Market Commentary

PORTLAND INVESTMENT COUNSEL™

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News Highlights on Current Holdings

- **ABB**, the Swiss power and automation company, announced better than expected results driven by demand coming out of the emerging markets and an ambitious cost cutting program. The company's operational strength also allowed for the preservation of a high EBIT margin, at 13.2%, in a historically tough year for the capital goods industry. The superior business focus allowed for record cash flow generation in 2009, which leaves the company at more than 7 billion USD net cash position and allowed for a 6% increase in the dividend to the shareholders.
- The cost cutting initiatives are expected to continue in 2010 and are targeted to yield an additional 1 billion USD of savings, on top of the 2 billion USD budgeted two years ago. Significant gains are expected from adjusting the global footprint to better reflect the demand dynamics and from the optimization of the global sourcing activities. The outlook for 2010 is cautious, yet management points out that there seems to be a stabilization in the order intake rate and that the company's short cycle businesses such as the automation products appears to have bottomed.
- **Wesfarmers** reported its half year results as of December 31, 2009, for the 2010 fiscal year ending June 30. Given the broad scope of the company's operations, acting as an Australian retailing and industrial giant, the results are a reflection of the Australian economic upswing. All retail units, including the grocery chain Coles, the home improvement chain Bunnings, the department store Target and the discount chain Kmart, have reported improved results. Most notably, the turn-around stories of Coles and Kmart seem to have gained traction, posting trading volumes above expectations and improvements in their earnings before interest and tax (EBIT) margins: 3.6% for Coles from 3.4% the year prior and 6.9% for Kmart from 3.3% in 2009, albeit we expect the Kmart margin to moderate as they pursue top-line growth.
- The most significant drag on the group performance was their coal mining operations, affected by a weaker pricing environment, compared to the same period ending December 31, 2008. All in all, the results point to a robust 2010 fiscal year for Wesfarmers supported by good cash generation. As a result management decided to increase the interim dividend by 10% and to continue at the same time the ambitious investment program in the newly acquired retail division as well as in capacity expansion in its coal mining operations.
- **Reed Elsevier**, the British-Dutch professional information services provider, reported full year 2009 results which were broadly in-line with the analysts estimates and position the company for growth in the coming years as some of its cyclical businesses recover. The revenue line was significantly improved by the addition of the newly acquired ChoicePoint, the US personal information database used for risk management by the insurance industry, government, lenders and various employers.
- Revenue and profit generation were robust in the science and healthcare information solutions division, Elsevier, as well as in the legal and risk solutions division, LexisNexis, despite significant weakness in the US legal market.
- Most affected by the current downturn, the advertising and promotion businesses of Reed Business Information and Reed Exhibitions are expected to recover as the business environment improves and benefit from the restructuring initiatives overtaken over the course of the last two years.
- The overall business reported a resilient adjusted operating margin of 25.9% and continued to deliver strong cash flow generation with a cash flow conversion rate of 99%. With dominant position in key markets, LexisNexis being the leading global legal services business and Reed Exhibitions a solid global number one in promotion activities, the company stands to profit from the return to global economic growth.
- **BNY Mellon** announced last week it was buying the corporate trust business from CIBC Mellon. CIBC Mellon is a 50/50 joint venture between CIBC and BNY Mellon engaged in two activities: corporate trust services through CIBC Mellon Trust Company (CMT) and custodial and asset services through CIBC Mellon Global Securities Services. No financials were disclosed and it appears that this deal is focused on CMT. CMT, which files with Canadian regulators, had a book value of approximately $220 million as of Q3/09 and annualized 2009 earnings of $27-30 million. While this is a small transaction, it may signify that CIBC is willing to sell its custody business as well.
- **AXA** confident on 2010 strategy as profit surges… AXA, Europe's second-biggest insurer, almost quadrupled annual net earnings and said it expected improved profitability from price increases and new products as the cyclical downturn bottoms out.
- **Barclays Wealth** aims to jumpstart growth: In an interview Tom Kalaris, CEO of Barclays Wealth said that it plans to double the number of bankers serving its high-end rich clients and jump start sluggish asset growth with a surge in new investment. He added that the wealth management arm of Barclays will invest an extra £350m over three years, with two thirds spent on products and upgrades and the

remainder on hiring bankers.

- **Investor PCP** (a wholly owned indirect subsidiary of Abu Dhabi state fund International Petroleum Investment Co.) has paid £1.24bn to convert warrants (82.65% conversion at 197.775p/sh) in Barclays. This gives PCP a 5.2% direct stake and 6.3% in total assuming remaining warrant conversion. In aggregate, the Middle East investors control ~10% of Barclays. Barclays' CEO estimates the conversion would have boosted 2009 core Tier 1 capital by 0.40% to 10.4%. The total number of Barclays outstanding warrants is 510.8 million. PCP holds 131.6 million and fellow Mideast investor Qatar Holding PLC, which has a 7% direct stake in the bank, holds the balance of 379.2 million warrants. PCP said it would remain an investor in Barclays. "PCP has no plans to sell such shares," a PCP representative said. "We continue to have a high regard for Barclays and we will seek to continue to maintain a close commercial and strategic relationship with Barclays in the future," he added.
- **Credit Agricole and Intesa Sanpaolo** have executed an agreement, the terms and conditions of which shall be finalized by June 30, 2010, whereby Credit Agricole will extend its coverage in Italy as a result of the disposal on the part of Intesa Sanpaolo Group, at market conditions, of a network of branches mostly operating in geographical areas neighbouring those where Credit Agricole already has a presence. The branch network will include 150 to 200 branches and can also be entirely or partially made up of an Intesa Sanpaolo Group subsidiary. Terms and conditions of the agreement as well as the branch network perimeter will be duly disclosed to the market once finalized.

Economic Activity, Consumer and Business Conditions

- UK unemployment falls for second month in a row: Per the data published by the Office for National Statistics (ONS), the number of people unemployed in the UK has fallen slightly. Total unemployment stood at 2.46m for the three months to December, down 3,000 on the figure for the previous three months. But long-term unemployment, covering those out of work for more than a year, rose by 37,000 to 663,000, the highest figure since 1997. And the number of people claiming Jobseeker's Allowance climbed by 23,500 to 1.64m in January.

Financial Conditions

- The Federal Reserve's announcement last Thursday that it would increase the interest rate it charges banks for emergency loans by 0.25% to 0.75% does not mean that it plans to enact significantly tighter monetary policy in the near future. The announcement stated "Like the closure of a number of extraordinary credit programs earlier this month, these changes are intended as a further normalization of the Federal Reserve's lending facilities. The modifications are not expected to lead to tighter financial conditions for households and businesses and do not signal any change in outlook for the economy or for monetary policy." As of February 10th, there was less than $15 billion outstanding of primary credit borrowing via the discount window, down from a crisis peak of above $110 billion… and so we should expect migration of the residual amount back to the interbank market… impacting (modestly) those banks which remain wholesale funded and favouring those banks which are retail funded / lenders into the interbank market – like HSBC, Standard Chartered, Santander and JPMorgan.
- Policymakers continue to accommodate a recovery in bank profits. The U.S. 2 year/10 year treasury spread is 2.89% and the U.K.'s 2 year/10 year treasury spread is 3.11% - enabling financial services companies' assets booked at these levels, to be very profitable, so enabling them to accelerate the absorption of anticipated consumer credit losses.
- Our concerns are mostly focused around the later cycle issues facing financial services companies – particularly commercial real estate and unsecured consumer loans/ credit card loans. However, commercial real estate exposure is more acutely held by US regional banks – rather than larger more diversified global financial services companies. The number of small U.S. banks failing continues to grow (20 to-date in 2010 and 140 in 2009) but their franchises are being acquired/absorbed as convergence of the financial services industry accelerates – favouring we believe the stronger, better managed banks. Typically banks acquiring collapsed bank franchises from the Federal Deposit Insurance Corporation (FDIC) are paying little or no premium for deposits, assets are purchased at a discount and are covered by loss sharing agreements – so that such deals can be expected to be Immediately accretive to earnings per share.
- A concern which remains is the extent to which loan modifications are an exercise in loss deferral but for the larger franchises the quantum of proactive provisioning continues to act as a differentiator of quality which we believe has still to be fully appreciated.
- The VIX (volatility index) is 20.4 substantially below the levels

experienced last August/September (and well off the highs of 70-80 witnessed late September/October). While, by its characteristics, the VIX will remain volatile, it is we believe further evidence of markets reacclimatizing to risk – typically we believe a VIX level below 25 augurs well for quality equities. And credit default swaps across most leading financial companies are trading in a gradually improving range of 1%-2% (compared to 5%-7% late September/early October).

- We believe the next few years will highlight the growing polarization between strong and weak institutions. Financial services companies that have capital strength will buy assets from those required to divest. Companies that have a strong presence in emerging markets will likely grow quicker than those that do not. Banks that have strong retail deposit franchises will take market share from those that rely on wholesale markets to fund loan growth at attractive margins. Financial services companies that have breached client trust will keep losing business to those reputations that have been enhanced by the crisis. We believe all the Funds are extremely well positioned to benefit from the strength of their portfolios of strong, dominant, attractively priced financial services companies.

Closed-End Funds

Spreads on the closed-end funds are narrowing but remain wide and so in our view are very attractively priced to purchase.

At the close of business on Fridays and at the end of each month we publish the Net Asset Values (NAV) of our funds onto our Portland website at http://www.portlandinvestmentcounsel.com/Funds/WeeklyPricing.aspx. The NAV for the AIC Global Financial Split Corp. can be found on the AIC/Manulife website at http://www.aic.com/EN/PricePerformance/AICClosedEndFunds/Pages/Price.aspx and the Copernican World Financial Infrastructure Trust, Copernican World Banks Split Inc. and the Copernican International Financial Split Corp. can be found on the Copernican website at http://www.copernicancapital.com/Funds/WeeklyPricing.aspx.

The details published last Friday are replicated here below from which you can see we also highlight whether the funds share prices are trading at a premium or discount to their respective Net Asset Value.

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