
Top Funds Report

Monthly Commentary

Investor sentiment improving, but still has a long way to go. Diversified portfolio is critical.

Since 2007, global equity markets have been on a wild ride. In 2008, the global credit crisis rocked the financial world with many global markets dropping 30%, 40% or more in a matter of months. Since early 2009, markets have begun to climb back, only to be hit with more uncertainty, thanks largely to the debt crisis that is now raging in Europe.

It's no wonder that investors have been scared and reluctant to step back into the markets. Despite the turmoil, there are signs that investor confidence is returning. Between February 1st and 3rd, a survey was conducted by Angus Reid to gain an insight into the current attitudes of investors.

The survey, sponsored by Franklin Templeton Investments found that 40% of investors describe themselves as "opportunistic, risk taking or analytical, the three categories that typically suggest buying behavior." This was up from 37% from a similar study that was done in July 2011.

The survey also showed that while some are looking to jump back into the markets in today's volatile environment, most investors remain cautious. Of the conservative investors, 15% consider themselves to be "timid", while 27% are "suspicious" about the markets. An encouraging sign is that the number of investors who are "not sure" about the investment climate is shrinking, with only 17% unsure about the markets compared to 30% back in July.

When asked about what actions investors intend to take, it was evenly split between sticking to their current plan and not making any further investments.

The biggest fear among those surveyed was that they would outlive their retirement savings, while only 10% of those surveyed cited market volatility as their biggest concern.

At its core, the fear of running out of money suggests that investors need to find a way to overcome their immediate concern regarding the state of the markets and get their money working for them. The best way to do that is to devise a financial plan that will focus on growing savings.

With the low interest rates being paid on savings accounts and GICs, a well diversified portfolio consisting of stocks, bonds and cash is the best way to grow savings over the long term. The key is to have a portfolio mix that is in line with risk tolerance. In other words, you want to have a portfolio that will allow you to grow your savings while still being able to sleep at night.

The key to doing this is not looking at each individual investment on its own, but rather as part of the overall portfolio. When a portfolio is properly constructed, there will always be some investments that are performing better than others, while some investments may be performing poorly. For example, when stocks are performing well, bonds tend to perform poorly while when bonds are performing well, stocks tend to lag. In the context of a portfolio, this is what you want to see happen. It shows that you have constructed your portfolio properly and you have a good mix of investments in the portfolio.

This type of portfolio will also result in less fluctuation on a month to month basis, which will make it easier for you to stick with the plan. For ideas on a portfolio that may be right for you, I would encourage you to check out the portfolios in our Mutual Funds/ETFs Update newsletter or through the Paterson & Associates Research package.

**Please send your comments to
feedback@paterson-associates.ca.**

Funds You Asked For

Readers ask about Tradex Global Equity, RBC O'Shaughnessy U.S. Value and more!

Tradex Global Equity Fund - The Tradex Global Equity Fund is only available to current and former public service employees and their families.

This global equity fund is managed by Barry Olliff of the City of London Investment Plc. Mr. Olliff conducts a top down review of the various global markets to determine which have the best potential rate of return. Once this is established, he gains that investment exposure through a mix of closed end funds and exchange traded funds.

When reviewing closed end funds, Mr. Olliff seeks out those that are trading at a discount to the net asset value (NAV), which has the potential for additional return if the gap between the trading price and the NAV narrows.

The manager has a go anywhere mandate and may invest up to 20% in emerging markets and may also invest up to 25% of the fund in individual Canadian stocks. Country exposure is capped at 35% of the fund, except for the U.S, where exposure can be higher.

As of December 31, the fund was invested 44% in the U.S., 25% in developed Europe and 14% in developed Asia. The Fund has 12% invested in the emerging markets.

Despite posting a five year loss of 5.37%, the performance of the fund has been decent on a relative basis. More often than not, this fund has outpaced the majority of its peer group. The Fund has been more volatile than both the index and its category average.

The MER of the fund is 2.76%, which is high when compared to other global equity funds.

All in, this isn't a bad offering for public service employees. Considering the fund's exposure to Europe and the emerging markets, we expect that the volatility of the fund will remain high for the near term. For those looking to reduce volatility, we would suggest **Ivy Foreign Equity**, **Renaissance Global Markets** or the **Mutual Discovery Fund**.

Templeton Global Smaller Companies Fund -

In March 2011, Brad Radin, long time manager of the Templeton Global Smaller Companies Fund, left the company. He was replaced by Martin Cobb, who has been with Templeton since 2003 and has been in the industry for the past 18 years.

Under Mr. Cobb's leadership there has been no major change in the way the investment team operates. They are still following the same disciplined, multi step, value focused process and they are still selecting names from the same database of buy candidates. At Templeton, while it is the lead managers who are ultimately responsible for the names in the fund, they are supported by a dedicated team of analysts, as well as the entire 36 member Templeton Investment Management team. On the Global Smaller Companies Fund, there are seven dedicated analysts involved, including the funds back up PM, Harlan Hodes.

Despite this consistency in process, the fund had a very rough 2011. The fund was down 23% during the year, well below the MSCI World Index and its peer group. Some of the underperformance to the benchmark is attributable to the fact that in 2011 many investors eschewed small and mid cap stocks in favour of the higher quality large cap names. But the underperformance relative to the benchmark is due to calls made by the manager.

These calls include the fund's underweight exposure to the U.S. (currently at 18% of the fund), which was by far the best performing market in the fourth quarter, the fund's relatively high exposure to the emerging markets, and the fund's exposure to U.S. and Asian financial stocks.

The manager continues to take advantage of the lowered valuations in small cap names to improve the quality of the portfolio. He has also been able to add some select mid cap names that were previously unavailable to it.

Despite that, we expect that 2012 will be a tough year for small cap stocks and for this fund. Looking out medium to long term, we expect that investors will be rewarded.

TD Canadian Bond Index Fund - For cost conscious investors seeking exposure to the Canadian bond market, this mutual fund is a good choice. The fund is designed to track the DEX Universe Bond Index, after fees.

Like the index, the fund is approximately 57% invested in Government of Canada bonds and 42% in investment grade corporate bonds.

Given the lower fees charged by this fund, it is not surprising that it has consistently been in the first or second quartile in virtually every time period, except for 2009, when it was in the third quartile. The fund pays a variable monthly distribution which has ranged between \$0.02 and \$0.04 per unit. At current prices, the annualized distribution yield on the Investor series units is approximately 3.1%

The fund is available in a traditional Investor series, which carries an MER of 0.83%, or it can be bought directly online from TD with a low MER of 0.51% (e-units).

Despite the strong relative performance and distribution yield, we would favour the **PH&N**

Bond, PH&N Total Return Bond or the **TD Canadian Bond** over this fund given their more active management styles.

RBC O'Shaughnessy U.S. Value Fund - Manager Jim O'Shaughnessy uses a very quantitatively driven approach to stock selection. He has poured over decades of historical stock data to determine the factors which have, at least on a historic level, delivered excess returns to investors. He outlined his findings in his book *What works on Wall Street*. The key factors that are considered by the model include sufficient trading size, trading volume, growing sales and cash flows. Another metric is what O'Shaughnessy calls "shareholder yield" which is a combination of dividend payouts and stock repurchase programs.

The long term results of this fund have been strong on a relative basis however it should be noted that the fund does hedge all of its currency exposure, which will boost returns in periods of an appreciating Canadian dollar and hurt returns when the dollar falls.

Despite using a value screen in its stock selection process, the volatility of this fund is considerably higher than one would experience with a traditional value fund. On a month to month basis the volatility of this fund has been nearly double the volatility of the S&P 500 Index. The fund has also experienced periods of significant drops. Between June 2007 and February 2009 the fund lost a mind blowing 61.8%.

The costs of this fund are reasonable, with an MER of 1.54%.

Investors who have a relatively short time horizon should avoid this fund because of its higher volatility. However, for those looking for long term capital growth within the U.S. market, this may be a fund to consider.

AGF Canadian Small Cap Fund - After a very strong 2009 and 2010, small cap stocks struggled through 2011, giving back some of the gains of the previous two years. The AGF Canadian Small Cap Fund was no exception, losing 14.7%, for the year, which was slightly worse than the BMO Small Cap Index.

The Fund has been managed by Caterina Prato since April 2008. Ms. Prato uses a bottom up, growth focused process. She takes a very patient approach and typically sets an expected holding period on each stock of between three and five years. The portfolio tends to be fairly well diversified, holding around 100 individual names with the top ten making up 35% of the fund.

Performance has been middle of the pack in all time frames. The Fund has lagged the benchmark and the peer group in virtually all time periods. The volatility of the fund is in line with the category average, but is higher than the broader S&P/TSX Composite Index.

The Fund has an MER of 2.81%, which is higher than the category average. This high MER has the potential to drag the overall performance of the fund in sideways and volatile markets.

Looking forward, we would expect that the performance of this fund will remain in the middle of the pack. We have not seen anything which causes us to believe that performance will dramatically improve anytime soon.

Mutual Discovery Fund - Since taking over the reins of this go anywhere global equity fund two years ago, Philippe Brugere-Trelat and Peter Langerman have continued to deliver strong risk adjusted returns for investors. The team uses a bottom up, value focused security selection process which looks to identify companies that are trading at a discount of between 25% and 30% below their estimate of the company's true worth. Not only

must the companies be trading at a discount, there must also be a near term catalyst which will help to close the valuation gap, bringing gains to investors.

In addition to the traditional value focused stock selection approach, the fund can also invest up to 10% of the portfolio in more opportunistic strategies including covered call writing, merger arbitrage opportunities and distressed debt.

The team places a strong emphasis on managing risk within the portfolio. This is done by analyzing the potential downside for any stock in the portfolio. Further, the portfolio tends to be fairly well diversified, holding more than 100 names, with the top 10 making up less than 30% of the fund.

There is evidence that this focus on risk works. The volatility of this fund is among the lowest in the category. Since the fund was launched in Canada in 2003, the worst peak to trough loss has been 32%. In comparison, the MSCI World Index experienced a peak to trough decline of 43% during the same time period. While 2011 was the fund's worst year since its Canadian launch, posting a 3.4% loss, it managed to outpace its peer group, finishing in the first quartile.

As of November 30, the fund was nearly fully invested, holding 3% in cash, 91% in equities, 5% in bonds and just under 2% in preferreds. Geographically, the fund is 48% in the U.S., followed by 15% in the UK. Direct exposure to the troubled Eurozone is approximately 24%.

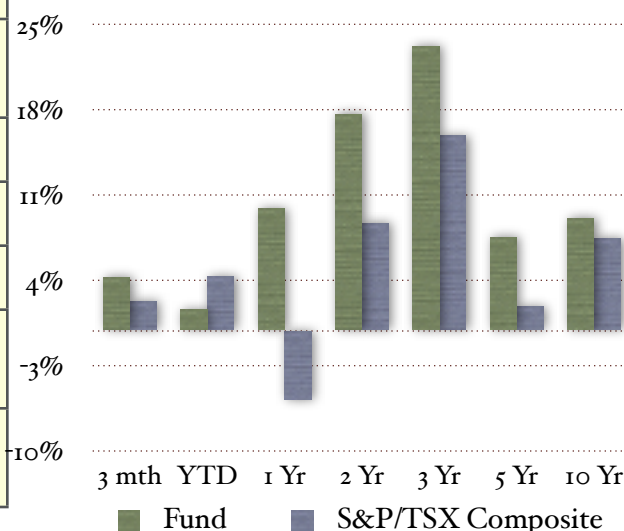
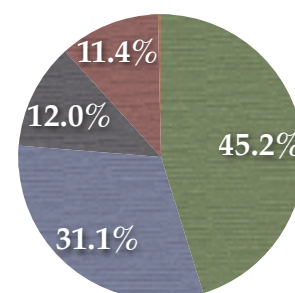
The fund runs a bit on the pricey side, with an MER of 2.77%. In comparison, the category average is approximately 2.59%. Another thing investors should be aware of is that the fund is not for those who wish to follow a socially responsible investing approach, given its high weightings in tobacco companies.

Fidelity Canadian Large Cap Fund

Asset Mix

Fund Company	Fidelity Investments Canada
Fund Type	Canadian Focused Equity
Rating	\$\$\$\$
Style	Value
Risk Level	Medium
Load Status	Optional
RRSP/RRIF Suitability	Good
TFSA Suitability	Good
Manager	Daniel Dupont since May 2011
MER	1.18%
Fund Code	FID 231 - Front End Units FID 531 - DSC Units
Minimum Investment	\$500

- Cdn Equity
- US Equity
- Cash
- Int'l Equity
- Other



ANALYSIS:

Since taking over the management duties of this fund, Daniel Dupont has not skipped a beat. If anything, the relative risk reward profile appears to have improved, with relative volatility dropping while relative return increased. Obviously seven months is too short a period on which to judge, but the signs are definitely encouraging.

Mr. Dupont uses a fundamentally driven, value focused approach, looking for stocks that are trading at a significant discount to his estimate of intrinsic value. The portfolio has also become more concentrated, now holding anywhere between 20 and 50 names, down from 70 or more under the previous manager. As of December 31, the fund held 40 names with the top 10 holdings making up 43% of the fund.

The manager has the option to invest up to 49% of the fund in non Canadian securities. He is taking advantage of that with more than 40% of the fund invested in foreign equities. Given the fund's value bent, it

is not surprising to see that financials make up 24% of the

fund, followed by consumer discretionary stocks which make up 15% of the fund.

Performance has been strong, with strong relative and absolute numbers for the past five year period. The volatility of the fund is slightly lower than the S&P/TSX Composite Index and is in line with the category average.

The costs are reasonable, with the front end version boasting an MER of 2.28%, which is 20 basis points lower than the category median. The fund can also be bought in a corporate class structure which will help minimize the potential tax impact of any large distributions for investors in non registered accounts.

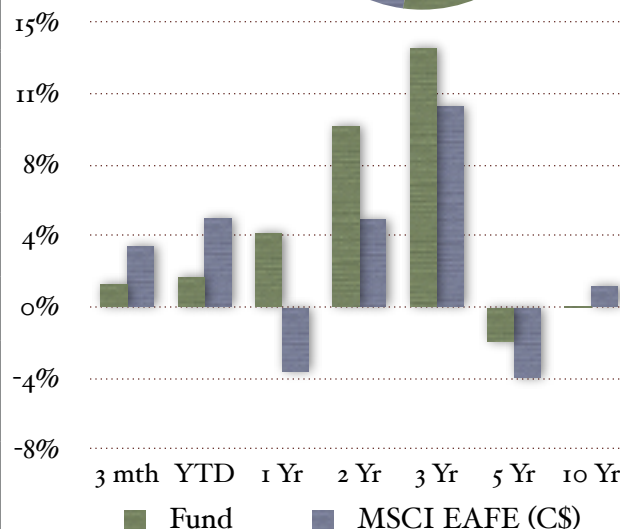
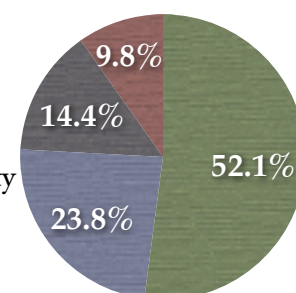
This fund has been and continues to be a staple on our Recommended List of Funds. In our opinion, it is a great core holding for investors looking for Canadian focused equity exposure for their portfolios.

Renaissance Global Markets Fund

Asset Mix

Fund Company	CIBC Asset Management
Fund Type	Global Equity
Rating	\$\$\$\$
Style	Value
Risk Level	Medium
Load Status	Optional
RRSP/RRIF Suitability	Good
TFSA Suitability	Good
Manager	David Winters since October 2006
MER	2.74%
Fund Code	ATL 1029 - Front End Units ATL 1873 - DSC Units
Minimum Investment	\$500

- Int'l Equity
- U.S. Equity
- Cash
- Canadian Equity



ANALYSIS:

Since taking over this fund in 2006, David Winters has done a good job for investors in this go anywhere global equity fund. Over the past five years, the fund has outpaced the benchmark and peer group, and has done so with a level of volatility that is significantly lower than the category average.

Mr. Winters uses a value tilted approach, looking for strong businesses which offer an identified competitive advantage and a strong management that are trading at a discount to its intrinsic value. The manager takes a long term, patient view when evaluating a stock. This is reflected in the fund's portfolio turnover, which is approximately 30%.

The portfolio tends to be fairly concentrated, holding less than 40 names with the top 10 making up more than two-thirds of the assets. It is benchmark agnostic, so the manager is able to take significant sector bets when the risk reward trade-off warrants it. Cash is a by-product of the manager's stock selection process. As of October 31, cash was approximately 13% of the fund.

Geographically, the fund is invested heavily in the U.S. and Canada, which combined make up just less than half of the portfolio. While avoiding direct exposure to the troubled euro zone, the fund has a 19% weighting in Switzerland and 14% in the UK.

The fund is pricey. The most recent MER is 2.74%, which is higher than the category average. Another concern stems from the concentration. Concentration can be a double edged sword, helping to amplify gains, but it can also amplify losses as stock specific risk increases in a more concentrated portfolio. The largest holding makes up nearly 10% of the fund.

The fund is heavily invested in tobacco stocks. The investment rationale is that the tobacco companies generate significant cash flow to investors. However, those following an ethical screen in their portfolios will want to avoid this fund.

Another risk is key person risk, as most of the heavy lifting is done by David Winters. Were he unable to continue managing the fund, investors would be significantly affected.

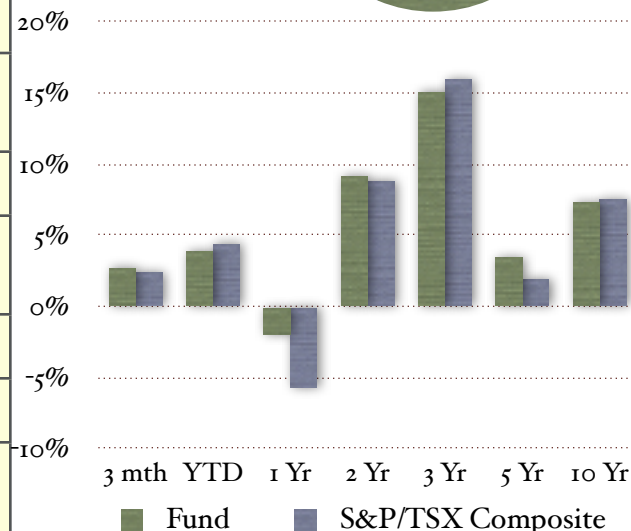
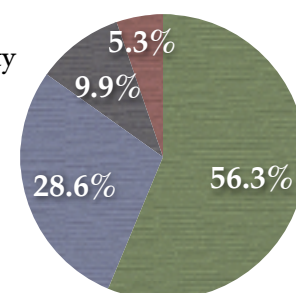
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RBC North American Value Fund

Asset Mix

Fund Company	RBC Global Asset Management
Fund Type	Canadian Focused Equity
Rating	\$\$\$\$
Style	Value / Growth Blend
Risk Level	Medium
Load Status	No Load
RRSP/RRIF Suitability	Good
TFSA Suitability	Good
Manager	Stu Kedwell since December 2004 Doug Raymond since Dec, 2004
MER	2.09%
Fund Code	RBF 554 - No Load Units
Minimum Investment	\$500

- Canadian Equity
- U.S. Equity
- Cash
- Other



ANALYSIS:

In managing the fund, the team of Stuart Kedwell and Doug Raymond use a multi stage portfolio construction process that incorporates both quantitative top down screening and fundamental, bottom up analysis.

The first stage in their process is a series of quantitative screens which weed out the undesirable companies in their selection universe. Then the team conducts fundamental analysis on each of the companies, including a series of scenario analysis, looking at a wide range of possible outcomes for each stock. Stocks are analyzed using a 2 Factor Matrix Model which evaluates earnings projections relative to valuation. They are looking for companies that are attractively valued, fundamentally sound, and offer above average returns on capital.

The fund can invest up to 49% in non Canadian stocks. They look at both Canadian and U.S. stocks, with the country allocation being a by-product of the stock selection process. The fund's cash position will be determined by two main factors: the availability of quality opportunities and

the team's macro call on the markets. As a policy, half of the fund's foreign currency exposure is hedged.

The portfolio tends to be fairly well diversified holding more than 100 names, with the top 10 making up 32% of the fund. The managers tend to be active, with high levels of portfolio turnover.

The fund has performed very well of late, outpacing the S&P/TSX Composite and its peer group, posting solid first quartile performance. Volatility has also trended lower than both the broader market and the Canadian equity category average.

In recent months, the managers have been increasing their exposure to the U.S. market. As of December 31, the fund was 51% in Canadian equities, 38% in U.S. equities and 9% in cash. From a sector perspective, the fund is 34% invested in financials, 16% in energy with 10% each in consumer discretionary and materials.

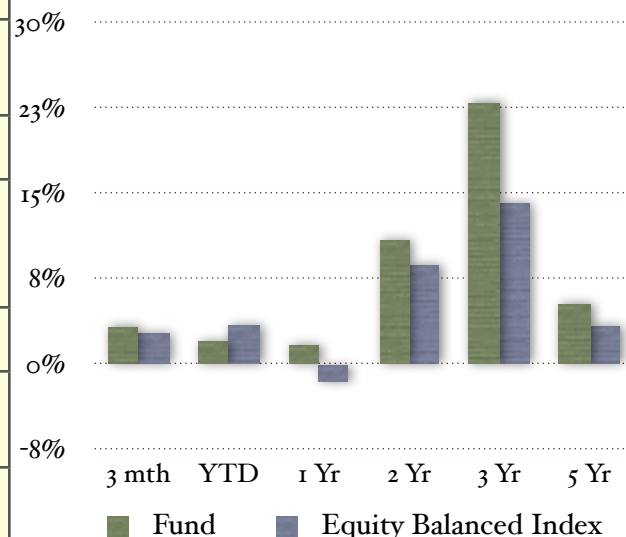
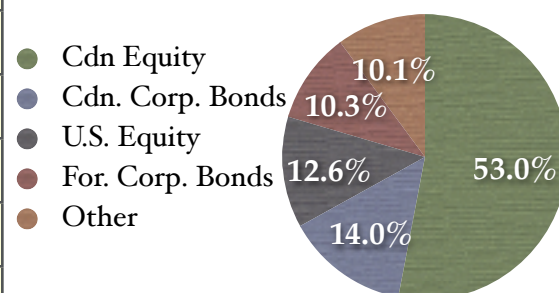
We like the fund because the management team and investment process, the volatility profile of the fund, and the fact that the fund is still small enough at \$424 million to allow the team to effectively manage the fund.

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AGF Monthly High Income Fund

Fund Company	AGF Investments Inc.
Fund Type	Canadian Equity Balanced
Rating	\$\$\$
Style	Blend
Risk Level	Medium
Load Status	Optional
RRSP/RRIF Suitability	Good
TFSA Suitability	Good
Manager	Peter Frost since April 2010 Tristan Sones since April 2006 Tom Nakamura since April 2006
MER	2.42%
Fund Code	AGF 766 - Front End Units AGF 6898 - DSC Units
Minimum Investment	\$500

Asset Mix



ANALYSIS:

Peter Frost took over the lead manager duties in April of 2010. Mr. Frost is responsible for setting the tactical asset allocation mix of the fund and managing the equity portion of the fund. Tristan Sones and Tom Nakamura are responsible for the fixed income portion.

The fund has a neutral weighting of 50% equities and 50% fixed income. The manager has a very flexible mandate and will set the asset mix based on the relative income opportunities and the risk/reward characteristics of each asset class. Equities are permitted to range between 20% and 80% of the fund's assets.

Peter Frost employs a bottom up approach that uses both qualitative and quantitative factors to identify companies that have shown sustainable dividends, strong balance sheets, stable earnings and cash flows and a strong management team.

On the fixed income side of the fund, the managers use a top down approach to determine the appropriate

duration strategy. The team looks for bonds that provide an attractive yield relative to the risk. The fund has the ability to invest in non investment grade credits.

Performance has been strong, handily outpacing its peer group with first quartile performance in all time frames, except for 2008 when the fund dramatically underperformed. The volatility is on par with an equity fund. While it is considered a balanced fund, investors should think of this more as a hybrid equity fund, given the risk characteristics.

The fund pays out a variable distribution, averaging 6.2 cents per unit, which at current prices is an approximate yield of 7% per year.

Costs, like most of the funds offered by AGF, are on the high side. The fund has an MER of 2.41%, which is in the upper half of the equity balanced category.

For investors who are comfortable accepting a higher level of volatility risk, while looking for a mix of income and capital gains, this is a fund that should be considered.