Monthly investment commentary

NOVEMBER 2007

OCTOBER HIGHLIGHTS

- The Canadian dollar has set a new modern-day record high, cracking the previous record of $1.06 U.S. set in 1957.
- Oil prices moved above $94 U.S. per barrel (15.7% rise in October alone).
- Gold prices rose to $790.60 (up $156.10 or 24.6% so far in 2007).
- Canadian unemployment rates hit 33-year lows at 5.8% in October.
- The resource sectors combined for 60% of the monthly gain in the S&P/TSX (up 3.7% for October).
- Information technology companies re-emerge with strong growth in 2007.
- U.S. Federal Reserve lowered target interest rates by 25 basis points (0.25 per cent) at the end of October.

MIXING OIL AND WATER

For those of us who've been around long enough to remember the stock market crash of 1987, the words "stocks" and "October" mix like oil and water. But despite those 20-year old memories of a stock market crash, Canadian investors overcame any apprehension this October. Rising oil and other commodity prices greased the wheels of the Canadian stock market this October. The S&P/TSX boasted a 3.7% rise in the month which helped our Canadian index reach a very impressive 13.3% return year-to-date. (see Table 1)

TECH IS BACK

October proved to be a strong month for both the Energy and Materials sectors (see Table 2), benefiting from rising oil and other commodity prices. However, the top performing sector was the Information Technology sector. In Canada, this relatively small sector is dominated by one company - Research In Motion (RIM). RIM was the largest single contributor to the S&P/TSX Composite this month, accounting for 88 points in total. But the re-emergence of technology companies extends across the border as well. The S&P500 Information Technology sector is up 23.9%

Table 1– Summary of major market developments

Market returns	October	YTD
S&P/TSX	3.7%	13.3%
S&P500 (US$)	1.5%	9.2%
S&P500 (C$)	-3.2%	-10.9%
NASDAQ	5.8%	18.4%
Russell 2000	2.8%	5.1%
FTSE 100 (U.K.)	3.9%	8.0%
NIKKEI 225 (Japan)	-0.3%	-2.8%
EAFE (C$)	-0.9%	-6.1%
EAFE (local currency)	2.3%	7.0%
Canadian Bond Market	0.6%	1.6%
World Bond Market (US $)	0.7%	2.5%

*local currency (unless specified); price only

year-to-date, and one look at the strong performance of the technology heavy NASDAQ shows a similar trend (see Table 1). Investors are once again turning to technology companies to deliver consistent growth in a slowing earnings growth environment. The re-emergence of the Information Technology sector is signaling an end to the tech-bust hangover and a re-emergence of growth versus value stocks in the U.S.

BALANCING RISKS

The bond markets were boosted this month by an uncertain economic outlook in the U.S. weighing negatively on business sentiment and extending the 'flight to quality' in favour of bonds. Looking forward, the Bank of Canada must balance an appreciating currency, with an economy that's operating above its capacity limits. For the time being, it is anticipated that the Bank of Canada will continue to remain on hold until one side of its balance of risks begins to overtake the other.

TOO MUCH OF A GOOD THING?

While the Canadian market and economy seems to be firing on all cylinders lately, worries of 'too much of a good thing' are beginning to surface.

Strong oil prices

Oil prices have risen as a result of a number of current factors, including heightened geo-political concerns between Turkey and Iraq, tightening supply, and the weakening U.S.

dollar. Rising oil, natural gas, gold and other commodity prices have no doubt fuelled the resource-heavy S&P/TSX, but they also lead to higher consumer costs. Higher consumer costs are sure to be an added strain on the already burdened U.S. consumers, and any additional pressure on the American consumer these days is not a good thing.

Strong Canadian dollar

As the U.S. dollar weakens, oil costs (priced in U.S. dollars) have risen in relation, and in turn have helped the Canadian Loonie set a new modern-day record high, cracking the previous record of $1.06 U.S. set in 1957. The pace of gains has been record breaking as well, with September and October's one-month gains being the fastest on record (6.1% and 5.3%). Figure 1 shows the dramatic rise in values, as well as the strong correlation between the price of oil and the value of the Canadian dollar.

Table 2 - Sector level results for the Canadian market

S&P/TSX sector returns	October	YTD
S&P/TSX	3.7%	13.3%
Energy	4.1%	8.5%
Materials	6.3%	33.1%
Industrials	-1.5%	16.3%
Consumer discretionary	3.5%	10.7%
Consumer staples	2.3%	3.2%
Health care	-0.8%	-19.2%
Financials	1.6%	3.6%
Information technology	14.0%	51.2%
Telecom services	3.0%	24.9%
Utilities	6.8%	10.6%

*price only

While a strong currency is clearly an indication of a country's economic strength, the impact of the rising Canadian dollar has become a growing concern for Canadian exporters, manufacturing companies and retailers. Layoffs in manufacturing sectors (such as the auto industry) have already begun, and we can't ignore that the export sector still remains a key element of our economy. Canadian retailers have also come under great pressure to reduce prices and keep shoppers in Canada. With the upcoming holiday season approaching, retailers are sure to find themselves under even more pressure.

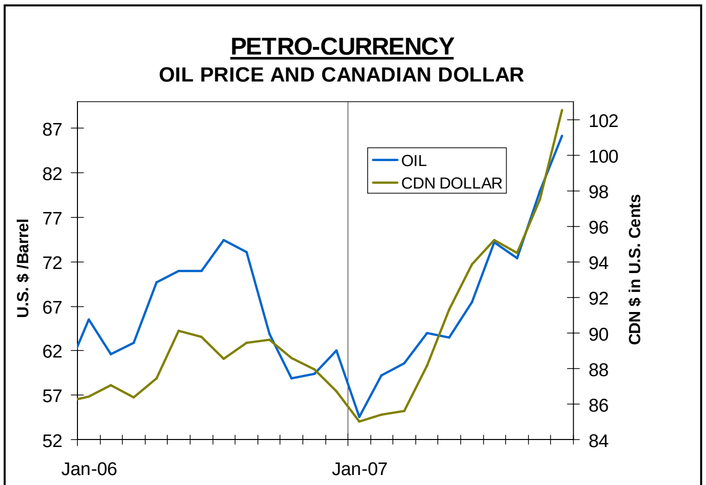
Strong employment

Both Canada and the U.S. have reported impressive employment results - an important piece of good news! A steady pay cheque in the pockets of consumers goes a long way to fight off any recession worries by supporting robust consumer spending. It remains to be seen, however, if it will be enough to mitigate the effect of an ever-weakening U.S. housing market (which is still in strong contrast to the healthy Canadian housing market). It is our ties to the U.S. economy, rather than our actual current economic scenario, that creates the concerns.

YOUR BEST BET

Today, as in 1987, the U.S. economy appears to be slowing; the U.S. dollar has weakened against other major currencies; commodity prices are rising; and the merger and acquisition activity that helped buoy stock prices has slowed. And yet, two decades later, it is the long-term investors who refrain from panic selling and continue to invest at regular intervals, that are best positioned to reap the rewards of capital market gains. Whether you see the current market and economic insights with a bullish or bearish view, a long-term investor's best bet, as it was in 1987, is to maintain a long-term perspective, invest in a diversified and age-appropriate allocation, and to keep their cool, no matter what the markets deliver.

Figure 1.



Source:: Andersen Economics, October 31, 2007