



The Quarterly Letter

Published since 1992

The Quarter in Review...

As increasingly frequent signs highlight the sturdiness of the world economy, stock markets pursue the progression they began in the spring. This has allowed the portfolios of our clients exposed to these markets to post an interesting appreciation during the quarter ending September 30th; for our typical client this represents approximately 5.1%.

Although, we cannot expect, in the future, a progression of the same scale as the one seen in the last six months, and taking into consideration that cooling-off periods or downturns are inevitable, we remain optimistic that the stock markets will continue to be favourable to

portfolios in the next quarters. We believe that the balance found in our portfolios, whether by sector or by geographic region, will promote growth without taking undue risks. Furthermore, the short duration of the average term of our fixed income securities limits our risk in the event of a spike in interest rates, as the current economic recovery becomes a reality.

In our Info Sabius of last February, we mentioned that: "... it seems clear to us that an important turnaround in the stock market is to be expected." It is easier to assert this today than it was last winter.



Our move to Desjardins Securities is henceforth a thing of the past and the far from spectacular routine of portfolio management has returned to its ways of days gone by.



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
June 2003	3.09	3.61	4.45	6983	8985	1026	0.7404	0.6495	88.85
July 2003	2.85	3.84	4.84	7258	9234	1049	0.7139	0.6294	85.88
Aug. 2003	2.68	4.16	4.88	7510	9416	1072	0.7222	0.6577	84.48
Sept. 2003	2.60	3.78	4.56	7421	9230	1103	0.7391	0.6375	81.91



The Bond Market

As expected, on September 3rd, the Bank of Canada lowered interest rates by 25 basis points to 2.75% for the second time since July. The Canadian economy, which had the fastest growth within the G7 at the beginning of the year, was manhandled by the SARS epidemic, mad cow disease, the strengthening of the Canadian dollar and a power blackout in Ontario.

By sliding back to 2.75%, the leading rate returns to its level at the beginning of 2003, that is to say just before the two increases of 25 basis points by the Bank of Canada last winter to contain inflation. These two increases were afterward cancelled by two decreases of the same order within the space of two months.

In Washington, the American Federal Reserve did not modify its leading rates either in August or in September, as expected by

financial markets, but moreover, it added that leading rates would stay at their current level, their lowest in over 45 years, for a "considerable time". The call (day-to-day) money rate between banks, that of the *Federal Funds*, remains at 1% and the discount rate at 2%. The American central bank lowered its rates 13 times since January 2001 to stimulate the economy. The last decrease of 25 basis points was last June 25. It was the only one since the beginning of the year.

During the last few months, bond investors lived through an uncommonly turbulent period. Indeed, since June, the American bond market has plummeted by 3.35%. We have to go back to 1994 to find an equivalent fall.

The American bond market hit a record high on June 13, when the 10-year Treasury rate posted an exceptionally low 3.11% yield.

The market has made a radical roundabout turn since then, to take off in the opposite direction. From 3.11%, ten-year rates have reached 4.5% within a few weeks. In Canada, because the initial decline in rates was not as significant, the ascent was less breathtaking. For the same period, the 10-year bond yield fell to 4% in June, only to rise again to 4.8%.

During this bumpy period, the Canadian bond market, measured by the *Scotia McLeod* index, surpassed the American market this quarter. It posted a return of 1.3%, while the American market posted a negative return of -1.0% for the same period.

The Bank of Canada lowers its rates twice this quarter.

The Currency Market

Following years of less than shiny performances, the loonie has taken flight. The Canadian dollar recorded the strongest appreciation in its history in the first six months of 2003: + 17% against the American dollar, which brought the currency from \$0.63 US last January to almost \$0.75 US at the end of June.

However, this pronounced and very rapid appreciation, coupled with the appearance of SARS and mad cow disease, has forced the Bank of Canada to modify its monetary policy. On July 15, the Bank of Canada surprised financial markets by decreasing its rate by 0.25%. Although justified, this decline, unexpected by the finan-

cial markets, was a real letdown for the Canadian currency. This decrease in rates combined with the recent appreciation of the USD against all major currencies, pushed the loonie down. During the month of July, the loonie lost 5.4% against the greenback. But its performance against other currencies is far from disastrous since its peak on June 18. The loonie has lost only 0.3% against the Euro and 1.4% against the Australian dollar. It gained 0.18% against the pound sterling. However, the decline of the loonie in July was short-lived.

While writing these lines, the loonie has increased to its highest level in two months, passing the

\$0.74 US mark. The loonie strengthened its position against the American dollar following a statement from the G7 Ministers of Finance. They tried to convince countries to allow floating exchange rates. The yen, which reached its highest value in over two years and a half on September 8th, should pursue its ascent on exchange markets in reaction to the G7 communiqué. The communiqué does not specify names, but doubtless to say that the message was intended for China and Japan.

The yen reaches its highest value in over two years.



Canadian Stocks



In Canada, the S&P/TSX composite index has increased by 6.3% this quarter. Seven of the ten sub-indexes on the Toronto trading floor ended on a positive note. Due in large part to the good performance of cyclical securities, the Canadian stock market has behaved better than the American market since the end of June.

The information technology sub-index leads the pack with a gain of 32.1% this quarter. The technology industry, which is recovering from a significant clean up (bankruptcies and acquisitions), gains 62.5% to date in 2003. Companies have renewed spending in technology to replace their obsolete equipment, suppliers' order books are filled and there is very little merchandise in stock.

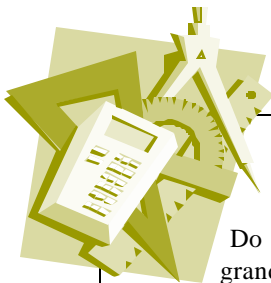
The basic materials sub-index also recorded strong progress this third quarter, ending with an increase of 16.0%. The recent increase in the price of raw materials is justified by the acceleration of world economic activity. In addition, the industrial sector, the discretionary consumer goods sector and the financial sector end with respective returns of +10.9%, +6.5% and +3.9%.

Contrary to our southern neighbours, the pace of the Canadian economy slowed down. According to the latest data, the decline in GDP can be explained to a great extent by a decrease in inventory and a faster growth of exports against imports. After having performed well during all of 2002, the labour market in Canada is facing a difficult time.

However, consumers continued to support economic activity, and let us note that consumer expenditures represent 60% of the country's GDP. The governments followed suit, increasing their expenses. Construction starts also took off in Canada this summer.

In short, the good behaviour of several indicators (notably gains in productivity) and the sheer amount of liquid assets that offer no more than a very modest return can supply enough fuel to sustain the stock market over the next few months.

The key Toronto index rose 6.3% this quarter and the Canadian economy is taking a break.



Registered Education Savings Plan (RESP)

Do you worry about your child's future education? The future of your godchild, granddaughter or grandson is close to your heart? Accumulate capital now for education purposes. The RESP can satisfy this specific need.

This plan allows you to act as a subscriber and to contribute regularly on behalf of a beneficiary of your choice. The growth of the RESP is accelerated thanks to the Canada Education Savings Grant (\$400 for the 1st \$2,000 contribution or 20%) added to the tax-exempt status of the investment income. The amount accumulated will be used to finance the beneficiary's post-secondary studies (college, university or other).

The maximum annual contribution is \$4,000/beneficiary and the **contribution expiry date is December 31 of each year**. After your contribution to a RRSP and the reimbursement of your debts, a RESP is the vehicle of preference to invest supplementary annual savings.

For additional information, do not hesitate to contact us. Close to one hundred of our clients, in addition to us, already take advantage of a RESP. This savings plan is particularly popular amongst grandparents.

US Stocks

The economic recovery and very low interest rates belied the prevailing custom that the stock market posts a stable or negative performance during the summer months. The S&P 500 index, which is the best reflection of the health of the American stock market overall, exceeded the critical threshold of 1,000 points during several consecutive sessions this quarter and ends with an increase of 2.2%. The Dow Jones, for its part, closes the quarter on the rise at 3.2%.

The Nasdaq, the reference mark for American technology stocks, gains 10.1% this quar-

ter, bringing its increase to 33.8% since January. Having undergone the strongest depreciation with respect to other market indexes, the Nasdaq has profited the most from the return to an upward swing of the pendulum.

At the end of the summer season, Uncle Sam's economy pursues its second quarter momentum. A first in almost 4 years, U.S. growth surpasses that of Canada according to recent economic data. This can only be a good omen for the Canadian economy, which depends on the American market for a third of its output.



Supported by tax cuts, Americans continue their spending. However, in spite of signs of recovery, the employment situation remains the weak link in United States. The manufacturing index strongly increased, particularly with respect to production and new orders. This increase in productivity, combined with a prolonged expansionist monetary policy, provide significant support to growth. This scenario is motivating strategists to anticipate further increases in profits for the current year, a first since April 2000.

Signs accumulate and confirm the dynamism of the current economic recovery in the United States.

International Stock Exchanges

The prospects for the world economy improved in the third quarter of 2003. The OECD composite leading indicator progressed strongly this summer.

Signs of recovery appear in Germany. In August, the investor economic growth forecast index reached its highest level in a year. The same story applies to the service index, which surpassed the peak set in July 2002. This series of good news prompted the European Central Bank to opt for the status quo and to maintain interest rates unchanged in September.

Japan also offered good news this summer. Taking advantage of the upturn in Japanese industrial production, of the strong economy of its Chinese neighbour and of expectations fed by the American recovery, the NIKKEI 225 jumped 8.2% in August, the best performance amongst major world indexes and its best performance since 1999. Furthermore, companies began to invest again in machinery and equipment, and exports are rising. The rebound in bank securities is also sending an encouraging signal for the economy. The Japanese stock exchange ends the quarter with an appreciable gain of 12.5%.

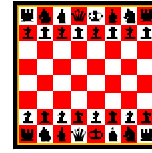


Showing signs of its vigour in this quarter, China's industrial production was up 17% in August. With over 20% of world industrial production, China will be one of the major beneficiaries of a resumption of world-wide demand.

Following in the trail of American stock markets, world markets ended the quarter on the rise. Germany, France and the United Kingdom posted respective returns of 1.1%, 1.7%, and 1.5%. As to the Hong Kong Hang Seng index, it gained 17.3%.

Following years of lean times, the Japanese economy revives.

Review of Portfolio Activities



We did not intervene within the fixed income securities portion during the quarter. We maintained our policy to favour a short average term approach by using either securities with near-term maturities or ones bearing a floating interest rate. We do not wish to relive 1994, when a sharp increase in interest rates significantly rolled back the market value of income securities.

On the equity securities front, we proceeded with the sale of the balance of Telesystem International (TIW) shares, the latter representing an insignificant weight within portfolios, in spite of their rebound of almost 200% lately. The disappearance of this security from monthly statements will stop reminding us of the few misfortunes of the 2000-2002 period.

We cut approximately a third of our participation in Alcan to stash away some of our profits

(35% within a year) after the significant increase of the security following the Pechiney transaction. We remain confident that this acquisition, done within the context of an economic recovery, will be beneficial for Alcan, explaining why we are holding on to the majority of our investment.

Finally, we have added to our participation in Asia; we were in South-East Asia but not in Japan. There are increasingly stronger signs that the Japanese economy is coming out of its sluggishness and that stock markets are beginning to recognize this. Our Info Sabius of September 18 draws attention to this point. To put everything in perspective, let us remember that the Japanese NIKKEI is at a quarter of the value it reached 15 years ago, while the American Dow Jones has increased 3.5 times during the same period. The pendulum will eventually return to favour Japan,

and we believe that it likely has just begun.

Finally, we sold our participation in the Nasdaq 100 index vehicle at the end of the quarter. The 35 percent increase in the index in 2003 seems exaggerated to us considering the current and foreseeable progress of the underlying corporate earnings. The valuation of these securities brings back memories of the spring of 2000 leaving us with an unpleasant impression. Furthermore, we wish to reduce slightly our exposure to the American dollar, which according to us will continue to be under pressure.

Stock market indexes might face a setback in the next few months. We shall take advantage of this situation to make a few tactical purchases.

Profit-taking in Alcan, and investment in Japan. Sale of Nasdaq 100.



Portfolio Management Quiz

During 2003, we will quiz you to measure your understanding of the analysis of your investment portfolio return and to understand your appreciation of our role as investment advisor.

Question 5: Which of the following two portfolios is more likely to better perform in a bear market ?

	<u>Portfolio A</u>	<u>Portfolio B</u>
% cash assets	5%	5%
% income securities	70%	45%
% shares	25%	50%

Answer:

Portfolio A, being less exposed to the stock market (lower % in shares), will perform better in a bear market. However, its performance will be lower in a bull market.

Question 6: The manager of Portfolio A indicated above generated a 7% return last year, while the manager of Portfolio B generated an 8.5% return. Which of the two managers has done the better job?

Answer:

It is impossible to determine without further information. At first, we might be tempted to favour manager B, however the yield differential of 1.5% was made possible by doubling the weight of equities within the portfolio (doubling the 'risky' portion). It is possible that a return of 7% with a portfolio composed of only 25% in equity represents a better result than a return of 8.5% with twice the equity percentage.

The risk/return relationship is the basis of any work assessment of the work performed by a portfolio manager.

Question 7: How do we assess the work of a portfolio manager?

Answer:

Comparing one manager's performance with others for similar portfolio profiles and for the same periods is the most accepted and simplest method.

Statistics for many types of portfolios or asset classes are published monthly for most Canadian managers. This is a very useful basis for comparison. Among other things, the statistics show the performance for the 1st quartile (the best 25%) and the median (best 50%) portfolio managers for a given period.

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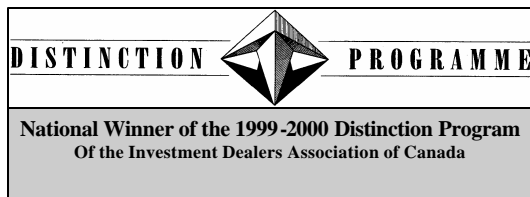
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The Dalpé-Milette Group



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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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