



The Quarterly Letter

The Quarter in Review...

Published since 1992

The first quarter of 2005 paid off correctly for our typical customer, but things would have been even better if not for the month of March. Canadian stock markets were generally favourable, but our choice of securities also helped our cause. The financial sector (i.e. banks) as well as the base metal industry allowed us to post significantly better results than comparable indices.

As mentioned in the *Review of Portfolio Activities* column on page 5, we were not idle during the quarter, a period of the year that is already quite busy.

We look to the end of the year with a rather careful optimism.

Stock markets have performed relatively well in the past two years and are trading at levels, which we do not consider exaggerated as many advance, but which are not at bargain prices either. We are worried by various factors which could slow down the current fragile economic growth even further and by the numerous and potentially "explosive" effects of the gradual transfer of economic power from the West to the East.

Long-term opportunities are still present for patient investors, but it is clear to us that their long-term convictions will be tested again in a few years (similar to the period at the



beginning of 2000) in an environment of short-term volatility. We shall try then again to take advantage of the markets rather than being subjected to them.



The Dalpé-Millette Group

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Selected Statistics

Month	Interest Rates			Stock Exchanges			Currencies		
	Canada Short-Term	Canada Mid-Term	Canada Long-Term	CAN TSX/SPX	USA DJII	Intern. EAFE	USA\$	EURO	YEN
Dec. 2004	2.47	3.68	4.30	9247	10783	1515	0.8303	0.6077	85.60
Jan. 2005	2.43	3.71	4.21	9204	10489	1487	0.8072	0.6194	83.56
Feb. 2005	2.46	3.77	4.29	9668	10766	1549	0.8072	0.6097	84.95
Mar. 2005	2.56	3.87	4.32	9612	10503	1504	0.8220	0.6350	88.40



The Bond Market

As expected, the Bank of Canada once again opted for the status quo with regards to key interest rates, during its meeting of March 8th. The last increase of Canadian key interest rates dates back to October 19th, 2004, when the monetary authorities increased the cost of renting money by 25 basis points, for the second consecutive time. It is necessary to underline that this break in monetary tightening is justified because of the difficulties engendered by the sharp appreciation of the Canadian dollar in the second half of 2004. In its monetary policy decision-making process, the Bank of Canada must inevitably take into account the behaviour of the Canadian dollar, which influences both foreign demand for goods and services manufactured in the country and

Canadian demand for goods and services manufactured abroad. The bank's key rate has thus been kept at 2.5% since last October.

Meanwhile, the American Federal Reserve began its campaign of monetary tightening. Since June 2004, the American central bank has increased its leading rate on seven occasions, by 25 basis points each time, for a total of 1.75%. Consequently, the American leading rate has risen to 2.75% from 1% eight months ago.

Since mid-February, long-term American bonds have dropped by \$8 US, from \$116 US to \$108 US. The rate of return has risen to 4.82% from 4.36%. On the Canadian market, even if the reaction was more mitigated, the tendency was the

same. The increase of raw materials and petroleum will inevitably have an impact on inflation. For this reason, long-term rates began to rise. In a context of increasing inflation, investors in long-term bonds demand higher rates to compensate for the deterioration of purchasing power. What Mr. Greenspan had difficulty understanding last month was that bond rates were falling while the central bank was increasing short-term rates. The enigma has been resolved since long-term rates are now rising.

For the first quarter of 2005, the Canadian bond market, represented by the Scotia McLeod index, surpassed the American market. It posted a return of 1.10% compared to -0.40% for the American bond market over the same period.

The Bank of Canada stays put while the Federal Reserve increases its rate once again.

The Currency Market

The economic and financial context has changed significantly over the last few months, which has disrupted the upward movement of the Canadian currency. Having reached a peak of a little over \$0.85 US on November 26th, 2004, the loonie is in a definite downward trend over the last months. In January, the loonie took its worst monthly tumble since last April, losing 3% against the USD.

Faced with the Bank of Canada's status quo and the cycle of tightening in American monetary policy, Canadian rates are now lower than American rates over the entire yield curve. Usually, this situation should cut the

Canadian dollar's oxygen supply in its rise against the greenback, nevertheless the loonie reached a six-week peak on March 8th of this year. What happened?

One factor threw a monkey wrench into the equation over the last few weeks. The price of raw materials continues to set new records, which masks the unfavourable effect of interest-rate spreads for the loonie. The Reuters-CRB index, the natural resource benchmark, hit a 24-year high. This index, which includes petroleum, corn, wheat and metals, increased by 11% last year, 9% in 2003 and 23% in 2002. Raw materials com-

prise 35% of Canada's exports and 10% of its economy. Canada thus continues to benefit from a significant shock to the terms of trade that props up the currency.

In conclusion, since the beginning of the year, the Canadian dollar has retreated by 0.83% against the American currency.



Resources lead the attack and the loonie takes advantage of the situation.

Canadian Stocks



The year 2005 seemed to start off on the wrong foot but, after taking a few steps backward, the S&P/TSX ends the first quarter with a return of 4%. With three months into the new year, the Toronto Stock Exchange still thumbed its nose at its American colleagues, which are still bogged down in negative territory; a vague recollection of last year. In spite of this weak start, better than expected results in the 4th quarter of 2004 have stirred investors' optimism and confidence this quarter.

Overall, 6 out of 10 sub-indexes were on the increase at the end of the quarter. It is no big surprise that the energy sector is ranked first. Indeed, the latter posts the most significant gain of the TSX, i.e. 17.6%, thanks to a cold spell in North America, which had the effect of ballooning oil prices beyond \$55 US. Alone, the gas and petrol industry harvested 17.7%. The firmness in the price of oil, as well as in the price of metals, such as zinc or copper which reached

record prices this quarter and which are dependent on the industrialization of China, acts like a valve to the Canadian market, these two sectors representing 37.2% of the TSX. For their part, the telecommunication services, industrial and consumer staples sectors followed each other closely with respective returns of 6.4%, 6.5%, and 5.1%.

On the other hand, the lowest performance for the 1st quarter is attributable to the information technology sector, which posted the worst results of the TSX and which ended with a return of -10.4%. As for the health sector, in spite of a good start in 2005, the latter finds itself in negative territory at -5.9%. In spite of the positive contribution of 6.4% from pharmaceutical products, biotechnologies sunk the sector with a disastrous performance of -16.4%.

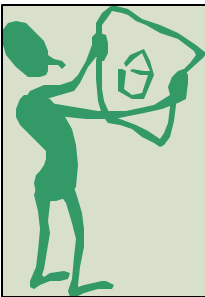
The Canadian economy started 2005 out of breath and in full swing with its two-speed dy-

namic: weakness from the outside and firmness inside. Exports resulted mainly from energy and automobile products, while imports emanated from almost every sector of activity, a sign of the vitality of Canadian domestic demand.

Building activity remained steady. In February, national housing starts were an annualized 200,000 units for the 21st consecutive month, the longest period since 1989.

However, inflation remains under control in Canada, still falling within the median target range of the Bank of Canada. The stability of inflation, added to the vigour of the loonie, gives our Central Bank a significant leeway in the application of its monetary policy.

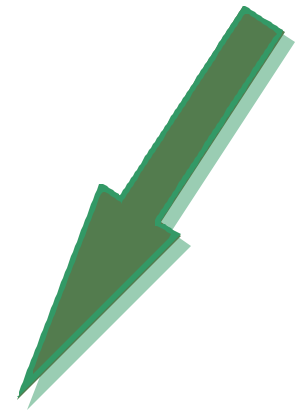
In spite of some turbulence at takeoff, the TSX posts a satisfactory return.



Over the past few months, we have been drafting a document with respect to our customer investment policy. **The aim of the investment policy is to clearly define the customer's objectives and constraints as well as to define the tools and strategies available for the manager to meet the customer's objectives, taking into consideration the latter's constraints.**

Regulatory authorities require that such a document be prepared for each customer having one or more managed accounts and that it be approved by the customer. The document must also be reviewed and updated when appropriate.

You should have received this document in the last few days, completed it and returned it in the pre-addressed and postage paid envelope. If this is not the case, please do so as soon as possible. Thank you for your understanding.



US Stocks



Unlike the Canadian stock exchange, American indices were not off to a good start at the beginning of 2005. The index of the 500 largest American companies slid 2.7% in January alone. Less present in the natural resources sector and more affected by the increasing price of oil since the beginning of the year, U.S. stock markets attempted a vigorous return in February and in early March to remedy the drop of January, but to no avail.

The Dow Jones and the S&P 500 posted identical drops of 2.6% in this first quarter of 2005. For its part, the Nasdaq is in a shaky state and lost 8.1%. After taking a few steps backward at the beginning of the year, the Dow Jones index shot

off in March and narrowly missed the 11,000-point mark, its threshold set in June 2001.

Afterwards, the American stock exchanges experienced many animated sessions, marked by spectacular variations in oil prices. Moreover, the price of a barrel of oil jumped to a record high in New York, in mid-March. OPEC (Organization of Petroleum Exporting Countries) was prompt to react and its president announced an increase in oil production for the fourth time within a year in order to control the increase in the price of oil.

The trade deficit remains the Achilles's heel of America's growth. The deficit for January is the second largest ever re-

corded in the United States. It can notably be explained by the jump in imports of consumer goods. For its part, the labour market is in a better state. The most recent employment figures at the beginning of March surpassed expectations. Furthermore, statistics demonstrate that consumer spending in the United States was solid at the beginning of 2005. However, productivity is running out of steam, increasing unit labour costs.

A trying beginning of the year for American stock markets.

International Stock Exchanges



Under very expansionist monetary policies, the leading indicators of the world economy continue to be on the rise at the beginning of year. However, high and volatile world oil prices remain a risk factor for global economic growth.

In the euro zone, the economic situation is not improving. In Germany, unemployment reached a new record high, representing the highest unemployment level since 1932. Furthermore, business confidence fell to an 18-month low in March. This increase in unemployment and the surge in oil prices have caused retail sales to fall in the twelve countries of the euro zone. Never-

theless, German industrial production experienced its sharpest increase in the last ten years. France, Italy and Germany end the first quarter of 2005 with respective returns of 6.5%, 4.1% and 2.2%.

The United Kingdom's economy is maintaining a steady course. Its stock index ends the first quarter on a positive note with an increase of 1.7%.

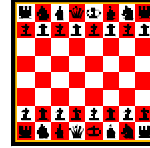
The Japanese market has been supported by favourable economic data; exports, production and business hiring are progressing. The NIKKEI 225 ends the first quarter with a return of 1.6%.

Chinese exports have been growing at a robust pace and foreign trade has posted a surplus for a tenth consecutive month. Industrial production rose at a rate higher than expected in the first two months of 2005. It should be noted that Chinese growth alone represented nearly a quarter of world growth in 2004.

Following an increase of approximately 22% in China's consumption of nickel last year, demand continues to grow this quarter. As a result, the price of basic metals climbed to a new record.

The appreciation of black gold continues to be a worrisome factor.

Review of Portfolio Activities



We were fairly busy with portfolio transactions this quarter, as we were at the same period last year.

Our portfolio transactions revolved around three general themes:

1. the reduction of approximately 15 to 20% in the weight of shares within balanced portfolios, in reaction to the increase of stock market prices in the last two years and our desire to maintain a neutral, if not slightly conservative, asset distribution (% of income securities versus % of equity securities). We find it quite difficult to be very optimistic while faced with stubbornly high oil prices, an American currency constantly under pressure and an American central bank that persists in raising short-term interest rates (and has tried to do the same with medium to long-term ones) in spite of a fragile economic background;
2. the end of transactions within our fixed-income securities, which aimed to extend the average duration of the latter. To achieve this, we have reduced our liquid assets and purchased longer-term

securities (2010 and 2035). The result of all these transactions, which began in the fall of 2004, was to bring the average duration of our income securities (excluding the portion invested in the very short term) to approximately 10 years with a return of approximately 4.6%. To counterbalance this relatively long duration, we still hold a portfolio with approximately 27% in liquid assets, i.e. close to half of all our income securities; and

3. we liquidated our investment in Europe, reduced our investment in Saputo and liquidated our Novelis shares received after their distribution by Alcan. We reinvested a portion of the total in Falconbridge, which has since received an offer from Noranda to purchase its outstanding shares. At the end of quarter, we disposed of approximately a quarter of our investment in Teck Cominco and Falconbridge (soon Noranda-Falconbridge) for the following reasons:

the stock prices for these two securities have greatly appreciated since

their acquisition and considering the cyclic nature of the shares in this sector, profit-taking seemed appropriate; and

the unremitting increase of short-term interest rates in the United States makes us feel less comfortable with regards to the strength of the economy and with the maintenance of the price of raw materials at current levels. We wish to reduce the weight of our securities in this sector with these sales. Let us be clear, we still believe in the sector and particularly in these securities, but we prefer to adjust the proportion.

A busy quarter where asset distribution became more conservative and where both income securities and shares were affected.

Members of the Dalpé-Milette Group:

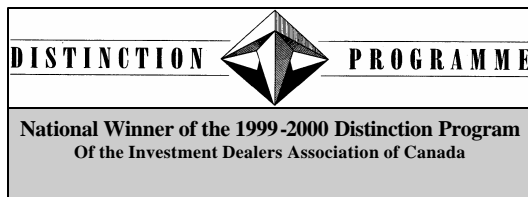
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The Dalpé-Milette Group



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Info Sabius



For our clients who wish to obtain more information about financial markets as well as the views and thoughts which direct our portfolio management decisions, our Info Sabius meets these requirements. It is sent on a daily basis either by fax or by e-mail to our clients who wish to be kept abreast of their portfolios and the many issues which affect them. Please do not hesitate to contact us should you be interested in receiving it.



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