



## News Highlights on Current Holdings

### Financial Services Companies

Bank of America is to charge a \$5 monthly fee for debit card purchases.... U.S. Senator Dick Durbin ( who lead the implementation of the regulatory changes to debit card fees which has now caused the banks to increase charges) released the following unsurprising statement on Friday: "It seems that old habits die hard for Bank of America. After years of raking in excess profits off an unfair and anti-competitive interchange system, Bank of America is trying to find new ways to pad their profits by sticking it to its customers. It's overt, unfair and I hope their customers have the final say."

Credit Agricole France's third largest bank by market capitalization has announced a reduction in financing needs to boost capital following a credit rating downgrade. Credit Agricole - has been under funding pressure since end of June 2010, with a decline of €3.6bn short term funding from US sources, including €8.4bn from US money markets. Liquidity reserves have fallen by €10bn since the end of 2010, and are currently at about €10bn. Adjusting its business plan to this funding pressure, Credit Agricole has announced a €5-52bn reduction in financing needs (33% Corporate & Investment Bank, 20% Specialised Financial Services, 47% retail), through a mix of deleveraging (CIB, SFS) and access to alternative sources of funding (SFS, deposits in retail). Credit Agricole is working on cost reductions to offset the negative revenue effect of the change in plan, with ultimately the goal of a neutral impact on earnings. There is no change of Core Tier 1 target at Group level (9% fully loaded in 2013).

HSBC has approached Prudential, Bupa, Allianz, AXA and Zurich to gauge interest on a sale of their Global General Insurance unit according to the Morning Post, Japanese insurer MSIG would also be an interested bidder according to the article.

ING is looking to sell its 36% stake in Brazil's SulAmerica in deal that may be valued at about \$1 billion according to the Financial Times. Axa and Tokio Marine are interested bidders according to the article.

Lloyds Bank - The Financial Times reported last week that NBNK have tabled a formal bid for the 632 Lloyds branches put up for sale by the bank under EU state aid rules. NBNK, the banking venture set up by Lord Levene, is thought to have offered about £1.5bn, somewhat lower than the £2bn rumoured.

Intesa Sanpaolo - could avoid tapping the wholesale funding market for the next two years if market conditions continue to deteriorate, CEO Corrado Passera said in an interview with Affari e Finanza last week.

Royal Bank of Scotland/Santander - Santander may buy more than 300 branches from RBS for about £100m less than the price originally agreed, Sky News reported, without citing sources.

Santander: Gazeta Wyborcza has reported that Santander has made a preliminary offer for KBC's Polish business, citing two people it didn't name. KBC will decide within two weeks whether to accept the bid or to invite other offers the paper states, according to Bloomberg. Such a deal would lift Santander to 3rd in terms of market share in Poland. Also, according to El Confidencial, Santander will sell up to €bn of foreclosed real estate assets in an effort to further clean up its balance sheet. The bank, which hired Spanish financial consultants, MaC Group, in May to value the assets, will also sell a portfolio of bad loans for €bn.

Standard Chartered – CEO Peter Sands, at a news conference in Hong Kong last Friday, said the mood in Asia is confident and buoyant, Asian fundamentals are still strong. The crisis in Europe will slow economic growth in Asia, not stall it.

### Financial Infrastructure Companies

ICAP: Pre-close trading update. Trading in line with revenues to be marginally ahead. ICAP is seen as a beneficiary of the very strong trading in August. The group saw strong performance in rates in August. There has been a shift of volume to Emerging Markets. The Singapore office has been rebuilt with an encouraging statement on current trading. ICAP has agreed to co-invest in the iSwap platform in the interest rate swap market with Barclays Capital, Deutsche Bank, JP Morgan and Bank of America Merrill Lynch. This is subject to regulatory approvals but (1) increases the likelihood of adoption, usage and growth for the platform whilst (2) changing the economics for ICAP. The second of these factors will become clear once the co-investment is finalised.

### Dividend Paying Companies

Carrefour – Announced results from Carrefour Planet stores which were ahead of expectations, with four pilot stores seeing a 13% increase in customer numbers, which drove the revenues numbers higher by 14%. The Carrefour Planet, a revamping of its core hypermarket concept, is the company's answer to declining hypermarket business in developed Europe. The group is on target to having 50 Carrefour Planet conversion completed



by the end of the month, in France, Belgium and Spain. The newer stores are reported to be 50% cheaper to convert as economies of scale have started to kick in. Management emphasised the particularly good performance of the new concept in Belgium.

Nestle – proceeded with changing its CFO as the current executive, the Canadian Jim Singh has reached 65 and has served the company for 35 years. Wan Ling Martello, a US citizen of Chinese and Philippine origin is set to replace him, moving over from Walmart where she oversaw the retailer's global e-commerce function in emerging markets. Her previous experience includes NCH Marketing Services, a stint at Borden Foods and 10 years with Kraft. Although she does not appear to be a high profile replacement for Singh, analysts point out at the benefits she could bring to Nestle in term of providing diversity (female, emerging markets heritage) and a fresh outside perspective.

Wesfarmers – Subject to regulatory approval, Wesfarmers announced the sale of its thermal coal business Premier Coal to Austar Coal Mine, a Chinese controlled entity, for \$297mm. Successful completion of the deal would lead to Wesfarmers booking \$90mm of pre-tax profit in the second half of its fiscal 2012.

## Economic Activity, Consumer and Business Conditions

The German parliament last week approved the European Financial Stability Fund amendments (to expand it to EUR 440bn) by a wide margin: 523 in favour, 85 against and 3 abstentions. The landslide win is a good sign that Germany will keep its commitment to bringing the current crisis under control and so is an important step in creating the next bailout structure.

NEW Zealand : Both Fitch and S&P have downgraded New Zealand - from AA+ to AA for LT foreign currency rating (stable) and local currency rating from AAA to AA+ (stable). It appears that the recent deterioration in the fiscal balance, a lack of household balance sheet repair, and the projected expansion of the current account deficit were triggers for the actual downgrade with S&P appearing to blame earthquake-related expenses as the trigger for a downgrade. By comparison, Australia's net external debt is around 50% of GDP (compared to NZ 70%) while the current account deficit is believed to be rapidly shrinking to -1.5% of GDP by year end. Household savings have risen and public finances are morphing from modest deficit to modest surplus within two years. None of these metrics suggest in our view there is any similar threat to Australia's AAA/Aaa ratings from the agencies.

US – News out of US revolved around the housing and the consumer sector. The new home sales continue to struggle, with August's 295,000 units annual rate still worryingly close to the all time low, a drop of 7,000 units annual rate from July. Not surprisingly, the Case-Shiller home pricing index for the 20 metropolitan areas is indicating a still weak housing pricing environment as the gage registered a 0.0% reading in July, just shy of the expected 0.1% increase and in line with the revised 0.0% reading for June. In year on year terms, the home pricing is 4.1% lower, an improvement from June's negative 4.4% level. Later in the week, the pending home sales number completed the uncertain picture with a 1.2% drop in August.

On the consumer side, as the personal income retreated 0.1% in August, against expectations for a 0.1% improvement, while the consumer confidence, as measured by the Conference Board, retreated in the month of September to a 45.4 level, against expectations for an improvement, to the 46.0 level. This reading is somewhat at odds with the other reading of the consumer sentiment, as measured by the University of Michigan, which moved higher to 59.4 from 55.7, powering through the expected 57.8 level. A clear improvement was seen in the consumer views towards the current conditions, while the consumer expectations surprised on the upside as well.

On the bright side, Thursday came with an upward revision of the US GDP Q2 result, to a 1.3% annual rate of growth, while the initial jobless claims registered a steeper than expected drop to 391,000 claims, below the now 'infamous' 400,000 threshold. The seasonal adjustment seems to have played a big role in this apparent improvement.

Finally, the core personal consumer expenditures price index, the Fed's favourite inflation gage remained steady at 1.6% in August, in a 'sweet spot' within the 1.5% to 2.0% comfort zone, providing the much needed breathing room for the mega-accommodative monetary policy.

Canada – The July GDP report revealed a 0.3% improvement, as expected, as the manufacturing and utilities sectors powered ahead. Retail trade offset some of the growth, while mining and construction bucked the recent trend, dipping slightly in the month. Of note, the economic activity in the month was not touched by the malign effects of the recent market turmoil, which was initiated in early August.

## Financial Conditions

European Sovereign Debt - European officials are understood to be working on a plan, resembling the US TARP ( Troubled Asset Relief Program), aimed at shoring up European bank stability.



October 3, 2011

The plan involves using the EFSF ( European Financial Stability Fund) to capitalize a special purpose vehicle that would be created by the European Investment Bank, a bank owned by the member states of the European Union. The special purpose vehicle would issue bonds from investors and use the proceeds to purchase sovereign debt of distressed European states. The bonds issued by the SPV could then be used as collateral for borrowing from the ECB, allowing the central bank to make loans to banks faced with liquidity shortages.

Financial Transactions Tax: The formal proposals for a financial transactions tax set the cost at 10bps for equities & bonds, with 1bp for complex derivatives. It will require approval from all 27 EU countries to be enacted, of which 4 currently oppose the plan (including the UK). The proposal will be presented at the G-20 in November. These plans to introduce a European financial-transactions tax is a “mistake,” according to the BdB Association of German Banks. “Such a tax is dangerous for European financial markets and ultimately puts at risk economic growth,” said Michael Kemmer, general manager of the BdB. Unveiling the proposals in Strasbourg last Wednesday as part of his annual State of the Union address and seemingly to claw back a central role for the Commission, José Manuel Barroso, the European Commission president, said the tax could raise some €5bn (\$75bn) a year to replenish government coffers. EC is proposing the tax be on all EU member states beginning 2014. The proposal requires unanimous approval from the European Union’s 27 member states and is staunchly opposed by the UK. The tax would apply 10bps on all transactions between institutions when at least one party is based in EU, with derivatives contracts to be taxed at 1bp.

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 1.63 and the U.K.’s 2 year/10 year treasury spread is 1.80% - 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 (77 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 has reached a new low at 4.01% - (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 increased to 9.4 months supply of existing houses – a 7 month high and much 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 increase 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 42.96 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](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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October 3, 2011

From: david.bailey@credit-suisse.com  
Sent: Monday, September 12, 2011 5:29 PM  
Subject: Credit Suisse - MONEY NEVER SLEEPS

From: Wong, Walter [mailto:wwong@kbw.com]  
Sent: Tuesday, September 13, 2011 7:58 AM  
Subject: KBW - EuroAsian Daily

From: Cordukes, James [mailto:james.cordukes@credit-suisse.com] On Behalf Of Ellis, James  
Sent: Tuesday, September 13, 2011 5:30 PM  
Subject: Credit Suisse - MONEY NEVER SLEEPS

From: Kari Ensor (Macquarie Securities) [mailto:Kari.ENSOR@macquarie.com] On

Behalf Of Martin Pommier (Macquarie Securities)

Sent: Wednesday, September 14, 2011 8:12 AM

Subject: Global Financials Daily ( ECB, STAN, NDAQ, HKEx, French Banks, SWEDA, UK Banks, Senate meeting 2pm, BBT, NTRS, HBAN, JPM, CMA, BK, SNV, ALL, AF, MS, SBS, SGx, OCBC)

From: Wong, Walter [mailto:wwong@kbw.com]

Sent: Wednesday, September 14, 2011 7:38 AM

Subject: KBW - EuroAsian Daily

From: Wong, Walter [mailto:wwong@kbw.com]

Sent: Thursday, September 15, 2011 7:44 AM

Subject: KBW - EuroAsian Daily

From: Bailey, David [mailto:david.bailey@credit-suisse.com]

Sent: Thursday, September 15, 2011 5:35 PM  
Subject: Credit Suisse - MONEY NEVER SLEEPS

From: Kari Ensor (Macquarie Securities) [mailto:Kari.ENSOR@macquarie.com] On Behalf Of Martin Pommier (Macquarie Securities)

Sent: Friday, September 16, 2011 8:01 AM  
Subject: Global Financials Daily (Liquidity, TRH/AWH, IBKR, MSCI, Thai Banks, HSB, UBS, UCG, SAN, GLE, CBG, INVP, Capital Market, ACAS, JPM, PGR, SCHWAB, Korean Non-life)

From: Kari Ensor (Macquarie Securities)

[mailto:Kari.ENSOR@macquarie.com]

Sent: Monday, September 19, 2011 7:28 AM  
Subject: Global Financials Daily (Greece, IBKR, LRE, AWH, ALTE, Thai banks, UBS, CSGN, BNP, LLoyds, HBAN, China Property, BOK, Australian Insurance)

From: Wong, Walter [mailto:wwong@kbw.com]

Sent: Monday, September 19, 2011 3:12 AM  
Subject: KBW - EuroAsian Daily

Financial Times – “US Wealth gap raises concerns” dated September 13, 2011.

Financial Times – “Pearson steps up push into online schooling” dated September 15, 2011

Source: Thomson Reuters, Bloomberg,

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