



News Highlights on Current Holdings

Financial Services Companies

Barclays: A US bankruptcy court judge has ruled that Barclays' purchase of Lehman Brothers' US broker-dealer in 2008 was fair and should not be revisited. This is material good news. Worst fears had suggested \$11bn of liability for Barclays (i.e. giving assets back that they had thought they acquired in the Lehmans transaction) which would have been c55p a share of value. Whilst that was a worst case, Judge Peck did agree with the Lehman Trustee that Barclays took some assets that were not part of the deal, believed to be in the order of £2.6bn (c16p a share) against which they have already taken a £600m provision .. within this amount approx \$1.9bn was held in a 'clearance box' held by Depository Trust & Clearing Corporation to which the Judge has ruled Barclays remains entitled – net from which it is understood Barclay's probably stands to relinquish up to US\$2.5 bn. The Financial Times reported that 'Barclays, pleased by the decision, had no comment on what it might owe.'

Bank of America: In a move that does not affect Bank of America Corporation's current or previously reported consolidated financial results and capital positions, the company has amended previously filed call reports for 2009 and 2010 for its FIA Card Services, N.A. (FIA) subsidiary. FIA is the legal entity that includes Bank of America's credit card operations. The restatement, which resulted from changes to processes covering legal entities implemented in 2010, covers eight quarterly periods of 2009 and 2010, and is in call reports filed with the Office of the Comptroller of the Currency and the FDIC this month. The restatement involves a non-cash, non-tax deductible charge related to a \$20.3 billion goodwill impairment at FIA, which has now been recorded for that legal entity for the first half of 2009. The goodwill writedown was caused by deteriorating credit quality and the adverse impact from The CARD Act on Bank of America's credit card operations in 2009. Included in the amended call reports was the reversal of a \$10.4 billion writedown of goodwill taken at FIA during 2010.

CI reported Q4/10 earnings per share of \$0.32 versus consensus of \$0.31. EBITDA was \$178 million (excluding stock option expenses and a one-time gain of \$3.7 million), helped mainly by better cost controls. CI did have net outflows during the quarter of roughly \$92 million, the first quarterly net outflow since Q4/08 although it seems reasonable to expect it will experience a reasonably solid RRSP season in terms of net inflows. The quarterly results indicate that CI purchased

Hartford for roughly \$95 million (net of \$20 million tax benefit) and should generate roughly \$20 million in EBITDA from the acquired operations. CI's flows should benefit from improved distribution access through the Hartford acquisition. CI did raise the dividend 7.0%, the second increase in two quarters and the fourth increase in two years, a sign, we believe, of continuing management confidence.

Credit Agricole, France's third largest bank, had a narrower than estimated 4Q loss as earnings at the investment banking business helped cushion provisions for bad loans at its Greek unit.

Eaton Vance reported January quarter EPS of \$0.45, excluding valuation adjustments to non-controlling interest, vs consensus of \$0.44. The valuation charge was \$21.8mn (\$0.15) and an unexpected investment loss hurt GAAP EPS by an additional \$0.03. Revenue and operating income were \$4-5mn above expectations. Along with previously reported AUM of \$191.7bn, reported inflows of \$1.8bn represent 4% annualized organic growth, easing as expected from 7% in the previous quarter. Long term funds had inflows of \$1.2bn, including -\$0.8bn of deleveraging, and separate accounts had net inflows of \$0.6bn. Inflows to floating rate (\$1.4bn) and alternative (\$0.8bn) strategies accounted for nearly all of the net inflows. Operating margin decreased 1.9% to 33.0%, reflecting a 6% sequential increase in operating expenses, driven by additional marketing expenditure and seasonal compensation as expected.

St James' Place PBT of £84.2m ahead of consensus of £80.7m. The cash element of the result was £48.3m, which compares to £23.5m in 2009 and an estimate range of £34.4m-£46m. The dividend has been increased 33% to 6p. The EEV per share was 352.9p ahead of our estimate of 326p and marginally ahead of consensus of 348p. We see the strong 2010 results as reflecting a year where business conditions were substantially improved and the underlying performance of the company has been confirmed with a strong bounce back. The outstanding indicator to us was the new business result for 4Q 2010 because it was to be compared to a record 4Q result in 2009. This suggests there is scope for the group to meet its long term growth targets in 2011 despite setting the bar at record levels through 2011. The commentary on the Retail Distribution Review is also likely to settle nerves about the risks from the RDR changes. The intention to rebase the dividend is set out clearly with a good increase in 2010 in place already.

Unicredit - Libyan risk, the Libyan State controls 7.6% of UniCredit (5.0% through the Central Bank of Libya; 2.6% through the Libyan Investment Authority). Libya is a long-term shareholder of UniCredit and act as a quasi-Sovereign fund;



historically, it has been supportive of the Foundations and Mediobanca, which together control 16% of UniCredit. The limited visibility on the future of the Libyan stake might act as a drag on the stock, although we are not expecting any imminent change in the shareholders' structure of UniCredit due to the Libyan crisis. UniCredit recently gained a banking licence in Libya. We believe that the exposure is not material. Total claims of Italian banks to Libya were USD19m. Total claims of European banks to Libya were USD950m, of which USD539m was UK (BIS quarterly review, June 2010). CEO Mr Ghizzoni said yesterday he is not concerned about the Libyan risk.

Royal bank of Scotland Group missed consensus analyst estimates as losses from Ireland rose and profit from investment banking fell. The group posted a net loss of £1.1bn for last year, down from £3.6bn in 2009, fuelled by a sharp fall in loan impairments, a faster than expected reduction of non-core assets and a revival in its core retail and commercial businesses. RBS will proceed with the sale of £1.6bn of unwanted legacy loans in commercial real estate. The decision comes as the bank prepares to announce in full-year results this week that disposals from its remaining £150bn of non-core banking business remain on track. RBS has asked some private equity groups to sign a non-disclosure agreement to open the process to bids for the £1.6bn of legacy loans, including Lone Star, Starwood Capital and Blackstone. Separately, RBS is facing criticism from its largest rivals by offering to undercut insurance quotes they issue to business customers.

Financial Infrastructure

Dividend Paying Companies

Bayer – announced fourth quarter and full 2010 fiscal year results in Leverkusen, Germany, Monday, broadly meeting street's expectations on the underlying metrics; while the outlook for 2011 was mixed, rather cautious in the pharma business and more up-beat in the crop science and materials science businesses. Group sales were up 13% for the year, supported by a very strong bounce back in the materials science (plastics and foams) business up 30% for the year. The materials science was also a key profitability contributor, its EBITDA margin moving 750 bps higher, not enough though to offset a drop in profitability at healthcare, EBITDA margin down 190 bps, and crop science, EBITDA margin down 420 bps, due to intense price pressure. The company has recently undergone a CEO change, with the M&A maverick Marjin Dekkers replacing Werner Wenning. Dekkers launched a cost cuts program,

including significant job cuts, trying to offset the loss in revenue of some of Bayer's key franchise drugs such as Betaferon (multiple sclerosis) under pressure from Novartis' Gyleneia oral pill or Yasmin (women's health) threatened by generics. The company's blockbuster drug to be, Xarelto (blood thinning) is expected to improve the company's top line starting with 2012; the €2+ bn revenue target was re-iterated. Contrary to most people's expectations, given Dekkers' background, the newly appointed CEO stated that a transformational M&A transaction would be an 'extreme option', as some speculated on a potential spun-off of the materials science business. The company guided for a 4-6% revenue growth in 2011, followed by a 5% growth in 2012, as business conditions are expected to be favourable in the materials science business and robust in the crop science area. The company's 2011 full year EIBTDA is expected to improve towards the €7.5 bn level from €7.1 bn and potentially reach €8 bn in 2012.

Economic Activity, Consumer and Business Conditions

US – Mixed signals coming out of the US housing sector once again. After a reduction in the S&P/Case-Shiller housing price index last week, the pending home sales dropped 2.8% in January, hinting at weak existing home sales for the next couple of months. However, in the month of January, the existing home sales sold at a rate of 5.36 million units annual rate, ahead of the expectations of a 5.24 million units annual rate. The new home sales level for January flirted with historical lows again as the 284 thousand units annual rate came short of the expected 310 thousand units level.

Better employment environment expectations, somewhat reflected by a slow improvement in the level of initial jobless claims, at the 391,000 level for the last week, down 21,000, helped improve the Consumer Sentiment, as measured by the University of Michigan. The final reading for February was 77.5, significantly higher than January's 74.2 level and the expected 75.3 level, supported largely by an improvement in the current conditions component, up to 86.9 from 81.8, although the expectations component also improved, up to 71.6 from 69.3.

The manufacturing sector seems to be suffering recently, as the durable goods orders report showed a 3.5% drop in January, as significant slow-down in capital goods orders, such as general machinery, computer and communications equipment all took a tumble in the month.



The US personal income report indicate a strong 1.0% improvement in the level of personal income January, a key determinant of the fate of the all important US consumer sector. However, the personal consumer expenditure inched higher by only 0.2%, weaker than expected, as the savings rate moved higher to 5.8% from 5.4%. Part of the same report, the core (excluding food and energy) personal consumer expenditure (PCE) price index, was indicated at a stable 0.8% year on year rate of change. This key inflation measure, the Fed's most trusted gage, is currently sitting at a historical low and is providing no incentive the country's regulators to reign in monetary stimulus.

US consumer confidence rose to a three-year high in February. The Conference Board, an industry group, said its index of consumer attitudes rose to 70.4 in February from a revised 64.8 in January as consumers felt more optimistic about the economy and their income prospects. It was the highest level since February 2008 and better than the reading of 65 that analysts had expected.

Canada – The one key economic report issued in Canada this week, the GDP by industry report, showed a 3.3% fourth quarter GDP growth, helped largely by the consumer sector and the improvement in the net exports. The December month alone, at a rate of growth of 0.5%, came significantly ahead of the consensus expectations, at 0.3%, boding well for the first quarter of the new year.

Financial Conditions

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 2.72% and the U.K.'s 2 year/10 year treasury spread is 2.20% - 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 (23 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 4.95% - (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 7.6 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 18.63 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>.



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Market Commentary



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Macquarie Securities - Global Financials Daily (Barclays, CBK, EU RE, STJ, RSL, UCG, G, SWED, LSE, TMX, G, GART, TNN, AMBR, BAC, ZION, NZ Quake, Korean banks, Chinese banks, IAG, SIAM, BKK) – email dated February 23, 2011

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