Market Commentary

PORTLAND
INVESTMENT COUNSEL™

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News Highlights on Current Holdings

Financial Services Companies

AMP – In Australia Minister Shorten introduced one more piece to the long list of super reform legislation. The "Superannuation Guarantee (Administration) Amendment Bill 2011 ", which proposes to increase the SG contribution rate to 12% from the current 9%. Whilst both expected and yet to be ratified by Parliament, it is a potential positive at a time when negative news on investment markets, the global economic back drop and regulatory reforms continues to dominate the landscape. The proposal is to increase the rate gradually with initial increments of 0.25% on 1 July 2013 and 1 July 2014. Further increments of 0.5% will apply annually up to 2019-20, when a 12% mandatory contribution rate is achieved. It also seeks to remove the age limit on contributions from mid 2013. Measured today, a 3pt increase in SG would add about $20bn in annual flows to the Superannuation market. AMP has about 5% share of the national Super market including AXA so, equates to an estimated $1bn increase in flows at 3% and $3-5m more in after tax profits. The longer term NPV impact is estimated at 3-4% positive.

Barclays, JPMorgan and Credit Agricole have been chosen by the EFSF to lead-manage its next issue.

Bank of America became the latest US bank to scrap plans for a debit card fee, acting after worries that customers of the second-largest US bank by deposits would move their accounts. BofA said its U-turn was a "response to customer feedback and the changing competitive marketplace". Analysts had worried that BofA could see deposits shift to other banks, denying it a source of liquidity strength. After a fierce reaction from the public and politicians, most large banks have said they will not make up for the profit hit with a debit card fee on consumers. Wells Fargo said last week that it was cancelling a pilot scheme to test a $3-a-month charge. JPMorgan Chase and Citigroup have also decided against a charge.

BNP Paribas : after adjusting for €2,257m impairments on Greek Govt bonds, €786m +ve Debt Value Adjustments, a €362m loss on the disposal of sovereign bonds and a €299m impairment on a stake in AXA, BNPP pre-tax 3Q profit reached €3,080m approx 6% above expectations. After factoring in the estimated tax impact on the one-offs, the underlying profit is estimated at €1,858m, or a Return on tangible equity of 13.1%.

Going forward, BNP has to absorb both the costs associated with the deleverage plan (€0.75bn recurring and €1.2bn one-offs) and with the reduction of the sovereign bonds portfolio. As the proceeds are utilized to reduce short term funding or increase central bank deposits, revenues in treasury operations would decrease. But BNP still achieves an estimated 11% ROTE, even after taking into account the ongoing deleveraging plan and a marked increase in provisions (deteriorated macro-economic outlook) and trades at an attractive 0.6x Tangible Book Value.

Credit Suisse 3Q11 results: Outside of CHF1.3bn of own debt gains which analysts had in their estimates the Investment Bank results were flattered by CHF538m of debit valuation adjustments. Stripping these out then the IB misses consensus by almost 20%. Costs also significantly higher. (-CHF5,697m). The positives include gross margins holding up ok and they saw CHF7bn of net new money… the group now claims it now counts 35% of the world's richest as its clients – up from 25% in 2008. They have also raised their restructuring savings from CHF1bn to CHF2bn through '2012/'13 and will reduce Fixed Income, Currency and Commodities risk weighted assets by 50% by 2014. Overall then a poor revenue quarter but some positive developments on restructuring. Credit Suisse has announced 1,500 jobs – about 3 per cent of global headcount – will be eliminated, on top of 2,000 job cuts announced in July. Nonetheless, the CEO, Brady Dougan was clear about Credit Suisse's purpose: to be an " integrated, client-focused, capital-efficient business model'.

ING Groep said it plans to cut 11% of the jobs at its Dutch bank and posted third-quarter earnings that surpassed analysts' estimates. The job cuts will help reduce costs by €300mn by 2014, the Amsterdam-based firm said in a statement today. Underlying pretax profit at ING's banking operations fell 29% to €1.06bn after a write-down on Greek sovereign debt.

LLOYDS - The Board of Lloyds Banking Group announces that following medical advice Antonio Horta-Osorio is taking a temporary leave of absence from his duties as Group Chief Executive of the bank due to illness. Antonio is expected to return to his position before the end of the year. Tim Tookey – the outgoing CFO is to be interim CEO.

National Australia Bank (NAB) / Australia & New Zealand Bank (ANZ) : ANZ became the third of the major banks to pass on last Tuesday's central bank rate cut in full, reducing its interest rates on variable rate mortgages by 0.25% on 14 November to 7.55%. However, NAB cut its standard variable home loan interest rate by less than its peers and the central bank, saying that it would cut its standard variable rate by 20bp to 7.47% per cent, from 7 November. Subsequently, Acting Prime Minister Wayne Swan stated that NAB was "greedy" for not passing on in full an interest rate cut by the Reserve Bank of Australia. He said as exit fees on new mortgages have been abolished in response to government measures, “NAB customers have the choice to walk down the road and get a better deal”.

National Australia Bank’s forthcoming issue of a covered bond has been given an initial AAA-credit rating as the bank is set to become the first Australian lender to tap funding markets with the new form of financing.

Royal Bank of Scotland Group operating profit Q3 of £267m, in line with expectations. Core business operating profit Q3 of £1,264m, in line with forecast £1,253m. Income was 4% better than expected, with Global Banking & Markets beating very low expectations. However, this includes “Portfolio mgt” gains which must be of questionable quality. Non-core run-off broadly in line with expectations, but still not generating capital. RWAs down £6.8bn at a loss of £997m – i.e. a loss rate of pre-tax 15%. Tangible NAV per share 52.6p against 50.2p forecast, bolstered by benefit of Fair Value adjustments. The shares are now trading on 0.45x 2011e tangible book .

Sarasin : Julius Baer raised its offer for the stake in Bank Sarasin held by Rabobank, SonntagsZeitung reported. Julius Baer has changed its offer for Rabobank’s 46.1% stake in Sarasin to cash only from the previous mixed offering. Rabobank will decide by the end of November which offer to accept. Swiss Raffeisen Group are also said to be interested in buying a stake in Sarasin from Rabobank.

Standard Chartered published its Interim Management Statement last week. Relative to what was expected, income looks weaker (mainly Wholesale Banking) and likely down on the 1H11 run-rate, which is more than offset by better costs and impairments, so consensus PBT for 2011 (U$6.8bn) looks fine. The company is still committed to double-digit income growth for the year (which counts on a good 4Q), and is confirming guidance of double digit income & PBT growth and flat JAWs for the full year. Although income growth is the main theme for Standard Chartered we do not think that a slowdown is a surprise in the face of a global macro slowdown. Consumer Banking continues to perform well while cost-income jaws in Wholesale Banking unsurprisingly turned negative.

Financial Infrastructure

CME reported third quarter EPS of $4.74, $0.09 above expectations —upside was driven by better than expected expense control (management reduced guidance on this front as well). This quarter’s results were marked by robust growth in clearing/transaction fees given the strong volume backdrop during the quarter—we continue to see the company as a primary beneficiary of macro volatility and continued uncertainty. Expense control was a highlight of the quarter. Also noteworthy, CME more meaningfully re-engaged on share buyback this quarter ($155 million in repurchases or 21% of the authorization announced in May) and OTC clearing initiatives appear to be ramping up ($44 Bn in 3Q with over $35 Bn cleared in October alone).

Total revenues of $874 million were up 19% yr/yr and up 4% from second quarter levels whereas Operating expenses of $302 million (+5% yr/yr, -1% qtr/qtr) were lower than estimated and drove most of the beat. Operating margins improved to at 65% this quarter. Tax rate was in line. Average share count declined slightly as the company began to engage on its repurchase program. Management updated its expense guidance and indicated it now expects full year operating expenses of between $1.230 and $1.235 billion, below their prior single point guidance of $1.235 billion. At September 30th, the company held $876 million of cash and short-term investments on its balance sheet, up from last quarter and in excess of management’s stated desire to maintain at least $700 million in cash. Outstanding debt held steady at $2.1 billion, implying a current debt-to-EBITDA ratio of 0.83x. During the quarter, CME Group repurchased $155 million of stock (590,000 shares). It is estimated that CME currently has $530 million remaining under its share repurchase program—we expect return of capital to accelerate over the next few quarters now that the company has reached its target leverage ratio of less than 1.0x and cash continues to build.

NYSE Euronext/Deutsche Borse - Speaking following their Q311 results last Thursday CEO, Duncan Niederauer, expressed confidence in the proposed tie-up with Deutsche Borse, and dismissed some regulators’ concerns about vertical integration as “idealistic”. But he also said he would abandon the deal if authorities blocked a substantial portion of it. NYX delivered a modest beat to 3Q11 consensus estimates on strong expense management and a lower tax rate.

Thomson Reuters 3Q11 adjusted EPS of $0.56 was $0.02 above consensus. Revenue from ongoing operations of $3.26bn was up 8% YoY, or 5% in constant currency. Underlying EBIT margin from ongoing operations of 22.0% was 80bp above expectations, driving the better than expected performance. Thomson Reuters continues to forecast mid-single digit revenue growth, at least 100bp of underlying operating margin expansion, at least 300bp of adjusted EBITDA margin expansion, and 20-25% free cash flow growth. During 3Q and through October, it spent $325mn to repurchase 10.8mn shares

(1% of outstanding shares). This was the first share repurchase since 2008. The program authorizes another 4.2mn shares.

Dividend Paying Companies

ABB – held a capital markets day last week, setting ambitious targets for the group and its operating divisions as part of a new five year plan. The company set an organic sales compound annual growth rate target of 7% to 10%. For the near future the company does not see a deep recession as imminent, although it did flag a possible slowdown over the next 12 to 18 months. Longer term, the higher than GDP rate of growth is predicated on higher demand for green technologies and the need to hook up renewable energy generation to smarter grids. The group's target for earnings before interest, taxes, depreciation and amortization has also been raised to fit in a 13% to 19% corridor. By division, most growth is expected to be realized in discrete automation and motion, as well as in power systems, while profitability is expected to stay high in low voltage products, discrete automation and motion and power products. Profitability would be considerably helped by cost cutting programs, as pricing pressures continue to be a reality for the industry. For 2012 alone the company targets $1bn in cost savings.

In term of use of capital, the company expressed its preference for acquisitions, to fill gaps in areas such as programmable logic controllers, followed by dividend payments and lastly share buy-backs.

BHP – announced the investment of $2.1bn, its share in a $4.2bn investment in a couple of large metallurgical coal mining projects. One of the projects, the Caval Ridge Mine, would add 5.5 million tons of metallurgical coal export capacity (BHP's share 2.75 million tons). The neighbouring Peak Downs Mine will expand production by 2.5 million tons a year, for a total of 8 million tons of metallurgical coal export capacity (BHP's share 4 million tons). The capacity could be further expanded to 10 million tons with little additional costs (subject to a separate approval). The expected resource life of the initial project is greater than 60 years. The investment will include the construction of a new coal handling and preparation plant at the Caval Ridge. Production is expected to be initiated during the calendar 2014.

GEA Group – the German engineering group leading the food processing technology announced a robust Q3 set of results, exceeding the consensus expectations by a significant margin. Order intake in the quarter was solid, higher by 11.4% on like for like basis, particularly strong in Process Engineering and Farm Technologies. Sales of €1.4bn were 24% higher on year on year basis, while earnings before interest and tax (EBIT) reached €131mm, 41% higher on year on year basis. Group's EBIT margin reached 10%, ahead of the consensus 9.5% target, helped by the operating leverage in the Process Engineering and Farm Technology businesses as well as by cost savings in the Heat Exchangers and Farm Technology divisions. Outlook for the full year was re-iterated, with orders targeted in the range of €5.4bn to €5.6bn, sales of €5.1bn to €5.3bn and an EBIT margin of 9.3% to 9.5% (excluding the newly acquired Convenience Food Technologies division, which is expected to have a margin of 8.5% to 9.5%).

Syngenta – announced that the Ministry of Agriculture in Argentina approved its triple corn stack trait, which had already been approved in Brazil and which will be available to Argentinean farmers starting with the 2012/2013 season. The trait combines herbicide tolerance and insect resistance, incorporating the company's industry leading Agrisure Viptera lepidopteran insects control, including the fall army worm, sugarcane borer and corn earworm.

Vivendi – announced in Warsaw that its pay-TV unit Canal+ and TVN SA of Poland will merge their pay-TV units in Poland, with Canal+ acquiring a stake in TVN, forming a strategic partnership. The terms of the agreement include the acquisition by the Canal+ of a minority stake in ITI, the parent company of TVN SA as well as the right for Canal+ to acquire the remaining part of a controlling stake from ITI. The combined entity will have a subscriber base of more than 2.5mm people.

Economic Activity, Consumer and Business Conditions

United States – US economic outlook turned sour once more following a string of decent business activity and manufacturing indicators readings, as both the manufacturing purchasing managers index (PMI) and the non-manufacturing PMI as maintained by the Institute for Supply Management (ISM) had lower readings than previously and were short of the expectations. The manufacturing PMI, at 50.8 in October, retreated from September's 51.6 level and was disappointingly short compared to expectations for a 52.0 level, still indicating expansion, but only barely so. Similarly, the non-manufacturing PMI inched lower to 52.9, from 53.0 in September and short of the expectations for a 53.5 reading.

The other piece of macro-economic news drawing attention last week was the employment report, which revealed 80,000 non-farm payroll additions in October, short of the 95,000 expected, but previous months' upward revisions, as well as a decent 104,000 private-sector payrolls additions were positive indicators. The unemployment rate dropped one tenth, to 9.0%, a positive surprise given expectations for a flat 9.1% reading.

US productivity moved higher in the third quarter by 3.1%, exceeding expectations for a 2.8% improvement and more than offsetting a second quarter 0.7% drop. Not surprisingly, also given a weak real personal income progression, the labour costs in the US dropped a significant 2.4% in the third quarter supporting the profitability of corporate America.

Canada – the employment report on this side of the boarder was more disappointing as the Canadian economy lost 54,000 jobs in October, compared to a 60,900 jobs addition in September and expectations for 12,200 more jobs. Worryingly, full time jobs dropped by over 70,000, with a key detractor being the private sector. Manufacturing and the construction sectors were the most affected. The unemployment rate unexpectedly moved higher in the month to 7.3% from 7.1%.

Greece - Last night, Prime Minister George Papandreou and opposition leader Antonis Samaras agreed to form a national unity government, with Prime Minister Papandreou stepping down to make way for an interim premier. The two leaders postponed making an announcement until today, with frontrunners including Lucas Papademos, a former vice-president of the ECB, and Stavros Dimas, a former European Commissioner. No date has been set for an election, which Mr Papandreou said should be held early next year. The Financial Times reports the statement was expected to reassure markets & Greece's international lenders that they are committed to carrying out fiscal and structural reform. European finance ministers, including Greece's Mr Venizelos, are due to discuss further the political chaos in Athens, today. Oil Rehn, EU Commissioner for economic affairs made clear that any new government would need to demonstrate that it had broad political backing for both the new bail-out programme and the debt reduction scheme in order for the EU to release rescue loans.

Italy – the Financial Times reports that Italian PM, Mr Berlusconi, is under intense external pressure to end months of procrastination over structural reforms and measures to cut Italy's €1,900bn ($2,600bn) public debt. A delegation from the European Commission is expected in Rome on Wednesday to monitor Italy's progress, and David Lipton, deputy head of the International Monetary Fund, is preparing to be in Rome next Monday. Mr Berlusconi is fighting to avoid his government being replaced by an emergency interim administration led by unelected technocrats. Throwing down his own challenge to the prime minister, Pierluigi Bersani, head of the main opposition Democratic party, said on Sunday he was considering calling a vote of no confidence in the government. Mr Berlusconi is using the threat of snap elections in January, with the prospect of a heavy defeat, to whip party rebels into line.

European Central Bank surprised markets, cutting rates 25 bps to 1.25% by unanimous decision in Mario Draghi's first meeting as ECB President. In his opening statement, Draghi highlighted financial market tensions (due to the debt crisis) and the resulting unfavourable effects on confidence and financing conditions. These factors have prompted the ECB to downgrade its outlook for growth and inflation (a new forecast will be released next month). Indeed, he noted that 2012 growth will very likely be downgraded significantly. Growth risks are deemed to have intensified on the downside, while some of those risks have materialized. The outlook remains subject to high uncertainty. Draghi said that the Euro Area is headed toward a "mild recession" by year end. On inflation, the President said that inflation is expected to remain above 2% well into 2012, but slow sharply next year to below 2%. Those expectations were a key driver of the rate cut. With respect to the Securities Market Program (SMP, the bond-buying program), Draghi said the ECB will continue the purchases in as much as they ensure the transmission of monetary policy. Considering Italian yields have risen of late, we believe that suggests that the SMP could pick up steam in order to transmit today's rate cut. He also reiterated that the program is temporary and limited, and added that the ECB cannot sustainably reduce bond yields.

Italian Austerity Measures - Berlusconi's govt late Wednesday night approved a "maxi amendment" to the stability bill which includes the commitments to raise the retirement age, ease rules on redundancies and to accelerate state asset sales.

BRICS aid - Russian President Dmitry Medvedev said yesterday "We have to help preserve one of the world's leading currencies, we are all interested in preserving the euro." The BRICS countries would contribute to Europe in line with their current voting rights at the IMF, Medvedev said. In return, they expect a bigger say at the IMF.

Financial Conditions

The Financial Stability Board (FSB) has published the full list of G-SIFI (Globally Systemically Important Financial Institutions), detailed below. As previously laid out, banks that are determined as G-SIFI will be required to have additional capital loss absorption capacity to be met by common equity of 1% to 2.5% of risk weighted assets. No detail is provided as to what amount is required by which bank. Implementation of the measures will begin from 2012 and full implementation is targeted by 2019. The list of G-SIFIs will be updated annually and published by the FSB in November.

Current list - Bank of America, Bank of China, Bank of New York Mellon, Banque Populaire CdE, Barclays; BNP Paribas; Citigroup; Commerzbank; Credit Suisse; Deutsche Bank; Dexia; Goldman Sachs; Group Crédit Agricole; HSBC; ING Bank; JP Morgan Chase; Lloyds Banking Group; Mitsubishi UFJ FG; Mizuho FG; Morgan Stanley; Nordea; Royal Bank of Scotland; Santander; Société Générale; State Street; Sumitomo Mitsui FG; UBS; Unicredit Group; Wells Fargo

At this stage it is a bit surprising that neither Standard Chartered (approx 6th biggest US$ clearer in the world), BBVA and Intesa San Paolo were not included (and so mildly positive for those banks) and conversely that Dexia, Lloyds, Commerzbank were included.

MF Global filed for bankruptcy last Monday morning, after the Federal Reserve Bank of New York as well as the major exchanges suspended dealings with the broker-primary dealer.

The European Central Bank (ECB) last Thursday announced additional details regarding the implementation of its second covered bond purchase programme. As reported by Reuters, Bankers welcomed a number of changes to the program including the fact that the minimum rating has been lowered to BBB- from AA which now only excludes Greek covered bonds. Also the minimum size has been lowered to €300mn from €500mn for the first program which will make it more flexible to support weaker issuers.

The advent of the US 'twist' means policymakers are no longer accommodating a recovery in bank profits (gained via them trading on a steep yield curve) . The U.S. 2 year/10 year treasury spread has been falling and is now 1.79 and the U.K.'s 2 year/10 year treasury spread is 1.75% - meaning investment banks will need to seek operational efficiencies, including job cuts, to maintain acceptable levels of profit – above their costs of capital.

As concerns have swung from commercial real estate and unsecured consumer loans/credit card loans to European sovereign debts the number of small U.S. banks failing continues to grow, albeit at a more moderate pace with (90 in 2011) compared to 157 in 2010 which was the highest annual tally since 1992 (140 in 2009). 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.

Influenced by the US 'twist', the U.S. 30 year mortgage market remains very low at 4.00% - albeit off its early October low of 3.94%(this is the lowest rate since the Federal Reserve began tracking rates in 1971), as the Federal Reserve effectively continues to give priority to incentivising home ownership. Existing U.S. housing inventory has steadied at 8.5 months supply of existing houses – below its recent 9.4 months high but still higher than what we believe is a more normal range of 4-7 months. While we still believe it remains premature to consider a recovery in house prices prospects of a measure of stability are likely to increases as a result of the Fed actions – which 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 and whether bank's have mis-represented the quality of those assets sold to Freddie Mac and Fannie Mae. Such legal debates are likely to drag on for years but from recent bank investor relations presentations it does seem the rate of "put backs" are now expected to decline and that litigation reserves have been increased suggesting overall current levels of total provisions should suffice, enabling banks to continue to post increasing earnings per share (as credit improves) over the next 2 years by when we expect more normalized earnings power to have returned. 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 31.78 and while, by its characteristics, the VIX will remain volatile, we believe a VIX level below 25 augurs well for quality equities.

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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