Market Commentary

PORTLAND INVESTMENT COUNSEL™

February 21, 2011

News Highlights on Current Holdings

Financial Services Companies

Axa reported FY10 NPAT of 2.75bn but this was affected by the 1.6bn charge on the sale of the UK to Resolution. On an underlying basis, the result was 3.9bn, up 1pct yoy. EPS of 1.57 was down 6pct, mainly due to higher share count. The dividend is 0.69 per share, up 25pct on 2009. Operating cashflow increased to 3.7bn, vs 3.1bn in the prior year. The primary driver of growth was the 600m increase from the life business. Embedded Economic Value per share is 14.90, up 11pct yoy. Return on EV was solid at 16%, despite a negative 7% impact from adverse investment variances. Net net these look like decent results and after a frustrating 2010 it has been the best performing large cap insurer this year and remains the most levered to an improving macro environment.

BNP Paribas : 4Q10 net profit came at €1,550mn versus consensus of €1,747mn due to one-offs in corporate centre (Axa stake write-down, IT spend in the Benelux and weak financing income). In terms of large divisions, the negative delta came from the corporate centre (€315mn negative non-recurrent impacts) and Corporate & Institutional Banking (higher costs, lower financing revenues). It was a good performance in Asset gathering, Consumer finance and Investment Bank revenues, in advisory and capital markets, both equity (+12%) and FICC revenues (-12% better than some other peers) were in line. Provisions this quarter amounted to €1,162mn, compared to consensus €1,229mn. The cost of risk movements were mixed across divisions (versus 3Q10): French retail (41bp/31bp), BeLux retail (32bp/35bp), BNL (105bp/108bp), BancWest (79bp/107bp), Europe Mediterranean (187bp/130bp), Personal Finance (210bp/224bp), in CIB (12bp/minus 1bp). 4Q10 expenses were up 12% YoY: +15% in CIB, +11% in Asset gathering. For operating divisions (at constant scope and FX rate), 2010 expenses were up by 0.7% YoY. Underlying EPS of €5.53 (4Q10 annualised). Capital adequacy remains strong: 11.4% Tier 1 ratio (11.2% in 3Q10), 9.2% Core Tier 1 ratio (9.0% in 3Q10), with Risk Weighted Assets down €7bn QoQ (-1.1%). Proposed dividend: €2.1 cash dividend with a 33% payout. Fortis synergies: revised from €900mn to €1.2bn (+33%), including €123mn in Turkey. Non Performing Loans: 4.4% (versus 4.3% in 3Q10), coverage at 81% (82% in 3Q10). CEO sticking to a 15% ROE target over the medium-term.

Credit Suisse CoCo's and EU Capital Raises: Credit Suisse announced last week that it had placed $2bn of contingent convertible notes with a very tight yield of 7.875% for the 30yr bonds with a 7% equity tier 1 trigger. Demand was reportedly a massive $22bn and this could trigger a raft of similar deals as the market is now seen to be open.

ING reported a net profit for Q4 of €443m, 4% below consensus of €462m. However, before special items (€211m) the result is actually better than expected at €644m versus consensus of €544m (+18%). The beat however is entirely driven by lower than expected taxes (€113m vs. €215m forecasted). Underlying result before tax is 1% weaker than consensus. The main weakness is within the retail banking operations and US insurance operations, although this partly (approx. 50%) seems to be driven by items with a one-off character. Net interest margin for the bank against expectations further increased to 1.47%, and is guided to remain around 140bps for the next few quarters. Interest income is clearly ahead of forecasts (€3,514m vs. €3,128m estimated).

JPMorgan raised 111.1 billion yen ($1.33 billion) from the first sale of Samurai bonds by a U.S. bank since the collapse of Lehman Brothers Holdings Inc. in 2008. The second-biggest U.S. lender sold 76.9 billion yen of five-year, 1.05 percent bonds priced to yield 25 basis points more than the yen swap rate, according to data compiled by Bloomberg. It also sold 34.2 billion yen of similar-maturity floating-rate notes yielding 40 basis points more than the three-month London interbank offered rate for yen. JPMorgan has also revealed it is midway through a five-year plan to reduce its foreign exchange trading platforms from 10 to 2 by using more efficient IT systems. The upshot: annual cost savings of US$300m by 2014 and the elimination or redeployment of up to 3,000 jobs.

Santander announces that is has sold shares representing 1.9% of the share capital of Banco Santander - Chile, for a total consideration of USD 291 million. This transaction generates a capital gain for Banco Santander of approximately Euro 110 million, entirely accounted for as reserves. Following the transaction, Banco Santander holds a 75% stake in the share capital of Banco Santander - Chile.

The Australian banking sector was caught by surprise last week by news that ratings agency Moody's Investors Service had placed the big four banks on review for a possible downgrade and restated its negative outlook on them. The global ratings agency has indicated that the ratings of the big four banks would be placed on review for downgrade, warning that the reliance on international wholesale funding markets raises the long-term risks for the banks.

Australia & New Zealand Bank reported underlying profit of circa $1.4bn, Pre-provision profit $2.3bn, Revenues $4.2bn, 2% sequential growth, Lending growth 2% sequentially (In line), Net interest margin (excluding Markets) "small increase" sequentially, Neutral revenue / expense jaws sequentially (FX adjusted), Bad debt charge $294mn, estimated 31bp charge including $35mn provision for natural disasters, Tier 1 ratio remains strong at 10.3%.

Zurich Financial Services / Santander : ZFS is buying a stake in Santander's Latin American insurance unit for $1.67bn (51%). The two companies are forming a long-term alliance. ZFS will pay mostly in cash and will use hybrid debt as well. The deal should be closed in Q1 2012. ZFS says deal is cash flow positive and has almost no impact on solvency and is consistant with their strategy. Santander will book a $1.21bn capital gain, which will strengthen its capital position. Deal looks like being done at 1.8x book (2.8x tangible) - the business does generate a 22% return on net tangible assets. We view this as positive for ING which has significant operations in the region..

Financial Infrastructure

Australian Stock Exchange : In a move to make the proposed ASX-SGX merger more palatable to the various Australian stakeholders, Singapore Stock Exchange and ASX last Tuesday announced some changes to the Board structure and spelled out some key commitments - in line with market expectations. These changes, combined with the other M&A activities among global exchanges, should increase the probability of the deal's success.The ASX-SGX Limited Board will now have 13 directors (5 Singaporeans + 5 Australians + 3 international) compared with the earlier structure of 15 directors (11 SGX + 4 ASX). The three international directors (including CEO Magnus Bocker) will at least initially come from SGX, giving it majority control of the board. Other key commitments were spelled out: (1) Key ASX staff will remain in Australia, (2) ASX-related clearing and settlement will be done locally and (3) annual capex of S$30 mn for Australia was committed. The deal timeline could stretch into 3Q 2011, with key approvals needed from Australia's Foreign Investment Review Board (FIRB), Australia's Treasurer, Parliament and ASX/SGX shareholders.

ASX reported a 1H11 normalised net profit after tax of $175.5mn, up 3% on previous comparable period (pcp) and ahead of consensus at $168.1mn. ASX declared a fully franked interim dividend per share of 90.2cps, up 1% on pcp, but in line with its 90% payout ratio policy. Revenues were $3mn ahead of expectations while costs were $1mn lower. The main upside surprise from revenues was in Listings where we assume that the IPOs were more profitable than expected. Little new was mentioned on the merger beyond the announcement detailed above about the new governance structure. Management has pointed to strength in primary markets overshadowing cash equity markets (up 1% on pcp) in the first 6 weeks of 2011. In addition, futures market activity has maintained its strong growth trajectory (up 15% on pcp). On a broader basis, the CEO pointed to stronger growth data emerging for the US and some European economies which should provide a healthier short term global growth outlook reflected in buoyant equity markets. While we see this result as slightly better than expectations, we see share price performance as contingent on developments relating to the proposed merger with SGX.

Dividend Paying Companies

Hutchison Whampoa : based on more financial data released by Hutch on Monday, it's now generally estimate that the NAV accretion from a listing of HPH Trust (HK/Guangdong port assets) will be HK$7-9/share if the listing can achieve a 5-6% dividend yield. This compares with previous expectations of HK$3/share accretion. With Hutchison's acquisition appetite seemingly now revived, we think more asset divestitures are possible this year in order to fund these ventures, thus unlocking value in the process.

Syngenta – We met Mike Mack, Syngenta's CEO, last week in Toronto and had a chance to clarify some of the key investment thesis points. He believes the company is well positioned to take advantage of the strengthening trend in the agricultural commodities space as farmers across the globe are more inclined to invest in better yielding technology. A lot of the upside potential is coming from the emerging countries space, mainly Latin American and Asian, where most of the growers are still catching up with the technology advances.

Syngenta is the largest agribusiness in the world, with a global distribution platform second to none, in the CEO's view with leading edge crop protection and seeds technology, and as a result is likely to benefit from the strong 2011 expected demand. The company's full year results announcement also revealed an ambitious internal merger project which is meant to leverage the company's commercial, R&D and corporate capabilities across both crop protection and seeds businesses. The company has made significant technology advances in seeds, now holding top quality germaplasm and key biotechnology traits, being the first to market corn seeds with ethanol production enhancing traits as well as corn with drought tolerance enhancements. Yield-wise, the company's corn hybrids are, in the CEO's view, as good or better when compared with the market leaders Monsanto and Pioneer (DuPont). These technology advances in seeds re-position the company allowing it to target significant market share gains in the increasingly technicized seeds markets. In this context the merger of the seeds and crop protection businesses makes perfect sense. At the commercial level, the seeds business is expected to leverage the company's well performing crop protection distribution channels, especially as the seeds related technical knowledge is being transferred to the crop protection salespeople. At the research and development level, the union of the two businesses is expected to nurse ever better performing technologies in an integrated crop management context. The process itself is not entirely new to the company as the internal merger has already been prototyped in key markets such as Brazil and Italy and allowed technological breakthroughs. In Brazil, through the cooperation of crop protection and seeds people, the company was able to perfect a new sugar cane planting technology, Plene, which is expected to bring as much as $500 million of potential new sales. The company's pipeline is very strong with peak sales of both seeds and crop protection products of $2.7bn for the two key crops of corn and soybean. All in, a highly informational meeting, providing a good feel for the strategic direction of the company and straight forward talk around main challenges.

ABB – announced solid fourth quarter and full year results last week, with some of the later cycle businesses such as the Power Systems showing clear signs of recovery. Sales in the last quarter of the year were 5% higher, while orders increased by 18% at constant exchange rates. Orders increase was supported by an increase in base orders (below $50 mm), which is an encouraging sign for the business climate and is also positively impacting company's profitability as base orders tend to carry better margins compared to large projects. The company managed to deliver an earnings before interest and taxes (EBIT) margin well within the EBIT margin target corridor of 11% to 16%, at 13.1%, as significant price pressures, in particular in the area of Power Products (transformers and switchgear), were more than offset by successful cost take-outs, to the tune of $1.5bn dollars in the fiscal 2010. Over the 2009 and 2010 fiscal year the company managed to deliver $3bn of cost savings and more than $1bn is targeted in 2011, mainly through improved productivity and better working capital management, better sourcing and improved footprint. The company reviewed a number of significant M&A completed or announced in 2010, amounting to about $6.5n spent, including the acquisition of Ventyx, the smart grid software maker, an increase to 75% of its stake in ABB India, as well as the acquisition of Baldor, the leading US electric motors manufacturer, emphasising the strategic fit of each of this deals. Showing confidence in the state of the company and the business environment going forward, the management announced an increase in dividend to $0.6 Swiss francs per share from $0.51 Swiss francs per share, equivalent to a 54% payout ratio. Due to a recent change in Swiss regulations, the company is able to make the dividend payment while minimizing the withholding taxes.

BHP – In line with the buoyant minerals markets, BHP interim results for the fiscal 2011 showed significant improvement in the underlying earnings before interest and taxes (EBIT), up by 74% to $14.8bn, while the cash flow generation also improved dramatically to $12.2bn, up 123%. The company announced a $0.46 per share dividend, up 10%, while at the same time expanded its share buy-back program by $10bn, which at the current valuation would amount to about 4.5% of the outstanding shares. Monday the company announced the acquisition of the Chesapeake Energy Corporation's Fayetteville shale gas assets for a $4.75bn consideration in cash. The acquisition is consistent with the group's policy of adding top tier (large, low cost, long life) assets to its roster of existing businesses, while at the same time increasing the company's exposure to the energy sector. Following the acquisition, BHP would control the second largest set of assets in the booming US shale gas business, a good complement, in our view, to the company's existing deep water Gulf of Mexico fields.

Nestle – announced Q4 and full year results largely in line with the expectations, reporting organic sales growth of 6.2% or 1.9% on as reported terms, the difference being largely due to the strong appreciation of the Swiss franc. The earnings before interest and tax (EBIT) margin improved 30 basis points to 13.4%, just short of the expectations of a 40 basis points improvement. The company reiterated its Nestle model target for 2011 (which is organic top-line growth of 5-6% and continuous EBIT margin improvement) and increased its dividend to 1.85 Swiss francs per share from 1.60 Swiss francs per share, ahead of the expectations of a 1.76 Swiss franc per share. The management however did not announce a new share buy-back program, as expected, leaving some to speculate that Nestle might initiate some significant M&A with the cash from the Alcon deal.

Schindler – full 2010 year results were mildly behind the consensus expectations, with elevators and escalator (E&E) orders up by 4.3%, while the E&E revenues were 1.1% lower. The company's profitability improved, with the earnings before interest and tax (EBIT) higher by 1.9% compared to last year and an EBIT margin of 12%. The strong Swiss franc impacted negatively the net result, subtracting some 35 mm Swiss franc from the bottom line. Most analyst found the company's outlook for 2011 to be unexpectedly conservative, as the company signals a relatively weak environment for its elevators and escalators business including increased materials costs, pricing pressures and foreign exchange headwinds. Schindler announced a 3 Swiss francs per share dividend, including the 2 Swiss francs per share ordinary dividend as well as a 1 Swiss franc per share exceptional payment.

Wesfarmers – the Australian retail to coal giant, announced a very strong set of results for the first half of its 2011 fiscal year, with eight of the nine divisions reporting improved return on capital compared to the previous comparable period, lead by the successful continuation of the turnaround at Coles, the grocery chain, as well as by exceptional profitability in its coal business, despite production interruptions caused by the heavy rains. Operating revenue at group level improved by 5.8% to over A$28bn, while group's earnings before interest and tax (EBIT) moved higher by 24%. The operational strength was translated into robust cash generation, with a cash realization of 120%. As a result, the capital expenditure program increased by over 11%, while the interim dividend moved 18% higher to $0.65 per share, fully franked.

Economic Activity, Consumer and Business Conditions

US – A rather disappointing retail sales report stateside revealed that retail sales grew only 0.3% month on month in January, compared to expectations of a 0.6% increase. Excluding sales of vehicles, the retail sales were up by 0.3% as well compared to expectations of a 0.5% increase. The consumer picture was however improved today by a Consumer Confidence report by the Conference Board, showing an increase to the 70.4 level, the highest level in three years, exceeding by far, the expectation of a 64.5 reading and almost 6 points higher than the 64.8 January number.

Mildly encouraging signs came through from the construction sector, with the building permits annualized value moving higher to 562,000 units, broadly in line with expectations, in January, while the actual housing starts moved to 596,000 units, 67,000 units higher than in December and 56,000 units ahead of the expectations. The S&P/Case-Shiller index for the 20 US metropolitan areas retreated 2.4% in December, worse than the expectations of a 1.8% reduction. The reduction in price is blamed on an expected increase in the housing supply, as a new wave of foreclosures is expected to hit the market.

On the inflation front, both headline consumer price index (CPI) and the core CPI (excluding food and energy) are inching higher, at 1.6% and 1.0% year on year in January, under the pressure of the raw materials price increases. The industrial production report disappointed, as the US industrial production retreated 0.1% in January, against a 0.8% improvement in December and an expectation of a 0.5% advance. The capacity utilization inched higher to 76.1% from 76.0%, short of the expected 76.3% level.

Canada – Inflation on this side of the boarder continues to stay within benign level with the headline value relatively stable at 2.3% year on year in January, compared to 2.4% in December and expectations for a 2.3% level, while the core reading (excluding the most volatile series) inched lower to 1.4% year on year.

Retail sales in Canada disappointed at the headline level, down 0.2% in December compared to the month prior, largely affected by a pull-back in the sales of motor vehicles. Excluding vehicle sales the retail sales were actually up 0.6% in December, pretty much in line with expectations.

Financial Conditions

According to the US Mortgage Bankers Association, the mortgage delinquency rate dropped to a 2-year low of 8.22% in Q4 from 9.13% in Q3, which suggests homeowners' finances are getting back into order. Even those who have fallen behind by 90 days or more are declining. Mortgage foreclosures, however, offset this positive development as the number of mortgages in that state rose to 4.63% from 4.39% in Q3, matching the record high in 2010 Q2. However, in the third quarter, a number of banks suspended their foreclosures due to possible administrative errors, then restarted the program in Q4, so this could reflect the backlog.

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 2.80% and the U.K.'s 2 year/10 year treasury spread is 2.19% - 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 (22 in 2011) compared to 157 in 2010 which was the highest annual tally since 1992 (140 in 2009). 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 at 5.00% - (the lowest rate since the Federal Reserve began tracking rates in 1971 was 4.17% on Nov. 11, 2010), as the Federal Reserve effectively continues to seek to incentivise home ownership. Existing U.S. housing inventory has increased to 8.1 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 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 16.43 and 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

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Sources: Thomson Reuters; Macquarie Securities - Global Financials Daily (EFSF, Barclays, Spanish banks, SEB, CBK, AMBR, CGL, BEZ,CS/Coco's, AAPH, TARP, CME, OMX, JPM, RDN, Schwabb, ASX/SGX, PICC, IAG, QBE, Asia Banks) – email dated Tuesday, February 15.

Global Financials Daily (ECB, UCG, ZFS, SAN, MAP, ING, ARL, JYSKE, NZ quake, ALPHA, NBG, RBS, DB1, UBS, ICE, WIBC, PMI, H&R, Indian Banks, CGF, SUN, BKK, SIAM, China) – email dated Tuesday, February 22

BMO Capital Markets, Economic Research- U.S. Mortgage Delinquencies (Q4), Philly Fed (Feb.), Leading Index (Jan.)- email dated February 17, 2011

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