Market Commentary

PORTLAND INVESTMENT COUNSEL™

May 23, 2011

News Highlights on Current Holdings

Financial Services Companies

Aviva: results driven by non-life business with premiums up 14% and a 5% combined ratio improvement down to 97%. On the life side new business volumes were disappointing with a decline of 14% to £8.8bn however the IRR was positive up to 13.1% from 11.3%. Weakness in life was reasonably broad based with only Asia (+4% YoY) delivering positive growth in life and pension new business volumes. While there are a variety of reasons for the weakness (eg, tough prior year comparatives in some parts of Europe, increased competition from banks looking to boost deposits), mostly, it was due to management actions which reduced with-profit sales by 39% YoY (with notable declines in France and Italy). It also reduced shareholding in Delta Lloyd from 58% to 43%. In our view the group seems on track to meet the group's near-term financial targets...its trading at an attractively valued 0.76x Embedded Value, 0.9x IFRS book, 7.8x '11 EPS and 6.2% yield.

Aviva will launch an internet-only UK motor insurance brand in the summer in a move widely seen as a way to secure a presence on highly competitive price comparison websites after the expected sale of RAC, its roadside rescue division.

Blackrock has bought back $2.5bn of stock from Bank America for $187.65 per share, issuing debt to do so. Barclays still owns 3m ordinary shares & 34.5m prefs. worth approx £4.6bn.

Credit Agricole has "very limited" exposure to Greek, Irish and Portuguese government debt according to CEO Jean-Paul Chifflet in an interview in Investir Le Journal. The bank has Eur805mln in Portugal, EUR631mln in Greece and Eur77mln in Ireland he said. Credit Agricole is offering €1.76 for the remaining 8% of Emporiki's shares it doesn't own. This is a 38% premium to yesterday's closing price, which values Emporiki c.EUR900m. The cash-out for CASA is c.EUR70m or 0.02% of Core Tier 1 capital. The deal has virtually no impact on earnings. Presumably by owning 100% of Emporiki Credit Agricole has greater flexibility in the accounting and remedial measures that need to be taken to address its Greek subsidiary.

Goldman Sachs : has shuffled the senior ranks of its investment banking arm as it works through rebuilding its reputation with regulators and politicians. It has appointed Richard Gnodde a London banker who has spent 8 years in Asia, as co-head of the investment banking division....reflecting Goldman's push to enhance their presence outside the US.

HSBC plans to add at least 200 staff in China annually through 2016, and expand its Singapore workforce by about 1,000 people as wealth migrates there from Malaysia, Indonesia, the Philippines and China, said Peter Wong, chief executive officer for the Asia-Pacific region.

Santander: Santander Brazil Chairman, Fabio Barbosa, has stated the bank will increase lending to Small & Medium Enterprises in a bid to improve margins, according to Bloomberg. The bank will target growth in SME lending of 25% in 2011, versus a total loan growth target of c.15% (SME lending represents c.23% of Santander Brazil's loan book). The bank will also focus on real-estate and credit-card lending. The Spanish banks have previously stated that margins in Latin America are under pressure due to increased competition.

Sarasin stock trading up significantly after CEO says that the Rabobank controlled Swiss Private bank has held talks about a management buy-out. The price being discussed is SFR 3bn which would still gives 20% upside from the current level. The Financial Times states that serious talks have also been held with Julius Baer however a management buyout is now believed the most likely option.

Dividend Paying Companies

Nestle – is reported to have paid an estimated $1.1bn for Prometheus Laboratories, a gastrointestinal diagnostics company with an expected turnover of $250 million in 2012. Nestle said that the company hoped that the acquisition would provide a boost to its own nutrition research. It is also likely that the company would benefit by using Prometheus' distribution network to promote its existing hospital nutrition products, such as Peptamen and Novasource. Conditions that Prometheus technology helped diagnose include the irritable bowel disease, Chron's disease and ulcerative colitis.

Carrefour – held a two day analyst event in Paris last week in which it detailed its plans for the spin-off of Dia, as well as the shelving of a plan to spin-off some of its property. Some analysts expected a profit warning with the same occasion, which fortunately did not materialize. The company's CEO, Lars Olofsson, defended the decision to part ways with James McCann, the former executive director for France, as the group's French operations exhibited like for like market share declines over the last several months which obviously needs to be turned around. Dia, the group's hard discount business, was responsible for €231mm of earnings before interest and taxes (EBIT), or 8% of the group EBIT, and delivered an attractive 27% pre-tax return on common equity. Meanwhile, the Carrefour Planet trial stores have seen encouraging results, with the rollout of the new hypermarket concept set to happen over the next couple of years. The management maintained its guidance of an improvement in sales and profit for the year.

Carrefour is rumoured to be in talks with Grupo Pao de Acucar in Brazil, to merge to the two retailers' hypermarket and supermarket Brazilian operations. Such a merger would result in a combined market share of around 28%roughly three times larger than the size of Wal-Mart's Brazilian operations. The move would benefit both parties with estimated cost savings as high as $1bn. Carrefour is in the process of strengthening its Brazilian operations, after last year revelation of mismanagement and accounting irregularities, while Pao de Acucar has recently suffered an erosion in margins after entering the home appliances business. However, Carrefour's French arch-rival, the publicly listed Casino, who controls 35% of Pao de Acucar is said to be opposing such a merger, at least for the time being.

BHP – is the first deep sea drilling operator to receive approval to explore for oil in the Gulf of Mexico after last year's BP accident. BHP's plan include a proposed deepwater well about 4,500 feet under water and about 124 miles off the coast of Louisiana.

Siemens – An arbitration court ordered Siemens to pay €648million to Areva as a result of the company's exit from a nuclear joint venture and the subsequent entry into a nuclear alliance with Rosatom of Russia. Siemens tried to overturn a non-competition clause with prevented the company for eight years by appealing to the European Commission. While the EU is still investigating the case, the arbitration court reduced the effect of the non-compete clause to four years, which would be effectively running until September 15, 2013. Siemens had already recognized a profit of €1.52bn as a result of the sale of its stake to Areva. The €648mm payment will be recognized on the company's third quarter financial statements.

National Grid's full year 31st March 10/11 EPS beat expectations by 4%, with performance driven mainly by a £433m swing from an under-recovery of regulated revenues to a modest over-recovery, partly due to weather. Adjusted earnings per share was 51.7p up 4% versus 49.5p the previous year. These timing benefits will unwind during the current year . Full year dividend per share of 36.37p is as expected. Underlying performance in the US is improving and we continue to believe that an Return on Equity of c9% could be achieved this year. The reported ROE of 8.2% (+130bps) excludes the impact of the recently announced $200m pa efficiency targets or a full year benefit from rate cases. Management continue to execute on strategy with improving US returns their key priority.

Telefónica reported slightly disappointing 1Q11 results that were in line with anaemic 1Q11 peer reporting . Brazil was again the top performer, whilst Spain positively showed stability. German and UK revenue growth was encouraging albeit arguably disappointing relative to expectations whilst Mexico and German showed the impact of competitive pressure. 1Q11 revenue of €15,435m was 1% below consensus. Net Income of €1,624m was 11% below consensus. Basic EPS of €0.36 similarly was 10% below consensus. Brazil was again the star performer of all Telefonica's businesses. 1Q11 revenue of €3,515m was in line with consensus which included outperformance by the wireless business (Vivo). The wireline (Telesp) business suffered moderately from the impact of Sao Paolo floods. Spain's 1Q11 domestic revenue of €4,372m was a touch above consensus estimates of €4,350m but this came at a margin cost. Domestic revenue has been underwritten by a margin investment and this is unlikely to change in the coming quarters. UK service revenue growth of 3.6% was disappointing but moderately better than the weak 1Q11 service revenue growth of 0.4% from the French competitor 'Everything Everywhere', highlighting the troubled UK consumer and resultant revenue pressures within European mobile. More positively 151k contract customers in UK were added in the quarter with 76k pre pay contract losses. German revenue of €1,228m was in line with expectations with 308k net wireless adds in the quarter with the majority contract customers (206k) notwithstanding Smartphone competitive pressures. LatAm revenue of €7,006m was below consensus estimate of €7,262m. This was largely driven by weak performance in Mexico with 1Q11 revenue of €417m 20% below expectations, driven by weak performance in the pre pay segment. We believe the benefit of Telefónica's investments will show through more clearly by end 2011 and that operational performance, especially the scale of contract customer additions in Brazil, Germany and UK, is a reason for optimism, in our view. Key to this view will be Brazil's growth and integration synergies, margin support in UK and Germany and signs of a sustainable recovery in Spain.

Economic Activity, Consumer and Business Conditions

IMF: European finance ministers for the first time floated the idea of talks with bondholders over extending Greece's debt-repayment schedule, saying that last year's 110 billion-euro ($156 billion) rescue has failed to restore the country to financial health. However HAngela Merkel, German chancellor, has spelt out her strong opposition to restructuring debt in any member state of the eurozone, contradicting speculation that Germany was pushing such a solution in Greece. Subsequently, the rating agency Fitch has downgraded Greece to B+ with negative outlook also saying extending maturity of existing bonds would be considered a default. From recent announcements it seems that Greece is required and / or motivated to accelerate sales of assets as part of a deal and has appointed to 9 banks to manage the sale of state assets and real estate. They aim to raise at least EUR 50bn to pay down debt

Australian Banks: Moody's downgraded its credit rating on Australia's four largest banks (Commonwealth, Westpac, ANZ, NAB) from Aa1 to Aa2 citing reliance on overseas debt markets.

The Federal Reserve wants to subject US banks to annual stress tests, reserving the right to veto dividend payouts if they do not pass. A draft of the new rule is expected to be released within weeks according to the Financial Times. Stress Tests were introduced in 2009 and repeated earlier this year to enable some banks to increase their dividends and initiate share buy backs.... and so to ensure 'robust risk management systems' are maintained it seems likely these tests will become an annual event as part of bank's capital deployment and regulatory requirements.

Five of the UK's top banks are backing a £2.5bn pound fund launched last Thursday to invest in Small and Medium Enterprises that are struggling to attract financing. The Business Growth Fund which will target businesses with an annual turnover of £10mn to £100mn - follows the "Project Merlin" deal between Britain and its banks. Project Merlin, which involved Barclays, HSBC RBS and Lloyds, would see top banks lend about £190bn to business this year, up from about £179bn.

US – Surprising signs of weakness in the manufacturing sector south of the border put under the question the strength of the economic recovery. The industrial production index, reported last week, posted a disappointing 0% growth, compared with expectations of a 0.4% month on month improvement and a 0.7% improvement the month prior. The main culprit was the motor vehicles production, but consumer goods and business equipment production also retreated in the month. The capacity utilization inched lower to 76.9%, from 77.0% in March, falling short of expectations for an improvement to the 77.6% level. Unfortunately, the outlook does not look a lot better either, with the US leading economic indicators index retreating by 0.3% in the month, compared with expectations for a 0.1% month on month improvement and a 0.7% improvement in the month of March.

A dismal picture was being drawn by a host of housing indicators released last week in US. The National Association of Home Builders Housing Index remained flat at a very depressed level of 16, short of expectations for a mild improvement to 17. The only component that improved was the traffic of prospective buyers, inching to 14 from 13. The index, which is normally hovering around 60, has been providing sub 20 readings for most of the last four years. The US housing starts missed expectations of a 568,000 units annual rate, at just 523,000 units annual rate, while the building permits were also lower than expected, at 551,000 units annual rate compared to 585,000 units annual rate. The existing home sales retreated to a 5.05 million units annual rate, from 5.09 million units annual rate and compared to expectations of 5.20 million units annual rate. The only ray of light came from the new home sales announcement, earlier today, indicating an improvement to 323,000 units annual rate, albeit very close to historical lows.

Canada – Inflation held steady in Canada in the month of April, tempering the need for short term rate hikes in the immediate future. The core consumer price index (CPI) year on year rate of changed clocked in at 3.3%, broadly in line with expectations for a 3.4% figure, while the core CPI (stripped of eight of the most volatile price categories, including food and energy) came in line with the expectations at 1.6%. The consumer however took a step back in March, with headline retail sales flat month on month, way short of expectations for a 0.9% increase, while the retail sales excluding vehicles actually retreated 0.1% in the month, which we believe goes to show that sometimes even the threat of higher interest rates is enough to temper over-stretching. It remains to be seen how many times the Bank of Canada can 'cry wolf' without losing its credibility.

Financial Conditions

PMI Data The Euro area Purchasing managers' Index data for May came out much weaker than expected. The Euro area manufacturing PMI fell to 54.9 in May, down sharply from 58, consensus was 57.5. The details were also poor with new orders falling from 57.4 to 53.8. With inventories up the new order minus inventories series fell to 4.6 from 8.5 (the third monthly decline in a row), signalling more downside to come for the headline series in the months ahead. The weakness was also broadbased, with the output, new export orders, order backlog and employment components all down. The Euro area services PMI also fell, dropping to 55.4 from 56.7. The business expectations component -- which has some leading indicator qualities -- fell to 63.9 from 66.1.

IMF: Dominique Strauss-Kahn has resigned as Chief of the IMF saying he does not want to damage the institution by remaining in place. He is also protesting his innocence. According to the Financial Times the French Finance Minister Christine Lagarde is favourite to assume the top job.

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 2.63 % and the U.K.'s 2 year/10 year treasury spread is 2.39 % - 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 (44 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 4.61 % - (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 again increased to 9.2 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 would be 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 18.27 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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Martin Pommier - Global Financials Daily (UK Banks, EU Capital, DB1, SAN, RBS, Nordic Banks, Spain, JPM, AIG, AEL, Japan, Philippines, AIA, Yuanta, Fubon, Suruga) email dated April 11, 2011

Robert Lee - IVZ: Estimate Modest Long-Term Inflows in March – email dated April 11, 2011

Thomson Reuters

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