

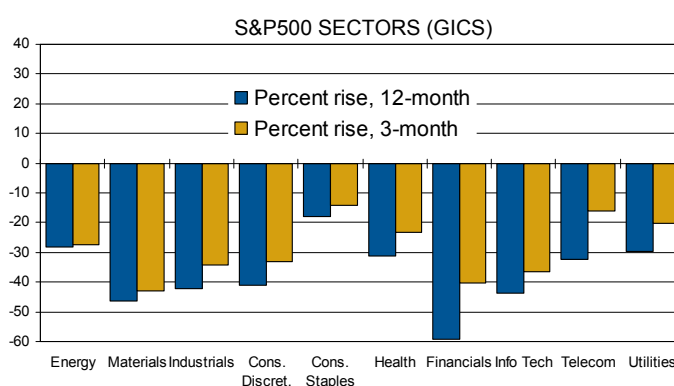
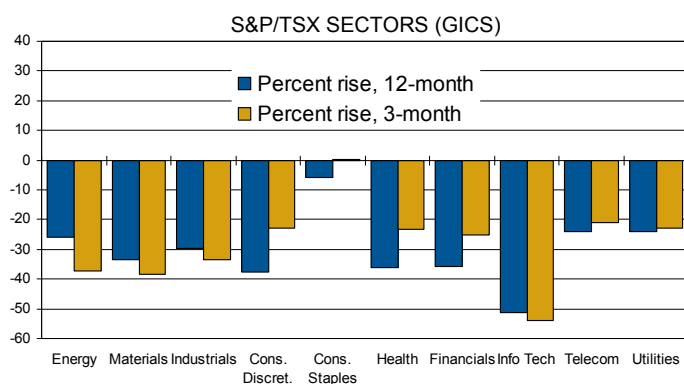
Market Monitor

December 10, 2008

by Dr. Martin Murenbeeld

		November MONTH-END 2008		
S&P/TSX SECTORS [GICS]		% of S&P/TSX	% rise 3-month	% rise 12-month
10	Energy	29.41	-37.19	-25.90
15	Materials	14.99	-38.29	-33.38
20	Industrials	5.49	-33.52	-29.79
25	Consumer Discretionary	4.59	-22.74	-37.76
30	Consumer Staples	3.08	0.20	-5.70
35	Health Care	0.40	-23.10	-36.00
40	Financials	30.71	-25.28	-35.94
45	Information Technology	3.52	-53.76	-51.18
50	Telecommunication Services	5.97	-21.15	-23.85
55	Utilities	1.84	-23.01	-23.88
S&P/TSX		100.00	-32.68	-32.28

		November MONTH-END 2008		
S&P500 SECTORS [GICS]		% of S&P500	% rise 3-month	% rise 12-month
10	Energy	14.30	-27.56	-28.34
15	Materials	2.98	-42.82	-46.18
20	Industrials	11.02	-34.20	-42.36
25	Consumer Discretionary	8.04	-32.93	-40.98
30	Consumer Staples	13.08	-14.28	-18.05
35	Health Care	14.04	-23.32	-31.36
40	Financials	13.36	-40.49	-59.14
45	Information Technology	15.10	-36.49	-43.80
50	Telecommunication Services	3.82	-15.94	-32.17
55	Utilities	4.25	-20.25	-29.80
S&P500		100.00	-30.14	-39.49



REVIEW

The tables and charts tell an awful story; only one sector of the equity markets in Canada and the US posted a gain over the last three months: *TSX Consumer Staples*. The gain was a negligible 0.2%, but in this environment, 0.2% is still better than cash, which is currently earning 0% in the US going by the T-Bill rate. No sector is positive over a 12-month period to November month-end. The TSX is down 32.3% year over year (yoy), whereas the S&P500 is down by 39.5% yoy.

Most of the declines in the two broad indices have come in the last three months furthermore. The TSX declined 32.7% over the last three months, or 14.7%, 16.9% and 5.0% for September, October and November, respectively. The S&P500 has declined 30.14% over the last three months, or 9.1%, 16.9% and 7.5% for September, October and November.

To put this three-month decline in perspective, we have to go back to 1937 to find a more negative three-month period for the S&P500. Our data for the TSX goes back to 1917 and there was no three-month period as negative as what we have just witnessed. The worst previous three-month period occurred in 1932.

The National Bureau of Economics (NBER) pronounced recently that the US recession started in December 2007, as that was when the US economy had peaked. (We know that the economy posted a reasonably solid 2008-Q2 growth rate, but that is not the determining factor. Employment growth, or lack thereof, is more important in the NBER recession dating process.) On October 15, we issued a report on equity market peaks and troughs in relation to US recessions, and we made the point that equity troughs typically occur three to six months before the end of a recession. (US recessions

S&P/TSX SECTORS	**	MODEL VALUATION*				
		Very Under	Under	Neutral	Over	Very Over
10 ENERGY	>>			X		
15 MATERIALS	<				X	
20 INDUSTRIALS	0					X>
25 CON DISC	0	<X				
30 CONS STPLS	<	<X				
35 HEALTH	0	X				
40 FINANCIALS	<<	<X				
45 INFO TECH	>>					X
50 TELECOM	>>>					X
55 UTILITIES	<	X				

S&P500 SECTORS	**	MODEL VALUATION*				
		Very Under	Under	Neutral	Over	Very Over
10 ENERGY	<					X>
15 MATERIALS	0	<X				
20 INDUSTRIALS	<<	X				
25 CON DISC	<<	X				
30 CONS STPLS	<<		X			
35 HEALTH	0			X		
40 FINANCIALS	>>				X	
45 INFO TECH	<		X			
50 TELECOM	0				X	
55 UTILITIES	0			X		

*MODEL VALUATION is determined with economic models based on over 20 years of published economic and financial data. The objective is to provide the reader with a sense of "fair value" for each sector once macroeconomic data, commodity prices and interest rates have been taken into account. Before the advisor over-weighs or under-weighs an "under-valued" or "over-valued" sector, the advisor should consider carefully company and sector-specific variables and expectations (which are not and cannot be included in the economic models).

** Change with respect to last month.

are more important for the TSX than Canadian recessions; Statistics Canada does not date Canadian recessions and the US equity market cycle is in any event the dominant cycle for Canadian equity markets.)

In this month's Economic Monitor we will argue that the US recession could well end by the summer of 2009. We have pushed the date out to August for no solid analytical reason other than US house prices should be flattening out around then (hopefully before). If that proves to be a good guess (in retrospect, my guess that the recession started in January 2008 proved to be close) then we would hope to see a final bottom to this horrible equity cycle by April-May.

STRATEGY

Ergo, as we have noted before, the best strategy is to stay the course because we are very likely within sight of the bottom. To be sure, "staying the course" has not been without pain. Obviously I wish we had been more prescient and could see all the disasters ahead more

RECOMMENDED ALLOCATION - November 2008 (month-end)						
	monthly change	RECOMMENDED ASSET WEIGHTING				
		very-over	over	neutral	under	very-under
CANADIAN PORTFOLIO						
BONDS	>					X
STOCKS	<		X			
US PORTFOLIO						
BONDS	>					X
STOCKS	<	X				
BOND PORTFOLIO						
CANADA	0		X			
US	0				X	
STOCK PORTFOLIO						
CANADA	0				X	
US	0		X			

Notes:

> means the direction of monthly change is to the right

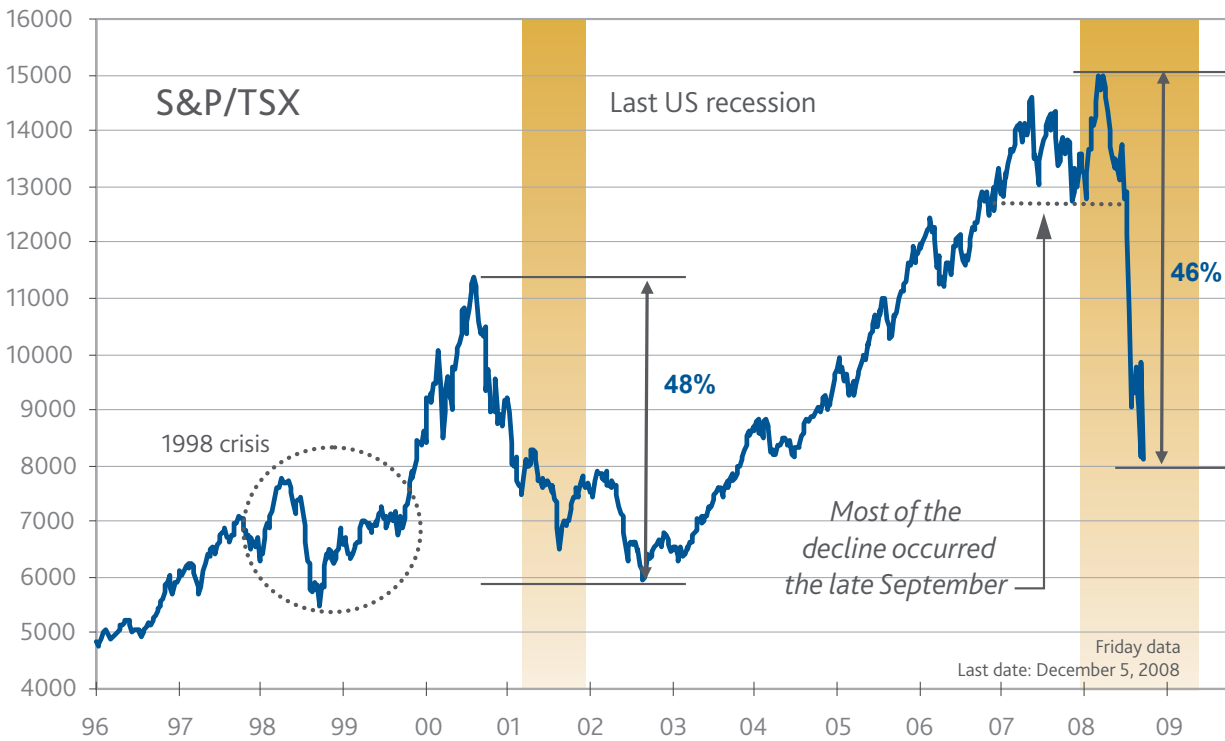
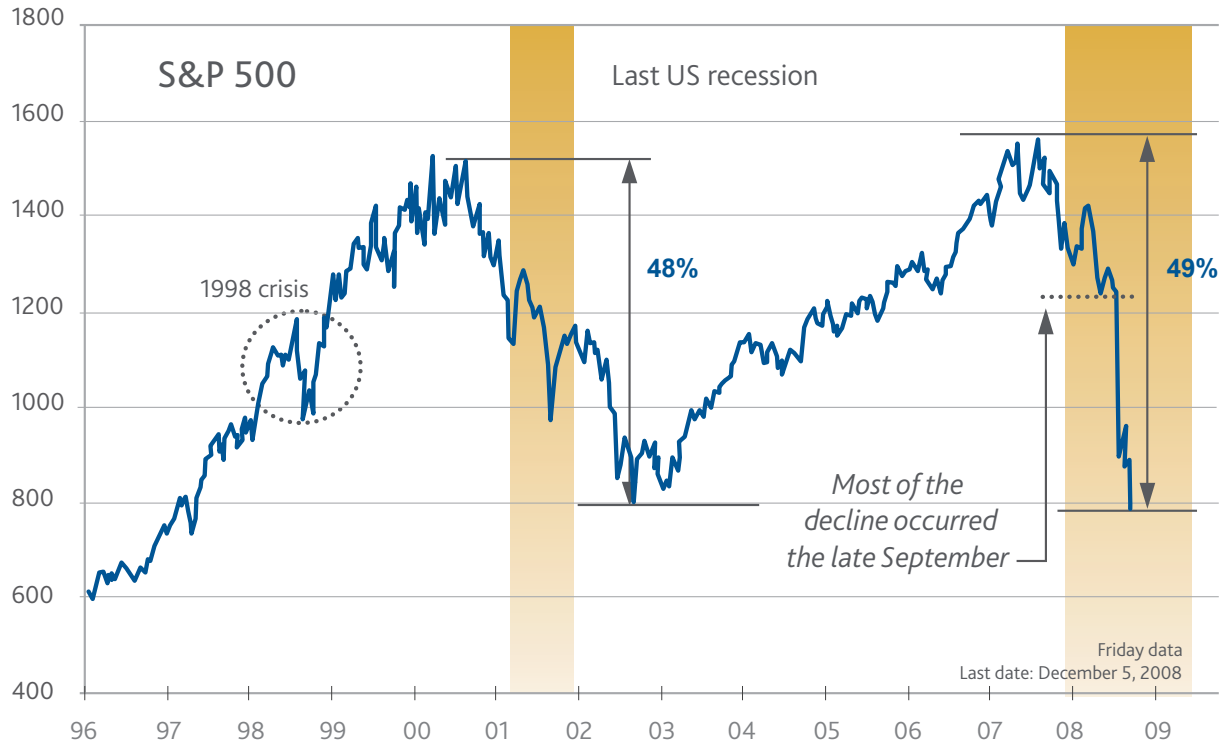
< means the direction of monthly change is to the left

clearly. But we weren't and we can't, which is why we don't "time the market" often or successfully. Indeed, most timers sell near the bottom and buy somewhere towards the top.

Rather, we try to estimate the probabilities of which sectors will do better or worse than other sectors of the market and invest accordingly. *Consumer Staples* is generally a more recession-proof sector of the market and it is no surprise that this sector has been the best performing one in recent months (see the charts on the front page).

Currently our models indicate that equity markets are seriously undervalued, even more so than last month. So we certainly think that an "overweight" of equities versus bonds is the right investment strategy at this time. (Canadian government bond yields and US Treasury yields have declined in recent weeks, which makes these assets less attractive than they were a month ago.) The tables herewith give a sense of which equity sectors within each index (S&P/TSX or S&P500) appear more undervalued (i.e., more attractive) than other sectors. Ergo, we'd focus our efforts on those sectors.

The two weekly charts on the following page indicate just how severe the market collapse has been. Whether the markets will fall even more is an open question which we cannot answer – they have fallen rapidly and dramatically. I think we are getting to the end of this virulently bearish phase however. The question going forward will be one of which sectors to overweight in order to take advantage of the economic recovery phase in the second half of 2009 – equity markets can post double digit gains even when the recovery phase is likely to be tepid.



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