



News Highlights on Current Holdings

- **HSBC** reported 2009 Profit Before Tax of U\$7.1bn, Earnings per Share of U\$0.35 and Dividends per share of U\$0.34. On an underlying basis, before own debt 'losses' of U\$6.5bn, Profit before Tax was U\$13.6bn. Global Banking and Markets was the weaker performing division (compared to Barclays and JPMorgan which have altogether stronger investment bank franchises) with revenues dropping off 22% HoH, driven mainly by rates, FX and balance sheet management revenues, with the cost/income ratio expanding 7% HoH to 43%.
- The Middle East is weaker, primarily on higher credit charges, which we ascribe to specific exposures rather than a general concern as Standard Chartered's results in this area were more robust. Impairment charges have come in at U\$26.5bn with Non Performing Loans usefully down to U\$30.6bn (1H09 U\$31.8bn). Geographically, the Middle East was a disappointment with 2H09 impairment charges of U\$943m (1H09 U\$391m) and NPLs running at 6.8% of the book (1H09 3.5%). Nonetheless, across the group the outlook is for loan impairments to decline in 2010 which is good news – albeit expected.
- In our view HSBC has used 2009 to strengthen its balance sheet, capital and liquidity which are now among the most robust for large, international banks with its core tier 1 capital at 9.4%. As per the CEO's comments HSBC expects growth in emerging markets of 6% versus 2% in developed markets – which suits how it has positioned its business franchises... and he has indicated January's performance was strong and ahead of expectations.
- HSBC has revived its branch expansion program across Australia, although it will limit branch openings to a handful of new capital city sites a year. The Australian business delivered a 25% increase in annual profit to \$251m, fuelled by solid-paced growth in mortgages and a surge in markets trading income.
- **Standard Chartered** – Results in-line with market expectations, attributable profit at \$3.38bn. Total revenues of \$15.184bn were modestly below expectations – mainly a result of lower dealing profits. Offsetting this, costs were US\$50m better, so net profit was pretty much as expected at \$7.232bn. They were a bit worse on credit quality, loan impairment charge of \$2bn and there was a \$102m impairment charge on other assets, but none of this in our view is material. Tax was a tad lower than forecast as well to get to the bottom line. Dividend Per Share a bit weaker than expected at 66c but Core Tier 1 ratio is strong at 8.9% and outlook statement very positive with the CEO describing the start to the year as 'very strong.'
- **MetLife and Prudential PLC** – This morning MetLife announced that it was acquiring ALICO from AIG for \$15.5 billion in cash and securities, or 1.16x 4Q09 book value (including Any Other Comprehensive Income) and 9.9x 2010E operating earnings. On the surface MetLife appears to have paid lower multiples than Prudential PLC paid for AIA but then we believe the future growth profile for ALICO, although strong, will be lower than that of AIA. MetLife will give AIG \$6.8 billion in cash and \$8.7 billion in MetLife securities issued directly to AIG. MetLife expects 2011 EPS accretion of \$0.45-0.55 (roughly 10% of consensus of \$4.89) and 2011 ROE accretion of 140-160 points. The integration is expected to close in late 2010.
- Following the deal, AIG's stake will represent roughly 14% of MetLife's outstanding stock and as much as 20% depending on the extent to which AIG chooses to sell its shares after the applicable lock-up periods. AIG is able to sell up to 50% of its common equity and equivalents after 9 months and another 50% (of the remaining amount) 3 months later. Once AIG has sold a "substantial amount" of stock (estimated by MetLife at roughly \$4 billion), AIG can then begin to sell in smaller increments.
- AIG's stake comes with voting restrictions, whereby AIG must vote its interest in the same manner as all of MetLife's other stockholders and is therefore not truly independent. Thus, we would not expect MetLife to be subject to government influence (via AIG) that has been an overhang on companies that took TARP financing. (Note MetLife did not accept any TARP funds).
- **Prudential** is in talks with Temasek about becoming a cornerstone investor in the funding of its acquisition of AIG's Asian life insurance business, AIA. Talks are reported to be at an early stage. This sounds like it will be more a placing than a sub underwriting of the existing rights issue.
- **Vivendi**, the French telecom and media giant, revealed its full year results Monday, beating the expectations in term of both revenues and operating earnings on strong performance from its telecom and digital games divisions. Despite increased competitive pressures, Vivendi's telecom businesses, SFR, the second largest mobile operator in France, and Maroc Telecom, leading operator in North Africa, posted improved revenues and resilient earnings. Activision Blizzard, the second largest video company in the world, controlled by Vivendi, reported an increase of almost 50% in revenues for 2009. Universal Music, the other significant asset in



Vivendi's line-up, was the main drag on the company's operating earnings in a tough year for the music industry. The reported earnings were impacted by on-going litigation provisions.

- We are watching closely how the integration of GVT, the Brazilian fixed-line broadband operator newly acquired by Vivendi, is panning out. The company announced its intention to step up its expansion plans to reach Rio de Janeiro and Sao Paulo as well as to potentially enter the mobile scene.
- **Santander and UK Banks** – in our view the thaw in the UK Retail Mortgage Backed Securities market continues. Santander successfully placed £1.4bn of UK RMBS on Friday priced at 3m Libor + 120bp. The deal is significant as it is the first transaction since the Greek concerns spiraled and the first deal since Lloyds Bank's transaction in January. We think this deal is a good read across to all the UK Banks. For instance, Lloyds has ~£12bn of term funding to replace this year, with £20-25bn p.a. in 2011 and 2012. A functioning RMBS market is a helpful supplement to the Covered Bond market and provides a welcome alternative to senior debt. Funding is one of the key areas of concern for the market so any improvement should provide a strong catalyst.
- **ING** is due to spin off its insurance business and other assets before the end of 2013 but according to press it might get more time from the EC for its disposal program.
- Morgan Stanley nears \$1bn sale of CICC stake to buy-out groups – Morgan Stanley is nearing the sale of its stake in China International Capital Corp. to two US private equity firms – Kohlberg Kravis Roberts and TPG – for about \$1bn, ending a strained relationship. A deal would produce a tidy profit for Morgan Stanley, which invested \$37m in the Chinese investment bank almost 15 years ago, and free the company to pursue a new joint venture with China Fortune Securities, a Chinese brokerage. Morgan Stanley wants to establish a new partnership to grant it the right to trade stocks and other securities on local Chinese markets. The New York-based bank, which has chafed at the limitations of its passive investment in CICC, wants management control over such a venture.

Economic Activity, Consumer and Business Conditions

- The US consumer credit grew in January stopping an 11 month slide. While this is hardly evidence of a significant rebound in the consumer sector, in particular after the disappointing consumer confidence data issued a week

before, it contributes to the overall improved economic outlook as implied by the manufacturing numbers and the financial conditions indicators (in particular the steepness of the yield curve). This improvement also comes to confirm the easing in lending standards as reflected by the Fed's Senior Loan Officer's Survey on Bank Lending Practices in January. The growth in consumer credit was of 5 billion USD, supported largely by the growth in non-revolving credit by 6.6 billion USD, offset by a modest 1.7 billion USD retreat in the revolving credit. In relative terms, consumer credit grew month on month by 2.4% annual rate.

- From the peak in 2008 to the most recent monthly data in January, revolving credit card debt is down about \$110 billion or 11.5%, which we estimate is about equal to industry wide loan charge-offs over the same period. Thus, upon excluding the population of credit card holders who have charged off, the remaining credit card population has continued to revolve and spend. To the degree that people who have lost their credit card privileges are still spending, they are either using debit cards or cash or checks. In its 1Q10, Visa grew US debit 15.4%, while credit card spend was off 1.1%. January is often one of the bigger months for revolving credit growth, so we believe it may be too early to call a bottom in revolving credit, particularly with charge-offs likely to remain elevated in the early part of this year. In addition, the implementation of the CARD Act should also cause some dislocations in credit availability to customers with lower credit scores. Nevertheless this growth in January is important...as the reason economic recoveries tend to progress slowly after financial crises is that credit simply does not flow – and so should credit now show signs of starting to flow it is an encouraging sign.
- The employment situation report, released Friday, surprised positively, with a drop of only 36,000 jobs in nonfarm payroll in February in US, versus the expected 50,000 job cuts. The unemployment rate stayed at 9.7%, while the average hourly earnings grew a benign 0.2% from an inflationary standpoint. The series of good news from the Department of Labor last week was completed by upward revision of US nonfarm productivity level, at 6.9% annual rate for Q4. Consequently, the unit labor costs retreated by 5.9% over the same time period, undoubtedly a boost for corporate America's profitability.
- The housing and construction sector in US continues to be the most important laggard as the Pending Home Sales number dipped 7.6% in January, well below expectations of a 1% improvement.



- In Canada, the Ivey PMI manufacturing index improved to 51.9 from 50.8, implying a much needed rebound in the Canadian manufacturing sector. The housing starts for February were 71% higher than the previous year's level, with the unusual warm weather being a significant factor.
- Greece has announced additional EUR4.8bn in additional spending cuts/revenue increases. New measures include VAT hike from 19% to 21%, 30% cut to civil servants' bonuses and pension freeze. In our view these actions should be viewed positively as they reduce the sovereign default risk and reassure the market about the effectiveness of the austerity plan.
- continues to act as a differentiator of quality which we believe has still to be fully appreciated.
- The VIX (volatility index) is 17.8 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.
- 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.

Financial Conditions

- Australia's central bank raised its cash rate by 25 basis points to 4.0 percent on Tuesday and flagged further hikes ahead, saying a surprisingly strong recovery allowed it to move policy toward more normal settings.
- Policymakers continue to accommodate a recovery in bank profits. The U.S. 2 year/10 year treasury spread is 2.81% and the U.K.'s 2 year/10 year treasury spread is 2.77% - 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 (26 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

Market Commentary



PORTLAND
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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 beginning of business on Mondays and at the end of each month we publish the Net Asset Values (NAV) of our funds onto our Portland website at <http://www.portlandic.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.

A handwritten signature in black ink, appearing to read "Chris Wain-Lowe". The signature is fluid and cursive.

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