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Market Comments

February 4, 2008

Global equity markets plunged in the first month of the New Year, with the MSCI World Index falling by 7.6% in U.S. dollar terms and 5.7% in Canadian dollar terms, reflecting some modest weakening of the Canadian currency during the period. Market participants were rattled by a variety of economic reports suggesting that the U.S. economy was slipping into a recession that might also trigger pronounced economic weakness in major overseas economies. Markets and sectors that had performed well in 2007 were among the hardest hit in January, including Europe and the emerging markets or the energy and industrials sectors. Emerging market equities especially struggled with the MSCI Emerging Markets Index losing 12.5% in U.S. dollar terms and 10.6% in Canadian dollar terms for the month.

The drop in the MSCI World Index in January ranked as the 17th most severe monthly percentage drop since the index started in 1969 (out of 459 months). In 13 out of the 16 prior episodes, the index moved higher over the next 18 months by an average of 28%. The exceptions were the 1973 and 2001 major bear markets, when stocks had started by being massively overvalued compared to fixed income. That is decidedly not the case today with global stocks in the developed markets trading at around 13.3 times trailing earnings compared to long-term government bond yields of 4% or less in many major markets.

The Fed is playing its role in trying to avert recession or soften its impact, having cut the Fed funds rate by 1.25% in two rounds in January. That brings the funds rate to 3.0% compared to a peak of 5.25% in mid-2007. The jury remains out on whether the U.S. economy will technically enter recession, but we believe that the steepness of the yield curve, prospects for further rate cuts, and the impact of sizable fiscal stimulus will lead to some acceleration of growth in the second half of 2008. Other central banks including the Bank of England and the European Central Bank may well decide to join the Fed in easing monetary policy in coming months to help ensure that the global slowdown results in a mid-cycle pause in growth as opposed to a coordinated global downturn. We believe that the mid-cycle pause scenario is still the most likely outcome from a global perspective, and would note that the International Monetary Fund is still expecting global growth of 4% in 2008 even after taking into account recent financial market volatility.

In conclusion, we think the odds favor a substantial global equity market recovery in coming quarters. In our international balanced funds, we continue to have a tilt toward

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equities with a target of 60% equities and 40% fixed income. In our global equity portfolios, we currently have approximately 49% exposure to North America, 27% to Europe, 15% to Japan, 6% to the emerging markets, and 3% to the developed markets of Asia-Pacific excluding Japan. In terms of sector exposures, we currently are tilted toward the information technology, consumer discretionary and health care sectors and are tilted away from the financial, consumer staples, utility, telecommunications, and energy sectors.

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