

ScotiaMcLeod™* Canadian Core Portfolio

March 2010 - Commentary

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February proved to be a positive month for equity markets, almost completely offsetting the declines experienced in the month of January. Investor sentiment was lifted by positive commentary from Fed Chairman Ben Bernanke and other Fed governors during the period which indicated they expect interest rates will remain low for an extended period, perhaps pushing out any rate increases in the U.S. into the third or fourth quarter of 2010. Generally positive earnings reports for Q4 also provided support for stock prices although there has been a trend toward more cautious management guidance which, if proven accurate, may serve to cap upside potential for equities later this year. That said, we remain optimistic that beyond the earnings rebound which is forecast for 2010, profit growth will continue at a more “normal,” 10%-15% rate in subsequent years, thus providing the necessary catalyst to justify modest total returns for equity investors this year.

Canadian markets were also supported in February by strong commodity prices despite the strength in the U.S. dollar: gold bullion futures crept up 3% to US\$1115/oz., crude oil jumped back up to the US\$80 per barrel level, increasing 9% in the month, while copper futures rallied almost 10%. Overall the CRB Commodity Price Index, a broader measure of industrial and agricultural commodities increased 3.5% for the month. The only major commodity to experience a decline was natural gas futures which fell 7.0% during the month after peaking back in late December. Regarding equity market performance, in Canada the S&PTSX Composite Index increased 5% while the large cap focused, blue chip S&PTSX60 Index did even better by advancing 5.1%. The TSX Small Cap Index lagged slightly while moving higher by only 4.5%. Due to lesser exposure to resource stocks in the U.S. market, the benchmark S&P500 Index climbed only 2.9% while small and medium cap stocks outperformed as illustrated by the small cap S&P 600 Index which increased 4.2% during the month while the mid-cap S&P 400 generated a 5.1% return.

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Fund Performance (CAD\$): (as of February 26, 2010)

1 mth	3mth	6mth	YTD	1yr	3 yr	5yr	Inception**
4.66%	3.01%	7.25%	-0.92%	58.90%	0.20%	1.41%	3.24%

Fund Performance (USD\$): (as of February 26, 2010)

1 mth	3mth	6mth	YTD	1yr	3 yr	5yr	Inception**
5.51%	2.75%	11.44%	-1.73%	90.76%	3.74%	4.52%	7.22%

SPTSX60 Benchmark Performance (CAD\$): (as of February 26, 2010)

1 mth	3mth	6mth	YTD	1yr	3 yr	5yr	Inception**
5.10%	0.68%	5.65%	-1.49%	43.08%	-0.33%	7.53%	10.17%

Portfolio Holdings (as of February 26, 2010)

Name	Symbol	% of Net Assets
Brookfield Asset Management Inc. Cl.A	BAM.A	5.41%
Agrium Inc.	AGU	5.14%
Rogers Communications Cl. B	RCI.B	5.13%
Royal Bank of Canada	RY	5.11%
Barrick Gold Corporation	ABX	5.06%
Bank of Nova Scotia	BNS	5.05%
Talisman Energy	TLM	4.99%
Research In Motion	RIM	4.97%
Great West Lifeco Inc.	GWO	4.95%
Thomson Reuters Corp.	TRI	4.92%
Shoppers Drug Mart Corporation	SC	4.91%
Canadian National Railway Co.	CNR	4.91%
Teck Resources Ltd.	TCK.B	4.91%
TransCanada Corp.	TRP	4.86%
Crescent Point Energy Corp.	CPG	4.81%
Canadian Natural Resources Ltd.	CNQ	4.76%
Nexen Inc.	NXY	4.75%
Manulife Financial Corp	MFC	4.64%
Sun Life Financial Inc.	SLF	4.55%
Suncor Energy Inc.	SU	4.33%
Cash		1.54%

Sector Breakdown (as of February 26, 2010)

	February	January	% Change
Financials	29.71%	34.07%	-4.36%
Energy	28.49%	23.93%	4.56%
Materials	15.10%	16.49%	-1.39%
Telecommunication Services	5.13%	5.26%	-0.13%
Information Technology	4.97%	4.31%	0.66%
Consumer Discretionary	4.92%	5.13%	-0.21%
Industrials	4.91%	4.85%	0.06%
Consumer Staples	4.91%	4.50%	0.41%

Fund Facts

Investment Objective	Long-Term Capital Appreciation
Purchase Status	Open
Fund Codes	Series A: FTC 511 CAD / FTC 512 USD Series F: FTC 515 CAD / FTC 516 USD
RRSP/TFSA Eligible	Yes
**Inception Date	October 1, 2003

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Not all the news was positive as mixed messages were delivered via U.S. and overseas financial authorities, along with the regular parade of monthly economic data. Although China has demonstrated strong economic growth, efforts by the Chinese central bank to curb lending have made investors question the sustainability of their economic growth, which in turn has implications for the global economic outlook. At the same time markets were volatile as they responded to the daily machinations surrounding concerns over sovereign debt in the Euro region. Near the end of the month, the S&P/Case-Shiller Home Price Index was released, down 3.1% year over year in December illustrating the ongoing weakness in the U.S. housing market; although still negative, this is the lowest rate of decline since May 2007, but still suggests consumer confidence is likely to remain compromised for some time to come. Latterly, investors were encouraged by the potential for resolution of the current debt crisis in Greece and the broader Euro zone. That resolution however will have consequences and will likely slow the pace of economic recovery in that region. At the same time however, Q4 U.S. GDP was revised upward to 5.9% from 5.7%; although not sustainable, U.S. economic growth is expected to remain strong through the first half of 2010 and then drop off somewhat in the second half.

Even though equity markets posted positive returns in February there was a certain amount of volatility in response to global news events, particularly earlier in the month. This is a pattern we expect to see repeated on a fairly regular basis this year as investors enter the market to pick up bargains whenever stocks stage a modest pullback. There have been four or five occasions since the market hit its low point last March, when stocks have sold off over several days, only to recover with renewed buying power, establishing an upward trend of higher lows and higher highs. Despite forecasts by some analysts for a market correction, so far there has not been as much as a 10% sell off in the broad market as in each instance of a decline, pent-up buying demand re-enters the market to increase equity exposure.

PERFORMANCE

All ten sub-groups of the TSX Composite Index increased during the month of February with market leadership coming from Information Technology, (largely a big move in the shares of **Research In Motion (RIM)** shares), Materials, and Financials; in contrast, defensive sectors were relative underperformers. Only three holdings in the portfolio experienced share price declines during February as lifeco holdings **Manulife Financial** and **Sun Life Financial** sold off as investors appeared to be switching out of insurance companies and into bank stocks. The largest decliner was **Suncor Energy** which dropped after the company released year-end financial results that were below expectations in terms of

profitability despite meeting production forecasts. Operating costs were temporarily higher during the first full quarter that includes the integration of **Petro Canada** and guidance was somewhat disappointing relative to consensus estimates

Bank stocks performed well during February but the best performing holding was **Brookfield Asset Management (BAM)** whose shares rallied in sympathy with one of its operating subsidiaries, 50% owned **Brookfield Properties (BPO)**, which got a boost from speculation surrounding the ultimate announcement of a restructuring initiative intended to surface value in the company. **BAM's** holding in **BPO** represents approximately 25% of the company's Net Asset Value. **RIM** shares rallied in response to an upgrade by a U.S. based analyst as well as being swept up in the general momentum witnessed in the U.S. technology sector. Other significant movers during the period were found within the resource sector as **Talisman Energy** shares rallied with the move in oil prices and **Teck Resources** responded to the rally in copper prices and an improving pricing outlook for metallurgical coal.

CHANGES

Early in February we made a switch in this portfolio, eliminating the holding in **AGF Management** and adding a position in **Crescent Point Energy Corp.** From a macro, longer term secular perspective we have become increasingly concerned about **AGF** and other mutual fund managers in the context of a shift in investor sentiment away from mutual funds and toward ETFs as an efficient method to get broad exposure to investments in certain asset classes, regions, and sectors. At the same time, **AGF** specifically has been falling behind in the competitive battle for fund assets and in fact the company has consistently suffered net redemptions from their mutual funds for some time, resulting in slow growth in Mutual Fund Assets Under Management, growth that has recently only come as a result of market performance, not new fund sales. On January 22, 2010 Scotia Capital analyst Kevin Choquette downgraded **AGF Management** from 1-Sector Outperform to 2-Sector Perform citing additional concerns including executive management and portfolio management changes at the firm and the impact of recent Canadian dollar strength on their Global Equities mutual funds.

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