

Asset Allocation	Q 1 2007	Q 2 2007
Can. Equity	12%	12%
US Equity	15%	12%
Global Eq.	18%	16%
Fixed Income	55%	60%

The US economy served up 2 dead canaries (sub-prime loans and the housing glut) and the price volatility in equity markets worldwide (for example the Shanghai market meltdown and subsequent aftershocks in late February), provided a third. Heeding these warnings our equities to fixed income allocation is now 40/60, or very conservative, with US and global equity exposure down by 5% since Q4 2006. Our expectation is that 2007 equity returns will be modest and that gains in one market may be offset by losses in another. It is, in our view, risky to make more than a cautious forward-looking call on equities (for now we only hold defensive and countercyclical stocks, and expect marginally higher returns from global equities), and far better to focus on preserving capital, diversification and finding stable returns elsewhere. Our focus on fixed income is also timely as Q2 and Q3 are seasonally lackluster periods for equity markets.

CANADIAN EQUITY: 12%
Unchanged
Benchmark: S&P TSX Composite
3 month C\$ total returns to March 31, 2007: **2.6%**

TSX returns in 2007, as previously noted, come with substantially more risk on the heels of 4 years of double-digit growth, with relatively high equity valuations (16.1 times 12-month trailing averages vs. 15.5 times for the S&P 500, Source: National Bank Financial), and a market that is skewed (approx. 40% of total market capitalization) towards resource producers, a sector vulnerable to a global slowdown. Accordingly our portfolio is light in Canadian equities with 8% devoted to a defensive position in a dividend index (favoring insurance, utilities and telecoms) and 4% in a Canadian-listed but international gold index. We expect near-term markets to remain volatile. Energy security concerns (which strengthen the C\$) and strong results from financials may mask the vulnerability of the domestic economy and constrain negative market sentiment for the time being.

US EQUITY: 12%
Reduced by 3%
Benchmark: S&P 500
3 month US\$ total returns to March 31, 2007: **0.6%**

The big question for US markets is no longer a matter of "if" but rather a matter "when" and "how hard" will the US economy slowdown? The sub-prime loan and housing situation is (and has been for over 9 months) leading the way but capital markets have been slow to acknowledge this. We reduced our US exposure by 3% in March following the turbulence earlier in the quarter to hold (as with the Canadian allocation) defensive (dividend index) and countercyclical (health care) stocks. As an insurance measure, our US position also shorts (a strategy to profit from falling share prices) the S&P 500 index.

GLOBAL EQUITY: 16%
Reduced by 2%
Benchmark: MSCI EAFE
3 month US\$ price return to March 31, 2007: **3.5%**

Given the body count, our exposure to global defensive large caps, primarily telecom, healthcare and utilities and the Euro 350, was trimmed from 18% to 16% of the total portfolio. The expectation is that if a US market pullback degenerates into a correction (-10% or more), defensive global stocks will suffer temporarily. The 16% global allocation remains limited to Europe and global utilities with some EAFE exposure that is nevertheless biased towards developed economies. In the longer term, Canadian dollar weakness may benefit these international investments.

FIXED INCOME: 55%
Unchanged
Benchmark: Citigroup World Government Bond Index
3 Month C\$ total returns to March 31, 2007: **1.7%**

In 2006, an expansive approach to fixed income provided a year over year return in excess of 8% and significantly moderated the volatility of the global balanced portfolio. The goal today is similar: that is for returns to lift the global balanced portfolio but, given more volatile equity markets, critically, the added goal is also to ensure that 2007 returns are positive (at a time when many other portfolios may not be). The fixed income allocation comprising investments in income trusts, gold instruments, US preferred shares and high yields, is essentially unchanged but for a 3% addition of US preferred shares.

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