

THE WALL STREET TRANSCRIPT

Connecting Market Leaders with Investors

Investing in Canadian & U.S. Value Stocks



JOHN WILSON is the Chief Investment Officer at Cumberland Private Wealth Management. He is also Cumberland's lead technology and telecom analyst, and has extensive experience in investment management and research. Prior to Cumberland, he founded DDX Capital Partners, an investment counselor that produced impressive results through the use of extensive risk management systems. Prior to that, he was Managing Director and top rated analyst of the technology group at RBC Capital Markets. Previously he was Director of Technology, Media and Telecom Research at UBS Canada. Mr. Wilson began his career at Northern Telecom in systems design and over 10 years he held several management positions in the areas of design, manufacturing, marketing, business planning and development. He is an MBA graduate of Wharton, The University of Pennsylvania. Mr. Wilson is a director and shareholder of Cumberland Partners Limited, the firm's parent company.



PETER JACKSON has been a Portfolio Manager at Cumberland Private Wealth Management since 1999, with overall responsibility for Canadian equities. He also manages the Cumberland Total Energy Fund and the Cumberland Special Opportunities Fund. Mr. Jackson is a member of Cumberland's investment committee. Prior to Cumberland, Mr. Jackson managed a private investment partnership that acted as a sub-advisor for Elliott and Page Investment Counsel. Previously, he was a Portfolio Manager and Investment Analyst at Barclays McConnell and Sun Life, respectively, with a focus on Canadian equities stock selection and research. Mr. Jackson has over 24 years experience in the investment management business. He is a director and shareholder of Cumberland Partners Limited, the firm's parent company.



PETER MANN has been an Investment Analyst at Cumberland Private Wealth Management since 2004, with responsibility for research and analysis of U.S. equities. He is a member of Cumberland's investment committee. Prior to Cumberland, Mr. Mann managed a U.S. private investment partnership. He has over 15 years of investment experience in portfolio management and institutional sales and trading. Mr. Mann is a shareholder of Cumberland Partners Limited, the firm's parent company.

SECTOR – GENERAL INVESTING

TWST: If one of you could just introduce Cumberland Private Wealth Management and what your respective responsibilities are there?

Mr. Wilson: Cumberland Private Wealth Management was founded in 1998, but our clients have actually been with us as long as 30 years. We've been managing wealth for high net worth individuals for decades and we have always approached it with the same two goals, which are first, protecting our clients' capital; and second, growing their wealth over time. That's at the very core of how we think about investing. I'm John Wilson, our Chief Investment Officer and I'm joined today by Peter Jackson, head of our Canadian investment team, and Peter Mann, head of our U.S. investment team.

TWST: What is the firm's investment philosophy?

Mr. Wilson: I'll go back to the two goals I mentioned earlier, protecting capital and growing wealth over time. Our philosophy is really driven by three things; number one, we've always had a value-orientation. We believe a focus on value provides the best opportunity for long-term returns and gives us a margin of safety in protecting capital. Number two, we very strongly believe we can best achieve our goals if we're process driven. By that I mean we have a defined investment process that we follow very closely, because we fundamentally believe it improves the timeliness of our investment decisions, increases the frequency of successful decisions, gives us confidence that those successful decisions are repeatable and it allows us to implement a very active risk management process to help us protect our clients' capital.

Finally, I would say that our philosophy is to be disciplined. We don't wander off into ideas and themes that we don't feel we know a lot about. We keep a high degree of focus on areas where we feel we have the most expertise and we stay disciplined to our process and value orientation. Those are the three keys to our philosophy and we drive them down through the entire organization.

TWST: You have a macro top-down approach which I suppose is necessary for both the U.S. and Canada. Would you give us a brief description of how the economy and the markets in Canada are functioning and how they are different in some ways from the U.S.?

Mr. Wilson: We do obviously have a very well defined top-down process of looking at the economic landscape and how that translates into opportunities and risks in financial markets. Obviously Canada and the U.S. are important elements of that, but I would say that particularly in the current environment, it's a much more global discussion than would have been the case 15 or 20 years ago. Number one, the opportunities are more global; but two, as we saw in 2007 and 2008,

the global community is much more connected and risks are much more transferable from one geography to another. A top-down discussion today is much more global than we would have had in the past.

In order to strengthen our global investment capability, we were aggressively hiring investment talent through a difficult period for most investment management firms and we were able to add considerable depth

to the global expertise within our investment management team. As for Canada specifically, there was no way to avoid being affected by what transpired in 2008. The U.S. has always been Canada's largest trading partner and a big part of the Canadian economy. So as the U.S. went into a very steep and protracted recession, that clearly had a significant negative impact on the Canadian economy as well.

That being said, in the context of how different economies around the world have been impacted, Canada has come through this more quickly than most and with less damage than most. This is partly because its financial system was in much better shape and didn't suffer through some of the difficulties seen in Europe and in the U.S. with their banking systems; partially because Canada has a heavy commodity bias and as we saw, Chinese demand for commodities came back very, very quickly as their economy went on to grow in 2009 by well over 8%. That demand for commodities has really helped Canada come back to positive growth relatively quickly following a two-quarter decline. When we look at Canada specifically today, unemployment is still lagging although it has never deteriorated to the levels seen in the U.S. The Canadian housing market

never went into the kind of decline we saw in the U.S. and has recently hit new highs in prices and sales. So generally, the consumer is in better shape and Canada enjoys the strong growth driver of emerging market demand for commodities, in particular from China.

Highlights

John Wilson, Peter Jackson and Peter Mann invest in Canadian and US stocks, believing that a focus on value provides the best opportunity for long-term returns and gives a margin of safety in protecting capital. They have a defined investment process and focus on areas where they feel they have the most expertise. They made an excellent call on energy and particularly oil in 2009 and although they have recently made a switch of some of the oil exposure to natural gas, they still see a good overall opportunity in energy stocks. They have also rotated their materials exposure to add more weight to agriculture and reduced exposure to gold somewhat. They are overweight in consumer discretionary, particularly fast service restaurants and financially strong auto parts retailers. More recently, in the US they see opportunity in health care. Risk analysis is a vital element of their entire investment process and unless that can understand and quantify the risks of a potential holding, it's a non-starter. Related to value, they like to see growing cash flow. They say that growth in cash flow improves the standing of stakeholders in the business, whether they are credit or equity holders.

Companies include: Ensign Energy Services (ESI:TSE); Bonavista Energy Trust (BNP:TSE); Magna International (MGA); Barrick Gold (ABX); CVS Caremark (CVS); URS (URS).

Wilson: *We have allocated capital in consumer discretionary generally, with particular emphasis on leading quick service restaurants and financially strong auto parts suppliers. More recently in the U.S. we see opportunity in health care as the proposed reform package loses momentum and we've been growing exposure to that element of the market.*

TWST: How is your portfolio generally positioned? You were defensive all through 2008. How has it shifted in emphasis over 2009 and preparing yourself for 2010?

Mr. Wilson: We've talked about this a lot. Really, last year there was effectively one important decision to make and that was whether you were willing to put capital to work or not. Fortunately for our clients, we made the right choice which was that it was a compelling and probably once-in-a-generation opportunity to put our clients' capital to work both in credit and in equity markets. As it turned out, 2009 was an enormous year for both of those asset classes. As we moved through

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2009, the value elements that we had recognized in the market at the start of 2009 became more difficult to find. There was some rotation in the portfolio as we came to the end of the year, with a greater emphasis on higher yielding equities. As we move into 2010 we see the market as more of a grinding market, where you are more likely to be rewarded for your expertise in selecting individual securities and rotating among sectors. I obviously think it's much more unlikely that we're going to get to the kind of overall lift across asset classes that we saw last year just for taking risk. We are still relatively well invested right now, but we believe we are likely to be much more active than we felt we needed to be last year. We remain very aware of what we think are considerable potential risks on the horizon as we move through the year.

TWST: **Have you changed your sector exposure or under-weighted other areas?**

Mr. Wilson: I would say, from a sector basis we made an excellent call on energy and particularly oil in 2009. We've made some rotation within energy over the past quarter to switch some of that oil exposure to natural gas, but we still see a good overall opportunity in energy generally. We made an excellent call on the commodity side with materials but have rotated as well here to add more exposure to agriculture and reduce our exposure to gold somewhat. As I mentioned earlier, we remain completely out of the large U.S. financials and will likely remain out of those names until visibility into the regulatory environment improves considerably.

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TWST: **Would you tell us about the actual stock selection process? Are the criteria for potential holdings the same for your Canadian portfolio as for your U.S. portfolio?**

Mr. Wilson: Our entire global investment team runs under the same investment process. It basically starts with a top-down view of the world in terms of a target investment framework, which is a template of what we project the investment landscape is most likely to look like over our investment horizon. This includes factors affecting the economy such as regulatory, fiscal and monetary policy, and a view on sectors most likely to benefit.

From there, our investment teams go out and apply the value discipline and our due diligence process to come up with their best view

of where opportunity lies to drive investment returns for our clients. That generally has some consistent elements to it, including the disciplined approach to value I mentioned earlier. We also like to see management teams with a track record of executing on what they say they're going to do. That gives us a high degree of visibility into what the future can be, which in turn lowers our risk. Risk analysis is another element that permeates our entire investment process. Very simply, unless we can understand and quantify the risks of an investment position, it's a non-starter. We must be able to understand what we're getting into and know what our risks are before we put our clients' capital to work. Finally, related to value we like to see growing cash flow. Ultimately, growth in cash flow improves the standing of stakeholders in the firm, whether they be credit or equity holders.

TWST: **Shall we turn to Pete and Pete and get their views on their respective portfolios?**

Mr. Jackson: Let me take a minute and talk about our strategy in oil and gas as this is a big component of what we invest in, in Canada. Coming into 2009, our focus was on oil-weighted producers as the outlook for natural gas prices remained quite weak. This strategy paid off throughout 2009 as oil rallied from about the mid-\$30s level up to the high-\$70s. Meanwhile, the U.S. gas drilling rig count

1-Year Daily Chart of Ensign Energy Services



Chart provided by www.BigCharts.com

Jackson: *Ensign is the second largest driller in Canada and about the fourth largest in the U.S. with a market capitalization of about \$2.6 billion. Ensign has no debt and its average return on equity over the past ten years is 21.7%. Even at the bottom of the gas cycle, which happened in 2002 and appears to have repeated itself in 2009, Ensign should still generate a low double-digit return on equity and positive net free cash flow.*

had collapsed through the first part of 2009 and production levels for natural gas in the U.S. and Canada started to decline. Add to this the potential for some stabilization in industrial gas demand as the economy bottoms out, and gas markets may be finding a bottom here.

As a result, we have started to tilt the portfolio more towards natural gas. We recently added two companies to increase our exposure to gas. The first company was **Ensign Energy Services (ESI.TSE)**. Ensign is the second largest driller in Canada and about the fourth largest in the U.S. with a market capitalization of about \$2.6 billion. It has a modern fleet of about 300 rigs with increasing exposure to the large gas resource

plays in both Canada and the U.S. **Ensign** has no debt and its average return on equity over the past ten years is 21.7%. Even at the bottom of the gas cycle, which happened in 2002 and appears to have repeated itself in 2009, **Ensign** should still generate a low double-digit return on equity and positive net free cash flow. As gas prices recover, drilling utilization rates should rise, which should be positive for **Ensign**. The stock pulled back from a high of about CAD \$25 in 2008 and it currently trades around CAD \$16. It pays a dividend yielding about 2.1%, which has increased every year and management and directors own 20% such that their interests are well aligned with ours.

Another name that we like in the natural gas space is **Bonavista Energy Trust** (BNP.UN.TSE). **Bonavista** is a gas-oriented trust with a market capitalization of about CAD \$3 billion. It has demonstrated top quartile finding and development costs since its inception and currently yields about 8.1%. Insider ownership in the trust is about 15%. During the third quarter of 2009, **Bonavista** had record production and a 98% success rate on its 2009 drilling program. It also announced a transformative gas acquisition that potentially offers exposure to some of the best economics of any gas resource play in North America. **Bonavista** plans to significantly ramp up its spending on this new core area in 2010. Given its significant tax pools, **Bonavista** should not have to pay any tax for at least the next three years, leaving plenty of room to maintain

1-Year Daily Chart of Bonavista Energy Trust



Chart provided by www.BigCharts.com

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its current distribution when it converts back to a dividend paying corporation later on in 2010. This means investors could be receiving a very attractive dividend on the stock as well as participating in the production growth upside from growing gas production.

Another stock that we added recently was **Magna International** (MGA). **Magna** designs, develops and manufactures automotive systems primarily for sale to automotive companies. **Magna** not only beat earnings expectations in the last quarter, but also was significantly profitable as a result of massive cost reductions and a pickup in third

quarter auto production. This positive operating leverage should carry over into the fourth quarter and into 2010. The consensus outlook for auto sales in North America for 2010 is only about 11.4 million units, but this is coming off a very low base in 2009. It's also about in line

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1-Year Daily Chart of Magna International



Chart provided by www.BigCharts.com

with annual scrap rates of 11 million to 14 million units. So we think the consensus may prove to be a conservative number for 2010. We have also seen improvements in used vehicle pricing as well as improvements in the credit markets, which should be positive for auto sales into 2010 and 2011. Domestic light vehicle inventories remain low so there is no glut of product in the dealerships at this point. **Magna** is trading right now at \$57. The stock looks cheap compared to most U.S. and Canadian comparable companies. It also trades at about one times tangible book value and has about \$7 per share of net cash on its balance sheet. If you look at previous auto cycles, auto part stocks typically bottom at around tangible book. We think **Magna** still has a lot of upside from here.

The last company I want to mention is **Barrick Gold** (ABX). **Barrick Gold** is the largest gold company in the world in terms of production and reserves. Its current reserves stand at around 138.5 million ounces of proven and probable reserves, plus there's an additional 100 million ounces of measured, indicated and inferred reserves. Last year, the price of gold increased in U.S. dollar terms by about \$216 per ounce or about 25%. While **Barrick's** stock rose a bit in U.S. dollar terms, it has generally lagged behind its peer group. Production is anticipated to grow about 500,000 ounces in 2010 and **Barrick** expects to add about 2.6 million ounces of annualized new low cost production over the next three years that will significantly lower its overall cost profile. With the elimination of the company's corporate hedge book in 2009, **Barrick** is positioned to participate in further increases in the price of gold bullion. Currently,

Barrick trades at a discounted valuation in terms of price to cash flow, and we believe for all of the above reasons that there is more upside in the stock into 2010.

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1-Year Daily Chart of Barrick Gold



Chart provided by www.BigCharts.com

TWST: Do you want to take up the U.S. side of things?

Mr. Mann: I know when we spoke last year we referred to a couple of U.S. healthcare names, **Medco** (MHS) and a convertible bond that was issued by **Hologic** (HOLX). Both of those are still holdings in the portfolio and we have been very pleased with those results. Today we're going to talk about two companies. The first idea is **CVS Caremark** (CVS). CVS is based in Woonsocket, Rhode Island. It is the second largest retail drugstore chain with over 7,000 outlets and the third largest pharmacy benefit manager in United States.

In 2007, CVS acquired Caremark, under much criticism, looking to create the first vertically integrated drug benefit manager. Concern centered around the independence of the combined entity and its ability to act as an intermediary for customers, while at the same time attempting to grow drug sales at the retail level. With Caremark's acquisition they have lost over USD \$12 billion in PBM contracts and the merger, while benefiting the retail arm of the business, has been anything but a success. In early November, CVS blindsided the street with a dramatic decrease in 2010 expectations for Caremark, creating what we think was an incredible buying opportunity.

The company currently trades at 11 times 2010 earnings estimates, a significant discount to both **Walgreen's** (WAG) and **Medco** and **Express Scripts** (ESRX) on the PBM side. We estimate that the retail chain is currently trading at 14 times expected 2010 EPS of USD \$1.68 and Caremark is currently trading at seven times it expects in 2010 EPS of USD \$1.12. CEO Tom Ryan, long lauded for his operational and leadership skills has come under fire. He has since fired the COO of Caremark and replaced him with Per Lofberg, the former Chairman of

Merck-Medco.

CVS is definitely wounded in the marketplace. They have lost market share to the larger independent PBM's and have been slow to react. Having said that, the company will earn approximately USD \$2 billion in EBIT next year and is in much better shape than consensus realizes. Firstly, new leadership with a Medco mindset, will help right the ship. Secondly, Caremark has little in the way of 2011 contract renewals allowing time to improve relationships and product offerings without the imminent concern of making promises that could prove difficult to keep. Lastly, two recently published independent surveys have recognized Caremark as number one in customer service. While anecdotal, it implies that all is not lost.

CVS retail is managing extremely well through the current environment. Same-store sales have compared positively throughout most of the downturn. The acquisition of Longs Drug Store last year has provided excellent penetration into the western states. CVS is continually recognized as the finest drug store shopping experience in the United States.

Our conservative discounted free cash flow estimates that **CVS Caremark** is currently trading at a 23% discount to its fair value. Applying achievable growth rates for 2011, our two-year price target is USD \$45 per share.

1-Year Daily Chart of CVS



Chart provided by www.BigCharts.com

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We want to own great businesses where the probabilistic risk-reward is tremendously skewed in our favor. We feel CVS fits this profile and provides multiple opportunities for a beneficial outcome to earn a more than satisfactory return with below average risk.

The last name we want to talk about is **URS Corporation** (URS). URS is a leading construction, engineering and technical services firm located in San Francisco, California. Since becoming public in 1993, URS has doubled its revenues five times, primarily through acquisition. The transformational acquisition of industrial construction

specialist Washington Group in 2007 vertically integrated **URS** and focused the company on all aspects of the design and build process. Almost all contracts are negotiated on a cost-plus basis. CEO, Martin Koffel, is a legend in the industry having run **URS** since 1989. The company operates out of 330 offices in 30 countries and has 47,000 employees.

URS has three main divisions; EG&G, **URS** and Washington Group. EG&G is the backbone of **URS**. Both the Department of Energy and the Department of Defense are lower margin (5%), but long-lived contracts of 7-8 years with a USD \$12 billion backlog. In fact, since the acquisition of EG&G in 2002, **URS** has lost one contract. EG&G provides a visible and dependable cash flow stream. There is also a moat around certain aspects of EG&G's work such as intelligence, space and

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1-Year Daily Chart of URS



Chart provided by www.BigCharts.com

mission support services. Approximately 1,000 employees possess military clearance. To put it in perspective, **URS** requires maintenance capital expenditures of approximately USD \$15 million a year to support a USD \$4 billion revenue federal business. The **URS** division is the highest margin (6-8%) and focuses on design, procurement and maintenance services. Contracts are shorter in duration and the backlog is approximately 18 to 24 months. Washington Group helps **URS** become the vertically integrated engineering and construction company. Extremely well managed with a strong focus on costs, margins are typically lower for the company (4-6%). Backlog is the shortest at 12-18 months. Firm-wide margins are currently 6%, up about 80 basis points year-on-year. **URS** provides the rare combination of consistent and steady growth, barriers to entry through specialty contracts and a long-term call option on nuclear power as the company has designed or built 19 of 104 nuclear power plants in North America.

The opportunity to acquire **URS** shares occurred as market fatigue over infrastructure stimulus spending intensified. While the company is not a huge beneficiary of the stimulus package, the psychology

around improving stimulus spending will remove an overhang.

Our DCF estimates that **URS** is currently pricing a 2% growth. We believe the company can grow well in excess of this, approximately 10% over the next five years. In fact, using very conservative assumptions, we think **URS** is worth USD \$60 a share. As the company continues to pay down acquisition debt with free cash flow, we would expect **URS** to be an acquirer of private engineering and construction businesses as they currently trade at a discount to their publicly traded peers. Management has done a tremendous job buying and merging entities and we would expect any acquisition to be immediately accretive.

TWST: **I know that part of your process involves looking at secular trends or themes. Are there any that you can talk about as we're in early 2010?**

Mr. Wilson: I will focus on the two trends that we felt were important in terms of catalyzing the rally last year. First among those were low interest rates as global monetary authorities, particularly in the U.S. and the UK, began a program of quantitative easing to keep long term rates low. Under this program they committed to be in the market purchasing longer maturity, fixed-income products and largely mortgage-backed securities. They did that on a scale never contemplated before, \$1.5 trillion in the U.S. and close to another \$0.5 trillion in the UK. They were successful in keeping rates low, but beyond that they also gave markets certainty that rates would stay low for some time. That was an important catalyst to getting people to take risk again.

The second important catalyst to our mind was the re-emergence of China. China was already an important theme in global markets before we went into the crisis, but once the crisis manifested itself there was a lot of concern that China, and emerging markets generally, were too heavily reliant on exports to the U.S. and would suffer disproportionately as the U.S. went into recession. That of course, has proven not to be the case. China's economy never stopped growing, the lowest growth they experienced was a 6% GDP growth rate in the fourth quarter of 2008. As we all now know, China's growth has come back very, very quickly and in fact most recently grew almost 11% in the fourth quarter of 2009. So in our view, both low rates and China's re-emergence as a high growth economy were important in terms of people feeling that there were growth opportunities worth taking, and that there was a reason to take risk.

The flip side of that though as we look into 2010, is that we are very wary; should either one of those falter we think the market could react very negatively. We worry less about China as the fundamentals there remain very strong. There are some risks, particularly surrounding the staggering rate of growth in their money supply and the resulting potential for speculation. There has been a tremendous amount of lending done very quickly and a lot of skepticism around the quality of that lending. We've also seen very heated activity in areas such as the stock and property markets in China. But underlying all of that is a massive economy with a tremendous amount of opportunity and a dynamic growth environment. So overall, China is a risk that we're less worried about.

What we are more focused on is rates. Governments around the world this year will be issuing even more debt than they did last year, and last year was by far an all-time record. This will mean a tremendous amount of supply coming into debt markets in 2010. From a demand standpoint, both the Federal Reserve and the Bank of England have indicated they will be ending their programs of quantitative easing by March of this year, effectively removing almost USD\$2 trillion in demand from debt markets. On top of that, governments are also pushing out the maturity of their new issues to try and lock-in what are relatively lower rates right now. We think all of that could put a lot of pressure on the longer end of the yield curve. We started to see that a little bit at the end of 2009, but we are concerned that it could move more meaningfully in 2010. Should that happen, it would clearly

have negative implications for fixed income investments, particularly longer dated ones. We have adjusted our portfolios to protect ourselves from that already. But more meaningfully, higher rates could start to unwind a lot of the benefits we saw from that easing program when it was put in place last year, including the willingness of investors to take risk. In addition, higher mortgage rates could undermine the stability that has started to materialize in the U.S. housing market. Higher yields also reduce the attractiveness of equities relative to fixed income. There are a lot of implications that could come out of that kind of move. I emphasize, we haven't seen it yet, but the factors are certainly there and it could start to play out. Now, one thing that could change, of course, would be if the Fed were to reverse course regarding the easing program and potentially continue, extend or even expand it. There is a lot of uncertainty around that element of risk and we are paying a lot of attention to it.

TWST: Are you still looking at convertible bonds?

Mr. Wilson: Convertible bonds, no, they're not a big part of how we're investing in capital right now. We do have the position Peter Mann mentioned, which has worked enormously well for us and we still see it as an attractive place to have capital, but generally speaking, we think the risk/reward right now in the equity market is probably a little more compelling than what is available in the fixed income market.

TWST: What about the sell discipline, what criteria do you have for triggering an exit from your portfolio?

Mr. Wilson: The best one and the one we prefer to use the most is the "happy ending", as Pete says. When our investment position has fully discounted the upside that we believe is reasonable for that position, we're happy to take our exit. We believe the value discipline is as important on the way out as it was on the way in.

The other reason we take money off the table is if the relevant information changes. We build an investment thesis for a position and a number of things could change as we move through time. Number one, the overall dynamic for the particular industry or sector that we're working with may change, in which case we'll take the capital back out of that position. More specifically, the sector may be fine but management may not have executed on the business plan that we felt was the right one for the company, in which case we'll double back and take our money off the table again. The third reason we'll exit a position is just to limit our risk. Even if we believe the business plan is still in place, and the initial investment thesis still holds, if the position moves against us beyond a fixed percentage from our cost, we limit in a non-discretionary way how much we are willing to lose on any given single position within a portfolio. At that limit, no matter how much we like it, we don't get to own it any more. We must exit the position.

TWST: What about the risk control that you try to incorporate within your process, can you tell us your risk management techniques?

Mr. Wilson: I just mentioned one element of it, our discipline regarding how much we will lose on any single position, but there are many other elements to our risk management process.

As a second element, we carefully monitor and manage what I'll call 'exposure limits'. That is understanding what our concentration is to any single source of risk, and that source of risk may be one particular security, it may be one sector or industry or it could even be a theme. Another element of concentration that we measure and monitor is our correlation risk. This is simply the correlation that exists between securities, sectors or themes within our portfolios.

A third element of risk we manage is liquidity risk. One hard lesson investors learned in 2008 is that the ability to liquidate a position and get your capital back can be very difficult in a time of crisis. While we have some clients who are specifically willing to take more liquidity risk than others, overall we're very focused on having very high liquid-

ity. As a result, we have minimum limits for trading volume and market capitalization in order for an idea to be approved for our client portfolios.

A fourth element is what we call 'volatility management', and that's the potential for large swings in asset prices to impact the portfolio performance over the short term. Regardless of the long term outcome, it can be very difficult for clients to see wild swings in their portfolio value over the short term. We do believe our value orientation limits this somewhat. If you own value, you should see less extreme movements in portfolio value, certainly to the downside in our view. But there can also be volatility between asset classes that we look to manage using our tactical asset allocation process – effectively reducing or growing exposure between equities, cash and fixed income depending on our risk outlook for each asset class. The other element of volatility that we look to manage carefully is currency swings. Exchange rates generally have become much more volatile in the last four or five years than were ever the norm, and for many of our clients we look to reduce that source of risk through selective currency hedging.

The final element of risk that I'll talk about managing in our process is what we call sensitivity analysis. We have proprietary quantitative tools that we run on portfolios to understand the sensitivity of the portfolio to underlying fundamental and macroeconomic variables like interest rates or the business cycle. This can help us to understand where we are positioned within a portfolio and whether that positioning really jives with the information we see coming in day to day. Does it really reflect where we think the economy will be going forward? So, those are the five key elements that I'd highlight as part of our active risk management process.

TWST: Would you say that your asset allocation models have a contrarian bias as part of your value approach?

Mr. Wilson: Historically, I think we've described ourselves that way. I would caution that we don't look to be contrarian simply for the sake of being contrarian. I would say that we are willing to be contrarian because we have tremendous confidence in our process and in our value orientation. We remain disciplined to our investment process and remain disciplined to having a value orientation, which allows us to still be comfortable taking an approach that may be contrarian to what other people are thinking.

TWST: Looking ahead into the rest of this year, are there any headwinds or challenges for Canadian investments or for U.S. investments that investors should be wary of at this time now?

Mr. Wilson: I mentioned two earlier. Certainly, we think the ability of China and emerging markets in general to continue on this path of growth that they've demonstrated since the bottom of the crisis early in 2009 will be key. Should they falter in any way on that path we would expect global equity markets to show considerable weakness. Recently, China in particular has been gently "tapping the brakes" from a policy standpoint to try and rein in growth a little bit and that has caused concern in global financial markets. I also mentioned rates earlier, which clearly could have some negative flow-through to both equity and credit markets. But I think more generally, the over-riding concern we have is that we're living through a very unusual time. There are a number of things that have been put into place around the world from a regulatory standpoint, from a fiscal and monetary policy standpoint, that have never been tried before and even if they have been tried, they're being implemented on a scale that's never been attempted before. That creates a significant amount of uncertainty. We currently believe that an unusually wide range of outcomes are possible as we look through 2010 into 2011. Some of those outcomes could be very good; some of them could be very poor and I would argue they're all plausible. Uncertainty in our business means risk and that gets back to our view that this year will require a much more agile approach to investing and we need to be ready and able to execute a much more active management style.

TWST: So to sum up, what differentiates Cumberland from other wealth management companies in Canada? What are you bringing to the table that others might not be?

Mr. Wilson: I think first, we look at investing not as a relative game. In other words, we would never be happy in a situation where our clients earned a negative return which was less negative than an index. That is not consistent with the objectives that we set for ourselves as a firm and it's not consistent with the objectives our clients have for their capital. We are built around the concept of an absolute return: protecting the capital of our clients and growing it over time. This idea of relative performance to an index, which is very popular in the industry generally, is not at all the way we look at our value proposition and that does make us very different.

Second, we are a privately owned firm whose partners invest their capital alongside their clients. Quite simply, we have the same investment objective as our clients. It's not just a job to us. It's the way we invest our own capital.

Third, we think we have one of, if not the best investment teams in the industry. We feel we can go toe-to-toe with any other firm and we are confident we have the right talent to make the right decisions for our clients' capital. That to us is an area of differentiation.

The last one that I'll mention is our investment process. We believe that our discipline to our process greatly increases both the frequency and repeatability of successful investment decisions, particularly

those that can be most difficult to view objectively in times of stress. In our view, our process mitigates downside risks and enhances portfolio returns for our clients over the long term, which in the end, is the element of differentiation we care most about.

TWST: Thank you. (PS)

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