

Founded 1876

NOT RATED

Rating Nature: Relative

Target Price: n/a

Key Data

| | |
|-------------------------|----------------------------|
| Share price | C\$20.24 |
| Est NAV | C\$27.9485 |
| Est. discount | 27.3% |
| Market cap | C\$422.2m |
| 52-week range | C\$17.37-20.85 |
| 52-week discount avg. | 29.1% |
| Div. yield | 2.3% |
| Sector | Investment Funds |
| Stock codes | CGI.TO / CGI CN / CGI LN |
| Gearing (debt :equity) | 25% |
| Rating benchmark | S&P/TSX Composite TR Index |
| Last published research | 24 February 2014 |

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INVESTMENT FUNDS FLASH CANADIAN GENERAL INVESTMENTS

Yielding play on North American growth

Canadian General Investment's (CGI) programme to rebase its dividend (from specials to quarterly) is incomplete. We expect the current quarterly dividend (12c per share) will be increased in 2015.

Currently trading on a 28% discount, the market looks to be ignoring the implications of CGI's on-going repositioning as a payer of a reliable and growing dividend to complement its strong relative investment performance. We believe that as this re-positioning is recognised, the fund will (over time) re-rate. Whilst we aren't forecasting parity, halving the discount to 14% implies 20% share price outperformance.

- ▶ **Dividend.** After doubling its quarterly dividend to 12c in 2014, the fund (excluding specials) yields 2.3%. We expect further growth funded initially by de-emphasising and then eliminating the special dividend (50c in 2014) and then as a result of income growth. By way of comparison, the Canadian market index yields 2.8% and Middlefield Canadian (MCT) yields 4.6% but hasn't grown its dividend in three years.
- ▶ **North American Growth.** Canada's proximity to the USA and the portfolio's positioning (u/w banks, o/w industrials and consumer discretionary) positions the fund as an attractive and discounted proxy play on the US economic recovery whilst continuing to benefit from Canada's robust economic performance.
- ▶ **Investment Performance.** CGI's NAV TR looks average (market like, see table 1) over 10 years and YTD 2014, and good over 1, 3, 5, 15 and 25 years. Commenting on recent performance, the portfolio manager (Greg Eckel) highlighted that over the last half decade the outperformance reflected a combination of stock selection and good sector calls on consumer (overweight) and gold (underweight).
- ▶ **Shale, tar sands and gas.** CGI highlight that US shale (a light crude) has, and will continue, to underpin demand for Canada's heavier oil. This support reflects the configuration of US refineries which necessitate a need to blend the lighter shale crudes with product from Canada's tar sands. The team also highlighted that the marginal cost of tar sands production is low (c\$30-40 per barrel) even if the average cost of production is high. Discussing hydrocarbon transportation, it was highlighted that east-west pipelines were being reversed (to shift gas to the population centres), that the US federal elections may improve the prospects for XL keystone, a key (if it ever gets completed) oil export pipeline and that companies such as Canadian Pacific Railways (CP CN, 4.2% of the fund) were making hay.

Continued

- ▶ **Underweight financials.** Reiterating a long standing theme, the fund is deliberately

underweight (23.6% versus 34.7%) financials. This reflects the tightly regulated nature of the banking sector that in the words of the manager, has resulted in the sector operating a low return utility model. This strategic decision enabled the sector and Canada to pass through the global financial crises unscathed. Total government net debt to GDP is below 50%.

- **Stresses and Strains.** The management team highlighted that the one area of concern for Canada is the state of its housing market (expensive), an issue that stimulated a regulatory response. The government mortgage insurer, CMHC, has tweaked its terms to dampen the market. Changes include higher deposits (20%), shorter amortisation periods (25 years), the introduction of limits on gross debt service ratios (39%) and total debt ratios (44%) and to limit the availability of insurance to homes worth less than C\$1m.

Table 1: Cumulative performance data

| | 2014 YTD | 1 Month | 3 Month | 6 Month | 1 Year* | 2 Year* | 3 Year* | 5 Year* | 10 Year* | 15 Year * | 25 Year* |
|----------------------|----------|---------|---------|---------|---------|---------|---------|---------|----------|-----------|----------|
| Canadian General | 7.3 | -1.8 | -3.7 | 0.9 | 14.5 | 14.4 | 13.2 | 13.6 | 7.0 | 7.9 | 7.6 |
| Middlefield Canadian | 5.5 | -3.5 | -5.0 | -2.4 | 12.0 | 13.2 | 11.3 | 12.7 | n/a | n/a | n/a |
| S&P/TSX Composite TR | 9.9 | -2.1 | -4.0 | 1.1 | 12.6 | 11.8 | 9.3 | 9.1 | 8.0 | 7.3 | 7.1 |

*Source Panmure Gordon and Bloomberg calculations as of 31 October 2014
annualised data

Table 2: Top 10 Holdings

| Issuer | Market Value | % of Portfolio |
|----------------------------------|--------------|----------------|
| Dollarama Inc. | 37,781 | 5.2 |
| Canadian Pacific Railway Limited | 30,016 | 4.1 |
| Enbridge Inc. | 25,605 | 3.5 |
| Bank of Montreal | 22,602 | 3.1 |
| Royal Bank of Canada | 20,141 | 2.8 |
| Element Financial Corporation | 19,737 | 2.7 |
| West Fraser Timber Co. Ltd. | 19,688 | 2.7 |
| Open Text Corporation | 18,718 | 2.6 |
| Yahoo! Inc. | 18,411 | 2.5 |
| Methanex Corporation | 17,765 | 2.4 |
| Total of Ten Largest Investments | 230,464 | 31.6 |
| Total Investment Portfolio | 729,392 | 100 |

Source Canadian General Investments as of 14 November 2014

Table 3: Sector Exposure

| Sector | Portfolio Weight % |
|------------------------|--------------------|
| Financials | 23.8 |
| Energy | 18.9 |
| Industrials | 16.0 |
| Consumer Discretionary | 15.5 |
| Materials | 11.0 |
| Information Technology | 6.4 |
| Telecom Services | 3.1 |
| Consumer Staples | 1.3 |
| Utilities | 1.0 |
| Health Care | 0.9 |
| Cash and Equivalents | 2.1 |
| Total | 100.0 |

Source Canadian General Investments as of 31 October 2014

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| | | | | | |
|---|-------------|-------------|--|--|--|
| Distribution of investment ratings for equity research (as of 8 Oct 14) | | | Rating: GUIDELINE (return targets may be modified by risk or liquidity issues) | | |
| Overall Global Distribution (Banking Client*) | | | Buy | Total return of >10% in next 12 months | |
| Buy | Hold | Sell | Hold | Total return >-10% and <+10% in next 12 months | |
| 68% (40%) | 24% (2%) | 8% (0%) | Sell | Total return <-10% in next 12 months | |

* Indicates the percentage of each category in the overall distribution that were banking and/or corporate broking clients

| | | | | | | |
|--|-------------|-------------|--|-----------------------------------|------------------------------------|------------------------------|
| Investment Funds Research Rating Tariff | | | Infrastructure Investment funds | | | |
| Relative Return (12 month outlook*) | | | Absolute Return (12 month outlook) | | | |
| Buy | Hold | Sell | Buy | Hold | Sell | |
| >3% | -3 to +3% | <-3% | >7% total shareholder return | 3% to 7% total shareholder return | <3% total shareholder return | |
| Note *Measured on a total shareholder return basis | | | | | | |
| Distribution of investment ratings for Investment funds (as of 17 Sep 14) | | | Other Investment Funds | | | |
| Overall Global Distribution | | | Absolute Return (12 month outlook) | | | |
| Buy | Hold | Sell | Not rated | Buy | Hold | Sell |
| 42% | 13% | 2% | 43% | >10% total shareholder return | 5% to 10% total shareholder return | <5% total shareholder return |
| | | | Note Corporate Investment Fund stocks are not rated | | | |

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