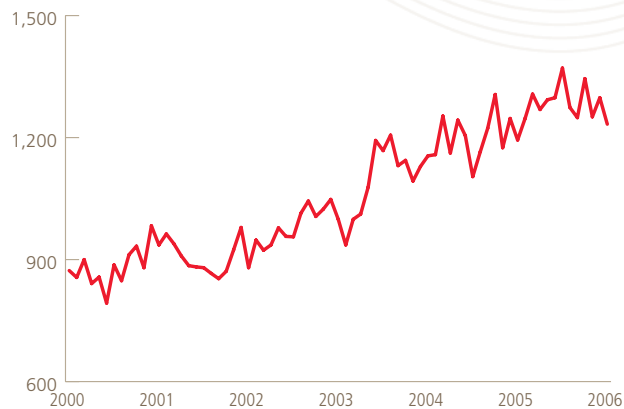


Review and Outlook

STRONGER FOR LONGER?

After many years of above average economic growth, the consensus view is that the U.S. economy will slow in 2006, lead by the consumer who is now heavily in debt. Much of the consumer debt (and spending) is the result of mortgage refinancing as consumers took advantage of historically low interest rates to leverage their rising home equity. Recent data on U.S. home sales and consumer spending confirms that the housing market is cooling off and consumer spending is slowing. It is expected that this will lead to slower economic growth and subsequently lower short term interest rates from the Federal Reserve, but it appears not yet. For the time being, the business sector seems to be picking up some of the slack from the consumer, and job growth remains good.

US New Housing Sales (000s)

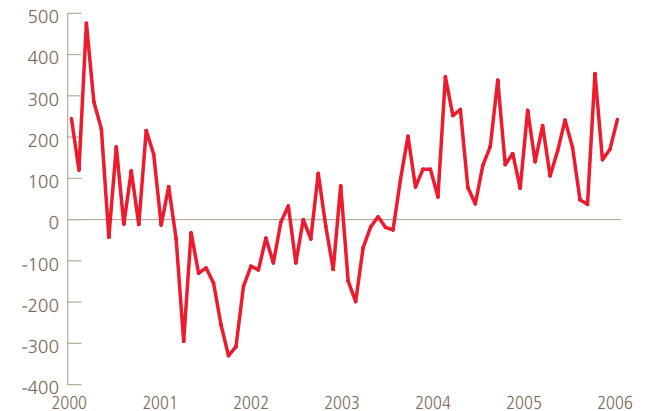


U.S. Federal Reserve; Is Bernanke a dove, hawk or data watcher?

Ben Bernanke, the new chairman of the U.S. Federal Reserve, was widely expected to be dovish on inflation prior to his appointment. There is pressure on him both to maintain the general policies of the Greenspan era, while remaining true to the mandate of the Fed; that is, price stability and growth. More recently, he has made it clear that he will be more of a consensus leader than Mr. Greenspan and that he will rely more heavily on economic data to guide the decision making process. Whereas Greenspan ignored potentially inflationary job growth, assuming improving productivity would contain inflation, Bernanke is more like to respond to such data by raising rates. Although unemployment appears to be rising, the recent employment numbers suggest that job growth is actually improving. Formerly unemployed workers are again joining the work force raising the participation rate and thus the unemployment rate. The bottom line is that the U.S. economy and inflation pressures are strong enough to continue to put upward pressure on interest rates over the short term. The risk is that the Fed goes too far while

awaiting data to confirm that monetary tightening is taking effect. It is a risk that Bernanke is forced to take, because, to stop raising rates in anticipation of a slow down, lacking the data, risks a policy error based on speculation. As a new Fed Governor seeking to build consensus, this is not the likely scenario.

Non-Farm Payroll Numbers Job Growth (000s)



Implications for Equity and Fixed Income Markets

Rising short term interest rates, an over extended consumer, and a weakening housing market are not typically factors leading to robust capital markets. The shift in growth to the corporate sector from the consumer is encouraging, but it cannot be expected to totally replace the economic growth driven by the consumer which represents 66% of the economy. These dynamics are largely confined to the U.S. market (which has been the worlds' largest consumer). What we have not addressed is the growing economies of the emerging markets and their impact on global growth.

Brazil, China, India and Russia (sometimes referred to as the BRIC countries) are growing their economies at more than twice the rate of the more mature G8 countries. This is creating tremendous demand for resources and industrial products to build the infrastructure to sustain a growing economy and upwardly mobile population. This has been most pronounced in the Energy sector where emerging market demand, combined with maturing and unstable sources of supply, have driven up the cost of energy and the related securities materially over the last two years. The

importance of emerging market demand has now been priced into many sectors as new equilibrium price points have been established at much higher levels. This is encouraging exploration, conservation and shifting purchase patterns that will result in less pressure on prices in the future.

For equity investors, some sectors hold more risk than others. It is clear that the consumer now has less disposable income making the discretionary sectors less attractive. The industrial sector continues to benefit from a relatively robust global economy with some sectors (Energy and Materials) having strong demand and cash flows, but with price risks.

Fixed Income markets have mirrored the changing views on the economy. The U.S. yield curve has shifted from an inversion of over 20 basis points to a positive slope of 6 basis points in the last few weeks, suggesting no conviction on either a material slowdown or the need for many more rate increases. However, rates are low on a historical basis, especially Canada bond yields, and may be under pressure if growth continues as is expected.

Conclusions

We think the near terms risks to financial markets have increased based on a further increase in short term interest rates, slower earnings growth, and geopolitical tensions in some oil producing countries. Global growth remains constructive with the support of very strong growth in the emerging market countries. We remain cautious for the near term and are moderately defensive as we wait for some of the above noted issues to become resolved. We are positioned to take advantage of any correction and will take appropriate action should the opportunity arise.

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