Market Commentary

PORTLAND INVESTMENT COUNSEL™

November 8, 2010

News Highlights on Current Holdings

Financial Services Companies

Manulife Financial (MFC) reported a net loss per share of ($0.55), above the consensus of ($0.73). Adjusting for market movements and other abnormal items (largely pre-announced), core EPS was $0.43. In aggregate, the adjusted operating earnings of $760 million fell within the upper-end of management's guidance range of $700-800M, reflecting the benefit of the higher equity markets and more favorable claims experiences in its US businesses.

Solid capital improvements: The MCCSR (minimum contingency capital solvency ratio) ratio increased 13 points to 234%, reflecting the $2 billion of debt raised in the quarter and the benefit of higher equity markets, which more than offset reserve strengthening related to assumption changes.

Reduced market sensitivity: The company made further progress on reducing its sensitivity to equity and credit markets, hedging an additional $3.3 billion of its in-force variable annuity business, bringing the aggregate amount hedged to 54%, up from 35% at the beginning of the year. In addition, it lengthened the duration of its fixed income investments, reducing its earnings sensitivity to interest rates by 19%, while also raising prices on its UL business to help maintain spreads.

The Hartford Financial Services Group, Inc. (HIG) reported third quarter 2010 net income of $666 million. HIG's "core" EPS of $1.43 beat consensus of $0.85. The underlying EPS was $0.92, after excluding the $0.34 DAC(deferred acquisition cost) benefit, $0.19 of P&C reserve releases, and $0.02 of net negative items. The Hartford's new 2010 EPS guidance range is $2.60 to $2.70 up from $2.10 to $2.30. This suggests 4Q'10 EPS of $0.80 to $0.90 vs. the previous guidance of $0.85 to $0.95. The 4Q decline reflects about $0.04 of higher than normal catastrophe losses, driven by severe weather in October.

P&C Commercial net premiums written (NPW) of $1.4 billion increased by 2% from a year ago (ex-a 3Q'09 reinsurance adjustment). Growth was in line with peers. The underlying combined ratio was 92.2% vs. 93.6% in 2Q'10; Price increases continued across all lines. Retention was steady in P&C Commercial, and declined as expected in Consumer Markets.

Life sales increased by 14% from a year ago, driven by universal life. Retirement Plans net flows were $508 million vs. $239 million in 2Q'10 driven by strong deposits and low surrenders. Funds flows in The Hartford's $50 billion-in-assets retirement business were solidly positive.

US statutory surplus grew by $700 million in the quarter to $15.2 billion. This was driven largely by $400 million of variable annuity reserve releases and $300 million of P&C operating earnings. The subsidiaries did pay a $200 million dividend to the holding company. Life statutory earnings (excluding VA) were negative $100 million, driven mainly by an increase in market value adjusted fixed annuity reserves due to the decline in interest rates. The company had a net unrealized gain of $1.2 billion in 3Q'10 vs. a net unrealized loss of $1.5 billion in 2Q'10. Pre-tax net impairment losses were $122 million in 3Q'10, down from $148 million in 2Q'10. The majority of the impairment was from CMBS and CRE CDOs. Total Book Value rose 10.3% to $45.80, and the statutory surplus increased to $15.2 billion.

Aviva trading statement plus strategy update overall positive. In the life business sales up 5% inline with consensus with strength in the UK offset by weakness in Delta-Lloyd and the US. The P&C results look generally better with the overall combined ratio at 97% for the 9M vs 99% in 1H. The UK was a major contributor to the improvement falling to 96%. Capital and cash generation continue to be the focus and the GBP1.5bn target for 2010 remains on track and growing into 2011. On the cost front they announced further savings of GBP200m p.a. plus another 200m of efficiency benefits.

BNP Paribas - reported net income €1905mn 10% above consensus €1743mn (3Q10 EPS reached €1.53 after €1.71 in 2Q) with divisional beats at the PBT line at Personal Financial Services, Belgium & Banc West. While total revenues were 3% better than market expectations (difference mainly coming from the Corporate Center), the cost of risk was slightly above estimates at €1.22 bn (72 bp over loans), 6% higher than expectations. Corporate Investment Banking PBT beat consensus 5% with revenues 4% ahead driven by Equity/Advisory up 95% qoq (equities -3.7%). BNPP estimates the Basel 3 impact on RWA at €70bn, or 11% of current Risk weighted asset versus consensus expectation of a 16% uplift & versus 39% at SocGen. This leaves Basle 3 Common Tier 1 at 9% at end 2012 versus SocGen at 7.5%. Return on tangible equity, adjusted for the Mark to Market of own debt reached 14.5% in 3Q and we expect will reach 15-16% next year.

BBVA has acquired a 24.9% stake in Garanti, the Turkish bank, for a total consideration of US$5.8bn (€4.2bn) and will jointly control the bank with Dogus Group, a Turkish conglomerate, which also holds a 24.9% stake. BBVA has bought 18.6% from

GE at TRY6.842/share (a 23% discount to the current price) and 6.29% from Dogus Group for €1.5bn or TRY11.162/share (a 25% premium to the current price). BBVA and Dogus will each have four seats on the board. Mr Sahenk will remain as Chairman and Mr Ozen as the CEO & President. The average price paid by BBVA (TRY7.99 per share) implies an 11% discount vs yesterday's close but an 11% premium vs the YTD share price. It also implies that Garanti is valued at approximately 2.0x book value.

BBVA has also announced a E 5bn. Subscription price of €6.75 per share, 1 new share for every 5 old.
The rights issue means 16% new shares (750m) at €6.75, or discount of 26% versus the closing price prior to the announcement and 25% versus the theoretical ex rights price. Because BBVA has issued more shares than needed the surplus should boost core Tier 1 capital by about 69bp with approximately 9%-10% earnings dilution next year (5% adjusted for rights). After the acquisition of Garanti and the positive impact of the capital increase (165bp), proforma core Tier I is approximately 8.2-8.5% plus the unrealized gain BBVA has through its ownership of Telefonica, suggests a proforma core tier 1 of 9-9.3%.

We think Turkey offers BBVA exposure to a rapidly growing retail banking market, giving the bank the opportunity to increase its emerging markets exposure and thus reduce the domestic earnings contribution, this strategy is similar to Santander's. We believe both HSBC and Santander tried to wrestle control of this well-run Turkish bank, recognising the growth potential, but without success. After five years, BBVA has a call option to acquire 1% of Garanti shares from Dogus, which would then provide BBVA with a controlling stake. . If this option is exercised, then BBVA will have six seats at the Board versus three for Dogus as long as Dogus' stake is at or above 15%. Below 15% stake, Dogus will have two seats at the Board, and below 9.95% stake Dogus will only have one seat.
BBVA's deal is therefore structured so it can gain control over the next 5 years... which was presumably the best deal on offer but does present protracted integration issues. Nonetheless, Garanti looks to be a good strategic deal for BBVA given (i) the ability to take control medium term (5 yrs) in a best-in-class Turkish franchise, (ii) opens up new potential markets (eg. Russia / North Africa), (iii) ability to participate in further potential Turkish consolidation (eg. state owned banks), and (iv) lowers Spanish contribution to ~31% (Garanti will comprise ~9% BBVA earnings). However, given BBVA's previous international experience has been in Latin America and the US it is perhaps no bad thing that there is an enforced protracted period to settle into this purchase – so giving BBVA time to decide whether indeed it does want to seek a majority stake.

BBVA will invest $601 Million in China Citic Bank's rights offering. BBVA holds 15% of the Chinese Bank and will make sure its shareholding will not be diluted.

HSBC 3Q trading statement advised income and profit run-rate in 3Q was lower than seen in 1H. GBM had higher revenues in Emerging markets, but lower in Europe and the US. Personal Financial Services and Commercial banking appears to be doing well and loan growth is accelerating at a group level. Costs are slightly higher than the 1H run rate. Group PBT is "well ahead" of last year, but below 1H10 run rate. Credit trends continue to be positive with the US business accounting for the largest share of improvement in the quarter. In 1H07 bad debts were $6.3bn. On the conference call management confirmed that 3Q bad debts were back to those levels. Overall revenues look to be guiding lower as the company points to lower activity in Global banking and potential "bumps in the road" in emerging market recovery.The Interim Management Statement implies continued improvement, notably in bad debts and Asian growth. The Core Tier 1 capital ratio of 10.5% shows that HSBC generated 60bp of capital, this in our view bodes well for future dividend paying capacity.

Lloyds Banking Group released their third quarter trading statement which in our view conveys a message of continuing improvement. Guidance was broadly unchanged from the first half. Income: underlying core income growth has continued in line with expectations. Margin: Lloyds expects to see 'modest' margin improvement in the second half, which is likely to mean rising from 2.08% to over 2.20% led by continued back book repricing....medium term target remains 2.5%. In the release Lloyds Bank referenced higher wholesale funding costs as a drag on the margin, albeit this was as a result of successfully completing the 2010 £25 billion term funding requirements within 9 months and already raising £2.5 billion for 2011 so enabling it to voluntarily accelerate the repayments of UK Govt. funding "public and central bank sources". Deposits have grown in the quarter, although it is not disclosed by how much. As a result of lower lending, the group's loan to deposit ratio continues to move towards the stated goal of 140% "over the next few years" (163% 1H10). Costs in the quarter "have continued to fall" and impairments " have continued to decline" In line with recent guidance", although they highlight Wholesale impairments as lower than expected and Wealth & International (Ireland) higher. At the Bank of America / Merill Lynch conference last month Eric Daniels said that bad debts would see a moderate fall in 2H10 versus 1H.

Lloyds Antonio Horta-Osario (current CEO of Santander UK) is to be the new CEO of Lloyds Banking Group. This is a positive surprise, Antonio Horta-Osario is well regarded and this potentially marks a cultural shift at Lloyds to a more sales driven environment, however this is limited given their market share. Mr Horta-Osorio has been CEO of the UK business since 2006, and prior to that he was CEO of Santander's Portuguese business, and Brazilian business also.

Santander: The departure of its CEO of UK business ahead of the UK IPO it is not positive given that the CEO has decided to defect to the largest incumbent player rather than try to steal more market share from it. Whenever Group CEO Emilio Botin (76) retires, Ana Botin (50) his daughter will now be considered "heir apparent" after leaving her role as Chairman of Banesto to become the new CEO of UK business. This will give her further experience and also more exposure to investors, although she has presented at the Bank of America / Merrill Lynch for the last 3 years and is already well regarded.

Prudential Financial (PRU) reported 3Q10 operating EPS of $2.12 (vs. $1.78, up 19%), which was well above the consensus estimate ($1.44). On an adjusted basis, operating EPS was in line(assuming a 35% tax rate for unusual items).

Three highest multiple businesses well above expectations Individual Annuities, Asset Management and International Insurance all exceeded earnings estimates for the quarter. Earnings in Individual Annuities, adjusted for unusual items, were 11% above forecast, earnings in Asset Management were 29% above forecast and earnings in International Insurance were 6% above forecast. These three businesses combined accounted for almost 75% of total adjusted operating segment earnings in the third quarter.

The key positive in the quarter was strong new business growth in certain segments. Individual VAs put up yet another very strong quarter, posting sales of $5.4 billion and net flows of $3.4 billion.

Balance sheet trends were generally good during the quarter. Book value per share excluding AOCI, was up 4.5% to $58.09. Book value per share including AOCI (any other comprehensive income) (i.e., stated book value) was up 13% on a sequential basis to $67.81. The investment portfolio delivered net realized investment gains of $278 million, versus $212 million 2Q:10 (both on a pre-tax basis). Gross unrealized losses (GULs) on all fixed maturity holdings were down modestly from $3.3 billion to $3.2 billion, while net unrealized gains improved from $5.8 billion to $9.6 billion.

RBS: Results ahead but the underlying performance mixed. Capital generation was disappointing with Core Tier 1 falling 30bps to 10.2%. Q3 PBT of £726m well ahead of consensus driven by provisions (£1,953m) and non-core performance. Pre-provision earnings for the core business came in at £2,514m. Strong results from UK Retail and Corporate banking driven by lower provisions. Weak performance from Global Banking Markets (operating profit £589m) and Insurance. In our view the outlook should be to expect good Retail and Commercial banking trends to continue in the fourth quarter with the pace of Net interest margin expansion to moderate – it already slowed in 3Q (+2bps QoQ vs +11bps QoQ in 2Q10), with Global Banking & Markets environment to remain challenging. Wholesale Funding requirement of £25bn for 2010 exceeded as £35bn term funding completed YTD. Basel 3 impact (negative 130bps) and there could be 200bps of capital generation from £100bn of Risk weighted asset reduction. 15% ROE remains the target regardless of capital requirements and management indicated a willingness to reprice assets to get there if needed.

Royal Bank of Scotland: is close to selling a portfolio of global oil, gas and power project finance loans to Mitsubishi UFJ for £4bn according to the FT. The deal could be finalised in the coming weeks, possibly by the end of the year as RBS continue their plan to shrink their balance sheet.

St. James' Place: 3Q10 new business. Annual premium equivalent (APE) £136.5m, compares to £104.6m +30%. 9 Months APE £429.1m slightly below consensus average of £430.5m but 40% ahead of actual 9 Months 2009. For comparison APE of £136.5m versus £133.3m 1Q10 and £159.3m 2Q10 which were both record new business levels for St James's Place. This is therefore the second largest quarter of new business on record for St James' Place in what is traditionally the slowest quarter because of the summer months. Single premium business which carried higher margins continues to drive sales. Net inflows in the quarter of £700m were 3% of opening funds under administration (FUA), a 12.5% annualised rate. Retention rates remain high at 95%. All of the above should bode well for profits. Strong net inflows supported by 8% investment return on FUA has boosted FUA to £24.8bn (1H10 £22.4bn).

Sun Life (SLF) reported Operating EPS of $0.79 vs. consensus $0.61, but included $0.17 of favorable unusual items. Absent these, normalized EPS of $0.62 was consistent with forecast and demonstrated good underlying performance allowing for the expected volatility related to the annual actuarial assumption review as well as the rise in equity markets and drop in long-term interest rates during the quarter.

Normalized ROE of 8.8% excluding the unusual items remained below the peer group and is still an area for improvement. Among the business lines, it was a good showing from Canada, MFS and Asia, as each posted strong sales gains.

MCCSR ended the quarter at 208% which was relatively unchanged from Q2/10. During the quarter, positive impacts from equity markets were offset by impacts from interest rate movements. In Q4/10, MCCSR will be positively impacted by the sale of the life retrocession business to Berkshire Hathaway (10-14 points) and negatively impacted by the redemption of $300mn Clarica debentures (5 points).

Management indicated that there is $300mn of contingent capital at the holding company, up from $250mn in the prior quarter. There was no capital down streamed to the operating companies in Q3/10.Deutsche Bank is close to gaining a controlling stake in Deutsche Postbank and plans to absorb the lender into its balance sheet and start increasing synergies by the end of the year according to FT Deutschland.

AXA stated that personal motor revenues were up 35% in the UK, on the back of strong tariff increases and higher volumes mostly as a result of the success of both Swiftcover and Axa branded direct businesses.

Financial Infrastructure Companies

Australia Stock Exchange: Prime Minister Julia Gillard has sent a warning to the Coalition not to destroy bipartisan support for foreign investment over the proposed takeover of the Australian Stock Exchange by its Singapore counterpart. Ms Gillard said yesterday she had raised the issue of the Singapore Stock Exchange's takeover bid with her Singapore counterpart during a visit to Hanoi for the 16-nation East Asia Summit.

Dividend Paying Companies

BHP – The Canadian government's decision against allowing BHP's bid for Potash Corp took everyone by surprise and is widely perceived to have had been influenced by the current political spectrum of the country, with the minority government deriving a lot of its support from the western provinces, which vehemently opposed the bid. It was in fact only the second transaction to have been blocked under the prerogatives of the Investment Canada Act, out of the about 1,700 transactions considered over the past 25 years, and it dealt in our opinion a blow to Canada's investment friendly image. BHP reaction was that the decision was disappointing and that it still believed that the offer would have been of a net benefit to Canada. The company said it is reconsidering its options, but many believe it is unlikely to continue pursuing the bid after already offering significant concessions to please the provincial and the federal governments. Speculation is rife as to what the company would do with its about $45bn in cash it aligned for the purchase, with shareholders hoping for a share buyback or a special dividend.

BMW – BMW delivered a solid third quarter earnings report with beats across the board in terms of revenue, earnings before interest and tax (EBIT) and net profit. The group was helped by strong demand pick-up in growth emerging markets, in particular China. One key indicator of business performance, the car business' EBIT margin, at 8.1%, beat expectations as well, although is still behind some of the competitor's (Audi inferred rate is 11.2%, while Mercedes posted a 9.5% margin). The company's management declared that it aims to increase group earnings significantly in 2010 and it raised the auto EBIT margin target from 5% in August to 'more than 7%'. Many analysts believe this outlook to be too conservative and are already factoring in better margins, with significant earnings up-grades being issued by most brokers.

Toyota – Despite significant headwinds from a much stronger yen, Toyota managed to deliver a robust first half year result, helped by favourable conditions in its domestic market as the government rolled out incentives to support the adoption of hybrid vehicles. The strength in the Japanese market helped the company to maintain competitive rates of capacity utilization in its domestic facilities. The group raised its full year forecast for an operating profit of ¥380bn ($4.7bn), up from its previous guidance of ¥330bn, while it expects to sell 7.41mm units (up from previous guidance of 7.38mm units) worldwide, with demand in Asia offsetting the weaker North American sales.

Economic Activity, Consumer and Business Conditions

Spain's jobless rate unexpectedly fell last week for the first time in more than three years from 20.09% to 19.79%. An increase in sales tax aimed at curbing the budget deficit pushed up the inflation rate to the highest in two years.

Australia: The Reserve Bank of Australia on Tuesday unexpectedly increased the benchmark interest rate by 0.25% to 4.75% amid concerns that stronger economic growth will cause inflation to accelerate, driving the Australian dollar close to parity with the US dollar.

Reserve Bank of India: raised the key benchmark rates by 25bps. Though the 25bps hike was expected, what came as a surprise was the explicit statement by the RBI that the likelihood of further rate actions in the immediate future is relatively low.

US – The US economic news last week was dominated by the highly anticipated Fed's decision on interest rates, in particular the amount of the quantitative easing and the pace at which it is expected to be released in the marketplace. Not in contrast to many observers' expectations, calling for roughly $500bn of balance sheet expansion, the Fed took the decision to expand its asset purchase program by $600bn meant to acquire longer-term Treasury securities over the next 8 months. The pace of securities purchases is hence of about $75bn a month. The Fed also maintained its policy of reinvesting principal payments from its securities holdings (mainly agency mortgages), which amounts to some $250bn-$300bn over the same time period. The Fed allowed itself some flexibility, saying that it would adjust the size and the pace of the securities purchasing according to the incoming economic information. Markets responded to the announcement, rallying strongly at the end of last week, while the US dollar depreciated in value against most currencies, as expected.

It's interesting that the Federal Reserve is potentially allowing strong banks to raise their dividends – a signal that came one day after the much anticipated quantitative easing 'II' was announced. It seems the Fed is keen to enable the reflation of the equity markets to create a wealth effect and so increase confidence and spending that goes along with it.

The markets were also helped by goods news coming from the employment front, with the US economy adding 151,000 new jobs to the non-farm payroll employment. The rate was just about enough to keep the unemployment rate at 9.6%. A higher rate of about 250,000 would be consistent with an unemployment rate reduction. The weakness in employment is illustrated by a lame figure for the average weekly hours, up marginally to 33.6 hours from 33.5hours, yet significantly lower than the expected 34.2hours. The average hourly earnings were barely positive on a year on year rate of change basis.

The consumer credit figure, released by the Fed Friday, showed month on month growth for the first time since January, as consumers added $2.1bn worth of credit. Other reports added to the overall good mood of the markets, with the non-manufacturing index from the Institute for Supply Management (ISM) gaining in October significantly more than expected while the US productivity gained at an annualized rate of 2.2% over the last quarter.

Canada – In Canada, the housing starts numbers surprised on the negative side as instead of amounting to the expected 183,000 units annual rate, it fell short by 15,000 units annual rate, to 168,000 units annual rate. A certain level of housing starts curtailment was expected, following a decrease in demand. Both single units and multi-family suffered a contraction in October.

Financial Conditions

Loans/Asset Growth is slowing returning: overall assets (among the US top 25 banks) grew in the 3rd quarter 2010 marking the first quarter of growth since 4th quarter 2008.

US Investment banking activity trends for Q4 show an uptick in fixed income and Emerging capital market volumes. Fixed income volumes for the week came in at $20.6B up 7.7% w/w. Debt capital markets volumes were relatively flat w/w but are on path to match or beat last quarter's total volume raised. Equity capital markets total issuance was up 36.4% w/w, the second consecutive weekly increase and is on pace to easily beat last quarter's total volume raised.

Policymakers continue to accommodate a recovery in bank profits, albeit less than 6 months ago. The U.S. 2 year/10 year treasury spread is 2.14% and the U.K.'s 2 year/10 year treasury spread is 2.31% - enabling financial services companies' assets booked at these levels, to be profitable.

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, Spanish and German regional banks (as identified in the European stress tests) – rather than larger more diversified global financial services companies. The number of small U.S. banks failing continues to grow (150 to-date in 2010) exceeding last year's 140 which was the highest annual tally since 1992. This supports our view that 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. The FDIC changed the loss share arrangement on assisted deals from absorbing 95% of losses down to absorbing 80% although this is still attractive to acquiring banks it does probably lower the Internal Rate of Return.

The U.S. 30 year mortgage market has remained low and has now fallen back to 4.24% - (the lowest rate since the Federal Reserve began tracking rates in 1971), as the Federal Reserve effectively continues to seek to incentivise home ownership. Existing U.S. housing inventory has increased to 10.7 months supply of existing houses – much higher than what we believe is a more normal range of 4-6 months. We believe it remains premature to consider a recovery in house prices but a measure of stability from which to build is welcomed….particularly for those financial services companies holding such assets in their portfolios.

A concern which remains is the extent to which mortgage foreclosures have been properly documented, thereby enabling mortgages to be "put back" to the originating bank. However, from recent bank investor relations presentations it does seem the rate of "put backs" are now expected to decline, suggesting current levels of provisions should suffice. 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 19.30, which is below the levels experienced prior to the ECB bailout and substantially lower than last August/September. While, by its characteristics, the VIX will remain volatile, 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. 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. We believe the Funds we manage 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, in our view, very attractively priced to purchase.

The Portland Investment Counsel Inc. 2009 Closed End Annual Reports are now available on the web site. Below you can find the link to access the closed end annual report.

http://www.portlandic.com/Info.aspx?disp=Financial_Reports

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.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.

Chris Wain-Lowe
Executive Vice President
Portland Investment Counsel Inc.
Phone: 905-331-4250 Ext. 4232
Fax: 905-331-4368
www.portlandic.com

PIC10-0162-E(11/10)