

Inside **INNOVA**

Solid. Stable. Considered.

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Rethinking Risk

For many investors the pendulum has swung too far in favour of low risk investing following the financial crisis.

While a prescription for conservative investments offers temporary relief of market volatility, the long-term side effects of this approach could stunt performance or delay plans.

Even as the Dow Jones industrial average struck a new all-time high in March of this year, a good degree of skepticism persists among the investing public. "Many investors were shell shocked by the 2008 financial crisis. While the market has certainly moved on, those same events continue to cast a shadow," says Neil Macdonald, Managing Director, Scotia Asset Management.

The tendency to place the greatest importance on events from the most recent past is known as Recency Bias. "It's the same occurrence that pushes sports fans to over emphasize an athlete or team's latest performance rather than their long-term track record. Or the poker player who doubles his bet on the faith of his last winning hand. The probability of success or failure hasn't

changed, but perception of them has," adds Macdonald.

The market is not the economy

At the same time as the economy sputters along the long road to recovery, equity markets at home and abroad continue to regain ground. Those investors that stuck with their plan through the recovery and maintained a balance of growth-oriented equities and less risky bonds and cash were well rewarded.

Live Long and Prosper

According to a Scotiabank poll*, 68% of Canadians are concerned about not having

enough money to support their retirement. Outliving your retirement savings is a very real risk, but one that can be managed with proper

planning and the right balance of investments for each stage of your life.

An overly-conservative

According to a Scotiabank poll, 68% of Canadians are concerned about not having enough money to support their retirement*

approach can handicap growth potential. It can also increase the risk of falling short of goals or running out of money, especially after factoring in inflation.

Too Little Risk is Risky

If your exposure to conservative investments exceeds your long-term requirements, you may need to rethink your definition of risky. "Diversifying your portfolio to include higher-yielding investments can help satisfy a thirst for income, while measured exposure to riskier asset classes such as equities has the potential to boost the value of your portfolio over the long run," adds Macdonald.

Any move to increase the return-potential of your profile comes with added risk. Scotia INNOVA Portfolios are available in a range of asset mixes and risk levels to suit a variety of investor needs. Speak to your Scotiabank advisor about the most prudent approach for your situation. ■

*Source: Scotiabank. Canadian Savings and Investing Attitudes and Behaviours, January 2013.



Great Input Leads to Great Output

Whether you are building a house or constructing a portfolio, it is the quality of the resources and workmanship that stand the test of time.

Inside **INNOVA** recently spoke with Judith Chan, Director, Portfolio Solutions at Scotia Asset Management about her approach and portfolio construction methodologies.

Portfolio construction

Q There are certain levels of risk an investor needs to take to realize returns. Could you address some of the key risks you consider when tailoring each portfolio?

More conservative portfolios are suitable for investors who have lower overall tolerance for risk.

A strong focus is placed on

capital preservation and absolute downside protection for these portfolios. Emphasis is placed on investment vehicles that provide current yield through interest and dividend income and avoid exposing the investor's capital to a high level of volatility. While we are mindful of maintaining purchasing power over the long term, we allocate larger weightings to

investments that typically exhibit higher levels of volatility but provide greater long-term return potential.

Manager selection

Q What are the benefits of having multiple portfolio managers on the programs?

There's almost as much variety in portfolio managers as there are investors. Portfolio managers differ in terms of their philosophies, approach and styles, not to mention their economic sector, security and company size preferences. These differences can lead to very different patterns of performance. Using multiple managers with complementary approaches will provide the portfolio with better diversification, lowering the overall level of volatility and potentially avoiding long periods of underperformance.

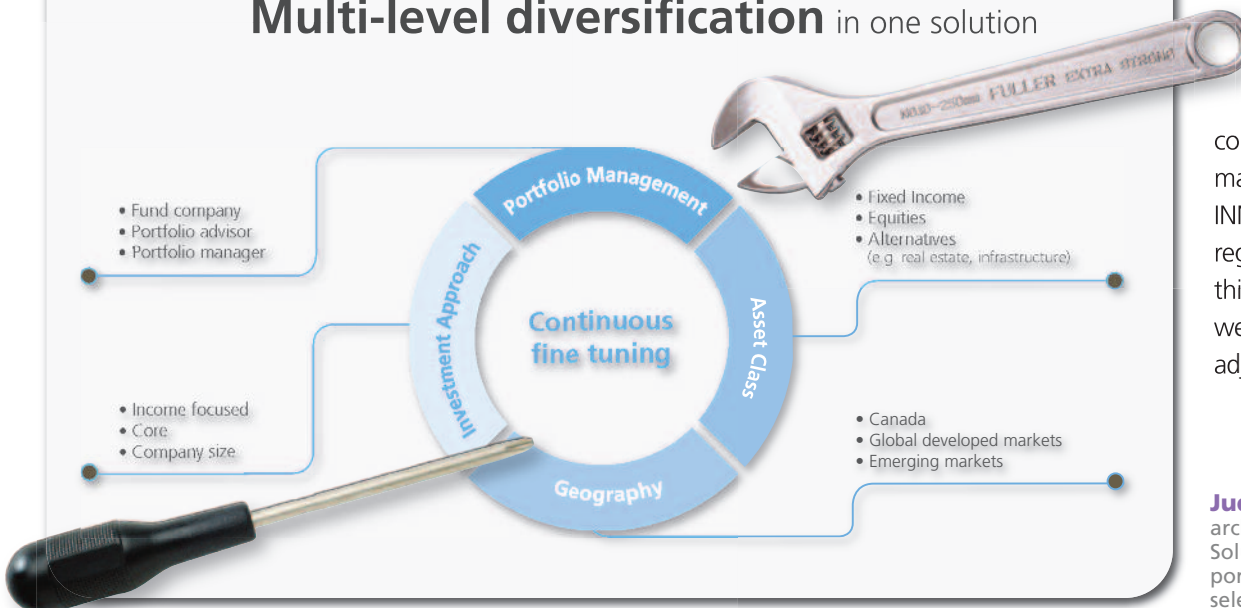
Ongoing oversight

Q Scotia INNOVA Portfolios are regularly rebalanced and re-optimized. Can you explain the difference between the two and why they are important?

A good way to think about rebalancing is like the regular tidying you do at home or in your office – putting things back in their usual spot. We rebalance Scotia INNOVA Portfolios using the daily cash flows into and out of each portfolio (e.g. investor purchases and withdrawals). This helps ensure that the balance of mutual funds within each doesn't stray from its target allocation and the overall portfolio remains on track.

Re-optimization is more like remodelling, where all of the elements in a room are examined for form and function. Like a remodel, where elements that no longer provide the same function or utility to a room are removed or replaced, the unique combination of funds that make up each Scotia INNOVA Portfolios are also regularly scrutinized. We do this in order to help ensure we are meeting our risk-adjusted return expectations. ■

Multi-level diversification in one solution



Judith Chan is the chief architect of Scotia Portfolio Solutions, responsible for portfolio construction, manager selection and ongoing oversight.

Equities dash out of the gates in 2013

Equity markets kicked off not with a whimper but a bang this year – and, in some countries, surpassed record highs – as many took a ‘glass half full’ approach to investing.

While many of the same concerns continued to exist – such as the U.S. fiscal challenges, ongoing Eurozone debt crisis and Japan’s struggles with economic growth – the worst of the crises appeared to be contained. “Investors have ignored political risks in Europe

mid-summer, being soothed by the promises that the European Central Bank will do ‘whatever it takes’ to maintain the currency,” says Peter Baughan, co-portfolio advisor of INNOVA’s Scotia Private Global Equity Pool. “As in the U.S. (and now Japan), investors are increasingly reliant on easy money from central banks,” he adds.

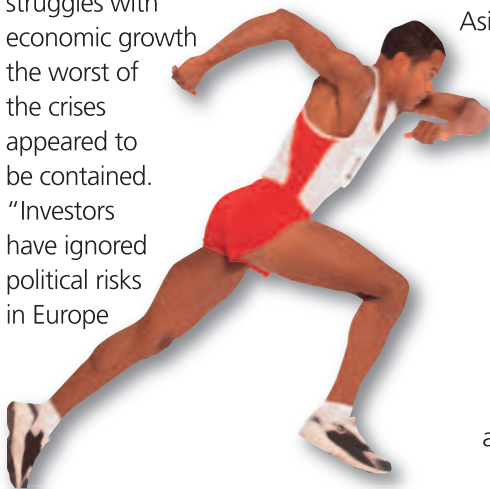
Aside from ongoing support from central banks, investors were also heartened by improving U.S. economic data, decisive action from Eurozone leaders to contain the debt crisis (as we saw in Cyprus) and a change of

government in Japan and China.

Over the quarter, the MSCI World Index delivered strong, double-digit returns of 10.3% in Canadian dollar terms. This performance was driven primarily by U.S. equities, with the S&P 500 Index hitting an all-time high and returning 13% over the quarter. Other markets, including Canada’s, lagged by comparison, but still rose in the quarter.

Money flowed more strongly into equities again, as many investors felt comfortable enough to take on additional risk for greater return potential. Fixed income continues to be an important diversifier to smooth out returns over time – particularly in the event of a market correction, which is anticipated this year but is not expected to be extreme.

A surge in equity returns is clearly a positive start for 2013. ■



Portfolio Performance (as at March 31, 2013)

SCOTIA PORTFOLIOS	3 Mths	6 Mths	1 Yr	2 Yrs	3 Yrs	Since Inception
Scotia INNOVA™ Portfolios Series A						
Scotia INNOVA Income	2.31%	3.22%	5.55%	5.13%	5.30%	6.96%*
Scotia INNOVA Balanced Income	2.91%	4.42%	6.24%	4.72%	5.35%	7.94%*
Scotia INNOVA Balanced Growth	3.96%	6.13%	7.06%	4.03%	5.33%	8.53%*
Scotia INNOVA Growth	4.69%	7.35%	7.60%	3.38%	5.16%	9.33%*
Scotia INNOVA Maximum Growth	5.97%	9.32%	8.53%	2.36%	4.97%	9.65%*
Scotia INNOVA™ Portfolios Series T						
Scotia INNOVA Income	2.31%	3.22%	5.56%	5.12%	5.31%	5.23%**
Scotia INNOVA Balanced Income	2.91%	4.42%	6.24%	4.72%	5.37%	5.31%**
Scotia INNOVA Balanced Growth	3.96%	6.13%	7.06%	4.04%	5.37%	5.16%**

* January, 2009

** January, 2010

The indicated rates of return are the historical annual compounded total returns as at March 31, 2013 including changes in unit value and reinvestment of all distributions and do not take into account sales, redemption, distribution or optional charges or income taxes payable by any unitholder that would have reduced returns. The rate of return shown is used only to illustrate the effects of the compound growth rate and is not intended to reflect future values of the funds or returns on investment in the mutual funds. Mutual funds are not guaranteed, their values change frequently and past performance may not be repeated.

Words from the wise

– Pearls of wisdom from some of our top investment minds

“At one point close to 40% of the S&P/TSX Composite Index was resource stocks. It’s been a good 10 years but it’s going to be challenging as time goes on. What you want to do is replace those resource stocks with more great North American companies that you can’t find in Canada.”

Jason Gibbs, Portfolio Advisor, Scotia Canadian Dividend Fund

“North America appears as one of the strongest regions globally in this economic recovery, due to a strengthened financial system, potential for energy self-sufficiency and the renaissance of manufacturing throughout the region. Over the next decade, Canada is a key part of the North American story.”

Alex Lane, Portfolio Advisor, Scotia Canadian Small Cap Fund

“Global growth is becoming an issue. Central banks are building a bridge from recession to expansion by easing aggressively, but many structural reforms are still needed to raise potential GDP growth rates. Otherwise, they’re building a bridge to nowhere.”

Romas Budd, Portfolio Advisor, Scotia Bond Fund ■

A LOOK at the Markets

U.S. equity markets continue to advance at a brisk pace.



Sunny

The U.S. equity market reached an all-time high on the last day of the quarter, supported by improving macroeconomic

data and a global monetary backdrop that continues to be accommodative. The U.S. economy continues to show marked signs of improvement, as evidenced by the continued housing revival, declining jobless numbers and an improvement in manufacturing levels.

Canadian economic data continues to be uninspiring.



Sunny with clouds

The Canadian economy is clearly stalling as annualized quarter-over-quarter real gross domestic product (GDP) growth has produced

less than one percent for two consecutive quarters. In our opinion, growth rates should rise over the longer term, although results may be subdued over the next quarter or so.

Macro headwinds obstruct recovery in Europe.



Cloudy

European markets were shocked early in the quarter following anti-austerity elections results in Italy and misspending allegations brought against Spanish Prime Minister Mariano Rajoy. Meanwhile, unemployment figures continued to highlight the divergence between the stronger and weaker countries in the currency bloc. European Central Bank President Mario Draghi took steps to ease

investor jitters by declaring, "monetary policy will remain accommodative as long as needed."

Cyprus brings eurozone back into the spotlight.



Rainy

Another European test challenged markets in March, and this time it centered on Cyprus, which threatened to send the region back into crisis. Global markets were on edge until Cyprus reached a €10 billion bailout deal with the international lenders to restructure Cyprus banks. ■

Index Performance

3-Months (as of March 31, 2013, C\$)

- ▲ 0.7% MSCI Emerging Markets Index
- ▲ 10.3% Global equities (MSCI World Index)
- ▲ 13.0% U.S. market (S&P 500 Index)
- ▲ 3.3% Canadian equities (S&P/TSX Composite Index)

Source: Bloomberg

Outlook provided by Scotia Asset Management L.P., portfolio manager to Scotia INNOVA Portfolios.

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