



The Quarterly Letter

The Quarter in Review...

Published since 1992

Our expectations for the beginning of 2006 finally materialized in 2007. Marked by significant market volatility, this quarter has not allowed the portfolio of our typical client to increase.

After some 45 days of interesting performance, stock markets were shaken in the second half of the quarter by a series of significant and disparate blows. Between the one day decline of 9% on the Shanghai Stock Exchange, the return to reality with respect to the phenomenon of sub-prime loans or of almost unlimited access to credit (especially in the real estate sector) in the United States, the fears of an economic slowdown and a rise in interest rates, the "bears" (i.e. the stock market pessimists) had a complete menu to select from.

Stock exchanges around the world ended the quarter in neutral or small rise territory. This kind of correction reminds us of the spring of 2006, but corrections have nonetheless been rather uncommon since the recovery in stock markets at the end of 2002.

We don't know if the correction is over, but in our opinion, it is nearing its end. If ever it continued, it would certainly offer us interesting investment opportunities, which we would try to take advantage of. Our typical client holds 27% of his portfolio in very short-term investments (less than one year); this represents a source of defensive investment but also of available cash should the need arise.



The table at the bottom of page 5 reminds us that our typical client had to wait until the third quarter of 2006 before his portfolio took off to end the year with a respectable performance. Annual returns can vary considerably from one year to the next, which is also true from one quarter to another within the same year.



Le groupe Dalpé-Millette

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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. 2006	4.17	3.99	4.09	12908	12463	2075	0.8581	0.6504	102..21
Jan. 2007	4.17	4.09	4.18	13034	12622	2087	0.8459	0.6528	102.21
Feb. 2007	4.19	3.95	4.03	13045	12268	2102	0.8614	0.6523	103.18
Mar. 2007	4.17	4.02	4.11	13165	12354	2147	0.8655	0.6491	102.06

The Bond Market



Over the past two years, bond markets have succeeded in fooling the experts, who believe that bond rates are too low and that a spike in rates will eventually result in negative returns for bonds.

Indeed, in 2005, as measured by the *Scotia McLeod Universe* index, the Canadian bond market posted a return of 6.5% and 4.1% in 2006. Will 2007 be different?

For the sixth consecutive time and to no one's surprise, the Bank of Canada kept its key interest rate unchanged on March 6th. The comments accompanying the announcement held no surprises, as the speech was essentially identical to the one at the beginning of January. The benchmark overnight lend-

ing rate remains steady at 4.25% since May 2006. Under the circumstances, the Bank of Canada is maintaining a steady course and is repeating that the risks of inflation are roughly balanced.

In the United States, the Federal Reserve maintained the monetary status quo for the sixth consecutive meeting. The announcement that accompanied the decision no longer mentioned an upward bias. The American benchmark interest rate held steady at 5.25%, its level since late June 2006, following 17 consecutive increases of a quarter of a point.

Bond markets faced significant volatility this quarter. Whenever stock markets experience strong shocks, investors tend to

take refuge in the bond market. This was the case on February 27, when the Chinese stock market plummeted, dragging the rest of the world's markets along in its wake. In one month, from February 13 to March 12th, the Canadian long-term bond yield dropped from 4.27% to 4.12%, while two-year bonds slid from 4.11% to 3.84%.

By and large, for the first quarter of 2007, the Canadian bond market, represented by the *Scotia McLeod Universe* index, has posted a return of 0.9% and the American market registered a return of 1.5% over the same period.

The Currency Market



The beginning of the year was rather difficult for the Canadian dollar. Since the end of 2006, the Canadian dollar has been sucked by a downdraft, victim of the decline in the price of raw materials, of lacklustre economic statistics and of a change in the expected timing for the first interest rate cuts in United States. In January, the Canadian dollar fell to its lowest level in more than a year at \$0.8437.

Nevertheless, the dollar made a comeback in March. Unexpectedly high inflation data and a higher than expected Federal budget surplus ended the lethargy that was shaking the Canadian dollar. The decline of short positions in Canadian dollars

also contributed to the appreciation in our currency. On March 20th, our currency increased by 125 basis points to end the day at \$0.8616 US. One would have to go all the way back to May to find a similar one day increase and to February 26 for a market close over \$0.86 US.

The American dollar began 2007 on a strong note with an increase of 1.4% (weighted with respect to other currencies). This strength was easily explained: almost all economic indicators published during January were above market expectations. But in February, the wind changed direction and the greenback surrendered all of its gains. This decline can be partly

explained by a series of disappointing indicators. However, the spark came from Fed President Ben S. Bernanke's report, which forecasted lower-than-expected economic growth. This change in outlook transformed speculators into net sellers of USD for the first time since the beginning of January. The American dollar will remain under pressure, especially if indicators continue to suggest economic growth lower than the trendline.

The Bank of Canada isn't budging.

The American dollar remains under pressure.

Canadian Stocks



The year 2007 has begun with a saw tooth wave pattern even though the Canadian economy is running smoothly. In January and February, the leading Toronto index suffered from the repercussions of the decline in the price of a barrel of oil. March began on a negative note, victim of the shockwave from the Chinese stock exchange, which dragged stock markets into a global selling trend. The TSX thus began the year with a return of 2.0% exceeding the S&P 500 at 0.2%, which is experiencing the same negative effects from China.

Even though the stock market has retreated in the 1st quarter, this did not prevent some sub-sectors from posting positive returns. The Telecommunications is a strong first with a return of 7.0% due, among other factors, to the excellent performance of Telus and Rogers, which have posted results greatly exceeding analysts' forecasts and BCE which benefited from take-

over rumors. Industrials follows in second place with 6.4%. The road and railway transport sub-sectors have performed well as has the air transport sub-sector, which has been very popular in this 1st quarter. The Consumer Discretionary sector comes in third place with 4.3%.

The Health Care (-3.3%) and Utilities (-6.9%) sectors remained stagnant.

If the Canadian economy is supported by internal forces, employment continues to amaze us with solid results, such as 141,400 new jobs in two months, propelling the employment rate to new highs. With employment helping the residential real estate market, construction starts jumped 17% in January. In spite of the increase in employment, this did not prevent the unemployment rate from rising marginally from 6.1% to 6.2%.

The Consumer Price Index

(CPI) increased by 0.7% in January and February, a stronger increase than expected, but in great part due to the strong increase in the price of gas.

The global rate of inflation is around 1% and in these circumstances the Bank of Canada is staying the course with a target rate of 4.25%. The slowdown in the rate of inflation is reflected essentially by the drop in the price of energy due to milder temperature. And the story goes on...

The Canadian stock market hardly ends the 1st quarter in positive territory, in step with world indices. The likely economic slowdown poses a threat to the cyclical Canadian resource sector.



More Movement Within the Dalpé-Milette Group!

Mrs. Audrey Sanchez is joining our team.

Audrey holds a degree in Business Administration from France. She has performed various assignments in executive coordination in France and in Quebec.

She will be responsible for supporting business development efforts and for providing administrative support to our ever increasing clientele.

US Stocks

In January, in the land of Uncle Sam, the main stock exchanges ended the first month of 2007 in positive territory (Dow Jones +1.3%, S&P 500 +1.4% and Nasdaq +2.0%). We cannot say as much for the second half of quarter.

The downturn in the American markets, triggered on February 27 by the massive sales on the Chinese stock market, ended a string of 228 consecutive days without a correction of 2% or more. The leading index, the Dow Jones, lost over 400 points that day, its strongest point decline since September 2001. In so doing, Wall Street experienced its worst week in four years.

Following four years of an al-

most non-stop bull phase, the reverberations felt by North American markets after the Chinese dragon's convulsion are not overly surprising. That said, the first quarter of 2007 ended with returns of X.X% for the Dow Jones, X.X% for the S&P 500 and X.X% for the Nasdaq.

Statistics are numerous and rather gloomy in the real estate market, which has been the main engine of growth for a long time. In March, construction starts tumbled 38% over the previous 12 months while sales of new homes sank to their lowest level in 13 years. The sluggish state of the housing market is omnipresent but, on Wall Street, economists think that the threat of contagion of the housing collapse is rather

limited. Combined with this weakness, the deterioration in the quality of mortgage credit remains an element of risk and is at the center of the latest worries. In February, manufacturing activity intensified whereas the non-manufacturing index, representing more than 80% of the American economy, reached its lowest level since April 2003.

Despite disappointing retail sales and a retreat in consumer confidence, industrial production is surprising with results stronger than expected. After impressive corporate profits in the 4th quarter, we will now have to await the upcoming results for the 1st quarter of 2007.



The stock markets perform an unavoidable about-face at the end of February and experience a moderate slowdown thereafter.

International Stock Exchanges

According to several strategists, the recent downturn on exchanges around the world is a necessary evil to absorb the excess liquidity in the financial markets and to restore a healthy awareness of the risks associated with investment.

The German, French and Italian indices end the first quarter of 2007 with respective returns of 4.9%, 1.7% and 0.3%. In the United Kingdom, the British index closes the first three months with a return of 1.4%. In this country, retail sales experienced their strongest increase in over two years in February.

The Hong Kong Hang Seng index ends the same period with a return of 0.8%, after experiencing its best year ever in 2006. In Tokyo, the world's second financial hub, the Nikkei 225 index ends at 0.4%.

The significant downturn of close to 9% on the Shanghai Stock Exchange last February 27 is not that dramatic considering the increase of 130% in 2006 and that securities were being sold on average 38 times their profits. Furthermore, this stock exchange is not the best barometer for the health of the Chinese economy. Of particular interest, industrial production increased by 18.5% during the first two months of year in China.

European markets were no exception and also experienced a painful awakening the day after the Asian storm, with investors fearing that events in China might trigger a slowdown in world growth. The Dow Jones Stoxx 600 index retreated 5.2% during this dark week, but ends the quarter up 2.5%.

Contrary to all expectations,

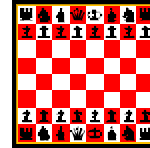
confidence indices in the euro zone improved according to February statistics. Data with respect to the labour market is encouraging; the unemployment rate, in particular, is decreasing. Exports also look good, growing at their strongest pace in 6 years. However, retail sales were weak following an increase of the sales tax in Germany, which put a damper on consumer spending.

In conclusion, both the U.S. Secretary and the Japanese Minister are seeking to reassure the public. They also both share the opinion that the fundamentals of the world economy are solid and that the markets should reflect this established fact.



Put in perspective, the episode in China is not overly disconcerting.

Review of Portfolio Activities



The first quarter of the year is always fairly demanding. There is, naturally, the RRSP season and then there are requests for fiscal information pertaining to income tax returns. But this year, in particular, we were rather occupied reading and analyzing the opinions of several analysts and financial market managers so as to form our own opinion on the direction of the markets.

We believe that the current market correction is only a correction and not a deep trend reversal in the economy or in financial markets. Our recent Info Sabius issues alluded to this often. We believe that the problems in the American real estate market will not degenerate in the United States, and even less so on a global level. Aside from the impact of this temporary volatility, we are of

the opinion that none of our investments will suffer in a significant or permanent way. In fact, we are rather optimistic about the next few years.

Since the current correction was not substantial and since we are close to completing our thoughts on the orientation that we want for our portfolios in the upcoming years, we chose to let things be and not intervene through trading.

As portfolio managers, we are always ambivalent between the hope to protect the current value of our portfolios and the wish to see the market fall in order to take up positions in undervalued securities and thus profit from them over the medium and long term.

Some years ago, we chose not to be invested in the United

States. This decision turned out excellent and recent events in the economy of this country incite us to stay the course. If the American economy were to suffer more than we expect from the current real estate collapse, monetary authorities would have no choice but to lower interest rates, which would, in our opinion, bring another significant decline in the American currency. A situation that does not incite us to return to this market for now.

We should be in a position to make our opinion regarding the desired structure of our portfolios clear in the next few weeks. To be continued...

When the markets are going nowhere or are in a slow decline, it is tempting to make major changes. In such cases, patience is still a virtue.

Our Typical Client

2006 Quarters	Quarterly Return	Cumulative Return (year-to-date)
1 st	3.94%	3.94%
2 nd	(3.36)%	0.45%
3 rd	4.60%	5.06%
4 th	6.43%	11.80%

Six months into 2006, the portfolio of our typical client had gotten nowhere, victim of a difficult second quarter caused by a downturn of the markets. This kind of behaviour is not unusual and often offers interesting opportunities.

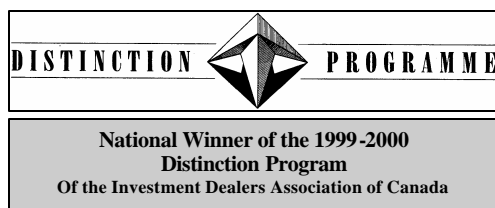
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Info Sabius



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