Leadership Reverses

The MSCI World AC Index declined 1.4% (in USD) in April and the S&P 500 suffered its first monthly loss since November 2011. The S&P/TSX (+0.3% in USD; -0.8% in CAD) outpaced the S&P 500 (-0.7% in USD). China bucked the global trend, with a 5.9% gain; Japan (-3.3%), Germany (-4.8%), and Brazil (-7.8%) lagged; and Mexico slipped 1.6% (all in USD).

Bonds outperformed in April and U.S. Treasuries bested Canadian government bonds. U.S. 10-year yields declined 30 bp to 1.91% and the TLT ETF advanced 4.6%. Hawkish rhetoric from the Bank of Canada flattened the yield curve and Canadian long-term bond performance (-0.5%) lagged the U.S. YTD in total return; the S&P 500 was up 11.9% and long U.S. Treasuries were down 2.5%. In Canada, the S&P/TSX (+3.8% YTD) has outpaced government long-term bonds (-1.3%) by 502 basis points (bp) so far in 2012; the S&P/TSX was also ahead in total returns.

Health care (+5.7 %) and Staples (3.5%) outperformed in April, while Materials (-6.2%) and Technology (-3.6%) were the most notable S&P/TSX underperformers. Health care (+22.3% YTD) and Staples (+13.9% YTD) continued their domination in April, but Financials (-0.5% in April; +12.6% YTD) leadership disappeared in the latter half of the month.

Year-End North American Benchmark Information

	Recent	2012E	2013E
S&P/TSX Composite Index			
TSX Level/Target	11,871.23	12600	
TSX Earnings	$855.41	$925.00	$975.00
TSX P/E	13.88	13.62	12.93
TSX Dividends	$344.38	N/A	N/A
TSX Yield	2.90%	N/A	N/A
S&P 500			
S&P 500 Level/Target	1,369.10	1425	
S&P 500 Earnings	$98.81	$102.00	$105.00
S&P 500 P/E	13.86	13.75	13.09
S&P 500 Dividends	$27.98	N/A	N/A
S&P 500 Yield	2.04%	N/A	N/A
Fixed Income & Currency			
BoC Overnight Rate	1.00%	1.00%	1.75%
Canada 10-Year Bond	2.020%	2.40%	3.50%
Cdn/U.S. Dollar	$0.9961	$0.99	$0.97
U.S. Fed Funds Rate	0.25%	0.25%	0.25%
U.S. 10-Year Treasury	1.8786	2.60%	3.75%
Euro/U.S.Dollar	$1.3084	U$1.29	U$1.27
Commodities			
Gold	$1,642.22	U$1650.00	U$1600.00
Oil (WTI)	$98.49	U$105.00	U$105.00

Source: Scotia Capital, Bloomberg.

The Canadian and Australian dollars advanced versus the U.S. dollar, while LatAm currencies declined. The CRB Index eased 0.8% in April, with WTI (+1.8%) edging Brent (-2.8%), natural gas (+7.5%) and copper (+0.2%) posting gains, and precious metals declining (gold -0.2% and silver -3.4%).

Asset Mix: Reiterate Neutral Equity Stance, overweight cash bias

We lowered our recommended equity weighting to neutral and raised Cash in our April strategy update and are sticking to this view. We are also sticking to our S&P 500 over S&P/TSX stance. Although most indicators remain equity supportive, the risk-reward outlook is not as attractive as it was in late 2011 and early 2012. The bottom line is that our tactical equity stance is cautious, and we would wait for the "risk-on" window to open up before adding more beta and cyclical exposure to our portfolios.

This report is an excerpt from the report titled the 'Strategic Edge Weekly" released May 7th, 2012, by Vincent Delisle, CFA - Director, Investment Strategist, Portfolio Strategy Group, Scotiabank GBM. For a full copy of the report, please contact your ScotiaMcLeod advisor.

Vincent Delisle, CFA – *Director, Portfolio Strategist, Portfolio Strategy Group, Scotiabank GBM*

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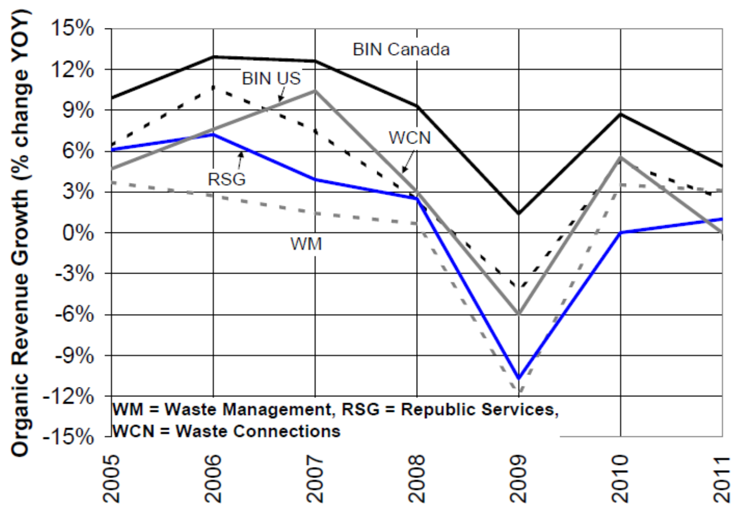
Canadian Equity Strategy

PROGRESSIVE WASTE SOLUTIONS (BIN):

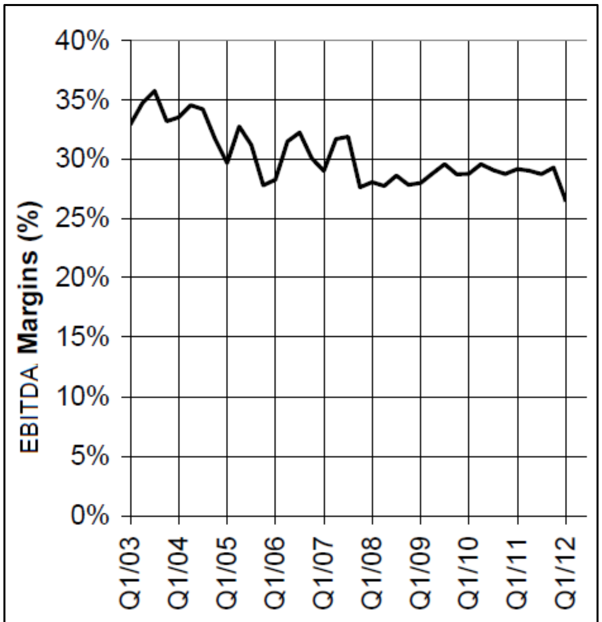
Overhang from slowing organic growth, rising leverage, and margin pressure

- **Given lack of catalysts, consider switching it up!** Considering the factors discussed in the following bullets, the shares of BIN at current levels appears to be fairly balanced in terms of risks versus rewards (ie. limited downside but also limited upside). Correspondingly, as capital gain opportunities could be elusive over the next six to twelve months, and considering the shares offer a fairly low dividend yield, the Portfolio Advisory Group recommends looking elsewhere for stocks with better risk/reward propositions.
- **Slowing Organic Growth.** In part reflecting upward cost pressures, foreign exchange headwinds, and a generally competitive landscape, the rate of organic growth among the major players in the waste management industry appears to have decelerated over the past few years. At first glance, some investors understandably view the industry as a fairly stable non-cyclical business. However, the slowing rate of organic growth clearly demonstrates that the industry can actually be quite economically sensitive and vulnerable to fluctuations in industrial and commercial waste volumes.



Source: Scotiabank GBM, company reports

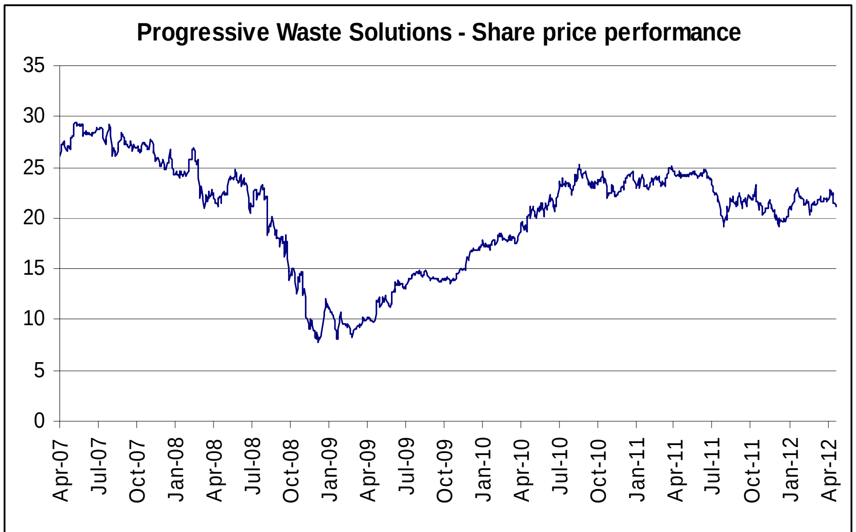
- **Signs of margin pressure.** Particularly noticeable in the most recently reported Q1 results, the impact of lower recycling fiber prices plus higher fuel costs appears to be weighing on BIN's earnings power. While one quarter does not make a trend, it is worth noting that EBITDA margins have progressively declined from the mid-30% range in 2003 to the current rate of 26.5%.
- **Acquisitive Growth Strategy.** Progressive Waste Solutions' acquisitive growth strategy has been a major earnings driver over the past several years. Between 2004 and 2011, the company materially expanded its footprint throughout North America by completing more than US$1.8 billion of acquisitions. During that period, BIN issued more than US$900 million of equity to help fund the transactions and correspondingly, the company has progressively increased their market capitalization from $650 million in 2004 to the current $2.4 billion. To management's credit, despite the material number of equity financings over the seven-year period, BIN was able to increase earnings on a per share basis at an annual rate of 9.5% during that time. Looking ahead however, in the absence of material acquisitions and if organic growth continues to decelerate, the concern is that the earnings growth trajectory over the next few years could be vulnerable.



Source: Company reports

- **Rising Leverage.** BIN's debt to capital ratio currently stands at 51.0%. This appears conservative relative to a peer group that has an average debt to capital ratio of 56.9%. That said, in absolute terms, it is worth highlighting that the debt to capital ratio has progressively risen over the years (the ratio was at 27% at the beginning of 2004). Although the company is not considered to be over-levered, increasing debt levels could potentially make it more difficult for BIN to capitalize on future acquisition opportunities.

- **Some supportive factors, but what are the catalysts for capital appreciation?** Shares of BIN face a number of near-term headwinds including a slowdown in the pace of organic growth, rising leverage, and margin pressure. Some of these risks, however, have arguably already been discounted in the share price. The shares are currently trading at a reasonable 7.2x forward EBITDA and this is slightly below the long-term average of 7.8x. Aside from valuation, also supportive of the shares at current levels is the company's active share buyback program. Scotiabank estimates that the company bought back approximately 1.4 million shares in Q1, at an average price of ~$21.50. For 2012, the company is targeting to spend approximately $90 million on share buybacks.
- **Downgraded to 2-SP at Scotiabank GBM.** Reflecting weaker-than-expected Q1 results, Scotiabank GBM recently downgraded the shares of Progressive Waste Solutions to 2-Sector Perform (from 1-Sector Outperform), as the analyst believed that company guidance remains too high and that negative earnings momentum could persist in the coming quarters.
  - The analyst highlights the chance that downward guidance revisions could weigh on the stock in the near term. While management made note of higher special waste activity so far in Q2/12, this appears to have already been baked into its original expectations.
  - The analyst also noted that they fail to see where the expected upside to results will come from. As such, management meeting its guidance could possibly be a best-case scenario at this point. Either way, there are no near-term positive catalysts on the horizon to move the stock higher. Consequently, Scotiabank GBM decided to take a neutral stance on the stock.
- **At current prices, the most compelling switch opportunity would be Potash Corporation.**
  - Shares of Potash have underperformed the broader index in recent months on concern over price settlements in Asia as well as signs of lackluster demand in calendar Q1. Regarding the first issue, the recently announced price settlements announced in China was better than street expectations. On the latter issue, producers such as Potash Corp. recently resumed production at select mines after temporarily shutting them down in January. From our perspective, these are positive developments and remove two key overhanging concerns, particularly as we approach a seasonally stronger period for the agricultural sector.
  - For more details on Potash Corp. or to discuss other switch opportunities, please contact your ScotiaMcLeod Wealth Advisor.



Source: Bloomberg

Geoff Ho, CFA – *Director, Portfolio Advisory Group, Canadian Equities*

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U.S. Equity Strategy

U.S EQUITIES STILL ATTRACTIVELY VALUED – FOCUS ON GROWTH SECTORS

The S&P is currently valued at 13 times 2012 earnings estimates, up slightly from 12 times in December. The multiple has not expanded much because of the reduced earnings growth expected for the remainder of the year plus global macro risks. So far the first quarter earnings surprise of 67% has kept the market afloat despite the deteriorating economic picture in helping sustain the growth as consumer confidence remains some what resilient. In recent U.S. economic releases, personal income came ahead of personal spending indicating that consumers are no longer borrowing to maintain consumption levels as they were at the beginning of the year.

Equity Indices - Weekly Performance

	Close	Weekly Change		YTD Return
Equity Index	05/04/2012	Points	%	%
S&P/TSX Composite	11871.23	-366.52	-3.0%	-0.70%
Dow Jones Ind. Avg.	13038.27	-190.04	-1.4%	6.72%
S&P 500 Index	1369.1	-34.26	-2.4%	8.87%
Nasdaq Composite	2956.34	-112.86	-3.7%	13.48%
FTSE-100 Index (London)	5655.06	-414.84	-6.8%	1.49%
CAC-40 Index (Paris)	3161.97	-104.30	-3.2%	0.07%
DAX Index (Frankfurt)	6561.47	-239.85	-3.5%	11.24%
Nikkei (Tokyo)	9520.89	-328.85	-3.3%	12.60%
Hang Seng (Hong Kong)	21086	344.55	+1.7%	14.38%

Source: Bloomberg

To date, 85 percent of the S&P 500 companies have reported earnings and the first quarter is tracking towards a 7.5% year-over-year growth rate ahead of the 1% estimates by S&P Capital IQ. We find of interest that earnings surprises have come from just three out of the ten GICS sectors when compared to S&P Capital IQ's expectations coming into this earnings season. Earnings for Industrials are up 19% ahead of the 10% expected by S&P, Technology is up 17% vs. the 5% increase expected by S&P, and Healthcare is up 12% vs. 3% expected. Utilities, Telecommunications, Materials, Consumer Staples and Discretionary, Energy and Financial have all reported close to S&P Capital IQ expectations quarter to date.

The S&P Industrial Sector Index has risen 7% year to date and the S&P Technology Sector Index 19%. Both sectors now trade at a 13 times multiple, in line with the S&P 500 Index. The earning growth momentum in these two sectors is expected to remain strong for the balance of the year. We feel comfortable that large scale projects will take time to unwind if the global economy happens to slow more than expected, helping maintain the earnings momentum in these sectors.

The Portfolio Advisory Group's U.S. recommended list includes companies we find attractive in the Industrials and Technology sectors:

Deere & Co. (DE, Buy 4-STARS, U$111.00)

- Deere manufactures farming and construction equipment**,**
- DE trades at 10 times multiple in line with Caterpillar (CAT) on 2012 earning estimates.
- Deere's expected earnings growth is strong at 8.0% for 2012 and 8.5% for 2013.
- Caterpillar earnings growth is higher, but we believe that farm cash receipts will remain strong and Deere's stock price will not be as volatile and correlated to mining as Caterpillar's.
- The company has exposure to the fast growing emerging markets by generating revenue in the more predictable agricultural sector.

Fluor Corp. (FLR, Buy 4-STARS, Target U$70.00)

- Fluor is a professional service company that provides engineering, procurement and construction services.
- Fluor's valuation in terms of price-earnings-ratio is in line to slightly higher vs. their peer's at 15 times. In terms of EV/EBITDA, it is in the low end vs. the group at 6.3 times vs. 9.2 times.
- Fluor's earnings are expected higher than peer's with growth of 11% for 2012 and 15% for 2013.
- The company has a strong balance sheet and favorable long term prospects.

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- It is expected the company will trade at a premium multiple to the group.
- S&P Capital IQ set their target price of U$70.00 on a 17.5 times multiple.

General Electric (GE, Buy 4-STARS, Target U$24.00)

- In terms of valuation, GE's price-earnings-ratio is at a discount to the industry.
- General Electric has slightly higher earnings growth expectations than its peer's at 13% for 2012 and 14% by 2013,
- The key growth drivers for the company will be Energy and Aviation, and we believe that GE Capital will soon contribute to the bottom line as credit margins improve and credit losses decline.
- GE has an attractive dividend yield of 3.5%.

Apple Inc. (AAPL, Buy 4-STARS, Target U$825.00)

- Apple has an attractive valuation with price-earnings-ratio and EV/EBITDA at a discount to its peers,
- Apple's earnings growth forecast is strong at 60% for 2012 and 15% for 2013.
- On March 19, 2012 Apple initiated an annual dividend of U$10.60 per share, a 1.8% dividend yield.
- Apple has strong cash reserves of $110 billion.
- We believe that Apple will continue to be the trend-setter in the personal electronics segment as rivals scramble to imitate Apple's products.

We believe that the market as a whole could see further downside in the short term, but we view any pullback as being healthy for the longer term outlook. We are expecting that some individual stocks may retreat much more than the major market indices, depending on how well they performed prior to the market pullback. Technology, Consumer Discretionary and Financial sectors had the most gains year to date advancing at almost twice the pace of the S&P 500 Index.

Marco Martin – *International Equity Consultant*

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Fixed Income Strategy

BONDS RALLIED LAST WEEK AS WEAKER THAN EXPECTED CANADIAN GDP, POOR US JOBS DATA AND EUROPEAN RISKS DROVE A FLIGHT TO QUALITY

Bonds rallied last week as global risks, weaker employment data out of the US and softer Canadian GDP led a strong rally in bonds. Since the Bank of Canada's (BoC) last rate statement when Governor Carney signaled a more hawkish tone and the possibility of rate hikes, Canadian bonds had been under pressure. With Canadian February GDP data registering a disappointing 0.2% m/m decline, the governor's warnings suddenly seemed to lose credibility as markets reversed much of the weakness initially seen after the Bank's statement. Although we saw a significant rally in Canada bonds on April 30, there was a good deal of follow through that left Canadian bond yields lower by 0.12-0.17% across the Canadian curve. Contrasting Canadian bonds, US bonds traded largely flat through most of the week ahead of Friday's non-farm payrolls report. With non-farm payrolls printing significantly lower than expected (115k versus the 160k consensus expectation) both Canadian and US government bonds rallied between 0.04%-0.06% across their respective curves. Adding to all of this the generally softer tone of European economic data, (and worries over the outcome of French and Greek elections), bonds seemed well situated for a strong rally – which is precisely what we saw.

Canadian Bond Yields - Weekly Change

	May 4	April 27	Change (bps)
Canada 2-Year Bond	1.25	1.42	-0.17
Canada 10-Year Bond	2.02	2.09	-0.07
Canada 30-Year Bond	2.51	2.63	-0.12
BoC Target Overnight	1.00	1.00	0.00
Prime	3.00	3.00	0.00
U.S. 2-Year Bond	0.26	0.26	0.00
U.S. 10-Year Bond	1.88	1.94	-0.06
U.S. 30-Year Bond	3.07	3.12	-0.05
Federal Funds	0.25	0.25	0
Prime	3.25	3.25	0

Source: Bloomberg

Bond Index Performance (YTD)

	May 4	Apr 27	Change
DEX Universe Bond Index	0.55%	-0.39%	0.94%
DEX All Government Bond Index	0.00%	-0.95%	0.95%
DEX All Corporate Bond Index	2.06%	1.16%	0.90%

Source: PC-Bond

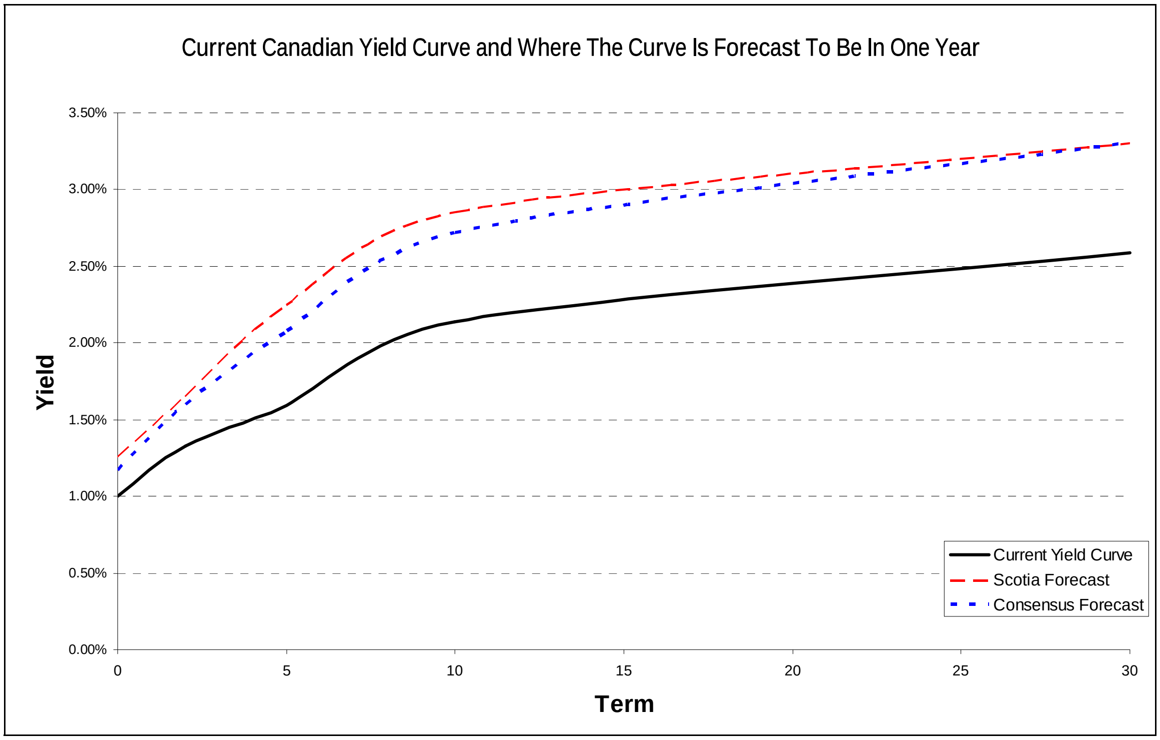
European risk and a softer tone in US employment numbers, left corporate spreads under pressure. The week closed out on a softer tone as weaker employment numbers cast further doubt on the strength of the US economy. There was further pressure on spreads ahead of the weekend's elections in Europe, which both went as expected. Those results put further pressure on overseas markets yesterday morning but some strength returned to risk markets as we entered the beginning of the North American week; we opened modestly softer in Canada to start the week. The focus will be increasingly on earnings this week with little in the way of market moving data expected on the economic front. Given the ongoing light new issuance calendar in Canada, there is a chance we could see Canadian spreads outperform relative to the US.

Canadian jobs data will pose a notable downside risk this week while initial jobless claims and the trade deficit will take the spotlight in the US. Canada's April **Jobs Data** (May 11) pose an interesting form of data risk. Canadian jobs growth accelerated substantially in March, with the Labor Force Survey showing growth of 82.3k jobs — one of the larger gains on record which should leave risks to the downside. As well, we have **International Trade** (May 10). Scotia is anticipating deterioration in the trade balance during March to -C$250 million as the price gap between generally used world benchmark oil prices and the more unique Canadian ones didn't close meaningfully. Scotia's autos economics group also expects that car and car-part shipments for export slid slightly in March. On the housing front, Scotia is expecting a slight cooling in April (May 08); **Housing Starts** have been at elevated levels through 2012 almost entirely on the strength of condominium supply in Toronto. The **US Trade Deficit** for March will be released on May 10. Scotia is expecting a meaningful deterioration to the -US$52 billion level. In what will be a quiet week in terms of US economic data releases, **Initial Jobless Claims** (May 10) should be a highlight of the week.

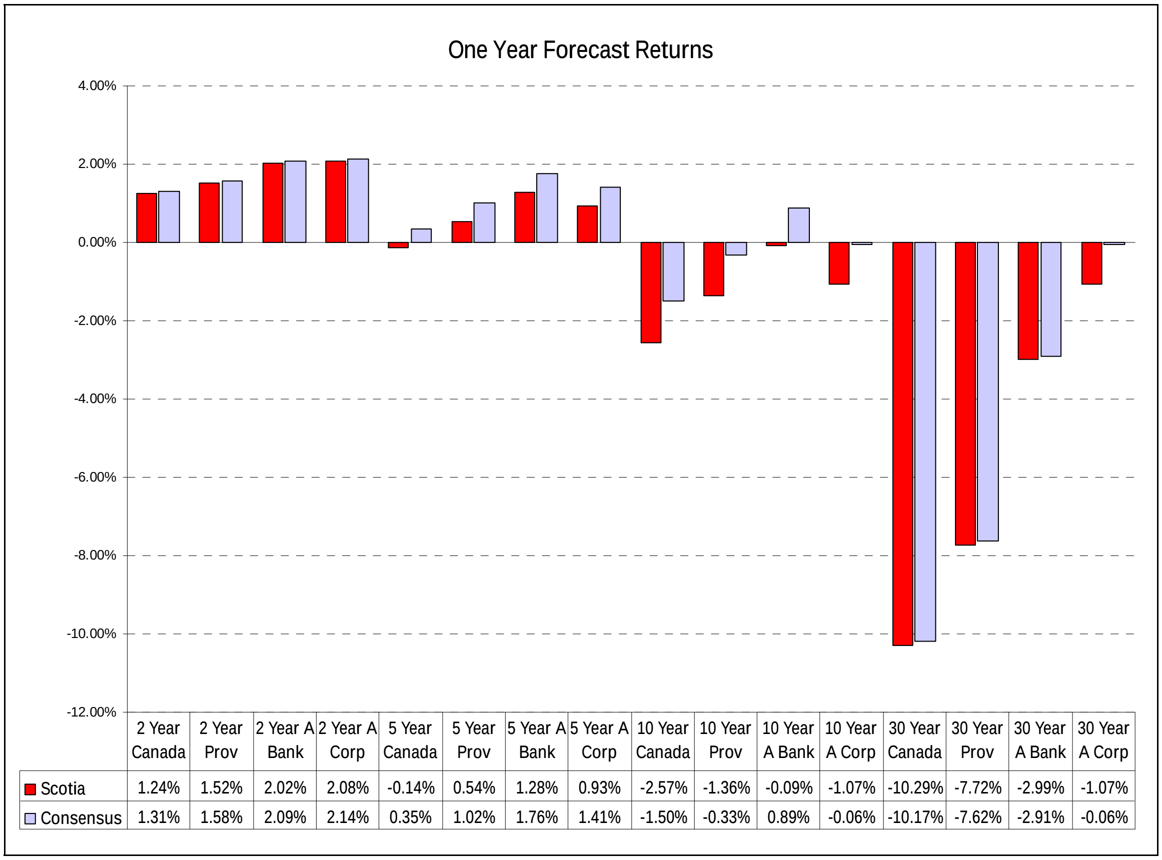
Current PAG Recommendations (changes in blue)

1. **Term Call –** Given historically low rate levels, we no longer see value in the mid to long end of the curve and recommend investors stay short at this time.
2. **Sector Call –** Underweight Canada bonds, overweight provincials, municipals and corporates
3. **Currency Call –** We recommend Canadian investors remain in Canadian dollars for their fixed income holdings.
4. **Alternative Strategies –** Market weight high yield, market weight emerging markets debt, underweight inflation protected debt.

1. **Term Call** – Scotia Economics' forecast is suggesting that Canadian rates should shift upwards by ~25-100 bps across the Canadian curve over the next 12 months. Given Scotia's current rate forecast, we do not see value in the long end of the curve and recommend investors stay short at this time.



Source: Scotia Economics and Bloomberg



	2 Year Canada	2 Year Prov	2 Year A Bank	2 Year A Corp	5 Year Canada	5 Year Prov	5 Year A Bank	5 Year A Corp	10 Year Canada	10 Year Prov	10 Year A Bank	10 Year A Corp	30 Year Canada	30 Year Prov	30 Year A Bank	30 Year A Corp
Scotia	1.24%	1.52%	2.02%	2.08%	-0.14%	0.54%	1.28%	0.93%	-2.57%	-1.36%	-0.09%	-1.07%	-10.29%	-7.72%	-2.99%	-1.07%
Consensus	1.31%	1.58%	2.09%	2.14%	0.35%	1.02%	1.76%	1.41%	-1.50%	-0.33%	0.89%	-0.06%	-10.17%	-7.62%	-2.91%	-0.06%

Source: Scotia Economics and Bloomberg

2. **Sector Call –** We recommend investors look to the provincial, municipal, and corporate sectors for yield enhancement. Credit spreads (the yield pick-up over Canada bonds) still remain relatively attractive.

3. **Currency Call –** Scotia Economics' and consensus forecast expectations are for the Canadian dollar to outperform most major currencies over the next year, therefore we recommend Canadian investors remain in Canadian dollars for their fixed income holdings at this time.

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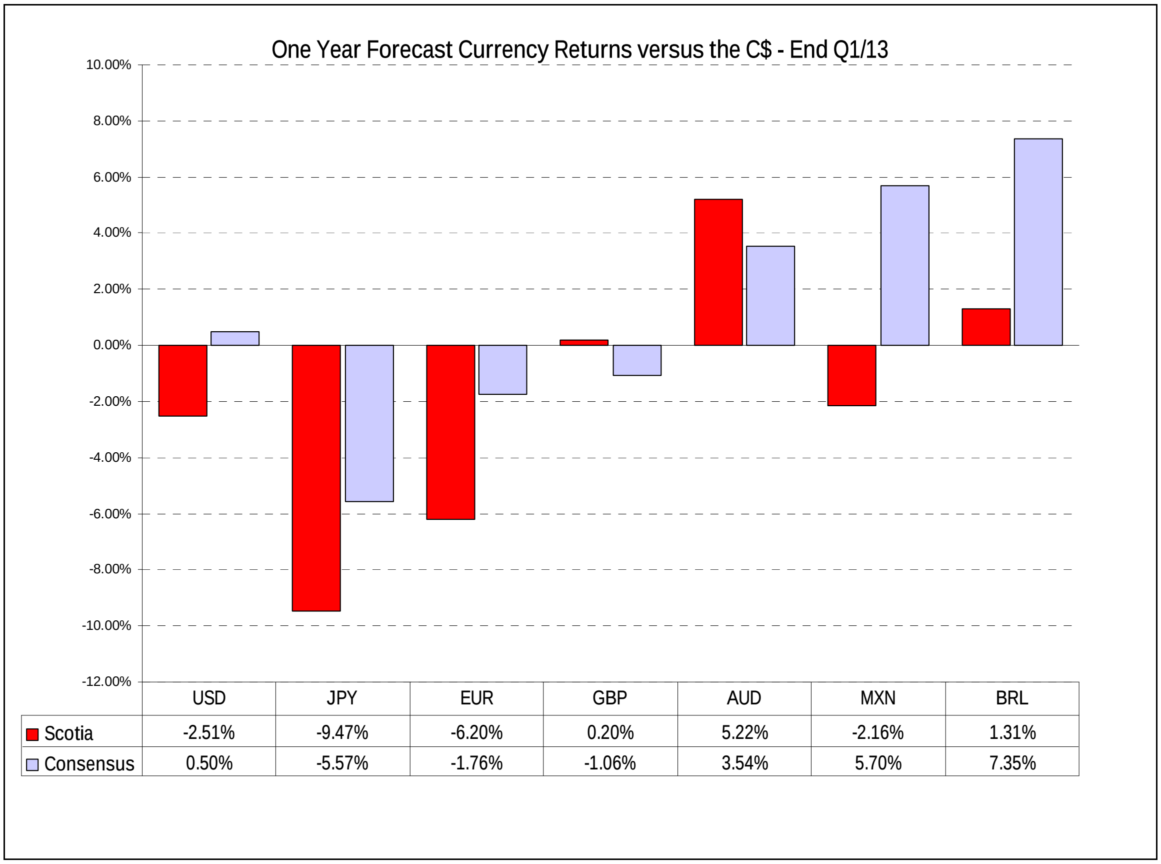

	USD	JPY	EUR	GBP	AUD	MXN	BRL
Scotia	-2.51%	-9.47%	-6.20%	0.20%	5.22%	-2.16%	1.31%
Consensus	0.50%	-5.57%	-1.76%	-1.06%	3.54%	5.70%	7.35%

Source: Scotia Economics and Bloomberg

4. **Alternative Strategies:** Within a broadly diversified portfolio our recommendations are as follows:

   a) High Yield – In conjunction with our continued positive equity market outlook for the next 12 months (based on the outlook for economic recovery), we recommend investors maintain a market weight position in high yield debt.

   b) Emerging Markets – Emerging markets sovereign debt has softened recently, in line with global risk markets. With the benchmark JPMorgan Emerging Markets Bond Index Plus (EMBI+) having yielded 5.24% to date (returned 12.45% last year) we feel there is still some upside in the corporate and local currency sectors. With Latam Investment Grade bonds still attractive relative to US comparables and High Yield names (particularly B grade) having some room to tighten before reaching fair value - we continue to suggest being market weight high yield and emerging markets debt at this juncture.

   c) Inflation Protected Bonds – with current real yields in the area of 0.54%, and nominal Canada bonds pricing in an effective long term inflation rate of 2.07% (versus March headline inflation of 1.9% y/y), we see limited value in Canadian Real Return Bonds and recommend an underweight exposure to the sector.

Andrew Mystic – *Associate Director, Portfolio Advisory Group – Fixed Income*

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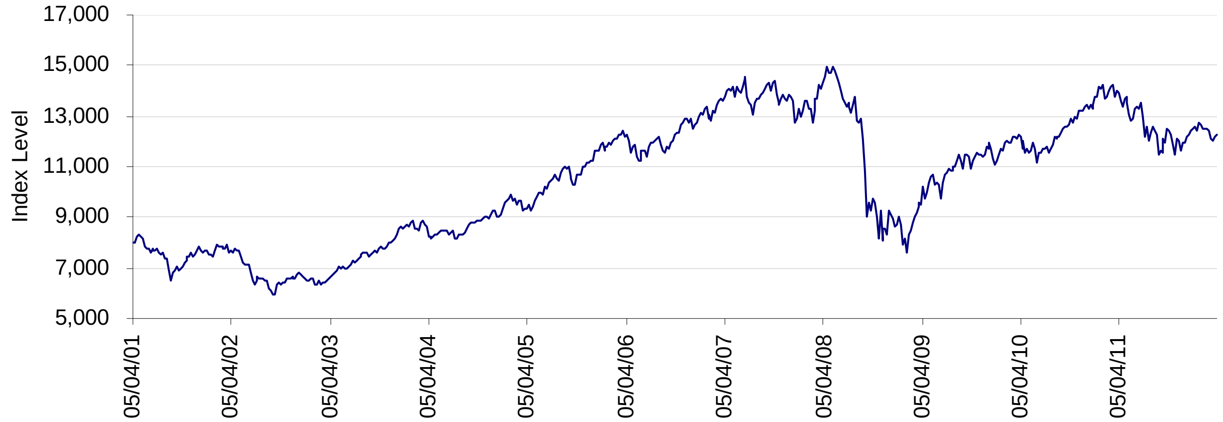
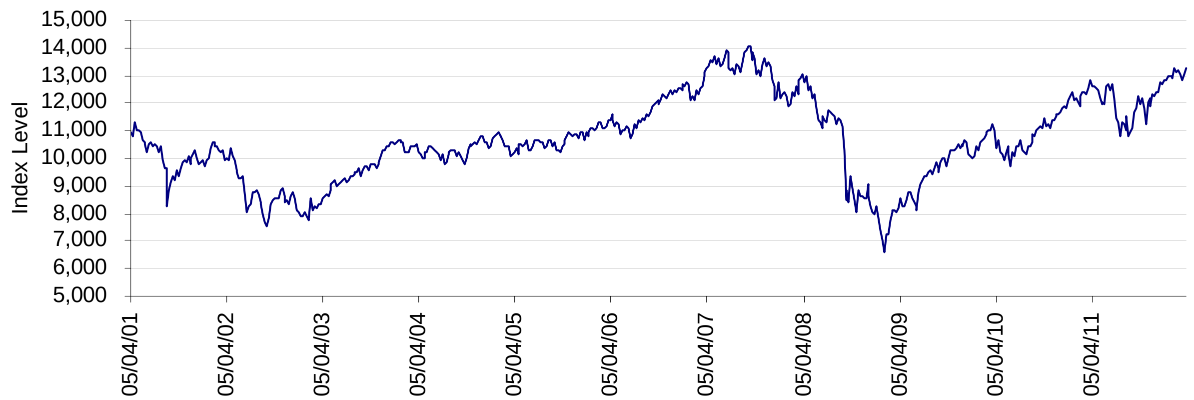
-S&P/TSX Composite Index



-Dow Jones Industrial Average



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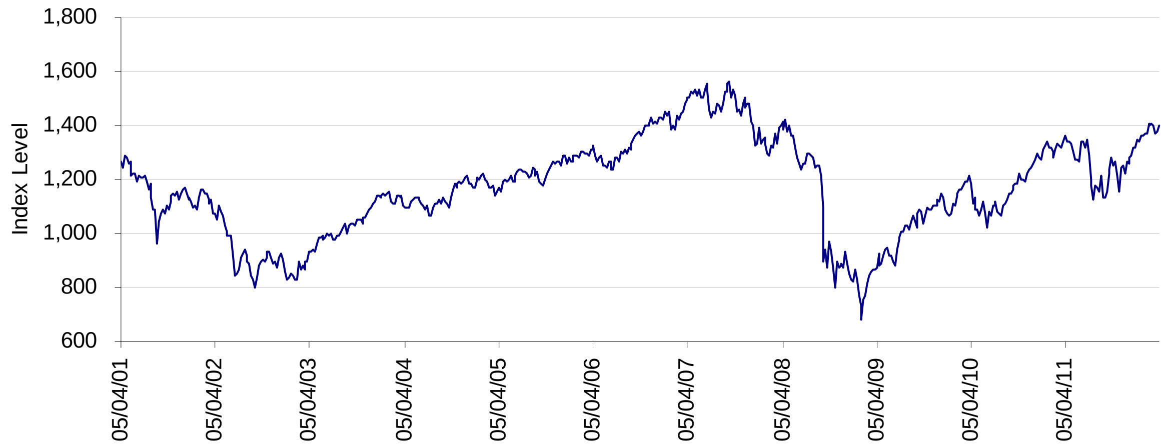
-NASDAQ

- S&P 500 Index



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Definition of Scotiabank GBM Equity Research Ratings & Risk Rankings

We have a three-tiered system, with ratings of 1-Sector Outperform, 2-Sector Perform, and 3-Sector Underperform. Each analyst assigns a rating that is relative to his or her coverage universe or an index identified by the analyst that includes, but is not limited to, stocks covered by the analyst.

Our risk ranking system provides transparency as to the underlying financial and operational risk of each stock covered. Historical financial results, share price volatility, liquidity of the shares, credit ratings, and analyst forecasts are evaluated in this process. The final ranking also incorporates judgmental, as well as statistical, criteria. Consistency and predictability of earnings, EPS growth, dividends, cash flow from operations, and strength of balance sheet are key factors considered. Scotiabank GBM has a committee responsible for assigning risk rankings for each stock covered.

The rating assigned to each security covered in this report is based on the Scotiabank GBM research analyst's 12-month view on the security. Analysts may sometimes express to traders, salespeople and certain clients their shorter-term views on these securities that differ from their 12-month view due to several factors, including but not limited to the inherent volatility of the marketplace.

Ratings

1-Sector Outperform
The stock is expected to outperform the average total return of the analyst's coverage universe by sector over the next 12 months.

2-Sector Perform
The stock is expected to perform approximately in line with the average total return of the analyst's coverage universe by sector over the next 12 months.

3-Sector Underperform
The stock is expected to underperform the average total return of the analyst's coverage universe by sector over the next 12 months.

Other Ratings
Tender - Investors are guided to tender to the terms of the takeover offer.

Under Review - The rating has been temporarily placed under review, until sufficient information has been received and assessed by the analyst.

Risk Rankings

Low
Low financial and operational risk, high predictability of financial results, low stock volatility.

Medium
Moderate financial and operational risk, moderate predictability of financial results, moderate stock volatility.

High
High financial and/or operational risk, low predictability of financial results, high stock volatility.

Caution Warranted
Exceptionally high financial and/or operational risk, exceptionally low predictability of financial results, exceptionally high stock volatility. For risk tolerant investors only.

Venture
Risk and return consistent with Venture Capital. For risk-tolerant investors only.

This report has been prepared by members of the ScotiaMcLeod Portfolio Advisory Group. ScotiaMcLeod is the full service retail division of Scotia GBM Inc

The author(s) of the report own(s) securities of the following companies.
None.

The supervisors of the Portfolio Advisory Group own securities of the following companies.
None.

Scotia Capital (USA) Inc. or its affiliates has received compensation for investment banking services in the past 12 months. ***Progressive Waste Solutions Ltd.***

The Fundamental Research Analyst/Associate has visited material operations of the following issuer(s): ***Potash Corporation of Saskatchewan, Inc.***

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