July 31, 2011

LORICA | INVESTMENT COUNSEL INC.

Focused Corporate Bond

Market Highlights

Domestic corporate spreads nudged tighter in July but without conviction. In contrast to global markets, the domestic market largely shrugged off disappointing economic data and the continued uncertainty over European peripherals and the US debt ceiling. Additionally, a lack of new issuance, in other than financials, resulted in an artificial bid to secondary product and new issue concession re-pricing of the credit curve. However, bid/ask spreads were noticeably wider, particularly for lower rated non-financials. There was also anecdotal evidence of international buyers moving into the domestic high grade space as they diversified away from dollar and euro denominated holdings.

The lack of market conviction was reflected in the primary market, which saw no fixed rate issuance for the first three weeks of July. Money continued to flow into corporate bonds but the appetite could not be met through new issuance as issuers and buyers were in a stalemate over pricing. It was only in the final week of July (and just prior to bank quarter-end), that we saw a number of opportunistic (perhaps debt-ceiling precautionary) jumbo deposit note deals come to market which absorbed much of this pent up demand. Of the $5.8 billion that came to market in July, $4.3 billion of this was comprised of deposit note deals from Royal Bank ($1.25B 5YR), Toronto-Dominion Bank ($1.75B 5YR) and Bank of Montreal ($1B 5YR and $300 15YR). After an absence of months, the issues marked the return of the banks to the domestic fixed-rate markets whom have instead been issuing globally ($13.1B in July alone of fixed and floating rate notes) to take advantage of comparatively cheap funding and diversifying their investor base.

Beyond the jumbo bank issuance, there was only one other notable issue, a privately placed $544 amortizing bond (33.5-year maturity) for a public-private partnership – Halton Hospital Infrastructure. In the high-yield arena, where non-traditional interest has been waning as of late, two deals came to market - a long anticipated Kruger Products deal ($175M 7YR) and a $90M secured 5-year amortizing issue from Noranda Trust, which was downgraded by DBRS into the high yield space (BB (H) from BBB) the week prior.

For the month, short, mid and long yield spreads tightened by 2, 4 and 3 basis points respectively, resulting in absolute returns (which account for changes in the yield curve as well as coupon income) of 1.08%, 2.54% and 4.15% respectively, according to the DEX Bond Indices. In the early part of the month, the combination of lingering exuberance over the Greek debt deal, lack of issuance and money that needed to be put to work in higher yielding assets, resulted in BBB marginally outperforming for the month. The best spread performance was reserved for Media (Yellow Media) and telecommunications (absorption of supply overhang). With the exception of real estate which underperformed (new Fifth Avenue Place issue pressured spreads), all other sectors generally performed in-line with the market.

Outlook & Strategy

We believe that the corporate bond market will continue to be more impacted by exogenous events and supply than a significant degradation in the general quality of credits. We feel there is little catalyst for significant spread tightening, and hence are not yet ready to lose our defensive bias. However, with the potential for increased volatility and event risk, we feel this presents an opportunity to capitalize on relative value and yield enhancement opportunities.

Gary Morris, CFA
President

Thomas Gomes, CPA, CFA
Portfolio Manager

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Firm Overview

Lorica is an investment counsellor, committed to providing an entire investment service including management, administration, communication and compliance. Lorica's investment team and process is characterised by stability, security and consistency and an ongoing commitment to delivering superior results.

Philosophy

Underpinning Lorica's investment philosophy is a belief that value can be added through active management in all market environments. We believe a comprehensive range of core bond market competencies can be used effectively to manage within a central risk management paradigm. Economies and markets are dynamic and we have learned they call for an adaptive, subjective approach to forecasting. However, construction of diversified, yet targeted portfolios is ideally suited to our proprietary computer-based models and algorithms.

Investment Strategy

An actively managed corporate bond strategy investing in investment grade corporate bonds and other investment grade securities issued by Canadian corporations. The investment strategy focuses on industry and issuer selection with an emphasis on credit risk management.

Managers

Gary Morris, CFA
President, Lorica Investment Counsel Inc.

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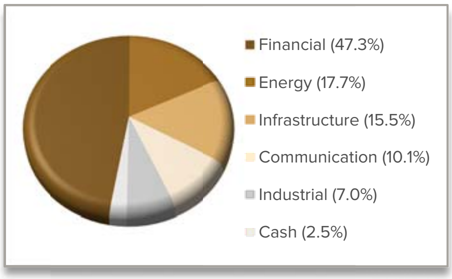
Inception: January 1, 2011
AUM (Mandate): $17M

Asset Mix



Risk Profile

	Lorica	DEX All Corporate**
Yield to Maturity	3.2	3.4
Average Term	7.7	8.6
Modified Duration	5.5	5.6
Coupon	5.5	5.3
Credit Rating (%)		
AAA	2.5	4.9
AA	21.6	33.2
A	56.6	37.2
BBB	19.4	24.8

Constraints

No. of Securities	10 – 25
Sectors	
Corporates	0 – 100%
Governments	0 – 25%
Min. Credit Rating	BBB
Max. Issuer Weight	10% (5% BBB)

Historical Performance*

Annualized Returns	1 Month	3 Months	1 Year	2 Years
Lorica Focused Corporate Bond*	2.07	3.57	7.25	7.58
DEX All Corporate**	2.11	3.49	6.95	7.92

Annual Returns	2010
Lorica Focused Corporate Bond*	6.99
DEX All Corporate**	7.34

**The investment performance of the Focused Corporate Bond ("Strategy"), as managed by Morris & Gomes, stops at the end of October 2010 with the departure of Morris from Laketon Investment Management Ltd. A valid continuation of performance of the Strategy commenced with the management of the Strategy at Lorica Investment Counsel Inc. on January 1st, 2011. The period following October 2010 will represent a discontinuity or gap in the performance track record for which there is no applicable active performance. Accordingly, we have substituted the appropriate DEX All Corporate Bond Index performance for that period.*

***DEX All Corporate Bond Index*