

Monthly investment commentary

DECEMBER 2006

Highlights

- Canadian mergers and acquisitions (M&A) totaled \$90.3 billion in the third quarter, shattering a quarterly record dating back to the peak of the technology boom.
- The Materials sector is the clear leader year-to-date with gold and precious metals benefiting from M&A activity, Chinese government plans to pursue foreign currency reserve diversification, and strengthening oil prices creating inflationary pressure.
- 'Tax Fairness Plan' had a significant, but brief effect on the markets. By the end of November the markets were moving to new highs for the year.
- In the U.S., November saw renewed interest shift back into the cyclical sectors from the more defensive sectors.

November put many investors in a festive mood as it was a strong month for the major global markets bringing year-to-date return figures into the double-digits.

MAKING IT ON THE 'GOOD' LIST

Looking at Table One, you can see that all of the year-to-date figures are positive, with many of those in double-digit territory. In the U.S., November saw renewed interest shift back into the cyclical sectors from the more defensive sectors. The Energy and Materials sectors had strong returns as investors became more comfortable with the U.S. slowdown in economic growth and the increased likelihood of a soft landing. Energy was the top performing sector in the U.S. benefiting from rising oil and natural gas prices. In effect, the U.S. saw the rally that 'could have been' in their Energy sector while the Canadian Energy sector was muted by news of the 'Tax Fairness Plan' and its negative effect on income trusts in that sector.

Falling behind in November, Japan has been experiencing a slowdown in their GDP growth, while in the U.K. rising personal debt levels created some worry for investors. However, European equity markets on the whole had an excellent run with the MSCI EAFE index (C\$) posting a return of 4.5% in November.

In Canada, large cap companies outperformed their small and mid-cap counterparts, pulling up the S&P/TSX index this month. Both the Canadian equity and bond markets have shown strong results this year - an anomaly caused by the uncertainty over the U.S. economic slowdown helping the bond markets, while the equity markets benefited from a surge in merger and acquisition activity and renewed strength in oil and commodity prices.

A CORPORATE SHOPPING FRENZY

It has been a year-long shopping season for companies looking to take advantage of healthy balance sheets with large cash build-ups, and favourable financing conditions. Corporate mergers and acquisitions (M&A) have hit a record pace this year, fueling the equity markets. Canadian mergers and acquisitions totaled \$90.3 billion in the third quarter, shattering a quarterly record dating back to the peak of the technology boom. At the end of September, over 1,430 M &A deals were struck in the Canadian market, worth a combined \$187-billion. The stampede of corporate shoppers hasn't been limited to Canada, M&A activity has been soaring in the U.S. and across the globe as well as companies pursue their 'bigger is better' strategies.

Table 1- Summary of major market developments

Market returns	Nov.	YTD
S&P/TSX	3.3%	13.1%
S&P500 (US\$)	1.6%	12.2%
S&P500 (C\$)	3.4%	10.2%
NASDAQ	2.7%	10.3%
Russell 2000	2.5%	16.8%
FTSE 100 (U.K.)	-1.3%	7.7%
NIKKEI 225 (Japan)	-0.8%	1.0%
EAFE (C\$)	4.5%	17.6%
Canadian Bond Market	1.1%	4.9%
World Bond Market (US\$)	0.6%	1.6%

*local currency (unless specified); price only

INVESTORS WANT GOLD AND 'PEARLS'!

While pearls are always in fashion, Research in Motion's (RIM) newest Blackberry product release, 'the Pearl', has been a welcomed newcomer to the market place. Its well-received response continues to create positive momentum for RIM shareholders; pulling up the relatively small Information Technology sector in Canada and making it the top performing sector in November (see Table Two). Commodities such as gold and precious metals have also had a strong run, and not just because they might happen to be on your shopping list! The Materials sector is the clear leader year-to-date with gold and precious metals doing well because of merger activity along with news that the Chinese government is considering pursuing foreign currency reserve diversification in which they would sell some of their U.S. dollar 'paper' assets. Should they do this, it would create downward pressure on the U.S. dollar, thereby increasing the price of gold and metals. Strengthening oil prices also contributed to the Materials sectors as higher fuel prices create inflationary pressure and cause investors to seek out hard assets such as gold.

To the downside, the Telecom and Industrial sectors were both negatively affected by the surprise "Tax Fairness Plan" announcement on Halloween night. Aimed at stemming the corporate conversions to income trusts, it hit stocks like Telus and BCE square between the eyes causing significant sell-offs, though overall the markets quickly recovered from the news. By the end of November the Canadian market had moved to new highs for the year.

SEASONAL WISHES

For those of us who watch the markets closer than a school-aged child listening to the school bus cancellation news on a snowy Canadian morning...we know anything can happen! The Canadian markets appear poised to finish a strong year, but we caution investors as they contemplate their portfolio positioning for 2007 – moderation is the key! Take a balanced and diversified approach to investment management and you will be merrier in the long run. And speaking of merry wishes, we want to take this opportunity to wish everyone a happy and prosperous 2007 and may you find your riches in good health and good company.

Table 2 - Sector level results for the Canadian market

S&P/TSX sector returns	Nov.	YTD
S&P/TSX	3.3%	13.1%
Energy	2.5%	4.0%
Materials	8.9%	37.5%
Industrials	0.0%	14.6%
Consumer discretionary	1.3%	12.0%
Consumer staples	2.9%	0.6%
Health care	6.2%	-4.9%
Financials	3.6%	12.4%
Information technology	10.6%	22.9%
Telecom services	-8.4%	13.5%
Utilities	1.2%	-3.2%

*price only

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