
Top Funds Report

Global Markets Rally Sharply Higher

Weakness in gold and materials continues to weigh on Canadian equities

Global equities continued their impressive streak of gains while Canadian equities were lower thanks to continuing weakness in the materials and energy sectors. The S&P/TSX Composite Index shed 2.07%, while the S&P 500 gained 0.95% in Canadian dollar terms. The star of the month was the MSCI EAFE Index gaining 4.43%, besting all other major indices. Regionally, both Europe and the Pacific Rim were sharply higher, gaining 3.7% and 5.9% respectively.

In Europe, news of a bailout agreement in Cyprus and the continuation of accommodative central bank policies were positively received by investors. Japan looks near unstoppable, with the Nikkei 225 index soaring by more than 33% since the start of the year. If we take the effect of a weakening Yen into account, the gain is lower, but still impressive at approximately 20% in Canadian dollar terms.

While the falling Yen has fueled most of the rally, there are a number of other factors contributing. These include a series of bold policy initiatives that contain significant monetary easing, fiscal stimulus and economic reform. Combined, these are expected to help provide some level of support to the nations flailing economy.

Many now believe that the valuation gap between Japanese and other developed market equities has now closed, and any further gains will be driven by improving company fundamentals. It is likely that recent momentum will carry the market higher in the short term, which will be followed by a pullback.

Canadian equities continued to struggle because of continued weakness in the materials sector, which fell by 13.5% in April. The price of gold continued its freefall, dropping another 9%, bringing the price of gold companies with it.

There are many who believe that the long term outlook for gold remains strong. This is because gold has historically been a great inflation hedge and the massive amounts of liquidity that central banks have pumped into the global economy are expected to fuel future inflation. While this may be the case, the shorter term outlook is considerably less positive.

Many central banks have begun to talk about unwinding their massive quantitative easing programs much sooner than many had predicted. The sooner this happens, the more the future inflationary pressures will be reduced, lowering demand for gold.

Many heavily indebted European countries are rumored to be selling some of their gold reserves into the markets to raise funds to help reduce their debt. Combined, the PIIGS nations of Portugal, Ireland, Italy, Greece and Spain own a combined 3,200 tons of gold. Should some of this hit the market, it will throw the delicate supply and demand equation out of balance, putting further pressure on the price of gold.

Yet another headwind comes from the continued strength in the U.S. dollar. Gold has historically shown near perfect negative correlation with the U.S. dollar. It has been strong of late, and many expect that until China and Europe show signs of a sustained recovery, it will continue to be strong, putting further pressure on the price of gold.

Regardless of the direction, we expect to see more volatility in the short term in the materials sector. Because of the high weighting in the broader index, volatility will likely remain elevated for many Canadian equity funds, particularly those which closely track the S&P/TSX Composite Index.

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

Funds You Asked For

This month, we take a look at offerings from CIBC, BMO, Franklin Templeton and more...

Renaissance Global Markets Fund (ATL 1029)

Despite dramatically underperforming the MSCI World Index in 2012, this go anywhere global equity fund can be a great core holding for most investors. Much of the underperformance can be traced to the fund's underweight exposure in banks, technology, telecom and healthcare. It was these sectors that led the way higher in 2012 and so far in 2013. Still, David Winters believes that the best long term opportunities are outside of these sectors.

Remaining true to his style, Mr. Winters uses a value tilted approach, looking for strong businesses which offer an identified competitive advantage and strong management teams that are trading at a discount to its intrinsic value. The investment process is very much a bottom up approach and he generally takes a long term, patient view when evaluating a stock. This is reflected in the fund's low level of portfolio turnover, which is approximately 30% per year.

The portfolio tends to be fairly concentrated, holding less than 40 names with the top ten making up roughly half the fund. It is benchmark agnostic, allowing the manager to be able to take significant sector bets when the risk reward tradeoff warrants it. Cash is a byproduct of the stock selection process. As of January 31, cash was approximately 13% of the fund, down from recent months as some high quality, out of favour opportunities have emerged. The recent rally has made finding opportunities more challenging, but he believes that they are available off the beaten track.

Geographically, the has significant exposure in the U.S. and Canada, which combined make up half the fund. While avoiding direct exposure to the troubled euro zone, the fund has a 21% weighting in Switzerland and 9% in the UK.

The most recent MER for the fund is 2.68%, which while down from a year ago, is still higher than the category average. Another concern we have with this fund stems from the concentration. This can be a double edged sword, helping to amplify gains, but can also amplify losses as stock specific risk increases in a more concentrated portfolio. The largest holding makes up nearly 10% of the fund.

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

Another risk of the fund is key person risk, as most of the heavy lifting is done by David Winters. Were something to happen to him, investors would be affected significantly.

BMO Diversified Income Portfolio (GGF 70149)

This Canadian balanced fund is designed to provide investors with a fixed monthly distribution and invests in a diversified portfolio of Canadian and international bonds and equities. Currently, it is tilted towards equities, holding just 26% in bonds and 5% in cash, with the balance invested in equities. Canadian equities are 31% of the fund, with the balance invested abroad.

Within the Canadian equity component, it is conservatively positioned. The managers are focusing on high quality companies with a history of growing their dividends. They remain biased towards the traditional

defensive, yield generating sectors such as financials, telecom, and utilities. They are less exposed to the more volatile materials and energy sectors. The fixed income sleeve of the fund is biased towards corporate bonds for their higher yield when compared to government bonds. There is also exposure to infrastructure and high yield through the **BMO Global Infrastructure Fund** and the **BMO U.S. High Yield Bond Fund**, which combined, make up more than 20% of the fund.

With its focus on generating cash flow, the fund has historically paid out a very high distribution. Until recently, it paid \$0.045 per unit, which worked out to an annualized yield of 8.5%. Given the total return profile of the fund, this was clearly unsustainable without eating into investor's capital. BMO realized this and cut the distribution dramatically, bringing it down to a more manageable \$0.025 per month, which is equal to an annualized yield of approximately 4.6%.

Shorter term performance has been strong, gaining 10.4% in the past twelve months. During the same period, its balanced benchmark rose by 4.4%. Volatility is higher than the category average and given the fund's overweight exposure to equities, we expect that trend to continue. We also expect that performance should continue to improve given the higher equity exposure and the 10% weighting in infrastructure.

Cost is a touch on the high side, with an MER of 2.25%.

Despite the improved performance of this fund, we would be reluctant to recommend it at this moment. It is our opinion that there are stronger Canadian balanced funds available.

Templeton International Stock Fund (TML 735)

Investing in companies located outside of North America, the Templeton International Stock Fund relies very heavily on the 26 member Templeton global equity team. Using a disciplined, bottom up value driven approach, they look for companies that have strong fundamentals, yet are trading below their true value.

The portfolio is quite diversified, holding approximately 60 names. The top ten make up about a quarter of the fund. From a country standpoint, again, it is quite diversified, with the largest weighting, 17%, being in the UK, followed by Switzerland and Japan with 11% and 10% respectively. It is heavily tilted towards financials and industrials, which combined represent 40% of the assets.

The managers use a very patient approach, with a long term time horizon. When considering a potential investment, they are looking out over the course of a business cycle. As a result, portfolio turnover has been in the low double digits for the past five years, and was only 4.6% in 2012.

While the process is sound, unfortunately the results have been largely disappointing. For the year ending April 30, it gained 14.5%, underperforming the 22.2% jump in the MSCI EAFE Index. Longer term, the results have been more encouraging, outpacing most of the peer group, but still lagging the index.

Part of the reason it has consistently underperformed can be attributed to the 2.61% MER, which is above the category average. Combine that with volatility that has tended to be higher than average and it becomes very difficult to recommend this fund to investors. It is our opinion that there are definitely better international equity fund choices available.

TD International Index Fund (TDB 964)

Those looking for a low cost alternative to the Templeton International Stock fund may want to take a look at this index offering from TD. As the name suggests, it is designed to replicate, after fees, the performance of the MSCI EAFE Index. It has no exposure to Canadian or U.S. based companies.

With this version of the fund, its currency exposure is not hedged. For those who do wish to hedge this risk, there is a hedged version available.

Our biggest beef with this fund was that its costs were high for an index fund. The MER was up around 1.40%. However, TD has cut that down to a much more reasonable 0.51%, which makes this a more attractive option.

Still, it is our opinion that a high quality actively managed International Fund will do better than this offering over the long term, even with the lower MER going forward. We would suggest that investors looking for actively managed international exposure take a look at **Mawer International Equity, Renaissance International Equity or Invesco International Growth Class**. Each of those is a high quality funds that we expect should outpace the index fund over the long term.

For those just looking for low cost exposure to International equities in a mutual fund, this would be our top pick.

Standard Life Canadian Dividend Growth Fund (SLM 255)

Many years ago, this dividend focused equity fund was a favourite among many advisors and analysts. Sadly, a number of managerial missteps over the years have brought us to where we are today. Recent performance has shown signs of improvement, but we are still far from giving it our recommendation.

Today, it is managed by Neil Matheson, who returned to the manager's chair in late 2010. Mr. Matheson had run this fund in its glory days, which gives us some cause for optimism. When considering investment opportunities, he looks for high quality companies that have consistent growth prospects. He favours those that have been able to show they can increase their dividends over time.

The fund is focused in Canada, but will invest abroad when opportunities are available. At April 30, he held nearly 80% in Canada, 18% in the U.S. with minor exposure to the Eurozone.

It is reasonably diversified, holding more than 50 stocks, with the top ten make up more than 40% of the fund. Given the focus on dividends, it is not surprising to see it heavily concentrated in financials and real estate, which make up about 40% of the fund. It is significantly underweight in materials.

Performance numbers, particularly the longer term have been largely disappointing. However, since Mr. Matheson has taken over, performance has improved and it now tends to be in the middle of the pack.

The cost of the fund is average, with an MER of 2.10%.

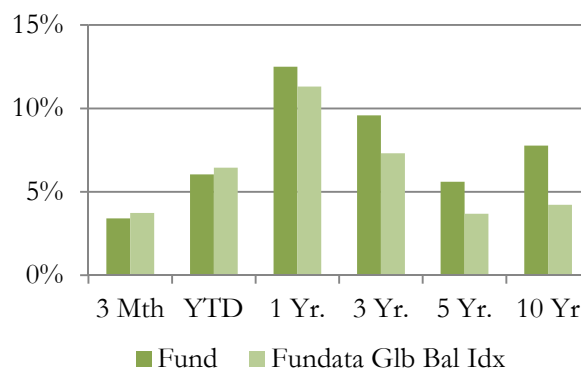
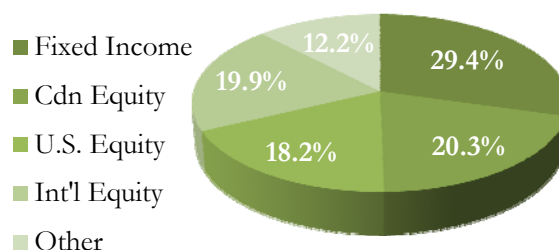
Even with the recent improvement to performance, we would be very reluctant to recommend this fund. We don't think it will hurt you over the long term, but we also don't expect that it will surprise you to the upside. Basically, we see no compelling reason to own it. We expect that it will continue to deliver average returns with average volatility, which just about sums this fund up nicely - average.

If there is a fund that you would like reviewed, please email it to us at feedback@paterson-associates.ca.

Mawer Balanced Fund

Fund Company	Mawer Investment Management
Fund Type	Global Neutral Balanced
Rating	B
Style	Blend
Risk Level	Medium
Load Status	No Load
RRSP/RRIF Suitability	Excellent
TFSA Suitability	Excellent
Manager	Greg Peterson since June 2006
MER	0.98%
Fund Code	MAW 104 – No Load Units
Minimum Investment	\$5,000

Asset Mix



ANALYSIS: If you are looking for a solid one stop portfolio solution, this is a fund that is definitely worthy of consideration. It invests in a number of funds that are managed by Calgary based Mawer Investments.

Each of the underlying funds is of the utmost quality. If we had to pick a weak spot it would be the Bond fund for the reason that it looks very much like the index. Duration is kept within half a year of the DEX Universe Bond Index and it is modestly overweight corporate bonds. This positioning may have been good for a falling rate environment, but we don't expect it to outperform once rates begin to rise.

The equity funds are managed using a disciplined, research driven process that looks to find great companies with strong management teams that are trading at a discount to its intrinsic value.

The target asset mix is set at 40% fixed income and 60% equity. The manager has the ability to change this

mix based on his outlook, but it really doesn't stray too far from the target.

Performance has consistently been above its benchmark and peer group for two main reasons. The first is the disciplined process that is used by the managers in the underlying funds. Second is cost. With an MER of 0.98%, it is one of the lowest priced balanced funds available.

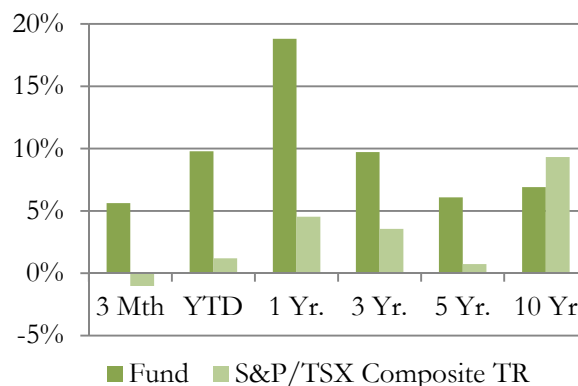
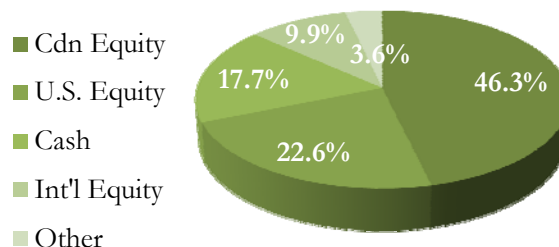
Considering the above, it is our opinion that this is one of the better balanced funds available. We don't expect it to shoot the lights out, but it also won't hurt you too badly on the downside.

This is a great fund for investors looking for a one ticket solution for their portfolio where they know they can rest easy, knowing their portfolio is in good hands. It is best suited for registered plans because it pays out distributions that are mainly considered regular income for tax purposes, which are taxed at the highest marginal rate.

Trimark Canadian Endeavour Fund

Fund Company	Invesco Canada Ltd.
Fund Type	Canadian Focused Equity
Rating	B
Style	Blend
Risk Level	Medium High
Load Status	Optional
RRSP/RRIF Suitability	Good
TFSA Suitability	Good
Manager	Clayton Zacharias since Aug. 07 Martin Uptigrove since Aug 07
MER	2.21%
Fund Code	AIM 1553 – Front End Units AIM 1551 – DSC Units
Minimum Investment	\$500

Asset Mix



ANALYSIS: This is a very solid offering that invests in companies of all sizes, with a focus in small and mid cap companies. Like other Trimark branded funds, it is a concentrated portfolio of high quality, industry leading, businesses run by capable management teams that are trading at a valuation that is less than its true worth.

The portfolio is built on a stock by stock basis and they pay no attention to the benchmark. As a result, the fund looks nothing like it, with a 21% weighting in industrials, 20% in energy and 19% in financials. It has minimal exposure to materials.

Not surprisingly, with its highly concentrated portfolio and mid cap focus, it is more volatile than more broadly focused Canadian equity funds. As a

result, portfolio exposure should be based on one's risk tolerance.

The managers believe that until steps are taken to deal with the massive amount of debt outstanding, that volatility will remain high. More than 17% of the fund sits in cash. While this is largely a result of the managers' investment process, it will help to buffer against any downside moves in the markets. It will also act as a drag should markets rise sharply higher.

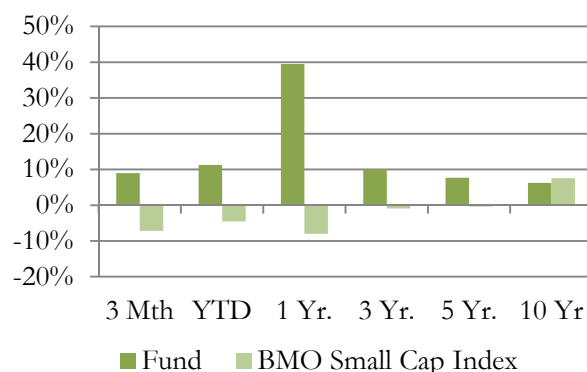
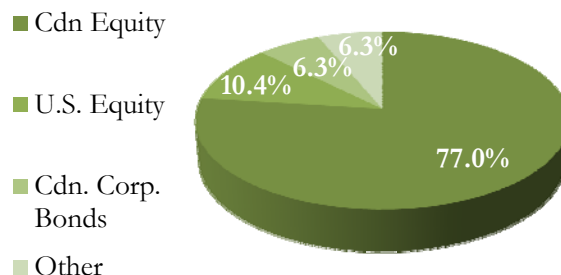
Costs are reasonable, with an MER of 2.22%, which is in the lower half of the peer group.

We like this fund, but do not believe it is suitable as a core holding for anyone, except maybe those with a very high tolerance for risk. Instead, we see it as a return enhancer as part of a well diversified portfolio.

Chou RRSP

Fund Company	Chou Associates Management
Fund Type	Cdn Focused Small / Mid Cap
Rating	B
Style	Value
Risk Level	High
Load Status	Front End
RRSP/RRIF Suitability	Good
TFSA Suitability	Good
Manager	Francis Chou since October 1986
MER	1.87%
Fund Code	CHO 102 – Front End Units
Minimum Investment	\$5,000

Asset Mix



ANALYSIS: Portfolio manager Francis Chou follows a well articulated, value focused approach. He looks for profitable, well managed, industry leading companies with sound balance sheets and strong cash flow generation. Being a value manager, he pays particular attention to the price paid for a stock and is looking to buy \$1 for \$0.50.

The portfolio is very concentrated, holding 16 equity positions and a very modest 0.9% cash balance. The sector mix is dramatically different from the index. It has nearly 71% invested in consumer services, 21% in materials, 5% in financials and 2.1% in technology. This can often result in higher volatility than the index, as well as periods where it will either significantly outperform or underperform its benchmark.

Long term performance has been strong, gaining 7.7% for the five years ending April 30, handily outpacing the 0.4% loss posted by the BMO Small Cap Index during the same period. Still, it is our view that this is a fund that is only suited to those that have a fairly high tolerance for risk.

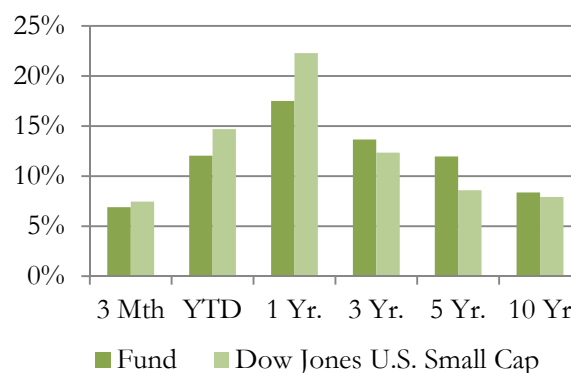
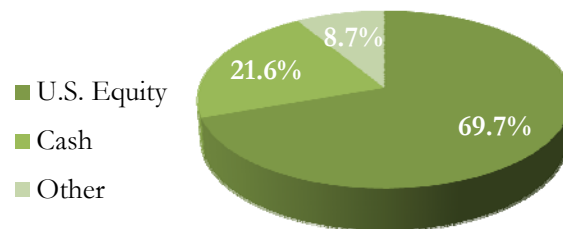
Besides being volatile, we have other concerns with the fund, including key person risk. Chou Associates is basically a one man show. If something was to happen to Mr. Chou and he was unable to continue managing this fund, investors would likely be negatively affected.

We do not recommend this fund as a core holding within a portfolio, but rather as a small cap fund in a well diversified portfolio.

Trimark U.S. Small Companies Class

Fund Company	Invesco Canada Ltd.
Fund Type	U.S. Small / Mid Cap Equity
Rating	B
Style	Blend
Risk Level	Medium High
Load Status	Optional
RRSP/RRIF Suitability	Good
TFSA Suitability	Good
Manager	Rob Mikalachki since Aug 2002 Virginia Au since August 2006
MER	2.91%
Fund Code	AIM 5523 – Front End Units AIM 5521 – DSC Units
Minimum Investment	\$500

Asset Mix



ANALYSIS: The fund is managed based on the Trimark philosophy of “business people buying businesses”. The process used is very much a value focused, bottom up approach where they look for high quality, well managed companies that are largely ignored by the rest of the investment world. They look for good management teams that are typically the number one or number two ranked company in their industry.

The portfolio is concentrated, holding just over 30 names with the top ten make up 45% of the fund. The managers take a long term view when assessing a company, which is reflected by the relatively low levels of portfolio turnover.

Cash, which is the byproduct of the team’s valuation discipline, made up nearly 24% of the fund

at March 31. In recent months, with the markets on a tear, this high cash position has acted as a drag on the performance. Still, returns have been strong, posting a one year return of 17.5% as of April 30. Longer term numbers are also strong, posting a five year gain of 12.0% and a 10 year return of 8.4%. Volatility has been in line with the peer group.

The team has used the recent market run-up to trim some positions that have experienced strong gains of late. Another consequence of the recent rally is they are having trouble finding high quality companies that meet their valuation criteria. This helps to explain the high cash balance. If markets continue to rally, this will continue to drag performance. However, when they do correct, the managers will be in a position to buy high quality names at attractive prices.