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Securities Industry Performance

Business and Profitability Trends
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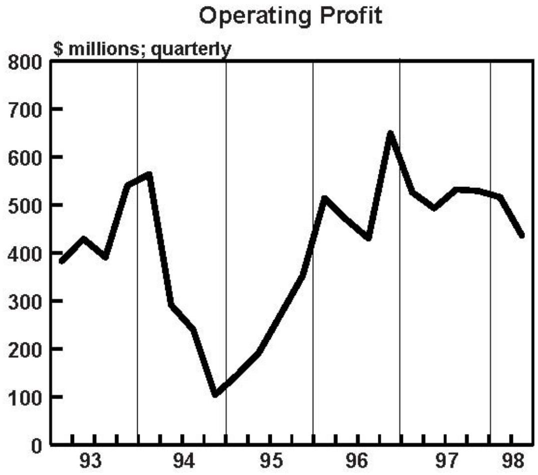
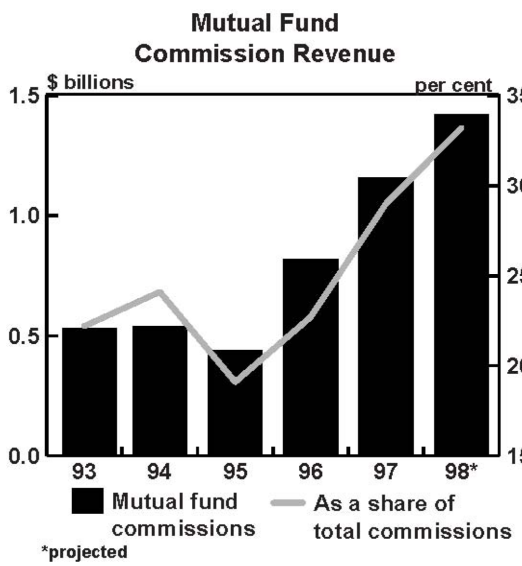
Industry performance slipped in the second quarter of this year in the wake of a sharp break in the upward trend of debt and equity markets and ensuing volatility in market prices. After peaking in April, domestic stock prices broke decisively lower in mid-June, and have been in a downward trend ever since. Similarly, in late May and early June mid and long-term Canada bond prices moved lower.

Industry operating profit fell 15% to $436 million in April - June, following a modest decline in the preceding quarter. For the first six months of this year, operating profit totaled $952 million, down 6% year-over-year. Given that market weakness has persisted through late August (at time of writing), operating margins will be squeezed even further in the third quarter- - particularly in the brokerage and underwriting businesses which account for the majority of industry revenues. Also, preliminary re-sults from proprietary and client trading in July and August suggest a deterioration in performance in response to stepped up volatility in domestic and global markets.

Poor results across all business lines in the second quarter - - brokerage, underwriting and principle trading - - contributed to the decline in operating profit. Despite this pervasive weakness, second quarter profits are still three times higher than the quarterly low in the 1993 — 97 bull market.



Commission revenues totaled $1 billion in the second quarter, down 8% from the previous quarter as choppy markets and related uncertainty caused retail and institutional investors to pull back from the marketplace. For example, average daily trading volume on the TSE in May — June this year was 10% below trading levels in the preceding four months. Commissions earned from mutual fund sales, however, did not mirror the decline in com-missions on listed equities as investors adjusted their portfolios of managed funds in response to increased uncertainty about equity markets. Mu-tual fund commissions as share of total commis-sions moved higher, accounting for 34% of overall commissions. Over the past three years, the distribution of mutual funds has accounted for an increasing share of the retail brokerage business - -mutual fund commissions earned in the securities industry represent nearly 60% of retail commissions on listed equities.

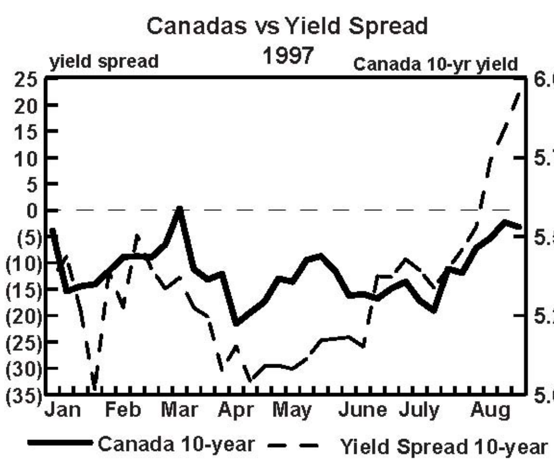


Earnings from underwriting and corporate advisory fees fell sharply for the second consecutive quar-ter. Revenues were down 10% in April — June, fol-lowing a 27% decline in the preceding three-month period. The collapse in common equity financings in the first half, down 30% from the second half of last year, in fact preceded the fall in equity mar-kets, due to increased uncertainty among issuers about the direction of share prices. The pace of corporate debt financing, which held up reasonably well in the first half of this year, fell away in July and then collapsed in August.

Institutional firms, notably domestic firms with a significant presence in domestic equity markets, were particularly hard hit. First-half results of the corporate finance operations of these firms were down 30% year-over-year and net profits off 47%. The integrated firms posted better results in the second quarter as merger and acquisition fees con-tinued as a strong earning source and shored-up the weakness in underwriting results.

The sudden downward move in equity and bond prices in May - June and concomitant volatility in market prices created treacherous conditions for market-makers. Revenues from principal equity trading were down 72% in the second quarter and down 10% in the first half of the year. Total earn-ings from institutional commissions and principal dealings to facilitate client trades (not adjusted for overhead) totaled $750 million in the first half this year, accounting for roughly 15% of total revenues.

Fixed income operations fared poorly in the sec-ond quarter this year as a sharp rise in bond yields and widening in spreads - - notably in early June - -caught market-makers by surprise and resulted in trading losses. For example, the yield on the ten-year Canada benchmark issue rose about 30 basis points through June - August. The spreads between corporate and Canada bonds, and between Canada bonds and US Treasury bonds, widened sharply through June - August this year.



Gross fixed income trading profits fell 7% in the second quarter and 9% year-over-year in the first half of 1998. The retail transactional flow in fixed income securities compensated integrated firms for losses from proprietary and institutional client trad-ing. Foreign affiliate firms without the benefit of retail business recorded much poorer trading results in the first half this year - - with revenues down 35% year-over-year.

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