Market Commentary

PORTLAND INVESTMENT COUNSEL™

October 29, 2012

News Highlights on Current Holdings

Financial Services Companies

Australia and New Zealand - reported Underlying Profit of $6,011mn (up 6% on $5,652mn FY 2011) in line with the consensus average. Final Dividend Per Share of $0.79 (up 4% on the $0.76 pcp) was also in line with consensus. Underlying profit was driven by steady gains in ANZ's domestic operations during the second half of the year and tight cost control in the domestic business. ANZ's costs, traditionally seen as a particular challenge for the bank, were a particular highlight. The group cost-to-income ratio declined 1.1% to 45.1% in the second-half as the bank downsized its workforce by more-than 2,000 people to 48,239. Margins, however, continued to be eroded by strong competition for deposits and high wholesale funding costs. ANZ will move more jobs offshore to cheaper Asian hubs in a bid to cut costs and boost productivity. ANZ CEO Mike Smith flagged that the bank would extend its productivity agenda to offset weaker revenue growth. As part of the plan to cut its cost-to-income ratio by 2% from the current 45.1% by 2014, Mr Smith said the bank would make greater use of its "operation and technology hubs" and use more automation in some processes.

AXA: Asset management revenues: €2460m up 0.7% on last quarter, but down -6% on like-for-like (LFL) quarter. Total revenues: €68358m up +3.7%, LFL +1.3%. Net inflows: -€8bn versus -€33bn. Life & Savings: Solid growth in protection and health, unit linked marginally down as a result of changes in savings legislation in Poland, a weak environment in the UK and France and lower bancassurance sales in Italy. P&C benefitted from 2.9% rating increases with revenue growth stronger in Commercial lines at 5% compared to personal lines of 3%. International saw a flat result in Corporate Solutions with lower liability and aviation lines but was supported by continued growth in AXA Assistance in the US and France and across travel lines particularly. Asset management revenues continued to reduce on a comparative basis but net outflows were at the same level as 1st Half 2012 which suggests some progress on legacy issues. The Solvency I ratio was above 220%. The results therefore confirm our view that the non-life insurance and asset management provide a defensive component while the life business is more than ever focused on growth markets and the protection and health business, which is less sensitive to interest rates. We think that Axa's EUR1.5bn cost-cutting plan is achievable and we expect the group to continue to expand its capital base organically thanks to its solid earnings capacity and become less sensitive to external shocks. Trading around a Price /Book of 0.5X 2012 year end estimates, the stock is amongst the cheapest in the sector.

BNP - S+P last week, as expected, downgraded BNP one notch to A from AA- (Moody's at A2, Fitch A+). The Financial Times highlights that S+P cited likely house price falls of 10-15pc over the next 2-3 years, increased domestic competition, said "strenuous efforts" to reduce balance sheets is in part offset by rising economic risks and stated that the economic environment and low interest rates would put pressure on domestic revenue growth in 2013-2014.

Credit Suisse - Has put its $17.2bn European ETF business up for sale. BlackRock and State Street Global Advisors, the asset management arm of State Street Corp, are among the firms understood to have bid for the business.

Credit Suisse: reported 3Q 2012 underlying pre-tax profit of CHF1,029mn above consensus of CHF0.9bn, excluding -CHF1.0bn Fair Value of Own Debt impacts, CHF382mn real estate gains, CHF144mn restructuring charges and CHF140mn gain from the final sale of the Aberdeen stake. The underlying beat against consensus was driven by a strong investment banking result from both improved cost control and good Fixed Income, Currency and Commodities revenues, but a disappointing result in the flagship wealth management division. Wealth Management struggled with both inflows and gross margins (down 6bp as average Assets under Management balances were boosted in September and the mix of Assets under Management continues to favor lower margin business in Ultra High Net Worth Individuals and Asia). However, there appear to be positive signs for the future: Credit Suisse has announced additional cost savings and has boosted guidance on capital (12% Basel 3 Core Tier 1 by end-2013 before dividend). If achieved, we believe Credit Suisse could not only return to a cash dividend for 2013 (paid in 2014), but also increase the payout.

Lloyds - The Financial Times reported that Lloyds is examining whether to ditch the concept of annual bonuses for senior staff and extend the timeframe of longer-term incentives to up to 10 years. The idea is being put to investors as Lloyds seeks to avoid the conflict seen between banks and shareholders over pay.

National Australia Bank: has raised its provisions to deal with the impact of an economic downturn by $250mn, a move that will negatively impact its full year earnings. NAB said low levels of consumer and business confidence had reduced the outlook for economic growth in 2013, while conditions in the United Kingdom had further deteriorated in the last three months. In response, the bank said, it had increased the economic cycle adjustment on its collective provisions by $250mn, or $175mn after tax, as of September 30. The increase in collective provisions will be reported in NAB's cash earnings for its fiscal 2012 year, which ended on 30 September.

Nordea - Bloomberg reports that Sweden's Social Democrats are signaling they are open to selling the state's 13.5% stake in Nordea, marking a shift away from the party's previous opposition to the government's planned divestment. " Nordea's 3rd Quarter 2012 net profit dropped 16% QoQ to €688m and missed expectations by ~8%. This comes on back of 2% revenue miss (Net interest income & trading), 1% higher costs (FX, €15m head office cost) and also due to higher Loan Loss Coverage due to higher generic reserves, regulatory charges in Denmark & sticky shipping. Non Performing Loan (NPL) ratio climbed 0.1% QoQ to 1.9% and coverage slipped 1.2% to 41%. Non Performing Loan growth accelerates further to +38% YoY vs. +31% in 2nd Quarter with absolute Non Performing Loans now +€1.4bn since YE11 (reserves only +€0.3bn). Capital formation was stronger at 40bp to 12.2% Basel II Core Tier 1 despite higher loan volumes (+1% on FX) but lower risk weights (RWA/loans drops 1% to 50.7%).

Royal Bank of Canada: is acquiring the Canadian auto finance and deposit business of Ally Financial Inc. for $1.4 billion net of excess capital. Including the excess capital, RY will pay a total consideration of $3.1 to $3.8 billion, depending on the size of the dividend taken out by the seller (74% owned by US Treasury) prior to closing. The acquisition is expected to close in the first calendar quarter of 2013 and will be financed with cash. The acquisition includes $11.5 billion in auto loan receivables and $3.8 billion in deposits. Ally Financial Canada is a leading Canadian auto finance business that offers inventory financing to more than 580 auto dealerships and its consumer business offers retail financing to Canadian consumers through approximately 1,600 dealerships and has approximately 450,000 consumer loans. The net investment of $1.4 billion includes a premium to book value of $0.6 billion, implying a rather high price of Price-to-Book Value of 1.75x. RBC expects the transaction to be modestly accretive with the Ally Canada business expected to generate approximately $120 million or $0.08 per share in net income on a standalone basis in the first 12 months after closing before integration costs, amortization of intangibles and transaction costs. Integration costs, amortization of intangibles and transaction costs expected to be $50 million in 2013. The acquisition will position RBC as the leader in auto financing in Canada with approximately $24 billion in receivables.

Royal Bank of Scotland - The U.K.'s biggest building society, Nationwide, is considering bidding for the 316 RBS branches up for sale according to the Sunday Times. Virgin Money has already expressed an interest in the business as has JC Flowers, the American private equity firm that has started to dabble in Britain's banking industry. Separately, the Wall Street Journal picks up on the speculation that the UK government is placing pressure on RBS to sell the US operation, Citizens…but we continue to believe that unlikely in the near future given its sub-cycle return on equity.

Santander: Q3 Recurring net earnings (before Real Estate clean-up and positive one-offs) at €1.2bn in line with consensus. However the bank has increased significantly its real estate provisions this quarter (€2.2bn) bringing reported earnings to €100mn, in line with 2Q 2012. Revenues were somewhat weaker dragged by lower Net Interest Income in Brazil – albeit the UK came in better than expected thanks to sharply lower costs. Costs were 2% higher than consensus expected on further expansion in Latin America. No let up in asset quality deterioration, with Group Non Performing Loan ratio rising from 4.11% to 4.33%. But capital ratio improved - up from 10.1% to 10.4%, which includes the benefit of the Mexican IPO.

Swedbank: reported solid SEK3.5bn profits (+11% QoQ, +1% YoY) beating consensus by 6/7% for a 16.3% Return on Net Asset Value. The beat was driven by 2% better revenues (due to better trading) with Net interest margin (average loans) only down 0.02% and a 5% beat on costs as Swedbank is ahead of its 2012 target to cut SEK1bn costs (i.e. SEK 937mn YTD). Loan growth was ~2% ahead of expectations due to more resilient SME/corporate volumes while deposits were up 13% QoQ. Asset quality trends remained benign with Non Performing Loans down 0.20% to 1.4%, with stable loss reserve coverage at 65%. Its capital ratios are very strong: 17.3% Basel II core Tier 1 capital and 14.5% Basel III core Tier 1 capital and deposit inflows improved Loan/ Deposit ratio to 198%.

TD Bank: Target Corp., the second-largest U.S. discount retailer, agreed to sell its $5.9 billion credit card portfolio to TD Bank Group. The portfolio will be sold for an amount equal to the gross value of the outstanding receivables at the time of closing, Minneapolis-based Target said last week in a statement. TD also agreed to a seven-year deal to underwrite, fund and own the retailer's future credit card and Visa receivables in the U.S., the companies said. Target suspended the sale of the credit-card portfolio in January after it had been unable to find a buyer for a year. Subject to the receipt of regulatory approvals and satisfaction of other customary closing conditions, this transaction is expected to close in the first half of calendar 2013. TD expects its Tier 1 capital ratio to decrease by approximately 0.2% on closing, on a pro forma basis as at TD's last quarter ending July 31, 2012, and its common equity tier 1 ratio to decrease by approximately 0.14% under Basel III on a fully phased in basis. In addition, TD expects the portfolio to produce a return on assets of approximately 1% in the first year. The transaction will be funded with available resources.

UBS/Credit Suisse job cuts - Der Sonntag said that UBS & Credit Suisse are set to announce further large job cuts. UBS are set to cut a further 3000 to 5000 jobs, 900 in IT alongside a further 2-4,000 layoffs in the investment bank and other central functions. Credit Suisse may cut 1,000 to 2,000 jobs.

Wells Fargo increased its stock buyback program by 200 million shares, valued at about $6.9 billion, while also declaring its regular 22-cent quarterly dividend, unchanged from the previous period.

Dividend Payers

ABB – The Swiss electrical engineering firm reported third quarter profit, which, at $759mm, was mildly below the consensus expectations of $764mm of net income. The management expressed caution about the coming months, as the euro zone crisis and slow down in other major economies caused a fall in orders intake in the third quarter. Orders fell 5% in the quarter, to $9.3Bn, dragged down by a 64% slump in Germany and 39% in India, which more than offset a 13% rise in the United States and a steady level in China. It should be emphasized though that part of the order growth in the US is due to the acquisition of Thomas&Betts, earlier this year, absent which, orders would've fallen even lower. The group's activities are supported by a solid order backlog, covering more than nine months of sales. The weakness in orders intake is seen as the result of tougher competition on prices and weak demand as clients have been postponing big capital expenditure projects and governments have been implementing austerity measures. The company's CEO, Joe Hogan, said that beyond the current economic turbulence, there are still good long-term prospects built on rising demand for energy efficiency and urbanization.

Carnival Corp – reached an agreement for the construction of two new cruise ships, a 99,000-ton/ 2,660 passenger ship for its Holland America Line and a 135,000-ton/4,000 passenger ship for its Carnival Cruise

Lines brand. The total cost for the two vessels combined will be approximately $195,000 per lower berth. Both ships will be a new class of vessel for their respective ship-lines. Carnival Corp, which is the largest cruise vacation group in the world, with a portfolio of cruise brands in North America, Europe, Australia and Asia, has currently nine new ships scheduled for delivery, spread evenly over the 2013-2016 period. The introduction of new ships has been strategically timed to allow time for the cruise brands to grow their passenger base and absorb the new capacity while minimizing revenue yield dilution in the remainder of their existing fleets.

Chemring – replaced its chief executive David Price last week, which was perceived by many as a sign that the proposed takeover of the company by the US private equity group Carlyle has a very small chance of happening. The new CEO is Mark Papworth, a former executive at oil industry services company, John Wood Group Plc, where he was credited with leading a successful turnaround, improving manufacturing capabilities and substantially improving profitability. The company, which makes defence equipment such as flares and explosive device detectors, is bracing for lower defence spending in the United States and Europe as governments try to rein in budget deficits. While we have no particular insight in the Carlyle takeover deal, we continue to believe that, at 6.5x 2013 earnings, the company is valued attractively and also believe that the relatively lower cost of its products, compared to the value of equipment and human lives they help protect, should provide it with a more solid footing even in a lower defence spending scenario.

Novartis – reported third quarter results which, at $1.34 earnings per share, were in line with the consensus expectations, as growth of new products in its key pharma division offset the loss in sales and profitability driven by patent loss of Diovan. The company kept its guidance unchanged: sales in-line with 2011, with core group margins slightly below. Growth of the new pharma products was led by: Galvus (diabetes) up 20% to annualized sales approaching $1Bn, Gilenya, the multiple sclerosis pill, up 116%, to $316mm, Tasigna (leukemia) with sales up 49% to $261mm and Afinitor (breast cancer), with sales up 82% to $261mm. Sandoz, the company's generics drug division, suffered a 13% decline as sales of its generic enoxaparin (Sanofi's brand name Lovenox) in US dropped following the expiry of its exclusivity. Outside the US Sandoz sales grew at double digit rates, 11% in Europe, 21% in Emerging Markets, 17% in Latin America, 16% in Russia, ahead of the market rates of growth. In the company's Consumer Health division, manufacturing woes continued at its Lincoln, Nebraska, facilities, which remain shut down in order to remediate quality issues.

Schindler Holdings – the leading elevators and escalators (E&E) Swiss engineering company announced its third quarter results last week, which were broadly in line with the consensus expectations. The order intake amounted to CHF2.2Bn, 4.8% higher year on year at constant currency rates, while earnings before interest and tax (EBIT) reached CHF259mm. The top line was driven primarily by the new installation business in growth markets, as the new product introductions, the 5500 commercial elevator and 3600 China affordable housing elevator rollout is on track and receiving a very positive customer response. The E&E business EBIT margin of 12.8% is higher by 0.3% year on year, supported by the successful execution of LEAP, the group's performance improvement programme launched in Q4 of 2011, offset by significant pricing and cost pressures. Geographically, Asia Pacific made the strongest contribution to order growth, followed by North, Central and South America, while a slight order increase was also noted in Europe. The company's full-year guidance of net profit before minorities of around SFr700mm remained unchanged and is seen as conservative. Management re-confirmed the extension of its share buy-back program to repurchase an additional 9.5% of nominal capital by end of 2015.

Syngenta – announced Friday it had partnered with Novozymes in an exclusive global marketing and distribution agreement to commercialize Taegro®, a fermented biological fungicide based on a naturally occurring bacterium. The product offers growers broad-spectrum disease control at very low application rates in a variety of crops. Its multiple modes of action make it highly complementary to Syngenta's extensive fungicide portfolio. Financial details about the agreement were not disclosed.

Vivendi – The credit rating agency Standard&Poor's affirmed Vivendi's BBB credit rating with a negative outlook, as it believes the management is committed to preserving the current credit rating on the group. The agency also said that, in the event of a business reshuffle, Vivendi would adjust its financial risk profile to balance any erosion in its business risk profile.

Wesfarmers – provided a trade update for the first quarter of its fiscal 2013, which revealed a stronger than expected like-for-like sales at its flagship retail operation, the Coles supermarkets. A long-running price war, which has seen Coles and Woolworths, together controlling over 70% of the grocery market, slash the cost of basic items such as food, milk and meat, is seen as the main reason for increased foot traffic and sales volumes. Woolworths like-for-like sales growth was only 2.3% over the same period. The food and liquor price deflation was 3.2% in the first quarter. The price war is also a consequence of consumer retrenchment, as Australians are coping with economic uncertainty and falling home and equities market values. Other retail divisions performed well, with Bunnings, the home improvement store chain posting 2.5% like-for-like sales growth, while Kmart, the deep discount retailer posted a 2.2% like for like increase. Turn-around at the department store Target continues, as the process got reset by the departure of chief executive Launa Inman's departure to Billabong. The stores reported a 4.1% like-for-like reduction in sales, blamed chiefly on the timing of a toy sale promotion, which arrived earlier this year. The group's coal mining businesses have been hit by a reduction in pricing of its commodities as demand from China slowed down, at the same time it has implemented measures to increase its mining output. The mining division agreed to a 26% reduction in the quarterly re-set price of metallurgical/coking coal, down to $160 per tonne.

Economic Activity, Consumer and Business Conditions

US – A better than expected third quarter output (GDP) reading for the US economy, up 2% annualized, failed to excite investors when it was reported, on Friday. The consensus expectations were leading towards a 1.9% annualized rate of growth for the US economy in the third quarter. Contributing to the growth in the quarter were the consumer sector, which representing over 70% of the economy added 1.4%, the fixed residential investment (read housing), which added 0.3% and, surprisingly, the government spending, which was a net contributor for the first time in nine quarters, pulling in a material 0.7% given its relatively modest size relative to the size of the economy. Detractors of economic performance in the quarter were business investment, inventories and net exports, each with a roughly 0.15% negative performance. Final sales in the third quarter, which excludes the effects of the inventory build-up in GDP formation, where higher by 2.1%, ahead of the consensus.

Also, last week, business activity indicators, notably durable goods orders, seemed a bit more encouraging, as manufacturing was able to offset in September some of the 13.1% drop in August. Durable goods orders were up 9.9% in the month, exceeding expectations for a 7.1% improvement. The core reading, which excludes the effect of the highly volatile transportation orders, showed improvement as well, to the tune of 2.0% in September, ahead of the consensus expectations calling for a 0.8% advance. Growth was driven by a 9.2% improvement in general machinery, while other capital goods orders such as computers and electronics and electrical equipment suffered. Motor vehicle and parts and electrical appliances orders also retreated in September.

The US housing sector continues to show improvement, with the new home sales in September improving to a 389,000 units annualized, ahead of the consensus of 385,000 units annualized and August's 368,000 units annualized level. This level represents a two and a half year high and led to a months' supply rate of 4.5. However, even at 389,000 units annualized level, sales are significantly below a normalized 30 year level of over 730,000 units. Pending home sales, which are a leading indicator of existing home sales, failed to meet expectations in September, with a 0.3% increase barely moving the needle and following a revised 2.6% drop in August.

Canada – The Canadian retail update for the month of August in Canada was largely in-line with the expectations, as the headline reading advanced by 0.3%, while the core, which excludes sales of auto vehicles and fuel, moved higher by 0.4%. Gas sales advanced by 2.9% and were a key growth driver in the month, while the core categories were led by sales of sporting goods and general merchandise. Sales of clothing products, building products and furniture were on the weak side in the month of August.

UK GDP grew 1% in 3rd quarter its strongest gain in 5yrs which beat expectations and was largely due to an extra public holiday and the boost from the Olympic Games.

Financial Conditions

US – UK: US Federal Reserve policymakers remain determined to flatten the yield curve as much as possible, having indicated they expect 'exceptionally low levels of interest rates through 2015 which is still an "exceptionally low level" in the grand scheme of things. Fed Reserve Chairman Ben Bernanke has indicated 1% or less would be considered exceptionally low. The extension of the US 'twist' (whereby the Federal Reserve is selling 3 year and less maturities to buy 6 years and longer) means all parts of the yield curve will benefit from a near-zero anchor until mid to late 2014. The U.S. 2 year/10 year treasury spread is now 1.41 % and the U.K.'s 2 year/10 year treasury spread is 1.57 % - meaning investment banks can no longer profit from a steep yield curve and instead are seeking operational efficiencies, including job cuts and lower compensation, to maintain acceptable levels of profit, i.e. above their costs of capital. It seems the top tier 8-10 investment banks will continue to command their market and possibly increase their share – as barriers to entry for newcomers have in our view been raised.

Influenced by the US 'twist', the U.S. 30 year mortgage market remains very low at 3.41% - (3.36% early October 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 is at 5.9 months supply of existing houses. So the combined effects of record low mortgage rates, near record high affordability, a more promising economic recovery, job creation, and low prices are finally supporting the housing market with housing inventory well off its peak of 9.4 months and we believe now in 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 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 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 beginning 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 18 – 24 months 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.

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 47 in 2012 (compared to 95 in 2011 and 157 in 2010 which was the highest annual tally since 1992). Franchises are being acquired/absorbed as convergence of the financial services industry accelerates – favouring we believe the stronger, better managed banks..

The VIX (volatility index) is 17.81 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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