CAPITAL MARKETS

Review and Outlook

SECOND QUARTER, 2001

THE ECONOMY

In response to continuing weakness in the manufacturing sector and evidence of further declines in business and consumer confidence, the Federal Reserve Board lowered interest rates twice in January and again at the end of March. Short-term interest rates in the United States now stand at 5.00%, compared to 6.50% at the end of 2000. Over the same period, the Bank of Canada reduced short-term rates from 6.00% to 5.25%, citing both potential risks from the United States slowdown and softer business conditions in Canada. With the European Central Bank now signaling rate cuts, central bank easing will likely become even more globally synchronized in the months ahead. The U.S. economy is forecast to post real GDP growth in the first quarter of approximately 0.9%, with most of the positive contribution to growth coming from the housing and consumer sectors. Recent estimates suggest the Canadian economy will advance at a 2.4% rate in real terms over the full year. Consensus forecasts are for real global GDP growth of 2.5% in 2001, down significantly from the 3.0% level expected as recently as January 2001.

BOND AND STOCK MARKETS

A Look Ahead

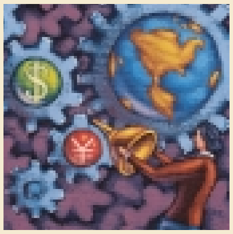
Industrial production, exports and business investment weakened in the United States over the last quarter, increasing the probability that corporate pre-tax profits will decline in 2001. In addition, softening consumer and business sentiment has raised concerns that the United States is entering into a recession, with negative implications for global economic growth. Further monetary easing by global central banks, lower interest rates and fiscal stimulus through the proposed Bush tax cuts will likely forestall a sharp economic contraction. However, reduced capital spending could translate into an extended period of below trend growth for the United States' (and global) economy and a gradual rather than rapid recovery in equity markets. Over the first quarter, we raised equities to a neutral exposure in terms of our long-term, strategic portfolio benchmarks. Our strategy is to maintain this neutral stance with a view to gradually increasing the commitment to equities as the earnings outlook stabilizes. Although recession risks remain, a weak cyclical outlook for corporate earnings is being increasingly factored into the equity markets.

TOTAL RETURNS

Period ended March 31, 2001

	Quarter	12 Months
SC 91 Day T-Bills	1.41%	5.72%
SC Short/Mid-Term Bond Index	2.22	9.41
TSE 300 Capped (5% max/issue)*	-8.33	1.49
TSE 300	-14.53	-18.61
S&P 500 (Cdn$)	-7.32	-15.01
MSCI EAFE (Cdn$)	-9.22	-19.34

* courtesy BMO Nesbitt Burns



Bonds

During the first quarter, ten-year and longer issues under-performed short-term bonds, which continued to benefit from actual and anticipated rate cuts. As a result, the yield curve finished the period at the steepest level since 1998. Given the current environment of central bank easing, we expect that short rates will continue to trend moderately lower over the next few months. However, the short end of the yield curve may come under pressure as the easing cycle matures. The recent retrenchment in long-term yields and the positive medium-term outlook for inflation have made longer-term issues more attractive. For eligible portfolios, we are therefore recommending some exposure to longer-dated Government of Canada and selected provincial bonds. With provincial debt trading at historically expensive levels and corporate spreads stable, we believe corporate bonds provide an excellent opportunity to enhance yield and performance. To reduce risk, we remain focused on higher-quality, liquid corporate issues with maturities of ten years or less.

Equities

The weakest performing TSE 300 sector in the first quarter was Industrial Products, which declined 39%, slightly exceeding the 38% decline registered in the fourth quarter of last year. Nortel Networks continued to weigh heavily on index returns. By the end of March, Nortel Network's TSE 300 weighting had been reduced to 10%, compared to its weighting of 18% at the end of the year and 28% at the end of September 2000. The Industrial Products sector, and the Technology Hardware area in particular, struggled with downwardly revised earnings estimates and the weakening outlook for capital spending. Despite the poor overall index return, seven of the fourteen TSE 300 sectors ended the quarter in positive territory. The best performing TSE 300 sectors were Transportation & Environmental Services and Conglomerates. The S&P 500 traded lower over the period (down 9.22% in US$) as the continuing inventory correction in manufacturing and negative earnings guidance eroded short-term optimism over interest rate cuts. Sectors ending the quarter with double-digit declines included Technology, Healthcare, Capital Goods and Financial Services. The Consumer Cyclicals area, traditionally an early beneficiary of economic recovery, was the only S&P 500 sector with positive returns for the period. Consistent with the pattern in North American equity markets, Technology and Telecommunications were the worst performing international sectors. All EAFE (Europe, Australasia and the Far East) markets traded lower over the quarter, with Europe under-performing the other regions.

THE LAST WORD

Rather than being symptoms of intractable structural problems, the current stresses in the United States economy are the result of an extended period of prosperity. It will take time to resolve the overcapacity in the technology sector and other economic imbalances. However, positive fiscal and monetary policy conditions are in place, valuations continue to improve and return expectations are becoming more realistic. With these favourable conditions in mind, we remain focused on a consistent and disciplined approach to equity selection and portfolio construction.

SCOTIA CASSELS RESEARCH TEAM . . . . .April 6, 2001

Scotia Cassels