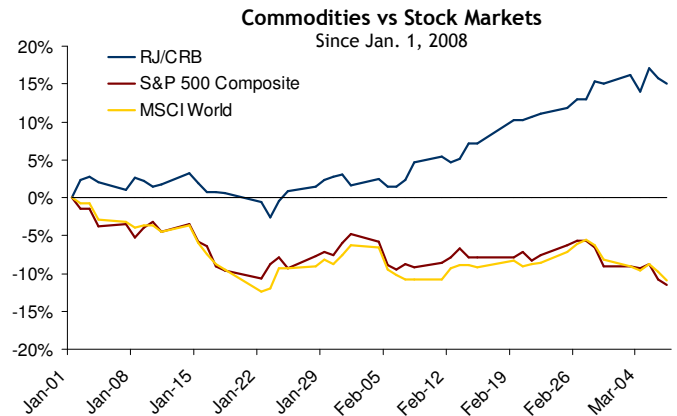


COMMODITIES RULE!

A powerful rally in the price of commodities has defied the unfolding global economic slowdown. In this week's edition of the Marker, we review some of the fundamental and technical factors behind these strong advances in an effort to understand the risks and potential rewards at hand.

EQUITY AND FIXED-INCOME ASSETS? THAT'S SO 2007

The prevailing financial crisis and economic slowdown are having well-documented negative effects on stock and bond returns. Investors have naturally looked to alternatives. Since the Federal Reserve began cutting interest rates while openly stating it would not focus on inflation measures, investors have flooded into commodity markets. Investors are generally aware of overall healthy supply-and-demand dynamics for commodities. They have seen prices run up over several years now and realize that because of the physical link between commodities and markets, these assets are not subject to write-downs such as those that sideswiped structure credit assets. New methods of investing simplify access to these markets; this is having a significant impact on prices. Electronic trading of commodities has exploded. Ninety-one percent of all trading in NYMEX's crude contract is electronic.



Source: Natcan

TOO MUCH MONEY CHASING TOO FEW BUSHELS OF WHEAT

NYMEX is the world's largest physical commodity futures exchange. It reports electronic trading volumes have exploded as hedge funds and individuals have gained direct access. The Futures Industry Association reported increases in agriculture, industrial metals, and energy products of 25-30% in 2007. The industry has launched several new investment vehicles, adding to the flow of new money in several commodities with historical small size. Commodity exchange-traded funds (ETF) now hold about \$30 billion in assets, up 90% relative to a year ago. Reports indicate commodity-index investors make up around 25% of total bets outstanding on agricultural commodity markets. These flows are seen by many as exacerbating price trends justified by strong fundamentals.

WHEN BULLS GET CARRIED AWAY

The fundamental case for higher agricultural commodity prices is centered on the twin factors of growth in developing world wealth leading to different eating patterns, and ethanol-based fuel production in the U.S. A large share of index and ETF-like investing is however insensitive to fundamentals. This key point highlights the potential for commodity prices to separate from fundamentals based on technical factors. An oil contract recently rocketed a record \$5 in one day. The price of oil is up over 69% in the past year, despite reports of falling demand in OECD countries in a row. Coffee offers further evidence of the risks imbedded in the prices of certain commodities. With demand up only slightly, the price of roasted beans increased 7.7% in 2007 while the price for green beans moved up 22%. Observers point to poor harvests in Brazil and the impact of financial investors as the primary cause for these moves. With open interest on coffee contracts up 50%, one must reckon momentum investors have piled in. How many are aware of the fact this year's Brazilian crop is predicted to yield 30% more beans?

NATCAN WEEKLY MARKER

Investors fled the stock market after the tech bubble implosion in 2001 and became obsessed with housing, inevitably leading to speculation. Analysts report anecdotes of investors now disappointed by housing chasing commodities as the next fool-proof thing. Every mania is accompanied by a new paradigm. Only the future will tell whether commodities will become the third great bubble in 15 years to grip investors' imaginations and money. Prior to taking the jump, investors need to make sure they can handle the high volatility that accompanies any investment where technical factors are afforded such great importance.

Michael Quigley, CFA
Senior vice president, Distribution

FINANCIAL MARKETS

RETURNS AS AT MARCH 7, 2008 (%)	MTD	QTD	YTD	RATES AS AT MARCH 7, 2008
S&P/TSX	-2.17	-3.57	-3.57	CAD/USD
S&P 500	-2.22	-11.92	-11.92	CAD/Euro
S&P/TSX Small Cap	-2.82	-4.16	-4.16	US Treasuries yield 10-yr/30-yr
Russell 2000	-3.27	-14.04	-14.04	GOC bond yield 10-yr/30-yr
MSCI EAFE	-2.38	-10.81	-10.81	Fed Fund Rate (target)
MSCI World	-2.18	-10.87	-10.87	
DEX Universe Bond	0.30	2.27	2.27	

Note: Returns in Canadian dollars, London 4h exchange rates. Source: Datastream, PC Bond, MSCI-Barra, and Bloomberg. PC-Bond, a business unit of TSX Inc. Copyright © TSX Inc. All rights reserved.

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