

NATCAN SMALL CAP EQUITY FUND

Management Approach We favour a growth-oriented style, which is particularly appropriate for the management of small caps. However, unlike other managers, we pay special attention to the preservation of capital and seek growth opportunities across all sectors so as to diversify value-added sources. We offer a real small-cap Canadian equity product and, as such, we don't hesitate to liquidate stocks where market capitalizations has grown too big. Moreover, we draw on U.S. stocks to enhance diversification in sectors with little or no representation in Canada. Stock selections remain a priority over the selection of individual sectors, the latter being a complementary decision. A natural bias favours industrial products that are particularly conducive to innovation, and consumer products and distribution, that are sectors in expansion. On the other hand, we maintain an unfavourable bias for the resources sectors given that size and economies of scale are predominant factors.

MARKET OVERVIEW

There is no doubt that the financial crisis that started in the U.S. over a year ago has now spread to the rest of the world, driving investor fears of a global economic recession. Against such a backdrop, lending markets tightened, and investors' appetite for risk shrunk. This downward spiral was further enhanced by outflows and noisy speculations.

In Canada, the S&P/TSX SmallCap Index pulled back 25.25% for the quarter, driven by a 19.72% setback in September alone. According to BMO Nestbitt Burns, this constitutes the third most severe monthly fall in 40 years.

Although every sector of the S&P/TSX SmallCap Index registered negative performances throughout the quarter, resources were the main laggards. Canadian mining and gas companies have been favoured by arbitrage funds in recent years. Their massive increase in capital, in light of the flight of many clients, brought about the hasty sale of many securities. A prudent investing approach was also a key factor, as investors worried about protecting their savings, found refuge in low-risk financial vehicles. Market liquidity in Consumer Staples, already quasi-absent, with the exception of natural resources over many quarters, was virtually non-existent in September causing many securities to plummet.

PERFORMANCE REVIEW

For the quarter, the portfolio outperformed its benchmark, bringing the year-to-date performance closer to that of the index. Although Garda's 470 basis point fall was harmful to the portfolio's relative performance, good stock picking enabled us to offset a large part of this setback.

Many of our holdings are struggling with the market's liquidity drought. The snowballing effect of Héroux-Devtek, Cangene, Aecon Group, Northstar Aerospace, and Forzani's setbacks has led to double-digit losses since the beginning of the year, despite the outlook, results, and the low level of indebtedness of these companies some have not debt at all, as is the case for Cangene and Forzani. For these reasons, we remain very confident in the composition of the portfolio, and strongly believe it is best to steady the course until valuation levels return to normal, in line with company fundamentals.

PERFORMANCE

	3 months	YTD	1 year	4 years	10 years
Fund ¹	-23.54%	-30.62%	-37.91%	-2.53%	10.40%
Index ²	-25.25%	-25.54%	-29.17%	3.64%	9.36%
Added value	1.71%	-5.08%	-8.74%	-6.17%	1.04%

¹ - Everywhere in this bulletin, "Fund" refers to the Natcan Small Cap Equity Fund.

² - Everywhere in this bulletin, "Index" refers to a combined index as calculated by Natcan (BMO Small Cap Index until August 2007, and S&P/TSX SmallCap Index since then).

PERFORMANCE ATTRIBUTION VS THE INDEX

Sectors	Attribution (basis points)	Securities	Attribution (basis points)
Cash	195	Positive	
Energy	-82	Monro Muffler Brake	104
Materials	190	Birchcliff Energy	58
Industrials	-360	Compton Petroleum	57
Consumer Disc.	193	Merit Medical Sys.	54
Consumer Staples	44	Mercator Minerals	50
Health Care	92	Negative	
Financials	-116	Garda World Secur.	-470
Technology	55	Iteration Energy	-137
Telecommunications	-53	Héroux-Devtek Inc	-125
Utilities	5	Cangene Corporation	-115
Total	163	Northgate Minerals	-109

Sector attribution includes sector allocation and stock selection. In green: not a Fund portfolio holding.

NATCAN SMALL CAP EQUITY FUND

OUTLOOK AND STRATEGY

Within the current environment, we prefer to remain cautious in our strategy by maintaining a substantial cash level. We will draw from the cash on hand in the coming months as opportunities to initiate positions in solid companies at bargain prices have already begun to emerge.

The small-cap universe has seldom provided investors with so many opportunities to purchase stocks that can grow their invested capital considerably over the medium and long-term. Among those, let us mention Sierra Wireless, Aecon, Forzani, Heroux-Devtek, and Cangene, stocks that currently trade at multiples that have not been encountered in over a decade while others, like Mediagrif, Tundra and Enghouse, are being offered at prices in line with their cash level.

The current environment resembles that of the early 2000's when large corporations' desperate need for growth launched a wave of privatization amid the small- and mid-cap universe. In our opinion, this scenario could repeat itself once the credit market stabilizes. The small-cap universe has in fact already begun to experience a number of these transitions since the start of the year.

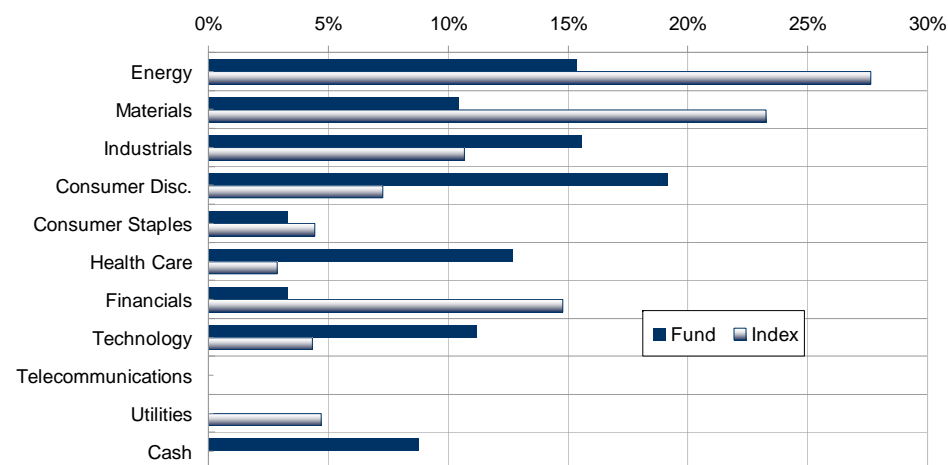
We continue to favour defensive sectors, notably Industrials, Consumer Staples, Information Technology, and Health Care, and maintain the portfolio's underweight in Financials and Utilities.

We are currently witnessing a market clean-up during which only sound companies are likely to survive while others, like marginal oil and mining companies, may disintegrate. Although the market pullback could provide opportunities within some of the best companies in the universe, the portfolio will remain underweight natural resources.

TOP 5 HOLDINGS

Securities	Weight
Héroux-Devtek Inc.	5.3%
Cangene Corporation	4.7%
Aecon Group	3.7%
Forzani Group Ltd.	3.6%
Uni Select Inc.	3.4%

SECTOR ALLOCATION



BUY AND SELLS

Additions	Sectors
Jaguar Mining Inc.	Materials
Manhattan Assocs Inc.	Information Technology

Withdrawals	Sectors
Cadence Energy	Energy
High River Gold	Materials
Merit Medical Sys.	Health Care
March Networks Corp.	Information Technology
Novatel Wireless Inc.	Information Technology

This publication is intended for your private information. The information and opinions herein are provided for informational purposes only, are subject to change based on market and other conditions. The views expressed should not be relied upon as the basis for your investment decisions. Past performance is not necessarily indicative of future performance. This document is not and should not be construed as a solicitation or offering of units of any fund or other security in any jurisdiction. No part of this publication may be reproduced in any manner without the prior written permission of Natcan Investment Management Inc. The Natcan Pooled Funds performance returns are calculated on a net of fees basis. All market index returns presented in this document were provided by Thomson Reuters.

