Portfolio Strategy Quarterly

Winter 2008

Professional Wealth Management Since 1901

RBC Dominion Securities®

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THE STRATEGY PROCESS

The RBC Investment Strategy Committee (RISC) consists of senior investment professionals drawn from individual, client-focused business units within RBC. The Committee regularly receives economic and capital markets related input from internal and external sources. The Committee's view includes an assessment of global fiscal and monetary conditions, projected economic growth and inflation, as well as the expected course of interest rates, major currencies, corporate profits and stock prices. From this global forecast, the RBC Investment Strategy Committee develops specific guidelines that can be used to manage portfolios. Members include:

Daniel Chornous, CFA (Chair)	Chief Investment Officer RBC Asset Management
Jim Allworth	Portfolio Strategist RBC Dominion Securities
Janet L. Engels	Senior VP and Director Private Client Research Group RBC Dain Rauscher
Stuart Kedwell, CFA	Senior Portfolio Manager RBC Asset Management
George Riley, FSI	Head, Global Investment Solutions RBC Global Private Banking
Jason Storsley, CFA	Institutional Portfolio Management RBC Asset Management
Martin Paleczny, CFA	Senior Portfolio Manager RBC Asset Management

The RBC Capital Markets Equity Selection Sub-Committee is responsible for determining the Canadian equity sector weightings and Focus List recommendations. The Sub-Committee is comprised of individuals from both RBC Capital Markets and RBC Dominion Securities, and includes:

Andrew Grimes (Chair)	Canadian Equity Product Manager RBC Capital Markets
Jim Allworth	Portfolio Strategist RBC Dominion Securities
Richard Talbot, CFA	Director of Canadian Equity Research RBC Capital Markets
Ray Hanson	Director of Trend & Cycle Research (Canada) RBC Capital Markets
Stephen Walker, CFA	Director of Mining Research RBC Capital Markets
Myles Zyblock, CFA	Director of Top-Down Research RBC Capital Markets

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ABOUT THIS PUBLICATION

This publication, *Portfolio Strategy Quarterly*, summarizes the conclusions and forecasts of the Strategy Committee to provide a practical framework for the management of private clients' individual portfolios.

PORTFOLIO STRATEGY QUARTERLY

Editor: Jim Allworth
Vice-President & Director,
RBC Dominion Securities

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STRATEGY SUMMARY & RECOMMENDATIONS

Jim Allworth, Vice-President & Director, RBC Dominion Securities

Historical Range*	Asset Class	Previous	Current	Recommended Action	Expected 1-year Returns
0% – 40%	Cash	15%	**20% ↑**	**Increase cash reserves**	4%
10% – 55%	Bonds	25%	**25%**	**Below-average bond commitment**	0% to 2%
40% – 70%	Stocks	60%	**55% ↓**	**Decrease exposure to stocks**	7% to 10%
**Since inception in 1984*		100%	**100%**		

U.S. 'SOFT LANDING' REMAINS OUR FORECAST, BUT RISKS HAVE RISEN

The turmoil in financial markets has raised the risk to our forecast but it remains essentially unchanged: the U.S. economy is likely to endure several quarters of much slower growth but will avoid recession. This should extend the life of the global economic expansion (and Canada's) over the next one-to-two years and is generally positive for the sustainability of earnings and for equities.

MONETARY POLICY SHIFT FIRMLY IN PLACE

The Fed has now cut its target rate three times since the summer and stands ready to reduce it further if the economy weakens from here. Other central banks have either joined the Fed in lowering rates or have abjured from raising rates any further at least for the moment. A shift in Fed policy toward rate cuts has typically underwritten a stock market advance over the year following the first cut. It usually also marks the beginning of a period over which bond yields rise (i.e., bond prices fall).

CANADIAN STOCKS ATTRACTIVE BUT NOT WITHOUT RISK

While a near-term 'risk window' could stay open into the first quarter as financial market turmoil remains a possibility, a U.S. economic 'soft landing' should allow stock markets to deliver average to above-average returns for at least the next year and probably longer.

It also remains true that the Canadian stock market is more aggressively valued than most other major markets. While we expect the TSX to join other markets in delivering worthwhile gains in the coming year, we reiterate our recommendation that investors heavily committed to Canadian stocks consider diversifying their exposure to include more broadly diversified markets where valuations are more compelling.

STOCKS FAVOURED OVER BONDS

Our view is generally a positive one for earnings and for equities. We favour stocks over fixed income and continue to carry a below-normal exposure to bonds. Fed cutting has improved the outlook and underpinning for stocks. The valuation concerns expressed above have persuaded us to pare back our equity exposure in an all-Canadian portfolio to 'neutral' from a modest over-weight. For a global portfolio a moderate over-commitment to stocks continues to be appropriate.

ECONOMIC BACKDROP

MONETARY CONDITIONS

Fed focused on growth slowdown
Bank of Canada plays for time

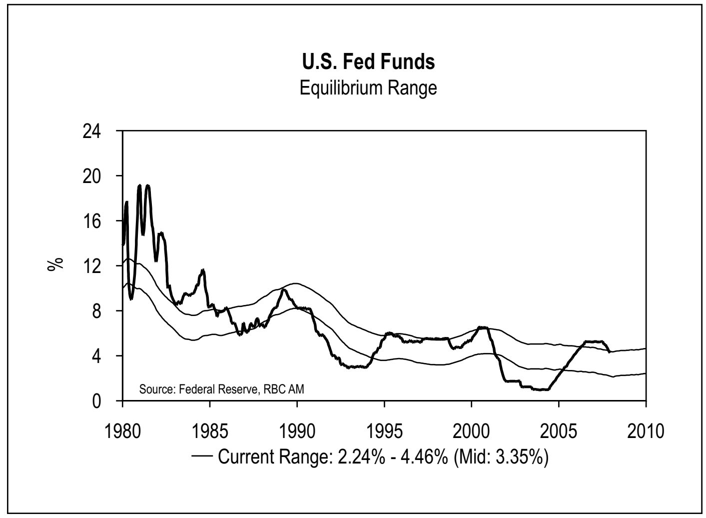
With core inflation not far outside its comfort zone, the Fed has become more focused on pursuing a policy course that ensures the growth slowdown now underway does not turn into anything worse. Chairman Bernanke has stated that Q4 will reveal a much slower rate of growth prompting the central bank to reduce its 2007 and 2008 GDP growth forecasts by half a percentage point. One more cut looks likely, however, should the data weaken further, particularly on the employment front, the way could open for a series of cuts. By our reckoning, a truly neutral policy setting would see the funds rate down near 3.50%, while an unequivocally stimulative one would require something less than 2.50%.

- The Bank of Canada finds itself confronted by a different set of conditions than it had expected even a few weeks ago: core inflation is below 2%; even well off its peak the Canadian dollar is nonetheless almost 15 cents above where it was a year ago; Western Canada and the resource economy have come off the boil; and the U.S. economy appears to be weaker than the Bank had expected. The inevitability of future rate hikes, so much a feature of Bank rhetoric in the spring and summer, has instead turned into a December rate cut and growing street conviction of more to come.

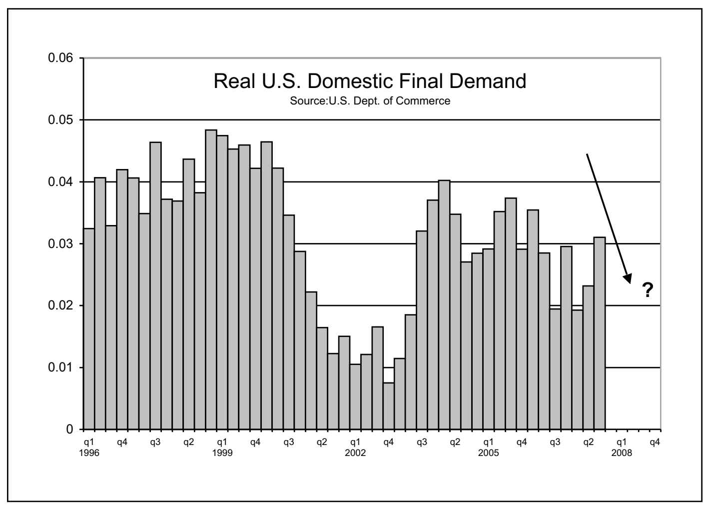
- Core inflation in the U.K. is low and now house prices are clearly shifting into a lower gear, having declined for three months running by a total of almost two-and-a-half percent. This has allowed the Bank of England to put one rate decrease in place and to publicly contemplate further base-rate reductions in 2008. By contrast the European Central Bank has taken a very tough line. With core inflation jumping higher, no relief forecast before summer, and large contract negotiations getting underway in January the Bank has not ruled out additional rate hikes for early 2008.

- The Bank of Japan is faced with a renewed bout of deflation and a softening economy. Any further contemplated rate increases are now off the table. However China is very much another story. Inflation is above 6%. Food prices have been particularly strong and drought conditions are promising no early relief. The government appears in no hurry to ease the tight credit conditions it has steadily put in place over the last two years.

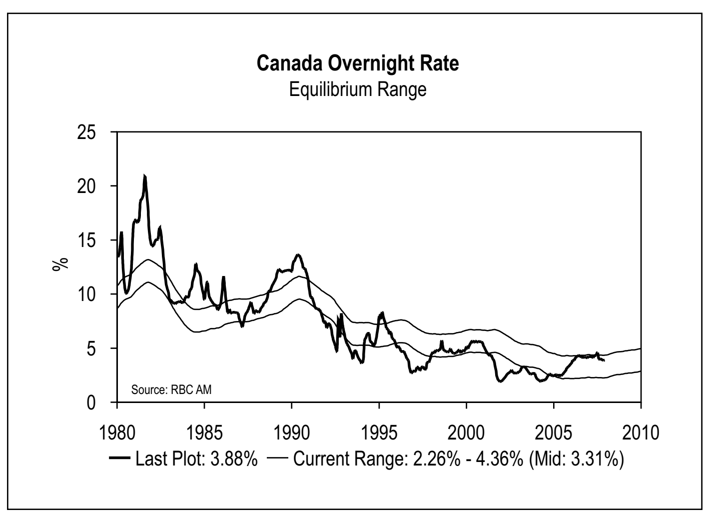
The Fed is ready to cut rates further...



... as it shifts its policy toward staving off a recession.



The Bank of Canada also has room to move rates lower...

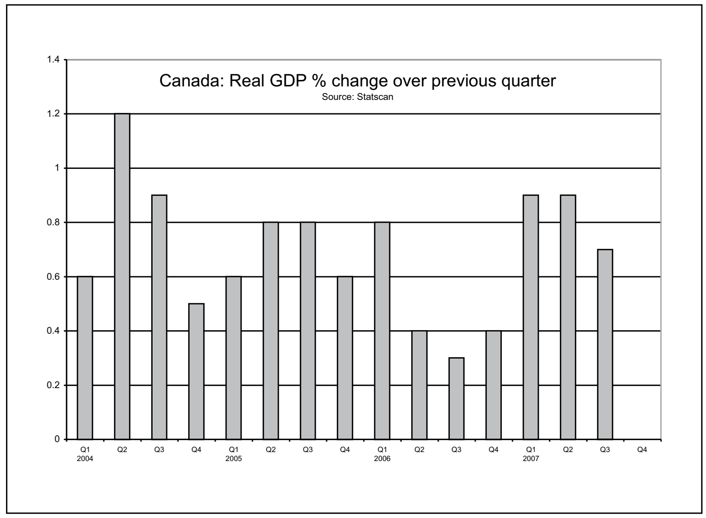


THE GLOBAL ECONOMY

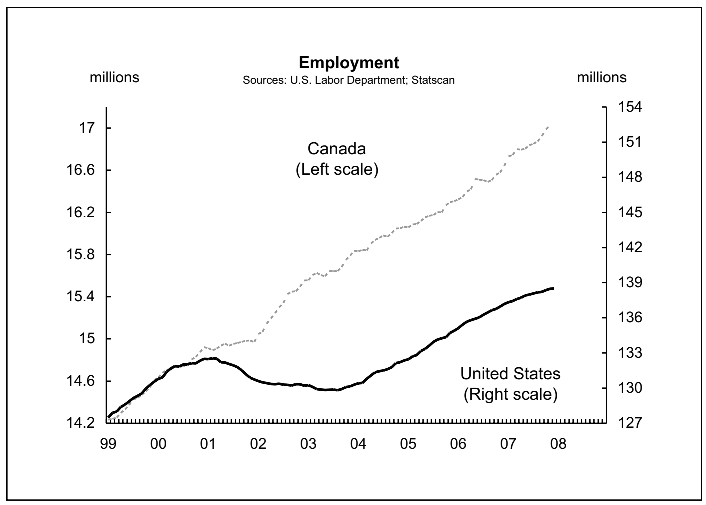
U.S. slowdown has arrived
Canadian economy resilient

- All eyes are on U.S. consumer spending, watching to see how big a toll will be exacted by the housing slump and sub-prime banking turmoil. So far the the impact has been relatively modest as household spending attitudes have been supported by average hourly wage growth of almost 4% and steady additions to payroll employment. Arguably surging gasoline and heating fuel prices have accounted for greater damage recently as these costs pre-empt an ever growing share of take-home pay. The first two quarters of 2008 are likely to see all these factors worsening somewhat leading to a noticeably weaker contribution from the consumer to overall GDP growth; our forecast has outlays growing by only 1%-2% down from an estimated 2.7% in 2007 and 3.1% in 2006.
- Apart from housing, business capital investment in the U.S. has delivered year-over-year growth of better than 4% under the influence of high profits, corporate balance sheets flush with cash, and a prevailing high degree of overall capacity utilization. There are, however, some signs that pace slowed in the fourth quarter and may slow further in the first half. Government expenditures, paced by defence and healthcare, are likely to go on growing at better than 2% in an environment where political outcomes have become both more uncertain and more vigorously contested. Trade is very much a bright spot as the depressed U.S. dollar has stimulated exports and constrained imports. Last year trade added almost as much to growth as housing subtracted. We continue to hold the view that a 'soft-but-bumpy landing' is playing out for the U.S. economy.
- The Canadian economy has come off the boil mostly in response to the surging currency. Manufacturers' new orders have been declining since the beginning of the year while unfilled orders have fallen for the past three months. Profit margins for many resource companies are being squeezed as Canadian dollar costs eat into U.S. dollar selling prices. As a consequence a number of large capital expansion projects have been scaled back or deferred.
- Housing remains no worse than 'firm' in most markets while consumer spending is being propelled by employment growth and wage gains of better than 4%. However there is some apprehension that credit market turmoil and a U.S. slowdown could spill over into the Canadian economy. Lower rates from the Bank of Canada should offer some remedy for these concerns particularly on the currency front.

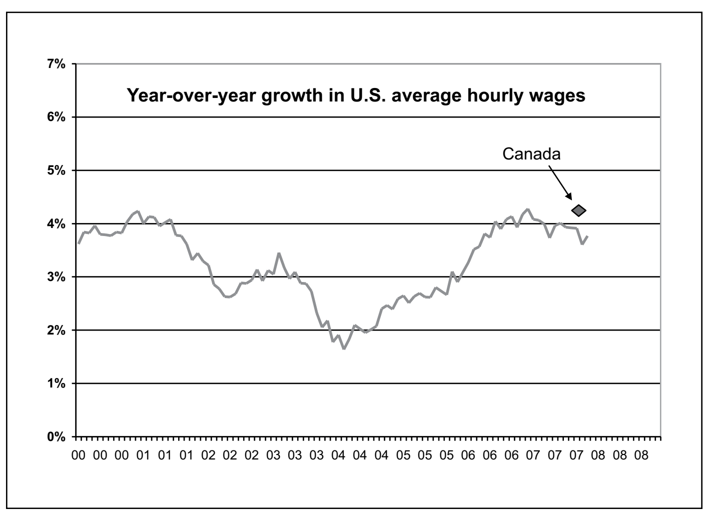
...but less reason to do so.



All eyes are on the employment picture.



Wage growth in both countries is supportive of no consumer-led recession.



› While surveys of business conditions in Europe have been fading for the past year, they mostly remain well above historical average levels. The exception is in the retail sector where growth in consumer outlays has been lackluster. Reasonable job growth has been offset by a near commensurate increase in the labour force, which has kept wage rates and consumer sentiment subdued. Industrial production, business investment, and exports have continued to post good gains. In the UK, domestic demand, which has been firm, looks to be softening in the wake of three successive months of house price declines.

› Japanese business sentiment has plummeted over worries about the durability of U.S. demand for Asian imports. The consumer remains cautious in the face of stagnating wages and renewed deflation. Japan's economy is slowing. In China, demand remains robust, however weaker U.S. growth together with the cumulative effects of credit tightening are likely to produce weaker performance later in the year.

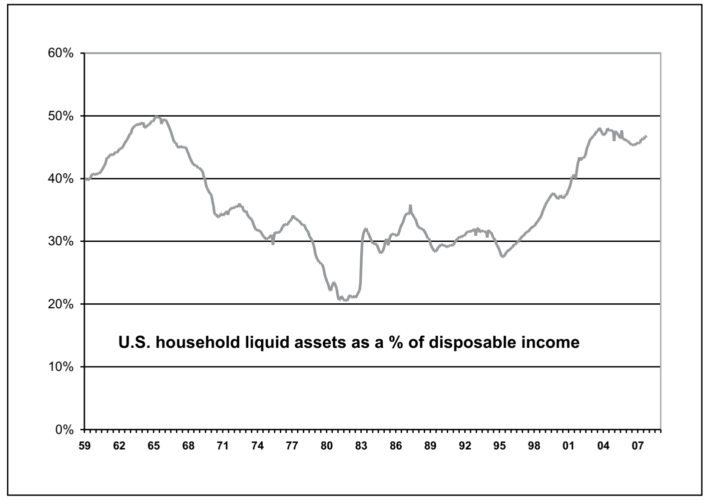
INFLATION

Core inflation well behaved
Future 'expectations' benign

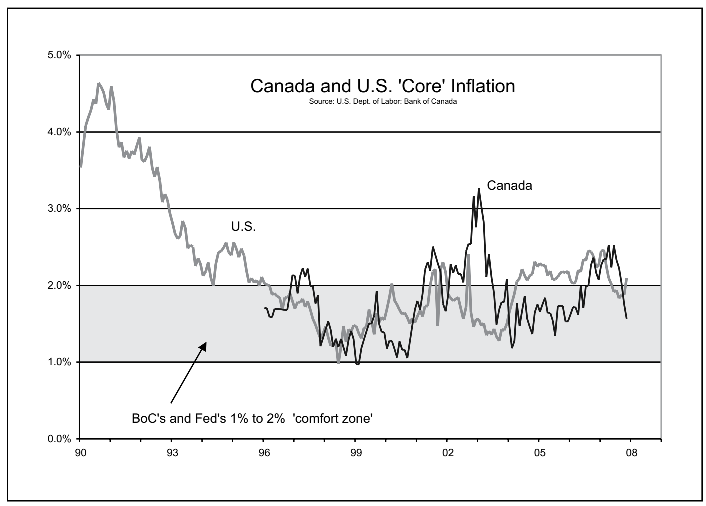
› In all the major economies, reported headline inflation rates, driven by surging energy and food costs, posted especially poor readings over the final months of 2007. Even 'core' inflation, which excludes those volatile components, has notched somewhat higher in the U.S. and Canada, ending an impressive string of downside surprises. Weaker consumer spending growth, forecast for the first half, should relieve some of the upward pressure.

Bond investors in both countries appear to be unconcerned. Although bond yields have been all over the map since the summer the yield spread between the normal fixed-coupon bonds and so-called 'real return' bonds has been comparatively steady. That spread represents the long-term inflation expectations of financial markets. Today, for both countries, it indicates that the average rate of expected inflation for the coming 10 years sits at about 2.4% per annum, well within the 2.20-2.60 basis point range that has prevailed for several years.

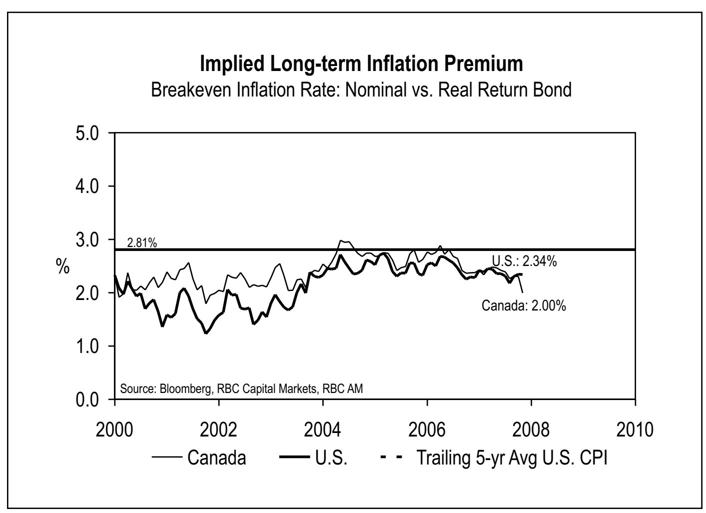
U.S. household liquidity is extraordinarily high.



Core inflation readings are not sounding alarm bells.



Inflation expectations in both countries are benign.



INTEREST RATES

Scope for short-term rates to ease further
Bond yields fail to compensate for risk

- Tighter lending practices and slowing growth in the real economy continue to shift the Fed's focus toward a more proactive and accommodative monetary policy, with at least one further cut likely in Q1/08 and perhaps more thereafter.

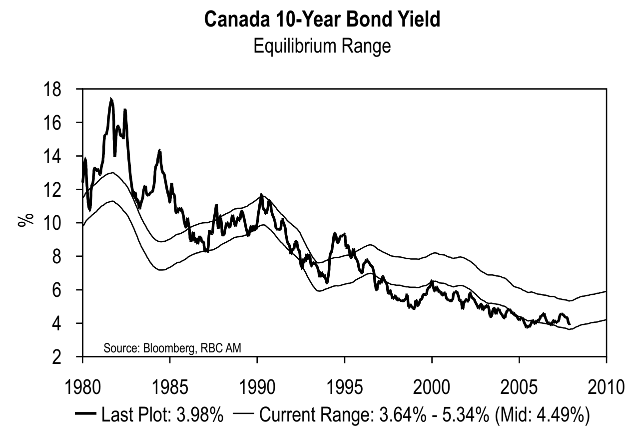
- The Bank of Canada switched gears and cut rates once in December while it waits for the domestic financial market to function normally once again. That may take some months. In the interval the bank will have time to assess whether the much elevated currency and slower U.S. growth will restrain the Canadian economy and reduce inflation pressures the way it imagined its previously proposed rate hikes would have done.

- In Europe, the ECB has periodically been willing to provide massive liquidity injections to keep the banking system functioning; however, it has so far resisted acknowledging any need for interest rate cuts, citing growing inflation pressures. Given these concerns, it would not be until the second half that inflation data could ease enough to make the Bank contemplate lowering the repo rate. The Bank of England has cut once and has strongly suggested that more rate reductions are likely.

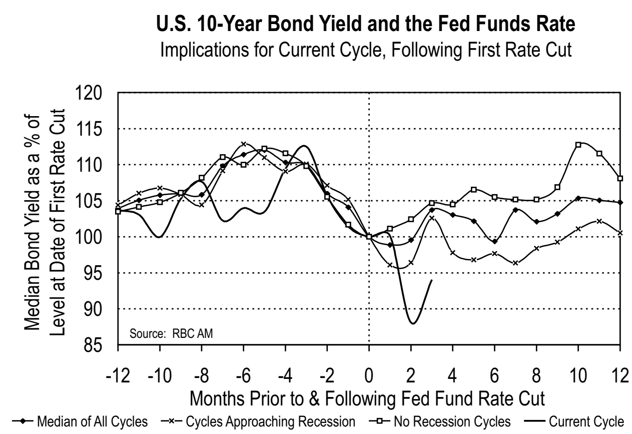
- The rapid weakening of the Japanese industrial economy and the return of deflation has taken the additional rate increases that were anticipated by the market off the table for the foreseeable future.

- The 'flight to quality' prompted by the global liquidity crisis has left bond yields artificially low and not compensating investors adequately for normal risks. Couple this with the observation that the year following the Fed's first rate cut usually sees bond yields moving higher, leaving a distinctly unattractive environment for fixed income investors. Total returns to bond investors over the next year are likely to be something less than the coupon rate. To one degree or another, this condition faces bond investors not just in the U.S. and Canada but in Europe, the U.K., and Japan as well.

Bond yields fail to compensate the investor adequately...



... for the risk that rates will rise in the wake of Fed easing.



INTEREST-RATE FORECAST

	Dec. 2007	Forecast Dec. 2008
Canada		
3-Month Yield	3.90%	4.25%
10-Year Bond Yield	4.00%	4.75%
U.S.		
3-Month Yield	3.15%	4.00%
10-Year Bond	4.00%	4.75%
Europe		
3-Month Yield	3.65%	3.90%
10-Year Bond	4.30%	4.50%

CURRENCIES

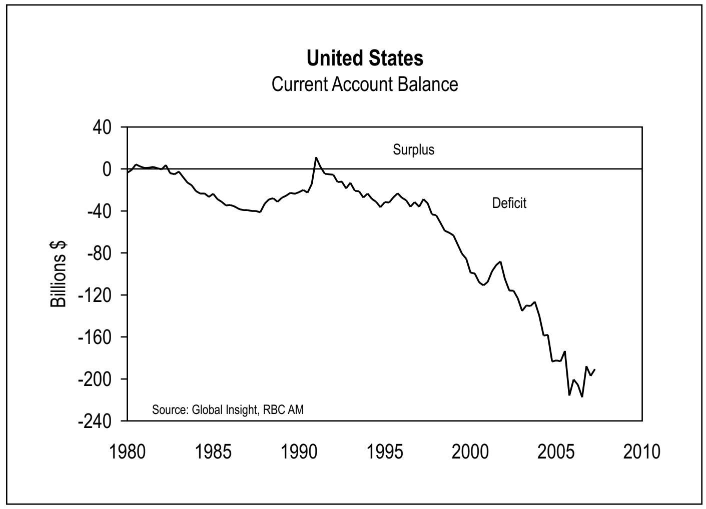
- **U.S. dollar** – *not yet at the bottom*
  With the Fed now committed to cutting rates if the U.S. economy weakens further, the promise of more generous 'real' yields in Europe and Japan will keep the dollar under some further pressure. The decline will likely continue until the ECB is ready to ease as well or until the Fed is clearly finished lowering its target rate. We look for a somewhat weaker dollar but not a profoundly weaker one.

- **Euro** – *uptrend intact for now*
  While there may be no further rate hikes coming from the ECB, any prospect for rate reductions looks to be at least six months away. That should be enough to keep the Euro's uptrend intact for now; however, by the second half we expect the currency to weaken modestly.

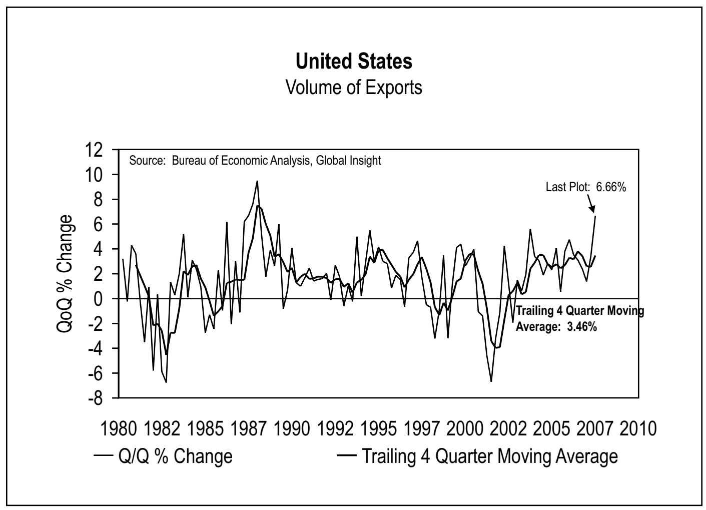
- **Yen** – *somewhat stronger*
  What is being characterized as a "temporary" return to deflation has widened real yields available in Japan and allowed the yen to appreciate moderately. For the currency to move beyond today's levels will require a return to economic 'normalcy'. That would feature, among other things, sustainable growth in consumer incomes and spending as well as prospects for a prolonged decline in the fiscal deficit.

- **Canadian dollar** – *consolidating*
  With the Bank of Canada's bias shifting from one that leaned toward further hikes to one featuring rate reduction(s), the expected 'real' rate advantage in this country has narrowed. This has taken the steam out of the currency. Further consolidation is likely as long as the Bank and the Fed appear to be headed in the same direction.

The U.S. current account deficit appears to be stabilizing…



… as U.S. exports surge propelled by a weak dollar.



CURRENCY FORECAST
In U.S. cents

	Today	Dec. 2008
Euro	147	140
Yen	0.92	0.89
Canadian $	100	100

EQUITIES

CORPORATE EARNINGS

Earnings growth still positive year-over-year but slowing
Expectations for this year need to moderate

- Recurring earnings for the S&P 500 grew by 7% in the 12 months ended November, somewhat ahead of consensus forecasts. However, earnings fell in each of the last two months of that period. Some earnings softness is expected to prevail through the first half of 2008 with better rates of growth not appearing until later in the year. Our full year forecast has earnings growing more slowly than the consensus, which calls for a reacceleration to 11% growth next year. The best earnings gains should come from technology, telecoms, and health care. Financials and materials are likely to post only minimal profit improvement.
- In the U.K., and Europe, and Japan earnings expectations moderated for the year just ended but consensus forecasts for 2008 all look for a reacceleration to double-digit growth – a goal that we think will be difficult to achieve.
- In Canada earnings in November were up only 4.5% year-over-year, a pronounced slowdown from a quarter earlier and the first sub-5% rate in almost five years. While consensus forecasts to next November are running almost 11% ahead of current earnings, they have been flat for four months, suggesting we are well into a period of less dynamic profit growth. Subsurface, fewer than 50% of all companies in the index are currently reporting trailing-twelve-month earnings gains, down from almost 75% earlier in the year, confirming slower earnings growth ahead. Technology, golds, and media are expected to deliver the best bottom line gains in 2008.

STOCK MARKETS

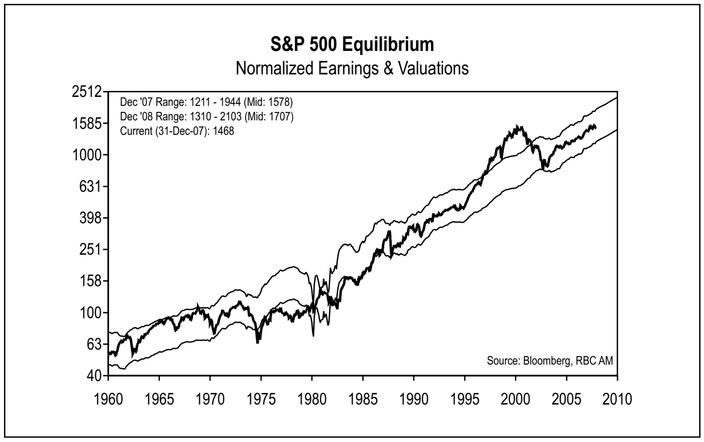
No-recession scenario offers worthwhile upside
"Risk window" still open, but Fed cutting underpins stocks

- The S&P 500 trades at a modest discount to 'fair value'. If it maintains that discount it should deliver all-in returns of about 10-12% over 12 months. However, an extended period of moderate economic growth with contained inflation has usually persuaded investors to pay well-above 'fair value' for stocks at some juncture in the cycle, which offers a prospect for even higher returns.
- Our expectations for average-to-above-average returns over the next one-to-two-years should be balanced against a near-term that could see the current 'risk window' remain open late into the first quarter. That said stocks have typically performed well in the year following the first Fed interest rate cut in a new easing cycle.

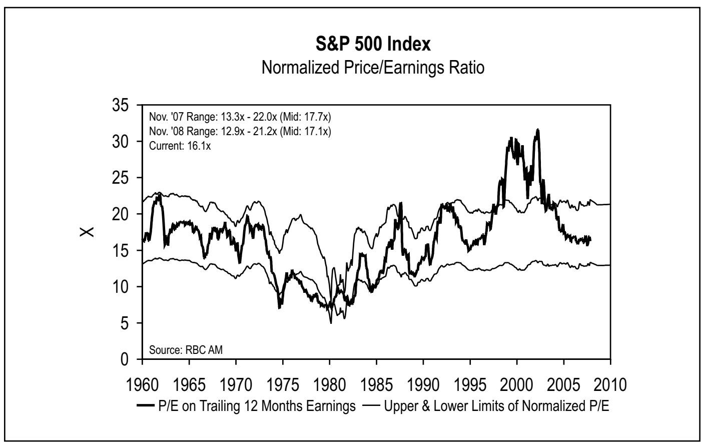
ESTIMATED-EARNINGS FORECAST
(Net of unusual items)

	2005	2006	2007	2008
TSX	$639A	$754E	$810E	$860E
S&P 500	$76.53A	$87.40E	$92.00E	$100.00E

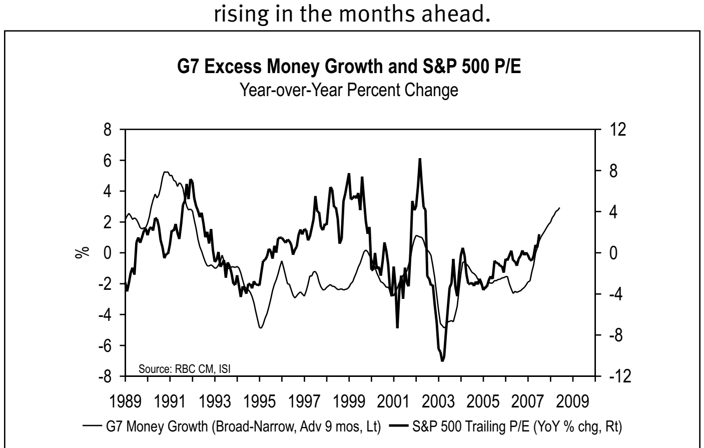
The S&P 500, like most major markets, is very reasonably priced in relation to sustainable earning power, interest rates, and inflation.



Price-earnings ratios are half what they were in 2000…



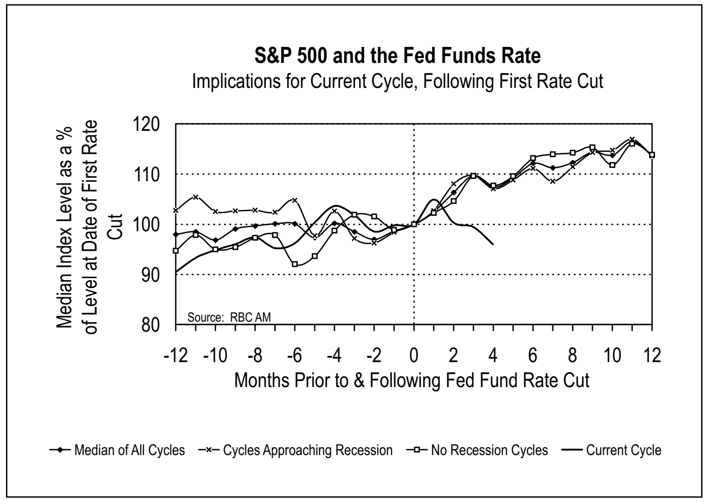
… and rapid money supply growth suggests they should be rising in the months ahead.



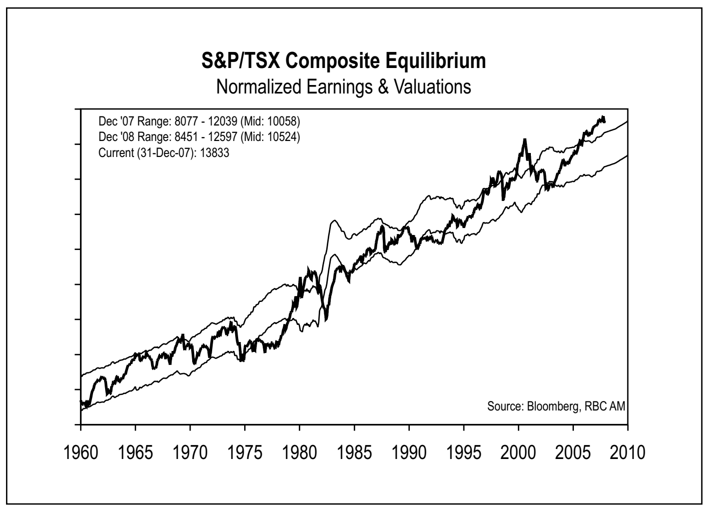
- As for the American market, large-cap markets in Germany, France, Italy, and Japan are all trading at or below the values dictated by our fair value models. In all cases 'fair value' one year out is well above current market levels.

- Canada's market presents a less comfortable valuation picture. Even after a correction, Canadian equities continue to be valued beyond the range that history would suggest is sustainable over the long term in relation to interest rates, inflation expectations, and sustainable earning power. The return potential of the TSX from here is reasonable given our expectations for a U.S. economic 'soft landing' and an extended global economic expansion. But valuation risks would come to the fore if the U.S. slowdown deteriorated into recession. As we have suggested before, this augmented risk should be acknowledged in portfolios. Investors heavily committed to Canadian stocks should consider diversifying their exposure to include more broadly diversified markets where valuations are more compelling.

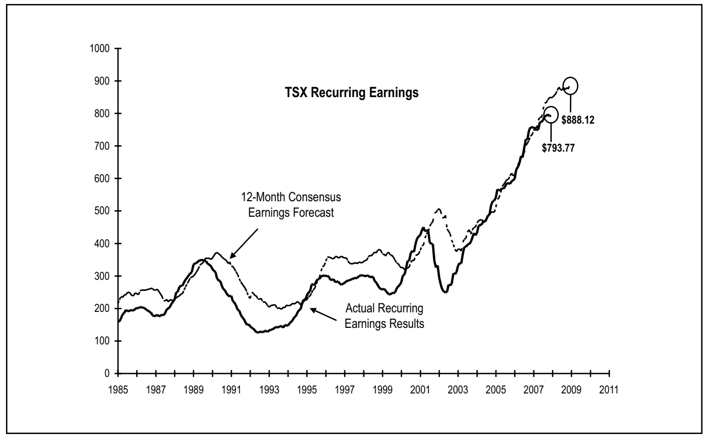
Fed cutting usually ushers in a period of rising share prices.



Canada's market presents a less comfortable valuation picture.



We look to corroborate our views for financial markets by taking input from two independent, proprietary disciplines: Quantitative Research and Trend & Cycle.



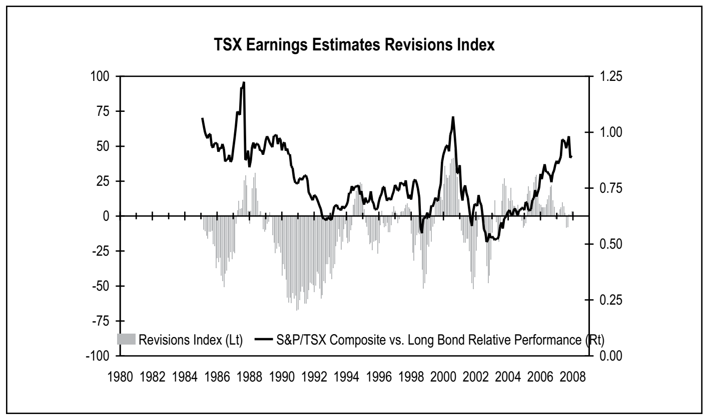
QUANTITATIVE RESEARCH

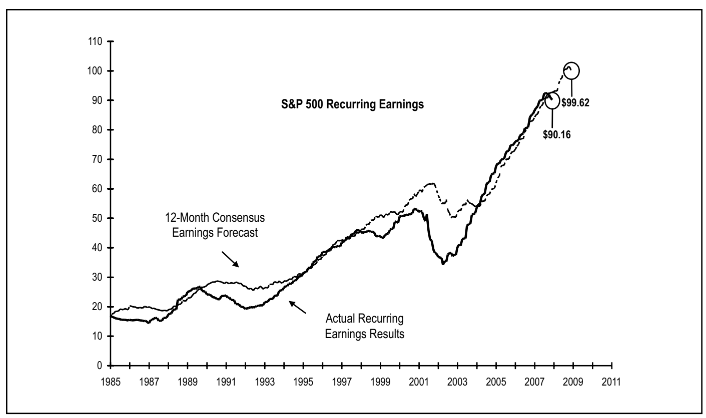
Earnings growth slowing
Leadership has narrowed further in Canada

- Recurring earnings reported by the TSX companies have flattened out in recent months and the year-over-year growth rate has slowed from 9% a quarter ago to just 7% at the end of November. The percentage of stocks in the TSX that are showing higher trailing twelve-month earnings has fallen to less than 50% from 60% a quarter ago and better than 70% earlier in the year.

- Analysts' estimates for TSX stocks have recently risen again after moving sideways for several months. Our Earnings Estimate Revisions Index is giving modestly positive readings.

- In the U.S. S&P 500 recurring earnings have fallen modestly for three successive months, breaking a three-year positive string of no monthly declines. Consensus estimates for earnings one year out have also retreated. Our S&P 500 Earnings Estimate Revisions Index continues to post positive readings although those too have been declining from earlier high ground.

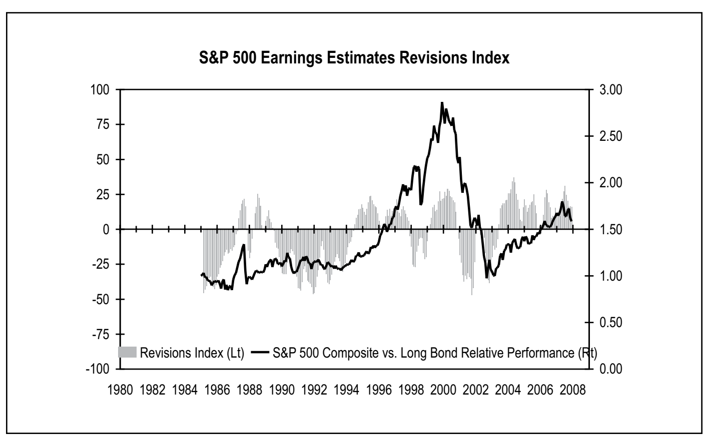




TREND & CYCLE

Downtrend likely to pressure stocks through much of Q1

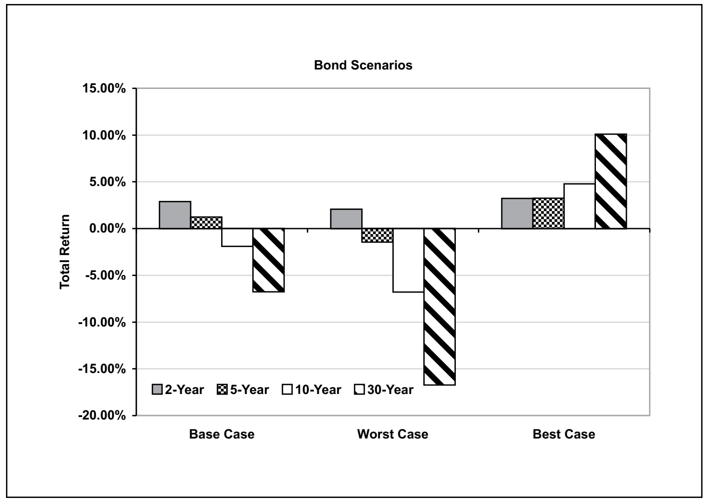
- An intermediate downtrend began from the October/November rally highs posted by most major markets and is still unfolding. Our arithmetic suggests that no significant relief from this downdraft is likely to materialize before mid-way through the first quarter. The eventual stopping point of the decline and the quality of any subsequent recovery will tell us a great deal about the potential market path for the remainder of the year and into 2009.



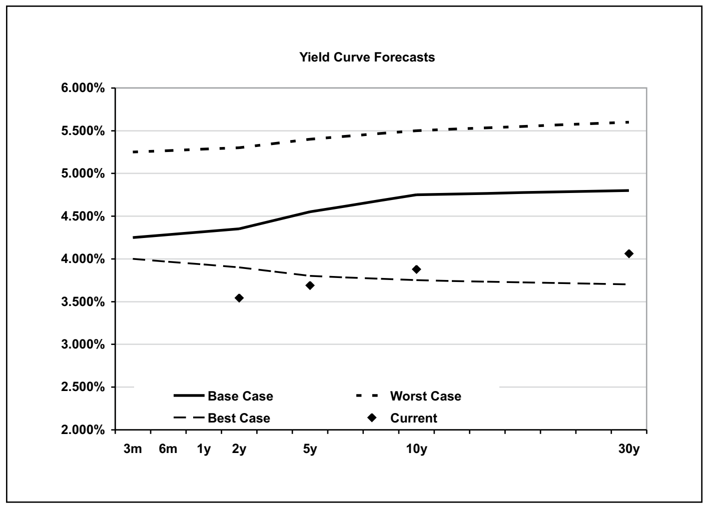
FIXED INCOME

SCENARIO ANALYSIS

Most clients use the fixed income portion of their portfolios for current income, to balance their exposure to equities and minimize volatility. For this type of investor, the popular laddered bond portfolio strategy is appropriate, and more detail on this strategy can be found on page 32. Some investors, however, will look to the bond market from a total return perspective, and the comments that follow pertain to them.



Attached is a chart showing the performance of each benchmark bond over a one-year term under each forecast scenario. The calculations take into account the forecast yield one year out and the passage of time. i.e. a 5-year bond will be a 4-year bond at the horizon date, so the analysis includes any decrease/increase in yield from the bond "rolling down" the yield curve.



- The flight to quality driven rally in place since August has government bond yields approaching multi-year lows, diminishing the total return potential of the asset class. Positive total returns only occur across the board in the Best Case, with Base Case returns either negative or below the bonds' coupons.

- The Base Case favours short-term issues as the 10-year and 30-year returns are negative. The 2-year's short duration causes it to outperform in this scenario.

- The 2-year is the only profitable option in the Worst Case scenario given the significant sell-off from current levels. Investors worried about higher growth and inflation risks in Canada are better off keeping a shorter duration position.

- Investors who see weak economic performance going forward coupled with a slowdown in inflation should look to the Best Case scenario. 30-year bonds may be the right fit for aggressive investors interested in maximizing their duration exposure and leverage to falling yields. Firm believers in the Best Case view who are wary of a 30-year bond's duration are best served in the short end as opposed to the 10-year. While the 10-year outperforms the 2-year by 155bps in the Best Case, it markedly underperforms the 2-year in all other scenarios (477bps in the Base Case and 883bps in the Worst Case). In our view, the risks of holding long-term bonds outweigh the rewards given our forecasts.

ASSET MIX

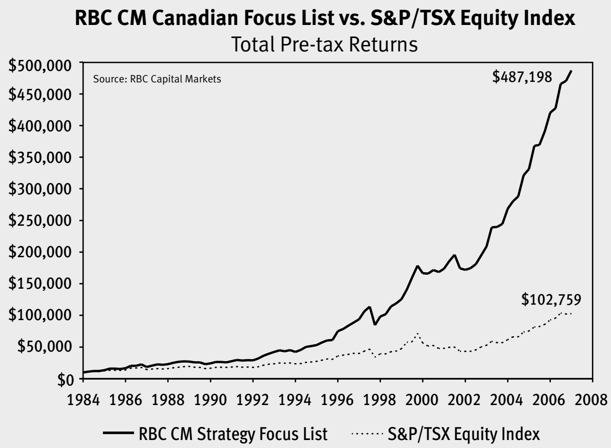
No U.S. recession forecast still favoured but risks have risen
Fed cutting underpins stocks, tough on bonds

- Our forecast has not changed materially – we expect much more moderate rates of economic growth in North America, with contained inflation and no recession. But the tighter credit conditions stemming from financial market turmoil means that the risks to that forecast have risen. That said, the Fed has many tools at its disposal to ensure that a liquidity event in financial markets doesn't take too great a toll on the real economy and it has demonstrated a clear willingness to use them.
- Bond yields, pushed unsustainably low by the 'flight-to-quality', are forecast to move higher over the coming year.
- Our stock market recommendation acknowledges that the 'risk window' will likely remain open through much of Q1 but that the one-to-two year return potential is attractive – and more likely to transpire now that the Fed has begun to cut rates.
- Global Portfolio – For a global portfolio, the attractive valuation levels offered by all major markets outside Canada, together with the prospects for an extended global economic expansion, continue to permit a moderate over-weight for stocks. We recommend a below-normal commitment to bonds.
- All-Canadian Portfolio – For an all-Canadian portfolio, where valuations are still very full, a worsening of the global economy (against our expectation) would exact a greater penalty. We have moved our recommended commitment to equities back to no more than a neutral setting for now together with maintenance of an higher-than-normal cash position.

Historical Range*	Asset Class	Previous	Current	Recommended Action	Expected 1-year Returns
0% – 40%	Cash	15%	**20% ↑**	**Increase cash reserves**	4%
10% – 55%	Bonds	25%	**25%**	**Below-average bond commitment**	0% to 2%
40% – 70%	Stocks	60%	**55% ↓**	**Decrease exposure to stocks**	7% to 10%
**Since inception in 1984*		100%	**100%**		

CANADIAN EQUITIES

Jean François Dion, Portfolio Advisor



The *Strategy Focus List* is comprised of 18 to 21 stocks, which our three-discipline selection criteria (Fundamental Analysis, Quantitative Research and Trend & Cycle) suggest offers solid return potential relative to the risk assumed. This implies that individual stocks may be removed from this list, even though they are still regarded as having good return potential by one or more of our various disciplines. Since its inception (December 1984), our model portfolio based on the *Strategy Focus List* has outperformed the S&P/TSX Equity Index with a compound annual return (excluding transaction costs) of 18.5% against 10.8% for the market.

** For important disclosure regarding Focus List performance, please see p. 33.*

THE STRATEGY FOCUS LIST

INTEREST SENSITIVE – 7 out of 20 positions

Financial Services
Bank of Nova Scotia
Royal Bank
TD Bank
Power Financial
Manulife
Sun Life (addition)

Telecom Services
Rogers Communications

Utilities
None

CONSUMER – 2 out of 20 positions

Consumer Discretionary
Shaw Communications

Consumer Staples
Shoppers Drug Mart

Health Care
None

INDUSTRIAL – 3 out of 20 positions

Industrial Products
Finning
WestJet (addition)

Information Technology
Research In Motion

COMMODITY / RESOURCE – 8 out of 20 positions

Materials
Inmet Mining
Goldcorp
Potash Corp

Energy
Imperial Oil (addition)
EnCana
Husky Energy
Petro-Canada
TransCanada Corp.

OUR DIVERSIFICATION APPROACH

Measured over the long term, stocks have provided superior returns to any other financial asset class. However, over shorter time periods, equities are the most susceptible to fluctuations in value.

Our approach relies upon diversification to give the best chance of achieving long-term return potential while minimizing the risks presented by near-term fluctuations. We follow three steps:

1. We divide the market into four basic sectors, distinguished by the macroeconomic factors, which tend to determine their outlook. The sectors are:
   - Interest Sensitive (Financials, Communications, Utilities)
   - Consumer (Consumer Discretionary, Consumer Staples, Health Care)
   - Industrial (Industrials, Information Technology)
   - Commodity/Resource (Energy, Materials)
2. We include core selections from each of the four sectors at all times.
3. We overweight the sectors that offer the best potential for the coming 12 to 18 months, and underweight those not expected to do as well.

Financial Services – 6 positions out of 20

Underweight – (29.5% recommended vs. S&P/TSX weight of 31.5%)

Bank shares are expected to continue underperforming the lifecos as they remain vulnerable to deteriorating credit conditions and wholesale earnings. News flow could remain negative as U.S. sub-prime mortgage delinquency rates increase and credit concerns continue, however valuations look more attractive following the recent pull back. Strong retail and wealth management segments are expected to drive earnings growth. Lifecos are less exposed to a potential deterioration in credit quality but are vulnerable to any further strengthening of the Canadian dollar. As a result of current financial market conditions, we have moved to underweight in the sector.

Company Profile	Investment Rationale
Bank of Nova Scotia (BNS) Canada's most international bank, with a highly competitive domestic presence. The domestic bank, wealth management included, delivers a steady contribution at ~40-45% of earnings, while international banking accounts for ~25%. BNS has a long and successful track record in the Caribbean and certain emerging markets. The wholesale division delivers the remaining 30-35% of net income.	› A strong capital position, judiciously employed, should allow incremental growth through international acquisitions and organic expansion. International operations are growing faster than the domestic and should go on doing so in Latin America and the Caribbean. The 15-30% growth rate at the Mexican operation is particularly notable. › Headline risk appears lower for Scotiabank. Exposures to U.S. sub-prime mortgages, LBO commitments, asset-backed commercial paper and structured investment vehicles appear small compared to peers. › BNS has the best loan-loss record over a 20-year period among its peers, and continues to be the most active of the Canadian banks in the U.S. and corporate loan syndication market. The latter could prove a liability in the event of a U.S. recession.
TD Bank (TD) A full-service bank engaged in personal, commercial, and investment banking, discount securities brokerage, and real estate investment in Canada and abroad. Earnings are split between TD Canada Trust (55%), TD Securities (14%), TD Wealth Management (12%), U.S. Personal & Commercial (13%) and TD Ameritrade (6%).	› Domestic retail momentum and higher U.S. earnings should drive above-average earnings growth. › There is less downside risk earnings risk for TD than for its peers as it is less exposed to wholesale earnings, and appears to have a more conservative mix of businesses within its wholesale division. › Strategic positioning in the U.S. is considered the best among the Canadian banks. Management is highly regarded and has an excellent track record for making and integrating acquisitions. › Efficiency improvements are likely to slow in 2008. Revenue growth should remain strong, but expense growth could increase as the bank extends opening hours and continues opening branches.
Royal Bank (RY) RY is the largest Canadian chartered bank, offering a full range of personal, commercial, and corporate banking services. Royal extended its reach into the U.S. through acquisitions in recent years that included Dain Rauscher, Centura Bank, Tucker Anthony Sutro, and Liberty Life.	› Leading leverage to capital markets, wealth management, and private banking in both the U.S. and Canada. Slower expense growth is expected to lead to improving bottom line growth in retail banking. › Retail model remains a real competitive advantage, with a broader, stronger product set than its peers, disciplined pricing (enabled by superior product diversity), and unique, in-house distribution. › A more diversified capital markets business should lead to lower volatility in revenue and earnings than for some of its competitors. › Commands a valuation premium, based on disciplined management, superior sales technology and execution, as well as leading wealth management and wholesale banking leverage.

Company Profile	Investment Rationale
*** Sun Life (SLF)** Sun Life is one of Canada's largest life insurance companies. The company generates 48% of its net income in Canada, 32% in the U.S., 15% in the U.K. and 5% in Asia. Sun Life has a substantial wealth management presence through 96% owned MFS, the 17th largest U.S. mutual fund company, its 36% stake in Canada's second-largest fund company, CI Investments, and a 56% interest in McLean Budden, an institutional money manager. * addition to Focus List	› Margins are rising following the implementation of a new funding structure for individual U.S. insurance products, while earnings in the group employee benefit segments have more than doubled following the acquisition of a line of business from Genworth. › Expected to continue benefiting from its exposure to attractive asset management businesses and its well-positioned domestic group platform. › Continues to trade at a discount to Manulife (MFC) and Great-West (GWO), the other large Canadian lifecos. While its earnings quality and growth has historically been weaker than its peers, the gap has recently narrowed, suggesting that the valuation discount may shrink.
Manulife (MFC) Canada's largest, and most diversified life insurance company, with substantial operations in the U.S. (more than 50% of revenues) and Asia (over 10%).	› Increasing market share and superior sales growth reflect consistent product innovations and leading service to distribution channels. MFC is well positioned to capitalize on growth opportunities in the Asian region. › Diversity of operations limits downside earnings risk and reserves appear conservative, with large provisions for adverse deviations relative to reserves and a track record of booking experience gains. The company remains well positioned if long-term interest rates increase, and to make acquisitions if attractive opportunities arise. › Over $3 billion of excess capital leaves room for both share repurchases and dividend increases. › Susceptible to foreign exchange translation, as nearly two-thirds of earnings are USD-based and unhedged.
Power Financial (PWF) A Montreal-based holding company with significant exposure to financial services through a 70% interest in Great West Lifeco (GWO) and a 56% interest in IGM Financial (IGM). Power Corp (POW) controls 66% of the common shares of PWF.	› Strong track record of consistent growth in Net Asset Value (NAV) and dividends. Attractive and diversified underlying assets in GWO and IGM. › The recent acquisition of Putnam asset management business by Great West Life could provide incremental upside despite the integration risks associated with the transaction. Improvements in margin performance and net sales are expected to drive returns. › Experienced management has had success with prior acquisitions and a track record of successful deals.

Telecom Services – 1 position out of 20

Underweight – (4.5% recommended vs. S&P/TSX weight of 5.9%)

While strengthening cash flows and dividend growth continue to underpin the sector, we are more cautious given a more challenging wireless environment due to the likelihood of a new national wireless carrier. While it appears unlikely that a new entrant could materially disrupt the wireless market in the next three to four years, the threat of increased competition could be an overhang for the sector. Moderation of wireless growth and the potential for downward estimate revisions could also limit upside.

Company Profile	Investment Rationale
Rogers Communications (RCI.B) Rogers consists of Rogers Cable, Rogers Wireless (now 100%-owned), and Rogers Media (magazines, radio and TV stations). It also holds 30% of Cogeco Cable, 100% of the Toronto Blue Jays, the Rogers Centre (formerly SkyDome), and other investments.	› RCI should outperform other telecom and cable stocks over the medium-longer term due to its favourable asset mix and improving free cash flow. › Cash flow from operations helps de-leverage the balance sheet. Management has indicated it plans to institute a free cash flow policy that could include dividend growth and/or share repurchases. › RCI is attractively valued relative to its peers, with the potential for a positive revaluation of the shares as the company de-leverages.

Utilities – 0 positions out of 20

Market-weight – (1.0% recommended vs. S&P/TSX weight of 1.5%)

Valuations appear stretched based on a price-to-earnings basis as well as in relation to current interest rate levels, and the sector remains vulnerable to increasing bond yields. However companies within the sector possess attributes we like in the current environment, including solid profitability, earnings predictability, and substantial dividends. Organic growth, while modest, is expected from power projects, oil sands opportunities, and ancillary gas services (processing, storage, and extraction).

Consumer Discretionary – 1 position out of 20

Overweight – (7.0% recommended vs. S&P/TSX weight of 4.6%)

We recommend an overweight for the sector. Despite some signs of moderation, the outlook for employment, wage growth and consumer spending remain firmly positive. Our positive bias towards the cable and media companies stems from expanding free cash flow and attractive profitability metrics. We remain cautious on the auto industry based on a slowdown for the U.S. economy and rising energy costs.

Company Profile	Investment Rationale
Shaw Communications (SJR.B) Shaw Communications is Canada's largest video broadcast company, with approximately 2.2 million cable subscribers in Western Canada and over 870,000 satellite customers. The company is also one of Canada's largest broadband service providers. In addition to cable, high speed Internet and satellite, Shaw has investments in interactive television, e-commerce, telecom, specialty programming networks, radio, and the digital delivery of music.	› Attractive economics are flowing from Shaw's VoIP offering, increasing subscriber growth, expanding margins and decreasing capital expenditure requirements. Pricing increases and subscriber growth at the cable and satellite divisions are expected to drive continued revenue and earnings growth. › Shaw's largest markets, B.C. and Alberta, enjoy the highest population and household formation growth in Canada, a key source of sustainable long-term revenue growth. › Shaw's strong financial focus and disciplined capital spending deliver the highest EBITDA margins among large-cap North American cable companies. Capital spending is focused and return on invested capital has improved significantly.

Consumer Staples – 1 position out of 20

Market-weight – (2.0% recommended vs. S&P/TSX weight of 2.8%)

Continued uncertainty in the grocery space due to increased pricing pressure (especially in Ontario), combined with lofty valuations elsewhere in the sector, lead us to a cautious view. We like the defensive characteristics of this sector and believe that support will come from investors' quest for high quality attributes and low level of economic sensitivity.

Company Profile	Investment Rationale
Shoppers Drug Mart (SC) Canada's only national drugstore chain, holds a #1 market share in prescription drug sales in eight of the 10 provinces and has nearly 1,000 retail franchises. It began trading as a public company in November of 2001.	› Consistent delivery of strong comparable-store sales and margins in a challenging retail environment. Valuation premium relative to U.S. peers is justified by quality of earnings and visibility. › Emphasis on health, beauty, and convenience should enable it to continue to outperform industry players in front-of-store where it is focused on improving returns by increasing its offering and modifying its private label program to maximize gross margins.

Health Care – 0 positions out of 20

Market-weight – (0.0% recommended vs. S&P/TSX weight of 0.5%)

Healthcare tends to outperform the broader market in an environment of moderating economic growth and it appears analysts' sentiment has bottomed. We remain concerned about a lack of visibility within the sector and we find it difficult to identify companies that are attractive using our multi-discipline stock selection process.

Information Technology – 1 position out of 20

Market-weight – (5.5% recommended vs. S&P/TSX weight of 5.8%)

Prospects for the sector are improving on a company-by-company basis, making stock selectivity key. In general, balance sheets are in good shape, free-cash-flow generation is strong, and revenue growth appears sustainable. ROEs are improving and there is potential for modest valuation expansion.

Company Profile	Investment Rationale
Research In Motion (RIM) Research In Motion is a developer, manufacturer, and marketer of wireless handheld devices, software, and messaging-based wireless services. The company's products include the BlackBerry wireless handhelds, radio modems, BlackBerry Enterprise Server software and the BlackBerry data service backed by RIM's Network Operations Centre infrastructure.	› Positive momentum should be supported by a strong product cycle of business and consumer handsets expected to launch over the next few quarters. › Global penetration of 1-2% leaves substantial room for further momentum and growth in international markets. › In the enterprise market, RIM's market share is expected to remain dominant but may moderate as the company faces competitive pushes from Microsoft, Motorola, Apple and Nokia. RIM's devices and services continue to be perceived positively by CIOs, and the company continues to innovate by offering new handsets and value-added services.

Industrial Products – 2 positions out of 20

Overweight – (8.5% recommended vs. S&P/TSX weight of 5.4%)

Despite the outlook for slower North American economic growth, we remain over-weight Industrials in Canada. Sluggish traffic statistics and our outlook for a slowing U.S. economy have driven us to reduce exposure to the railroad sector. A global upswing in aerospace and infrastructure investment as well as the longer-term view on the global resource industry provide a positive backdrop for a number of other companies in the sector.

Company Profile	Investment Rationale
Finning (FTT) Finning International Inc. is one of the world's largest Caterpillar equipment dealers. The company sells, rents, finances and provides customer support services for Caterpillar equipment and engines in Western Canada, the U.K., and South America (Argentina, Bolivia, Chile and Uruguay). Finning also owns Hewden, the largest equipment rental business in the U.K.	› An extended commodities cycle is driving revenue gains. FTT's competitive cost position should help to insulate it from any correction in commodity pricing. › The company's order backlog currently stands at $1.8 billion, providing good revenue visibility. Leveling off of the order backlog is partially indicative of faster delivery times and higher reported revenues.
*** WestJet (WJA)** WestJet Airlines provides discount jet service linking Canadian cities as well as several U.S. and Caribbean destinations. Since its first flight in 1996 with a fleet of only three aircraft, WestJet's fleet has grown to 68 new generation Boeing 737 jets. WestJet is Canada's second largest air carrier. * addition to Focus List	› Continues to benefit from a strong Canadian economy, which has increased demand for air travel, driving Westjet's load factor to in excess of 80%. › The strong Canadian dollar continues to benefit the company as it increases demand for cross border flights and decreases costs which are primarily reflected in U.S. dollars. › Significant growth opportunities are available as the company has only a 9% share of cross border flights and a 0% share of the international market.

Materials – 3 positions out of 20

Market-weight – (17.5% recommended vs. S&P/TSX weight of 17.0%)

The recent correction has brought the performance of mining shares more in-line with metal prices. Free cash flow generation and large cash balances at the corporate level could support consolidation within the sector and help underpin valuations. Global demand is expected to remain strong and buoy commodity prices over the longer term. Gold remains a primary focus among the metals.

Company Profile	Investment Rationale
Inmet Mining (IMN) Inmet is a diversified mining company with exposure to copper (approximately 55% of revenues), zinc (30%) and gold (15%). Assets include the Cayeli copper and zinc mine in Turkey, an 18% interest in the Ok Tedi copper and gold mine in Papua New Guinea, the Pyhasalmi copper and zinc mine in Finland and the Troilus gold and copper mine in Canada. Inmet also owns several undeveloped projects in Turkey, Canada and Panama, and a 70% interest in the Las Cruces copper development project in Spain.	› IMN is expected to double copper production by 2009 due mostly to the contribution of Las Cruces. Additional long-term growth is expected to come from Cerateppe in Turkey and the Petaquilla copper project in Panama. › Inmet's attractive development projects and approximately $14 per share of cash suggest it could be a potential takeover candidate. › The shares also offer high leverage to copper and zinc prices. Metal markets fundamentals remain robust, with inventories at low levels and growing demand exceeding supply. Absent a recession, metal prices are expected to remain firm.

Company Profile	Investment Rationale
Goldcorp (G) An established Canadian gold producer with interests in operating mines in Canada, U.S.A, Mexico, Argentina, and Australia. Goldcorp is now North America's newest Tier I gold producer after the acquisition of Glamis Gold as well as assets from Placer Dome.	› Goldcorp has the most attractive cost and production growth profile of all the North American Tier I gold equities, enhanced by the recent acquisition of Glamis Gold (GLG), which offers a good strategic fit. › Potential catalysts in the near-to-medium term include the successful ramp-up of new mines in Brazil, Guatemela, and Mexico, as well as pending exploration results and resource updates (notably from the Eleonore gold deposit in Quebec).
Potash Corp (POT) Potash is the world's largest producer of potash, nitrogen, and phosphate products for the fertilizer, feed and industrial markets. Its primary business is potash, where it leads with 22% of total production capacity, and 75% of estimated excess capacity. In nitrogen, it is the fourth largest producer in the world (2% of world capacity) and is strategically located in Trinidad where the relatively low gas costs provide a competitive advantage. With 6% of world capacity, Potash is the third largest phosphate producer worldwide.	› Fertilizer industry fundamentals remain very strong as increasing demand puts upward pressure on potash prices. › The recent announcement of a large crater at a flooded Russian potash mine increased concerns that subsidence could disrupt the area's rail transportation network and negatively impact potash deliveries from the region. While a supply disruption would be temporary, the impact on potash prices could last longer. › The company announced a major mine and mill expansion at Rocanville. The 2 million tonne project will cost $1.8 billion to build, is expected to be in service by the end of 2012, and will enable Potash to further capitalize on robust potash market fundamentals.

Energy – 5 positions out of 20

Market-weight — (24.5% recommended vs. S&P/TSX weight of 24.9%)

Seasonal demand weakness is now behind us, and there is potential for improving refining spreads. High natural gas inventories, well above historical norms suggest near-term caution on revenues while cost inflation and the high Canadian dollar negatively impact profitability. Above-average inventory levels for both crude oil and natural gas may continue to weigh on the market but the possibility of a supply shock can not be ruled out. The earnings of integrated producers should benefit from strong refining margins.

Company Profile	Investment Rationale
*** Imperial Oil (IMO)** Imperial Oil is the largest oil producer, refiner and marketer in Canada. The company has a long reserve life asset base with a 25% interest in Syncrude, a joint venture that is the world's largest producer of synthetic crude oil from oil sands. Additionally, Imperial Oil has a large and growing bitumen operation at Cold Lake, a large oil sands deposit in Alberta, Canada, and a stable base of conventional production in Western Canada. The company also holds a small interest in the Sable Island gas field and a large undeveloped gas asset base in the Mackenzie Delta. * addition to Focus List	› Refining margins are expected to remain above historical average for 2008, with the potential to surprise to the upside. An expansion in refining margins would lead to positive earnings revisions, with Imperial Oil potentially benefiting more than peers due to its leveraged position. › Prudent and conservative capital management could favour the company given cost pressures that many companies are facing. Share repurchase program and dividend increases offer evidence of disciplined capital management and focus on returning value to shareholders. › Long-term production growth is expected to come from the Kearl oil sands project at the end of this decade.

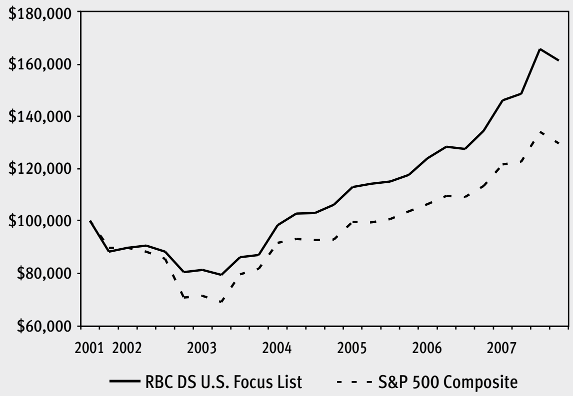
Company Profile	Investment Rationale
EnCana (ECA) A senior upstream oil and gas producer. Major assets include: significant shallow natural gas in Alberta, medium-depth natural gas production in Alberta and B.C., as well as U.S. Rocky Mountain gas production in Wyoming and Colorado. The 2004 acquisition of Tom Brown added long reserve life production in Texas.	› A unique platform of unconventional, low decline natural gas properties, freehold land holdings, and oil sands assets that would be difficult for peers to replicate. › EnCana recently entered into an agreement with ConocoPhillips (COP) to create an integrated North American heavy oil venture, consisting of a Canadian upstream partnership and a U.S. downstream partnership. RBC CM expects the JV's capital and operating costs to be among the lowest of all integrated oil sands projects, which should also yield best-in-class returns. › ECA trades at an attractive multiple to its net asset value, especially given its growth profile relative to its peers and potential acquisition candidacy.
Husky Energy (HSE) An integrated oil and gas company with a diversified portfolio of resource assets including heavy and conventional oil in Western Canada, oil sands leases, East Coast oil, and a 40% interest in a South China oil project. HSE also owns midstream assets including a heavy oil upgrader and infrastructure, and downstream assets predominately in asphalt and retail. Li Ka Shing (Chairman of Hong Kong-based Hutchison Wampoa) controls approximately 71% of HSE.	› HSE provides investors with exposure to a diversified energy play with solid production growth potential. › Recent joint venture announcement with BP puts focus on Husky's growing heavy oil production, while the Toledo refinery joint venture allows the company flexibility to optimize total downstream conversion capacity. › Strong track record of paying increasing dividends to shareholders.
Petro-Canada (PCA) Petro-Canada is an integrated oil and gas company with approximately 4,800 employees around the world. The company provides exposure to both upstream and downstream with major operations in the exploration, development, refining and marketing of crude oil and natural gas.	› High exposure to attractive crack spreads and strong refinery utilization should allow PCA to post record downstream earnings. › Continues to trade at a discount to the group and to its net asset value. Current valuation does not appear to reflect the potential associated to the company's oil sands assets. › Strong balance sheet should allow funding of capital programs and significant share buybacks.
TransCanada Corp. (TRP) Operates a network of approximately 41,000 kms of pipeline that transports the majority of western Canada's natural gas production to the fastest growing markets in Canada and the United States. TransCanada also owns, controls or is constructing approximately 5,000 megawatts of power generation, including a 31.6% interest in Bruce Power.	› TRP's regulated transmission operations, strong balance sheet, significant free cash flow, disciplined management team and visible earnings stream make it a comparatively low risk investment in the sector. › Bruce Power provides low-cost nuclear power in Ontario, and offers TRP opportunities to capitalize on higher spot/contracted Ontario power prices. › Future growth opportunities include northern gas development and the acquisition of hydro assets. Proposed Atlantic LNG terminals offer further potential pipeline opportunities.

UNITED STATES EQUITIES

Mark Bayko, U.S. Portfolio Advisor

RBC DS U.S. Focus List vs. S&P 500 Composite

Total Pre-tax Returns



The *U.S. Focus List* is typically composed of 20 stocks, which our three-discipline selection criteria (Fundamental Analysis, Quantitative Research and Trend & Cycle) suggest offers solid return potential relative to risk assumed. This implies that individual stocks may be removed from this list, even though they are still regarded as having good return potential by one or more of our various disciplines. Since its inception (June 2001), our model portfolio based on the *U.S. Focus List* has outperformed the S&P 500 Composite with a compound annual return (excluding transaction costs) of 8.0% against 4.2% for the market.

** For important disclosure regarding Focus List performance, please see p. 33.*

The U.S. Focus List is typically composed of 20 stocks, expected to do well in the economic and financial environment over the next one to two years. Each exhibits strong fundamentals, a leading position within its industry, attractive relative valuation and the prospect for good performance relative to the market.

U.S. FOCUS LIST STOCKS

INTEREST SENSITIVE – 5 out of 20 positions

Financial Services	Telecom Services	Utilities
Bank of New York Mellon (addition)	Verizon	Edison International
JP Morgan Chase		
MetLife		

CONSUMER – 6 out of 20 positions

Consumer Discretionary	Consumer Staples	Health Care
Walt Disney	Procter & Gamble	Thermo Fisher
McDonald's		Medco Health Solutions
Nike (addition)		

INDUSTRIAL – 6 out of 20 positions

Industrial Products	Information Technology
Cooper Industries	Oracle
L3 Communications	Intel (addition)
Textron	Dell

COMMODITY / RESOURCE – 3 out of 20 positions

Materials	Energy
Freeport McMoRan	Exxon Mobil
	Apache

Financial Services – 3 positions out of 20

Underweight — (16.0% recommended vs. S&P 500 weight of 17.6%)

Our underweight position is based on expectations of further deterioration in credit quality, limited improvements in net interest margins, and additional write-downs resulting from liquidity challenges in the asset-backed commercial paper market. Based on these concerns, we favour banks that are well capitalized and have diversified business models. The operating environment has grown more challenging for capital markets-driven companies given liquidity challenges in the financial markets, although conditions overseas remain relatively more attractive. Meanwhile, insurers face somewhat of a mixed outlook as trends in life and retirement-based products remain strong while property and casualty pricing remains at risk given heightened competition.

Company Profile	Investment Rationale
*** Bank of New York Mellon (BK)** Formed through the 2007 merger of Bank of New York and Mellon Financial. The company is one of world's largest providers of custodian and security services, transaction processing, and wealth management. * Addition to Focus List	› The merger has created significant scale advantages and the potential for substantial merger synergies. Profitability in custodian services and transaction processing is largely volume driven, and the combined company is now among the largest in the world. Furthermore, cross selling opportunities among customers presents new growth opportunities. › The company is primarily focused on its fee-based model, as opposed to traditional banks that continue to rely on net interest income. Given its business mix, BK is less leveraged to deteriorating credit conditions. › The company's Tier 1 capital ratio stands at 9.1%, above its 8% target and many of its banking peers.
JP Morgan Chase (JPM) Among the very largest U.S. banks with ~$1 trillion in assets, JPM derives approximately 25% of its revenues from each of the following divisions: Credit Card Services, Investment Banking and Retail Financial Services.	› The integration of recent acquisitions has provided the company with a more stable credit card and retail banking business, compared to its more volatile capital markets division. › Management has addressed profitability by way of disposing underperforming businesses and reducing the volatility of trading-related revenue. › We remain comfortable with JPM's exposure to credit-related activities based on its smaller exposure to CDO underwriting, limited exposure to off balance sheet structured financing activities, and a leveraged loan pipeline that is slowly clearing. JPM's Tier 1 capital ratio is 8.4%.
MetLife (MET) The largest life insurance company in the U.S. offering a variety of life, retirement, and investment products through the institutional (42%) and individual (30%) channels.	› Diverse offerings and distribution channels. Its focus on fixed rate annuities, as opposed to variable, has created a more conservative profile relative to some of its peers. › International results have been gaining momentum, particularly in Japan, Korea, and Mexico. This segment represents an attractive future growth opportunity. › The company has ample room to continue its aggressive share repurchase plan following the sale of some of its real estate holdings. In turn, this could drive ROE higher.

Telecom Services – 1 position out of 20

Overweight – (4.0% recommended vs. S&P 500 weight of 3.5%)

Consolidation has led to stabilizing wireline and enterprise trends resulting in improved profitability across the sector. Meanwhile, growth in wireless remains healthy and the rollout of fiber-related initiatives has highlighted the potential of bundled offerings. Despite elevated levels of capital expenditures, the sector continues to be supported by stable cash flows and attractive dividend yields.

Company Profile	Investment Rationale
Verizon (VZ) Verizon provides integrated telecommunications services to consumer, business, and government customers and is the largest wireless carrier in the U.S. by revenue. The company generates approximately 57% of revenue through its wireline segment, with the remainder coming from its Verizon Wireless joint venture with Vodafone Plc.	› Verizon is seeing some of stabilization in its wireline business. These trends are being driven by cost savings from the acquisition of MCI, improved pricing in the enterprise market, and higher ARPU from bundled service offerings. › Despite elevated levels of capital spending on its fiber-to-the-premise network, Verizon may start to see less earnings dilution due to improving penetration, cost per home, and ARPU metrics. › Verizon Wireless is the most profitable wireless franchise in the U.S., with leading churn rates, margins, and revenue per unit.

Utilities – 1 position out of 20

Market-weight – (3.5% recommended vs. S&P 500 weight of 3.7%)

Some companies continue to benefit from added scale, cost savings, and improving profitability as a result of recent consolidation, divestitures, and restructuring initiatives. We favour companies operating in markets where substantial investment in power generation infrastructure is required. We believe the sector will be supported by relatively stable cash flows and solid dividend yields.

Company Profile	Investment Rationale
Edison International (EIX) Utility holding company of regulated and non-regulated assets. Southern California Edison, operates a regulated utility in southern, coastal, and central California. Edison Mission Group operates coal-fired merchant generation fleets in the Midwest and MidAtlantic, as well as a business focused on financing infrastructure investments.	› SCE is benefiting from favourable demographics with its service territory covering areas that are experiencing some of the fastest population growth in the U.S. As a result, peak power demand in these areas has grown at above-average rates. › California enjoys one of the most constructive regulatory environments in the U.S. Since 2001, the California Public Utility Commission (CPUC) has undertaken various initiatives to avoid the state's chronic "under investment" in power generation and delivery infrastructure. These initiatives have resulted in significant capital expenditure, rapid rate base growth and stable returns on equity for SCE. › Edison's low cost coal-fired merchant generation assets operate in markets where power prices are typically dictated by more expensive gas-fired generation.

Consumer Discretionary – 3 positions out of 20

Underweight– (8.0% recommended vs. S&P 500 weight of 9.0%)

The sector is characterized by a diverse group of sub-sectors, ranging from retailers, restaurants, automotive, media, and home builders. We believe the sector is vulnerable to a potential slowdown in consumer spending driven by weaker housing prices, a moderation in job growth, and high energy prices. Stock selectivity remains a focus given the breadth of choices available.

Company Profile	Investment Rationale
Walt Disney (DIS) Disney is a media, leisure and entertainment company that derives its revenues from Theme Parks & Resorts (29% of 2006 revenue), Film (21%) and Television Networks (43%). It is one of the most diversified leisure and entertainment companies globally with networks such as ABC & ESPN, and Film Studios including Miramax, Walt Disney Studios, and Touchstone Pictures.	› CEO Robert Iger has undertaken initiatives to drive its content through new distribution platforms. › ABC's improved contribution to the company is expected to continue fuelled by advertising rates and continued programming success. › The 2006 and 2007 film releases ("Pirates of the Carribean" II and III, "Cars", and "Ratatouille") have led to improved results at the film division. The acquisition of Pixar has brought industry-leading expertise and content in house.
McDonald's (MCD) McDonald's is the world's largest fast food restaurant with more than 30,000 locations globally, and generates more than 50% of its system wide sales internationally. The company recently agreed to sell its Boston Market chain, and spin off its Pret a Manger chain in the U.K.	› Its restaurants are generating strong same-store sales trends globally, largely attributable to new healthier menu items, remodelling of restaurants, and premium pricing. › MCD raised its dividend by 50% in 2006 and 2007, respectively, and recently committed to returning up to $17 billion to shareholders via dividends and share repurchases between 2007-2009. › Potential exists to surface value through franchising more of its U.K. stores, and/or the further divestiture of partially-owned subsidiaries.
*** Nike (NKE)** The leading manufacturer of running and casual shoes, athletic gear, and other apparel and accessories. The company's products are sold in more than 160 countries. * addition to Focus List	› More than 60% of the company's sales are sourced from outside the U.S., providing it with leverage to a growing international consumer base. Despite an expected slowdown in U.S. consumer spending, Europe, Asia Pacific, and South America continue to generate impressive growth. › New product initiatives across multiple categories, including soccer, running, and performance apparel, continue to drive growth opportunities. Furthermore, various manufacturing initiatives are expected to enhance gross margins. › With no long-term debt and more than $3 per share in net cash, the company has a strong balance sheet. It remains committed to dividend increases and share repurchases.

Consumer Staples – 1 position out of 20

Market-weight – (11.0% recommended vs. S&P 500 weight of 11.0%)

This sector is comprised of sub-groups ranging from food, beverage, drug retail, tobacco, and consumer products. Despite defensive characteristics, the sector has been faced with rising input costs as many commodity prices remain near record highs. We favour those companies that have an ability to raise prices, generate volume growth, and capability of returning capital to shareholders.

Company Profile	Investment Rationale
Procter & Gamble (PG) The largest consumer and household products company in the world. The company operates under three segments; P&G Beauty, P&G Health, and P&G Household Care. In October 2005, P&G completed its acquisition of Gillette for approximately $54 billion.	› P&G should be able to grow revenue organically by 5-6%. This will be driven by its focus on health and beauty categories and "high frequency stores" in developing markets. › Management has guided for up to 100 basis points in margin improvement in 2008 driven by ongoing cost saving initiatives, systems consolidation, and distribution centre consolidation from its integration of the Gillette operations. › P&G plans on repurchasing up to $30 billion of its shares over the next three years, which represents close to 15% of its market capitalization. This demonstrates the company's commitment to returning value to shareholders.

Health Care – 2 positions out of 20

Market-weight – (12.0% recommended vs. S&P 500 weight of 12.0%)

The sector offers defensive qualities and favourable demographic trends. Earnings growth rates are improving across the sector following a period of contraction, particularly in the pharmaceutical sector. Elsewhere, medical service providers such as HMOs and hospital operators continue to face uncertainty over rising medical cost trends and growth of uninsured patient volumes. Ongoing pressures in the sector, include efforts by government to limit health-care costs and increasing generic competition.

Company Profile	Investment Rationale
Thermo Fisher (TMO) A manufacturer of analytical and laboratory instruments and supplies to a diverse set of end markets, including industrial, consumer, life sciences and health care. The company was formed through the 2006 merger of Thermo Electron and Fisher Scientific.	› Over 50% of Thermo's revenues are driven by healthcare consumables. This provides a relatively stable and recurring revenue stream. › The combined Thermo Fisher is benefiting from cost savings and synergies such as the cross marketing of products and increased scale. › New product offerings in areas such as radioactive material detection, quality control, pollution monitoring, and automation equipment provide new opportunities in different end markets.
Medco Health Solutions (MHS) The largest pharmacy benefit manager in the U.S. with coverage of more than 65 million individuals. The company acts as the intermediary between health insurers, corporate and government health plans, pharmaceuticals, and pharmacies.	› The company's profitability per prescription has expanded by 33% since 2003. We expect generic drug margins to continue to expand as up to $12 billion of branded drugs' patents expire through 2012. › Recent contract wins suggest the company has gained market share at the expense of rivals. Furthermore, earnings and cash flow estimates continue to be revised upwards. › The company's role as an intermediary with an objective of helping customers save money positions it well in an environment where the U.S. government is concerned about health-care costs.

Information Technology – 3 positions out of 20

Market-weight – (17.5% recommended vs. S&P 500 weight of 17.2%)

Growth has been driven by new innovative product offerings, substantial share buybacks, and in some cases significant restructuring initiatives. Overcapacity and intense competition have limited pricing power and resulted in margin compression in some sub-industries. Consequently, many companies have focused on improving profitability rather than gaining market share. We favour companies that have strong balance sheets, are exhibiting solid top-line growth, and can deliver stable and/or improving margins.

Company Profile	Investment Rationale
Oracle (ORCL) Provides database management software and applications software and consulting services focused on customer relationship and supply chain management, and business intelligence.	› ORCL has made several acquisitions over the past couple of years and has committed to supporting the acquired companies' platforms, while gradually integrating them with ORCL's core programs. These efforts have led to recent market share gains in application software for the first time in years, a trend expected to continue. › ORCL's focus on providing a more services oriented architecture longer-term may significantly expand the company's market opportunity. › The company's leading database business generates strong cash flow through a steady and profitable licence-driven business model.
*** Intel (INTC)** The world's largest maker of semiconductor chips and related products for use in computers, workstations, and servers. * addition to Focus List	› A strong PC product cycle is under way, driven by PC upgrades resulting from increasing adoption of Microsoft's new Windows Vista operating system. This provides a constructive backdrop for unit shipments. › Gross margins, an important measure of industry profitability, may improve in 2008 driven by new products that should command higher prices. › Intel appears poised to gain share as its emerging product line-up looks superior to that of main competitor AMD.
Dell (DELL) Dell produces, sells and services a wide range of computer systems, including desktop and notebook personal computers (PCs), enterprise systems, including servers, storage, and workstations, and printing and imaging solutions, software and consumer electronics.	› We believe the new management team – CEO, CFO, and COO – has a sense of urgency with respect to fixing the operational challenges facing the company. › A restructuring plan, focused on cost control, international growth, expanding distribution channels, and improved service levels will eventually lead to improved growth and profitability. › Windows Vista, launched earlier this year, may lead to a stronger PC buying cycle and result in potential upside to current industry sale estimates for 2008.

Industrial Products – 3 positions out of 20

Overweight – (12.5% recommended vs. S&P 500 weight of 11.2%)

The sector is comprised of diverse industry groups, including aerospace, defence, automation, commercial construction, and transportation. Productivity gains continue to offset margin pressures. This should translate into increased profitability were input costs to retreat. While U.S. economic growth has moderated, industrial activity remains healthy, capital spending trends are stable, and international growth remains robust. Our focus is on diversified companies that exhibit pricing power and offer exposure to later cycle end markets.

Company Profile	Investment Rationale
Cooper Industries (CBE) A manufacturer and maintenance service provider of electronic products and tools. Products include circuit protection, wiring, lighting fixtures, plugs and fittings, automated assembly systems and power tools.	› Cooper Industries offers good exposure to later cycle end markets, with 83% of its revenues generated by the industrial, commercial construction, and utilities markets while only 17% is tied to residential construction. › The utilities market in particular represents close to 20% of Cooper's sales. We expect strong results from this segment as infrastructure spending from domestic utilities and capacity growth in China and India accelerate.
L3 Communications (LLL) Supplies a range of products and services, including intelligence, surveillance, and reconnaissance services (ISR), mobile satellite communications, aircraft modernization and maintenance, missiles and munitions, training, and airport security systems. The company's primary customers include the US Department of Defense and the US Department of Homeland Security.	› Expertise in intelligence/surveillance/reconnaissance, communications, and systems positions L3 well for the U.S. government's increasing focus on the application of advanced technologies in both military and homeland security. › In 2006, the company generated nearly $7.35 a share in free cash flow, implying a FCF yield in excess of 8%. The company enjoys a strong capital position with the flexibility to pursue future acquisitions and share repurchase programs. › Expectations are low given the loss of a meaningful military contract in addition to its well respected CEO last year. With the potential for several contract wins, earnings estimates may be revised upwards over coming quarters.
Textron (TXT) An industrial concern operating principally in two areas: 1) business jets and turboprop planes under the Citation and Cessna brands, and 2) helicopters and parts through its Bell segment. The company also services its products and provides ancillary services such as armoured vehicles, weapons, and other aircraft.	› The corporate jet market offers strong growth prospects and earnings visibility as evidenced by Textron's growth in backlog and international orders. Asia in particular offers upside. › The upgrade of existing commercial helicopter fleets, which averages close to 20 years in age, presents a sizeable opportunity. Furthermore, growing use of helicopter transportation in industries such as oil and gas should fuel demand. › Textron owns several businesses, such as golf carts, off-road power utility vehicles, and power tools that may be designated as non core and provide opportunities to free up capital through divestitures.

Materials – 1 position out of 20

Market-weight – (3.0% recommended vs. S&P 500 weight of 3.1%)

We continue to subscribe to the longer-term positive secular outlook for materials markets due, in part, to the ongoing industrialisation of emerging markets. Our investment focus is on sub-groups where demand is strong but supply constrained, including copper, nickel, gold, and some bulk commodities.

Company Profile	Investment Rationale
Freeport McMoRan (FCX) The world's second-largest producer of copper and a major producer of molybdenum and gold. In March 2007, Freeport-McMoRan completed the acquisition of Phelps Dodge for approximately $18 billion. The combined company currently has estimated reserves of 75 billion pounds of copper, 1.9 billion pounds of molybdneum, and 41 million ounces of gold.	› The drivers of copper demand, particularly the industrialization of developing economies, appear favourable, while persistent supply constraints should keep copper prices at elevated levels until at least 2010. › With the acquisition of Phelps Dodge, Freeport now has producing mining facilities in North America, South America, and Indonesia, and exploratory properties in Africa. This diversification lessens its risks tied to one particular region and provides it with potential reserve growth in the future. › Freeport incurred $16 billion in debt to finance its acquisition of Phelps Dodge. In December 2007, the company announced the completion of its debt repayment associated with the acquisition, two to three years ahead of schedule. Subsequently, the company announced a dividend increase and share repurchase program.

Energy – 2 positions out of 20

Over-weight – (12.5% recommended vs. S&P 500 weight of 11.6%)

The long-term secular outlook for energy is constructive given supply constraints and relatively strong demand. However, rising finding, development and other operational costs and more challenging earnings growth make stock selectivity more important. We remain focused on companies that have attractive reserve bases, production growth, and the ability to contain costs more efficiently than peers.

Company Profile	Investment Rationale
Exxon Mobil (XOM) Exxon is the world's largest integrated oil and gas company, with operations in exploration and production, refining and marketing, chemical, and power generation. Exxon operates in 200 countries and generates approximately 68% of its revenues internationally.	› Less susceptible to price volatility than some as its refining and chemical divisions benefit from falling oil prices. › The company is well positioned for longer- term demand growth for alternative energy sources given its initiatives in liquefied natural gas and gas-to-liquids. › XOM's strong balance sheet gives flexibility for share repurchases, dividend increases, and acquisitions.
Apache (APA) Apache is an independent oil & gas company engaged in the exploration and production of natural gas, natural gas liquids and crude oil. In 2006, revenues were driven by crude oil (54%) and natural gas and natural gas liquids.	› A "portfolio approach" that has diversified its geological and geographical risks. The company is less dependent on the North American gas market relative to its peers. › Apache has attractive hedges in place for a sizeable portion of its gas and oil production for 2008. › Apache has a strong track record of production growth and reserve replacement. The company has meaningful growth opportunities in Australia, Canada, and Egypt.

APPENDIX 1: RBC INVESTMENT STRATEGY COMMITTEE ECONOMIC AND CAPITAL MARKETS FORECASTS

ECONOMIC FORECAST TABLE (RBC Investment Strategy Committee)											
		United States	Change from Sep-07 Forecast	Canada	Change from Sep-07 Forecast	Europe	Change from Sep-07 Forecast	United Kingdom	Change from Sep-07 Forecast	Japan	Change from Sep-07 Forecast
Real GDP	*2006A*	3.30%		2.80%		2.50%		2.80%		2.20%	
	2007E	**2.50%**	**N/C**	**2.75%**	**N/C**	**2.75%**	**N/C**	**3.00%**	**0.25**	**2.00%**	**(0.25)**
	2008E	**2.50%**	(0.50)	**2.75%**	(0.25)	**2.50%**	**N/C**	**2.25%**	(0.25)	**2.25%**	(0.25)
CPI	*2006A*	3.20%		2.10%		2.20%		2.60%		0.20%	
	2007E	**2.75%**	**0.50**	**2.25%**	**N/C**	**2.00%**	**N/C**	**2.25%**	**N/C**	**0.00%**	**(0.15)**
	2008E	**2.50%**	**0.25**	**2.00%**	**N/C**	**2.00%**	**N/C**	**1.75%**	(0.25)	**0.40%**	**(0.10)**

TARGETS (RBC Investment Strategy Committee)	Nov-07	Forecast Nov-08	Change from Aug-07 Forecast	1-Year Total Return Estimate (%)
Fixed Income Markets				
U.S. Fed Funds Rate	4.50	4.25	(0.50)	4.70
U.S. 10-Year Bond Yield	3.94	4.75	N/C	(2.0)
Canada 3-Month Yield	3.88	4.25	(0.25)	4.3
Canada 10-Year Bond Yield	3.98	4.50	N/C	0.1
Eurozone 3-Month Yield	3.88	4.00	(0.25)	4.1
Eurozone 10-Year Bond Yield	4.27	4.50	N/C	2.6
United Kingdom 3-Month Yield	5.65	5.25	(0.75)	5.9
United Kingdom 10-Year Yield	4.64	5.00	(0.75)	(3.1)
Japan 3-MonthYield	0.56	0.75	(0.25)	0.8
Japan 10-Year Yield	1.48	2.00	N/C	(2.3)
Currency Markets				
US-CDA	1.00	1.00	(0.04)	0.1
Euro-US	1.46	1.40	0.03	(4.1)
US-Yen	111.23	112.00	N/C	(3.9)
Pound-US	2.06	1.95	(0.05)	(3.7)
Equity Markets				
S&P 500	1481	1650	25	13.4
S&P/TSX Composite	13689	14600	275	9.1
MSCI Europe	2160	2300	100	9.6
FTSE 100	6433	6900	75	11.0
Nikkei	15681	17500	(1725)	12.9

APPENDIX 2: ASSET MIX
ACHIEVING PORTFOLIO RISK OBJECTIVES THROUGH ASSET ALLOCATION

By determining in advance what a portfolio's long-term target mix will be and setting suitable constraints for each asset class, one can tailor important characteristics like capital stability, income, and growth to an investor's individual requirements. Below we have applied this quarter's asset mix recommendations to portfolios constrained in different ways as an illustration.

	SECURE		
Asset Allocation	**Range**	**Target Mix**	**Q1/08**
Cash	0% - 35%	*20%*	**35%**
Fixed Income	65% - 100%	*80%*	**65%**
Equities	0%	*0%*	**0%**

	INCOME		
Asset Allocation	**Range**	**Target Mix**	**Q1/08**
Cash	0% - 35%	*5%*	**20%**
Fixed Income	65% - 95%	*80%*	**65%**
Equities	5% - 25%	*15%*	**15%**

	CONSERVATIVE		
Asset Allocation	**Range**	**Target Mix**	**Q1/08**
Cash	0% - 25%	*5%*	**20%**
Fixed Income	45% - 75%	*60%*	**45%**
Equities	15% - 55%	*35%*	**30%**

	BALANCED		
Asset Allocation	**Range**	**Target Mix**	**Q1/08**
Cash	0% - 20%	*5%*	**20%**
Fixed Income	25% - 55%	*40%*	**25%**
Equities	35% - 75%	*55%*	**55%**

	GROWTH		
Asset Allocation	**Range**	**Target Mix**	**Q1/08**
Cash	0% - 20%	*5%*	**10%**
Fixed Income	5% - 35%	*20%*	**15%**
Equities	55% - 95%	*75%*	**75%**

	AGGRESSIVE GROWTH		
Asset Allocation	**Range**	**Target Mix**	**Q1/08**
Cash	0% - 20%	*5%*	**5%**
Fixed Income	0%	*0%*	**0%**
Equities	80% - 100%	*95%*	**95%**

APPENDIX 3: LADDERED FIXED INCOME PORTFOLIOS

Most investors do not view one-year total-return potential as the prime objective for the fixed income portion of their portfolio. Factors such as increased safety through diversification, predictability of future income and the ability to adapt to a changing interest rate environment are usually of greater concern. Where these factors predominate over short-term appreciation potential, we recommend investors adopt a "laddered" portfolio approach. This approach entails spreading your fixed income capital over a range of maturities *(see "A Four-Step Guide" below)*.

It provides flexibility, stability of income, and does not require the investor to predict the future course of interest rates. The three ladders here illustrate the rates of Canada Government Bonds. In practice, an investor may wish to incorporate other debt instruments—such as GICs, Term Deposits, provincial, municipal and corporate bonds as well as foreign pay bonds—in the construction of a diversified ladder.

SHORT-TERM LADDER	
1 year	3.70%
2 year	3.55%
3 year	3.60%
4 year	3.65%
5 year	3.70%
Average Rate In Year 1	3.64%
Average Term	3 years

MID-TERM LADDER	
1 year	3.70%
3 year	3.60%
5 year	3.70%
7 year	3.80%
9 year	3.90%
11 year	3.95%
Average Rate In Year 1	3.77%
Average Term	6 years

LONG-TERM LADDER	
1 year	3.70%
4 year	3.65%
7 year	3.80%
10 year	3.90%
13 year	4.00%
16 year	4.05%
19 year	4.10%
Average Rate In Year 1	3.89%
Average Term	10 years

A FOUR-STEP GUIDE TO BUILDING THE LADDERED PORTFOLIO

1 Choose an appropriate average term

This should be the length of time over which the income from your portfolio needs to be most predictable.

In our view, most individuals are best served by an average term of between five and eight years.

2 Calculate the longest maturity to be used in the portfolio

Where each portfolio position is to be approximately equal in size and spaced at even intervals, the term of the longest instrument to be included would be roughly twice as long as the average term. For example, an average term of five years would mean the longest instrument would need to be about 10 years.

3 Determine how many steps on the ladder

The more positions used, the shorter the interval can be between each maturity date, and hence the smoother the transition from one interest rate environment to the next. On the other hand, too many positions can make the efficient reinvestment of interest difficult. For most portfolios, we recommend five to seven positions.

4 Formulate a reinvestment rule

To ensure the laddered portfolio retains the same average term over time, as each issue matures the proceeds should be reinvested out at the longest acceptable term, as determined in Step #2 (i.e. at the top of the ladder).

REQUIRED DISCLOSURES

EXPLANATION OF RBC CAPITAL MARKETS RATING SYSTEM

An analyst's "sector" is the universe of companies for which the analyst provides research coverage. Accordingly, the rating assigned to a particular stock represents solely the analyst's view of how that stock will perform over the next 12 months relative to the analyst's sector.

RATINGS:

Top Pick (TP): Represents best in Outperform category; analyst's best ideas; expected to significantly outperform the sector over 12 months; provides best risk-reward ratio; approximately 10% of analyst's recommendations.

Outperform (O): Expected to materially outperform sector average over 12 months.

Sector Perform (SP): Returns expected to be in line with sector average over 12 months.

Underperform (U): Returns expected to be materially below sector average over 12 months.

RISK QUALIFIERS (ANY OF THE FOLLOWING CRITERIA MAY BE PRESENT):

Average Risk (Avg): Volatility and risk expected to be comparable to sector; average revenue and earnings predictability; no significant cash flow/financing concerns over coming 12-24 months; fairly liquid.

Above Average Risk (AA): Volatility and risk expected to be above sector; below average revenue and earnings predictability; may not be suitable for a significant class of individual equity investors; may have negative cash flow; low market cap or float.

Speculative (Spec): Risk consistent with venture capital; low public float; potential balance sheet concerns; risk of being delisted.

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FIGURE 1

DISTRIBUTION OF RATINGS, FIRMWIDE
RBC CAPITAL MARKETS

			Investment Banking Serv./Past 12 Months	
Rating	**Count**	**Percent**	**Count**	**Percent**
Buy (TP/O)	471	43.25	193	40.98
Hold (SP)	538	49.40	159	29.55
Sell (U)	80	7.35	16	20.00

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