SELECTED COMMENTARIES ON U.S. EQUITIES, 2010-2015

KAMRAN KHAN

PORTFOLIO MANAGER, NORREP US DIVIDEND PLUS CLASS

NORREP INVESTMENTS

MAKING *ACTIVE* MANAGEMENT COUNT™

We are pleased to provide advisors with this collection of selected commentaries on U.S. Equities, 2010-2015, written by Kamran Khan. Please contact your Norrep sales representative for the most current information about Norrep US Dividend Plus Class.

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GROWTH IS OUTPERFORMING VALUE (LIKE IT'S 1999)

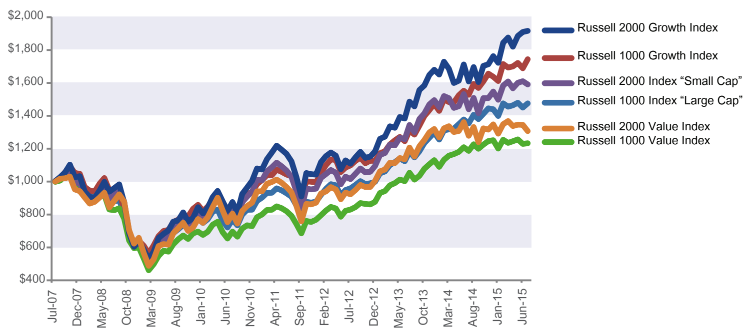
Kamran Khan, CFA

August 2015

At first glance it may appear that not much is happening in U.S. equity markets. The Russell 1000 Index which tracks the largest companies returned only 3.7% for the first seven months of the year. A lacklustre return no doubt but perhaps appropriate in light of the disappointing U.S. economic performance and muted earnings growth seen so far this year.

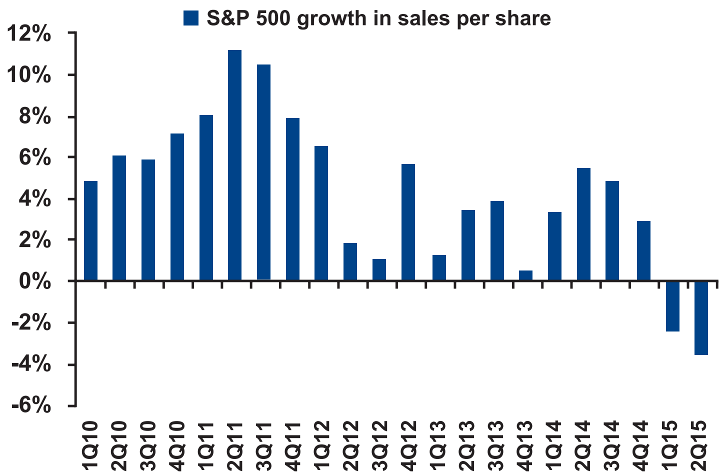
However, as we dig beneath the surface we find a large divergence between the performance of growth stocks and value stocks. The Russell 1000 Growth Index has returned 7.5% year-to-date, more than doubling the performance of the broader market. Meanwhile, the Russell 1000 Value Index has actually declined 0.2%. The difference in performance between these two groups of stocks amounts to 766 basis points over the seven month period, a relatively large spread between these two indices since data is available going back to 1992. The diverging performance between growth and value stocks is not just limited to the large caps. A similar trend is occurring among small and mid-cap stocks as well.

Investing styles go in and out of favour just like any other facet of the markets. The "value" style of investing – buying companies that look cheap relative to their fundamentals, such as earnings, book value or cash flow – has underperformed ever since the U.S. credit bubble began to burst in 2007. Meanwhile, the "growth" style of investing – buying companies that exhibit above-average growth regardless of valuation – has outperformed the broader market returns. Over the 8-year period ending July 31, 2015, the Russell 1000 Growth Index generated an annualized return of 9.0% while the Russell 1000 Value Index lagged behind with an annualized return of 5.4%. Essentially, growth stocks have outperformed value stocks by approximately 3.6% per year over the past 8 years. The degree of outperformance has certainly widened over the past year with the Russell 1000 Growth Index up 16.1% while the Russell 1000 Value Index is only up 6.4% amounting to a spread of 968 basis points for the one-year period ending July 31, 2015.



Some of the difference in performance can certainly be attributed to a relative underweight in top performing health care and technology industries across the value stock landscape. Another major contributor that is supporting growth stock outperformance is the sub-par economic growth seen in the U.S. Over the last 8 calendar years (2007 to 2014), U.S. GDP growth has generally remained below 2.5%, with the 5-year average close to 2.2%. During the previous six decades U.S. economic growth was typically well above 3%. Even 2015 GDP growth is coming in weaker than expected due to lousy weather, a stronger U.S. dollar and falling energy prices. All of these factors are joining forces to create a very difficult environment for corporate earnings growth. The first quarter of 2015 was the first quarter of negative sales growth for the S&P 500 since the financial crisis. Q2 of 2015 is expected to be worse and for the full year the S&P 500 is expected to show virtually no earnings growth.

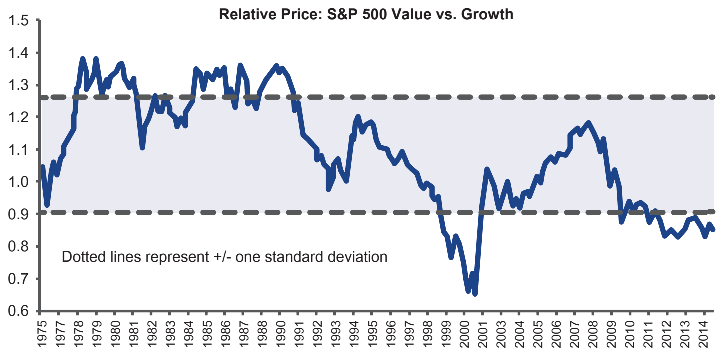
Top line growth has declined for the S&P 500



Source: S&P, Haver Analytics, Barclays Research

As growth has become scarce, the stocks of companies with high revenue growth are in demand. As investors flock to these higher-growth companies (and generally away from the value stocks), the performance divergence continues while also expanding the relative valuation difference between the two groups of stocks. In a recent research note, BMO Capital Markets' Chief Investment Strategist Brian Belski wrote "there have been only two other times where the relative price of value versus growth was at such abnormally low levels (1975 and 2000). Following such depressed levels, value embarked on a prolonged period of outperformance following both periods."

Exhibit 2: Growth Outperformance Has Reached Abnormal Levels



Source: BMO Capital Markets Investment Strategy Group, FactSet, Bloomberg.

Value Relative Performance Following Other Abnormal Relative Price Troughs

Period	CAGR	Duration (years)
4/75 - 3/78	15%	3
6/00 - 3/07	9.6%	7
Average	**12.3%**	**5**

Source: BMO Capital Markets Investment Strategy Group, FactSet, Bloomberg.

Belski also makes the case that higher interest rates and an improving economy will ultimately be beneficial for value stocks. "The relative performance of value has been highly correlated with the direction of interest rates over the past decade. More specifically, as rates have declined, value has underperformed. This makes sense to us because our work shows that more stable and mature companies – a common characteristic of value stocks – are better able to fundamentally withstand higher interest rates while growth stocks tend to perform better in low or declining rate environments. Thus, we believe value will benefit from the expected long and gradual march higher for rates in the coming years".

Value investing will also benefit as an improving economy will make growth more plentiful and investors will likely generate the best returns by owning the most inexpensive names. As profits start to improve growth becomes a plentiful commodity, while value looks rarer. The rising tide should help raise all boats, but as value stocks are cheaper, they typically perform better.

Aside from offering potentially better returns over the next few years, we also believe value stocks currently offer better downside protection as well. Market preference for growth stocks over value stocks has widened the valuation discrepancy between the two groups. The fastest growing companies usually trade at a higher price-to-earnings multiple than the S&P 500, but the gap is wider than normal currently. Many growth stocks look very expensive and are prone to pullback. Many of these popular names are burdened with unrealistic upside expectations and any disappointment in news or earnings could lead to a sell-off. Meanwhile, most value stocks already discount a lot of bad news and the low valuation multiples should help protect them from much further downside.

Interestingly, the last time growth outperformed value (prior to the current cycle which began in 2007) by such a wide margin it was in 1999 during the tech bubble. While not directly comparable to current conditions, the resilience of value stocks during the subsequent market correction is notable. After peaking in March 2000, the broad market Russell 3000 Index declined 22.0% over the subsequent year. The growth stocks within the Russell 3000 dropped a whopping 42.4% over the same period. Meanwhile, the value stocks managed to eke out a small gain of 1.9%.

If you would like to take advantage of the impending shift of investment style in favor of value stocks, consider an investment in Norrep US Dividend Plus Class. It is a core fund that offers exposure to U.S. dividend-paying companies of all sizes. It is managed using a strict value discipline using quantitative screening and fundamental analysis to filter through thousands of stocks to construct a concentrated portfolio of our best ideas. The portfolio exhibits very attractive value characteristics with a dividend yield of 2.9% and a price to earnings ratio of 14.6, which compare very favorably relative to the broad market and the vast majority of our peers. We believe the eventual shift back to value investing will provide a strong tailwind supporting the Fund's performance for many years to come.

WRITING OPTIONS TO PROFIT FROM SIDEWAYS MARKETS AND SELLOFFS

Kamran Khan, CFA

October 2014

The last five years was easy – simply buy and hold

You're not a raging bull anymore. There, I said it. It's okay to admit it. After all, the S&P 500 has almost tripled from the lows five and a half years ago. Plus, there's more than a few issues to be concerned about. The Fed may soon embark on a path towards higher interest rates. The European economic recovery remains uneven. China's economy is slowing down. Geopolitical tensions continue in Ukraine and the Middle East.

While we acknowledge the risks out there, we remain encouraged by the many positive traits exhibited by U.S. equities. The U.S. economy continues to steadily improve across a variety of indicators, including production, consumer confidence, housing and employment. In Q2 earnings growth came in at 9% year over year, the best quarterly growth rate in two and a half years. Higher earnings should remain the primary driver for higher stock prices going forward.

But I think we can all agree on one thing – while the outlook still looks positive returns for the stock market are likely to be lower over the next five years. After all, it's pretty difficult to top a five and a half year total return of close to 24% per year. Add in the possibility of more sideways markets and increased volatility, I think we can also agree that it might be time to consider additional investment strategies aside from simply buy and hold.

Need more options for the next five years?

Selling (or writing) call and put options within an equity portfolio can be a great way to generate income in a flat or moderately growing stock market, to protect gains on existing positions or to take advantage of market dips by acquiring stocks at lower effective prices.

The buyers of call and put options use the contracts to hedge positions, buy and sell stock, and speculate. The speculators are either very bullish (in the case of calls) or very bearish (in the case of puts) investors that want to make leveraged bets on a stock's directional move.

But if you are neither very bullish nor very bearish, and your return expectations are more modest, writing options might be a preferable strategy.

Call options have got you covered

Suppose you've been a happy owner of Apple stock, which has risen 32% in the preceding six months. Trading at $100 a share currently, you believe the stock's short-term prospects might be muted given the significant rally already witnessed leading up to the new product releases. To generate some income and protect existing gains, you can sell (or write) Apple call options with a strike price of $102 and an expiry date of October 31. The price (or premium) received for writing these call options is $2.35 per share. This strategy of owning the stock and selling call options against the position is known as a covered call strategy. For the sale of one contract (representing 100 shares of Apple stock) you will receive $235 (100 shares x $2.35 premium per share) in option premium income from the buyer of the option.

Under a variety of Apple stock scenarios, this strategy makes sense versus the alternative of just simply owning the stock. If Apple stock declines from $100 over the next month, the buyer's call option to purchase the stock at $102 will expire worthless. You will have pocketed the premium income of $2.35 per share, which would help offset the lower value of Apple's stock that you own. Theoretically, Apple's stock could decline by $2.35 (from $100 to $97.65) and you would still be break-even on your entire position over the month. If Apple stock is flat over the next month, you also win. The buyer's call options expire worthless while you have no obligations after earning the $2.35 premium. Essentially your return on the position for the month is 2.35% whereas a long only position in Apple stock would have returned nothing. The covered call strategy can be superior even if the stock's return is positive over the period. Even if Apple stock returns 2% over the month and rises to $102, the options will still expire worthless. So the seller of the option will have benefited from a $2.00 increase in Apple's stock price plus the $2.35 premium received for a total gain of $4.35 (return of 4.35%). If Apple's stock price rises above $102 the call options will ultimately get exercised by the buyer and the seller will be obligated to deliver their Apple shares for a price of $102 per share.

The covered call strategy makes sense as long as Apple's stock doesn't increase beyond $104.35, which is the stock price where the profits for the long-only position and the covered call strategy are equal. With any Apple stock price above $104.35, you'd be better off avoiding the covered call strategy because the premium income of $2.35 wouldn't compensate for the lost profits above the strike price of $102.

Put options will pay you while you wait

Selling put options is a great way to acquire a stock that you wouldn't mind owning if the price falls to a certain level. Suppose you like Apple's long-term prospects but want to be more opportunistic instead of paying the current $100 share price. To generate some income while you wait patiently, you can write Apple put options with a strike price of $98 and an expiry date of October 31. The price (or premium) received for writing these put options is $2.27 per share. This strategy of selling puts against stocks you wouldn't mind owning is known as a short put strategy. For the sale of one contract (representing 100 shares of Apple stock) you will receive $227 (100 shares x $2.27 premium per share) in option premium income from the buyer of the option.

Under a variety of Apple stock scenarios, this strategy makes sense versus the alternative of just simply buying the stock at the current market price of $100. If Apple stock increases from $100 over the next month, the put option to sell the stock at $98 will expire worthless. You will have pocketed the premium income of $2.27 per share, which would help offset the lost profits from not owning the stock outright. Theoretically, Apple's stock could increase by $2.27 (from $100 to $102.27) and you would still be indifferent between buying the stock or writing the put option. If Apple stock is flat over the next month, you also win.

The buyer's put options expire worthless while you have no obligations after earning the $2.27 premium. Essentially your return on the position for the month is 2.27% whereas a long only position in Apple stock would have returned nothing. The short put strategy can be superior even if the stock's return is negative over the period. Even if Apple stock returns -2% over the month and declines to $98, the options will still expire worthless. So the seller of the option will have avoided a $2.00 decrease in Apple's stock price while still retaining the $2.27 premium received for a total gain of $2.27 (return of 2.27%). If Apple's stock price falls below $98 the put options will ultimately get exercised by the buyer and the seller will be obligated to accept delivery of Apple shares for a price of $98 per share. Even under these circumstances, the short put strategy is preferable to an outright purchase of the stock because the premium received for the written puts helps subsidize the purchase cost of the stock.

Risks with options

The main risks when writing options comes with significant moves in the underlying stock prices. For example, a stock with covered calls written against it gets acquired and you miss the majority of the upside move in the price. Or, you've written short puts for a company that cuts their earnings outlook and the stock plummets. But even under these circumstances, it depends on how you view the situation. The alternative for writing puts against the stock that plummeted would have been to simply buy the stock since you liked it anyway. Without the option premium from the written puts you'd actually be paying more for that stock. And in the case of the covered calls, those are typically written on stocks where the short-term upside appears muted. It could be argued that without the income generation of a covered call strategy, the investor's alternative might havebeen to sell that stock outright and replace it with another with better near-term prospects. Either way, that significant upside move may not have been realized by the investor.

Getting active with options

Options allow you to tailor investment strategies to take advantage of different market environments. The possibilities are truly endless. It can be a daunting task to screen over a thousand companies with listed options available and then filter through tens of thousands of options with different strike prices and expiry dates.

The Norrep US Dividend Plus Fund has been writing options for several years. It's not a systematic approach that blankets the entire portfolio with options. Instead, it's quite opportunistic and tailored to the specific risk/reward expectations for existing and new positions. Their use was quite limited in the past however over the past year the Fund has broadened their use in the portfolio. In an environment where returns are more volatile and stocks might move sideways in the short term, we believe option writing can enhance the active management of the Fund, help differentiate us from our peers and most importantly add value for our clients.

ACCELERATING ECONOMY, HIGHER EARNINGS AND STRONGER USD

Kamran Khan, CFA

February 2014

Outstanding performance in 2013! Bright outlook for 2014.

U.S. equities delivered very strong performance in 2013, returning in excess of 30%. Strong performance came despite a wall of worries throughout the year – including the effects of a government shutdown, the threat of a U.S. debt default, prospects of Federal Reserve tapering, concerns over a hard-landing in China and geo-political turmoil in the Middle East.

As global equities end the first month of 2014 on a soft note over concerns such as tapering, emerging markets and valuations, many investors are asking what to expect for the remainder of the year. Our outlook remains positive based on improving global economic growth, higher corporate earnings growth and improving investor sentiment.

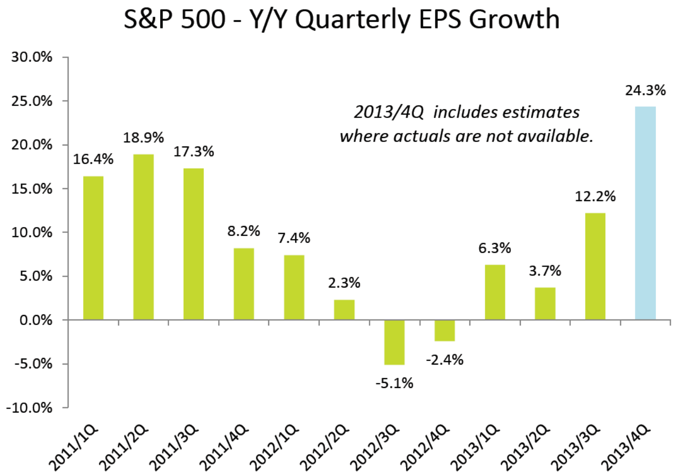
Economic growth is accelerating

U.S. GDP growth is expected to accelerate from 1.8% in 2013 to 2.7% this year, supported by fading fiscal austerity, higher spending from consumers and businesses, as well as improving exports.

With the U.S. federal budget on a sustainable course in the near term, the fiscal drag from tax hikes and spending cuts will fade almost completely after carving about 1.5% from growth in 2013. In fact, the federal fiscal drag in 2014 will be less than a third

of that in 2013. Rising state and local government spending could add to the growth. More states plan to lift infrastructure spending, while cities are re-hiring after laying off staff during the recession.

U.S. consumer spending is expected to strengthen in 2014 in response to record household wealth, supported by higher housing and stock prices, lighter debt loads, improved employment, and the highest consumer confidence levels of the past six years.



Additionally, for the first time since the Great Recession of 2009, consumers will see wages grow faster than inflation. All of these factors will likely support pent-up demand for housing and autos.

U.S. business investment should gain strength as the fiscal uncertainty fades this year. Companies are sitting on record amounts of cash, ready to be unleashed on capital and labour as the global economic outlook brightens. Less fiscal drag in the U.S., a return to modest growth in Europe, and a stabilizing Chinese growth rate all point to a notable pick-up in global GDP this year. In fact,

2014 will likely mark the first synchronized rise in global growth since 2010, which will also help boost U.S. exports.

Corporate earnings growth improving, fund flows should favour equities With recovering U.S. and global economic growth, U.S. earnings growth is also expected to improve to nearly 10% in 2014. With improved earnings and strong balance sheets, corporations should continue buying back shares and increasing dividends, which is great for shareholders.

Investors have taken notice of the improving prospects for U.S. equities as 2013 marked the first year of fund inflows since 2007 and the largest inflows since 2000.

As government fixed income yields grind higher and bond prices move in the opposite direction, share prices should continue to be supported by assets shifting out of bonds and into stocks.

Valuations are fair, the bull market can continue

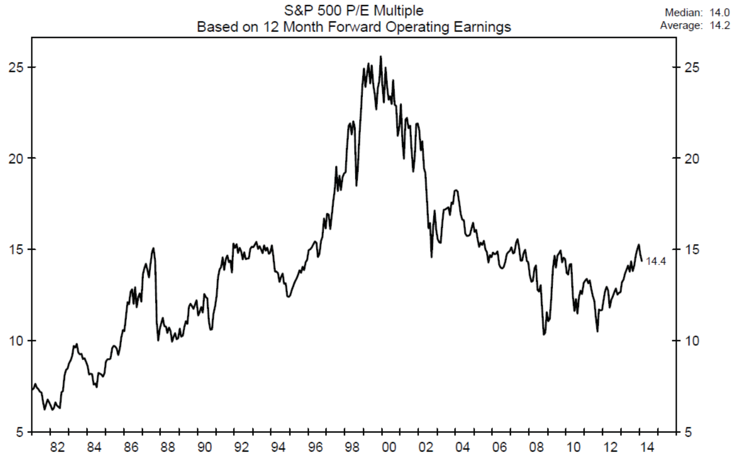
As is typical following any big performance year, some investors may be questioning whether stocks are overvalued and whether the gains can continue. A good portion of the rally last year was due to expanding multiples (investors paying a higher price for the same level of earnings or cash flows) as the market removed the valuation discount associated with lingering risks from the financial crisis. According to Bloomberg, the S&P 500 currently trades at 14.8 times current year's forecasted earnings. Equities may not be cheap, but certainly aren't in bubble territory either. By most measures, stocks are fairly priced and the forward path will depend on profit growth, rather than multiple expansion.

The bulls argue that stocks continue to look attractive, especially relative to expensive government bonds. Bond yields remain historically low, with 10-year U.S. T-bills yielding barely 3%. When yields are low, it is justifiable to pay a higher multiple for stocks because cheaper credit makes it easier for companies to make profits. Paying more for stocks also seems more palatable when bond yields are so low. The quality of corporate balance sheets today is unparalleled, which also warrants higher price-earnings multiples.

It is a mistake to confuse a bullish mind-set with the euphoria that often signals a market top. There is little evidence to suggest that investors are growing overexcited, as they usually do, towards the end of a bubble.

According to the widely followed AAII Investor Sentiment Survey, 32% of members consider themselves bullish, while 33% of members are bearish. These numbers hardly point to overly exuberant markets. Another telltale sign of a bubble is elevated M&A activity. On this measure, 2013 ranked as the slowest annual period for global deal-making since 2009.

The bulls also believe that March 2009 represented a generational low for stock prices, and that we are currently in the middle of a sustained bull market. The bull market, which celebrates its fifth birthday on March 9, 2014, is likely to remain strong in year six. History shows that secular, or multi-year, bull markets that last



more than five years tend to perform well in year six and don't normally end until a recession derails the rally by halting economic growth and crimping corporate profits. However, with the U.S. and global economies gaining strength, and monetary policy expected to remain supportive, a recession is unlikely.

Past market behavior also suggests "good years tend to follow great years". According to historical data compiled by S&P Capital IQ, since 1945, there have been 21 times when the S&P 500 gained more than 20%. In the following year, the S&P 500 recorded an average increase of 10%, versus an average price gain of 8.7% for all years over the same period.

Fed tapering doesn't mean tightening monetary policy

When Janet Yellen moves from board member of the Federal Open Market Committee (FOMC) to chairman early in 2014, she faces the challenge of exiting an era of easy monetary policies gracefully. Although the Fed indicated it would start tapering off its monthly bond purchases in December, it also said interest rates will stay at virtually zero until well into 2015. In fact, the S&P hit a record high after the taper announcement.

We expect the central bank to wait longer before raising rates. Instead, we see the Fed using "forward guidance". This means a lot of reassuring promises not to raise interest rates until the economy is strong enough to warrant it. For those still concerned about tapering, keep this fact in mind -- 2014 is set to be the second-most accommodative year in U.S. monetary history (after 2013).

Norrep US Dividend Plus Class can take advantage of investing opportunities in U.S. equities While we expect the upcoming year to be good for equity investors, we also acknowledge that returns are likely to be lower than the phenomenal returns of the past two years. We believe 2014 will be marked by higher volatility and as a result will favour experienced stock pickers. The enhanced volatility creates many great buying opportunities for Norrep US Dividend Plus Class, which has the flexibility to invest in large, mid-sized or small capitalization companies, depending on which offers the best return prospects.

Another factor which we believe will support Fund performance in 2014 is the strengthening U.S. dollar relative to the Canadian dollar. The Fund invests primarily in U.S. dollar denominated securities (U.S. equities) but is priced in Canadian

dollars, consequently the fund actually benefits from a strengthening U.S. dollar. A mixed outlook for commodities, a heavily indebted Canadian consumer, and a dovish turn by the Bank of Canada all argue for continued weakening of the loonie relative to the greenback.

LOOKIN' FOR DIVIDENDS (IN ALL THE RIGHT PLACES)

Kamran Khan, CFA

April 2013

Interest in dividend investing strategies continues to grow as investors are attracted to the lower volatility offered by dividend-paying stocks, the stable income in an environment of low government bond yields, and the potential for capital appreciation. If that weren't reason enough, stocks with higher dividend yields have outperformed their peers with lower dividend yields over the long-term. This superior track record has been witnessed in both large and small cap stocks in the U.S.

However, as more money finds its way into dividend-focused funds, we wonder whether investors are getting adequate exposure to all the dividend-paying opportunities available in U.S. equities. A closer look at the universe of dividend-paying stocks and the mutual funds available to Canadian investors highlights the disconnect between available opportunities and the typical fund composition. According to Morningstar Canada data, approximately 80% of the dividend-focused funds in the U.S. Equity category have an average market capitalization of more than $25 billion, suggesting significant exposure to larger companies. However, when you look at the universe of dividend-paying stocks in the U.S., the vast majority of these companies are not found in the large cap Dow Jones or S&P indices. They are small and mid-sized companies with market capitalizations under $10 billion. Some household names that investors might recognize in this segment are Iron Mountain, Ryder, Hasbro, Smucker's, Foot Locker and Safeway. By largely ignoring this segment of the U.S. equity market, most dividend funds are missing out on the majority of opportunities.

Quenching the thirst for yield and income

Having a larger universe of dividend stocks to choose from will help meet the challenge of delivering yield and income in the current environment of low bond yields. The dividend yields of many country stock indices around the world are now higher than their respective 10-year government bond yields. With the compression of corporate bond spreads over the past year, equity dividend yields are compelling even versus investment grade bonds. Many dividend-paying stocks offer a comparable yield to investment-grade bonds, offer potential upside from capital appreciation, and don't carry the same risks from rising interest rates. As an aging population confronts the challenges of generating regular income from their investment portfolio, dividend-paying stocks should become a more viable alternative for many investors.

	Yield
U.S. Treasury 10-year Bond	1.88%
BofA Merrill Lynch US Corporate Index	2.78%
BofA Merrill Lynch US High Yield Index	5.83%
Russell U.S. Large Cap High Dividend Yield Index	4.04%
Russell U.S. Small Cap High Dividend Yield Index	3.81%

Data as of February 28, 2013

Dividend strategies have room to run

Dividends continue to grow at a healthy rate indicating good corporate profitability and management confidence. With dividend payout ratios near all-time lows and corporate cash near peak levels, there remains significant potential for rising dividends going forward. Finally, the most tell-tale sign of a saturated trend or theme is when a majority of investors are replicating the strategy. According to Morningstar, only a small number of U.S. Equity funds in Canada (~11% of the funds in the category) emphasize a dividend focus and exhibit a portfolio yield over 2.5%. While dividend strategies have garnered more attention from the media recently, we believe these strategies are far from being saturated and will remain attractive to investors going forward.

Recovering U.S. economy and improving U.S. equity markets

U.S. equities delivered very strong performance in 2012, with small, mid and large cap indices up between 16% and 18% for the year. They have also had a strong start to 2013, with U.S. markets among the world's top performers year-to-date. Strong performance has been supported by healthy earnings growth, improving sentiment towards macro concerns (i.e., Europe, China, U.S. deficit), and a re-rating of valuation multiples from depressed levels. In hindsight, there were many reasons to be positive about stocks over the last year. We wrote a research piece at the beginning of last year titled "10 reasons to be positive on U.S. equities in 2012". Many of those same positives continue to ring true today suggesting a slow but steady continuation of this four year old bull market.

While several U.S. equity indices are hitting fresh all-time highs, the recovery in economic activity has been more subdued. Consumer and business spending has been muted over concerns of a slowing global economy, Washington budget theatrics, and the upcoming uncertainty over sequestration. All these factors should weigh on economic growth in the first half of 2013 and economic forecasts have been revised downwards to reflect that growing reality. However, uncertainty and restraint in the first half should transition into increased visibility and recovery in the second half. Consumer spending should benefit from a further recovery in housing prices, improving labor markets, rising stock prices and a much improved balance sheet from four years ago. Businesses should have more visibility and confidence over fiscal budgets and global economic growth prospects to increase spending on labor and equipment, especially considering the pristine condition of their balance sheets. The exciting prospects offered by a recovering U.S. economy have not gone unnoticed by investors and sentiment towards U.S. equities has certainly improved over the last few years. Strong performance, a recovering economy and attractive valuations have started to entice more investors.

A unique solution to deliver yield and growth in the world's largest market

The Norrep US Dividend Plus Class offers Canadian investors exposure to all of these themes and many other sought-after features in today's investing environment. The Fund delivers regular income, capital gains potential, exposure to a recovering U.S. economy, diversification away from resources, and a differentiated all cap approach that differs from its peers and most exchange traded funds.

THE RESILIENT PERFORMANCE OF U.S. MICROCAPS

Kamran Khan, CFA

August 2012

Large cap U.S. equities have garnered a lot of attention this year. The S&P 500 Total Return Index is up 11.0% year-todate until July 31, 2012 and is among the best performing indices around the globe. However, more surprising is the 11.3% return generated by the Russell Microcap Total Return Index over the same time period. The Index measures the performance of the microcap segment of the U.S. equity market with most of its constituents having a market capitalization under $500 million. At first glance, the strength of microcaps in a period of heightened economic uncertainty flies in the face of conventional wisdom. However, a deeper analysis of the situation lends credibility to the resilient performance of these small companies.

The U.S. is often considered a safehaven market that attracts fund flows in times of heightened uncertainty. As well, economic prospects have held up better in the U.S. while most other economies are experiencing a sharper slow down or even declining. While large cap U.S. equities will benefit from the relative strength of the recovering U.S. economy, it's important to recognize that large caps also have higher exposure to the global economy.

According to Bank of America research, 40% of S&P 500 profits are generated outside of the U.S.. Meanwhile, small caps (particularly microcaps) offer much more exposure to the recovering domestic U.S. economy.

While economic growth forecasts have been revised down over the past year, the implications for the U.S. equity market aren't necessarily negative. In fact, small cap performance in historical market cycles would suggest the opposite. In a low GDP growth economic environment (IMF forecasts economic growth of 2.0% in 2012 and 2.3% in 2013), small caps typically perform very well and outperform large caps. Recent research from Credit Suisse highlighted 11 historical periods when U.S. real GDP ranged between 2 – 3%. The average small cap return in those instances was 22% with positive absolute returns generated 82% of the time.

Another factor of slower economic growth is that it highlights the relative growth opportunities between large and small caps. Mega caps with large revenue bases and established global presences simply don't have the ability to grow as quickly as their smaller competitors. In contrast, smaller companies operating in niche markets or select geographies with limited international operations offer more avenues to achieve higher revenue growth. The ability to grow faster offers better return potential as has been proven over very long periods of time with small cap investing.

The growth challenge facing mature large caps also bodes well for small caps from an M&A (Merger & Acquisition) perspective. Today, large companies have strong balance sheets, large cash positions and healthy free cash flows. Given lackluster economic growth rates, they are likely to opt for acquisitions to augment their organic growth going forward. Acquisitions can often be an easier way for large companies to enter niche markets or geographies, enhance their growth profile and potentially be accretive to existing shareholders at the same time.

We remain excited about the prospects of smaller companies in the United States. Microcap valuations have declined considerably over the last five years. They now offer a compelling combination of value and better relative growth prospects, along with the possibility for M&A participation. The lack of analyst coverage and institutional following among many small caps also creates inefficiency from time to time that manifests itself in to great buying opportunities. The Norrep US Class is well positioned to benefit from the recovering U.S. economy and the many drivers supporting the performance of small caps. The Fund invests in a portfolio of small companies ranging from microcaps to mid caps. It is managed using Norrep's methodology that combines quantitative screening with thorough fundamental analysis. We've assembled a concentrated portfolio of high quality U.S. businesses that offer attractive return prospects over the next several years and provide attractive diversification for Canadian equity investors.

10 REASONS TO BE POSITIVE ON U.S. EQUITIES IN 2012

Kamran Khan, CFA

January 2012

As we begin another investing year, we would like to take this opportunity to thank you for your continued investment with us. 2011 was certainly a challenging year to be an equity investor. A barrage of negative events weighed on global growth expectations and conspired to lead stock markets lower throughout the second half of the year. While several risks and uncertainties remain on the horizon, we fear that excessive focus on these concerns may be overshadowing the many investment positives in the year ahead.

Therefore, to offset the negative headlines dominating the financial media and to re-focus attention on the longer-term thesis, we present our top 10 reasons to be positive on U.S. equities as we begin 2012.

1. U.S. economic data has recently been better than expected

Over the past few months, U.S. economic data has surprised to the upside. The outperformance has been broad based including positive surprises in industrial production, business orders, retail sales, consumer confidence and housing starts. Even the persistently weak labour market showed improvement with non-farm payrolls rising and the unemployment rate edging down to 8.5% in December.

2. Corporations continue to exhibit strong revenue and earnings growth, with mostly upside surprises

Despite the gloomy macro headlines last year, company financials have been resilient. A report from early December calculated that stocks within the small cap Russell 2000 Index posted 12.8% revenue growth and over 30% earnings growth for the latest reported quarter. Earnings also came in well ahead of analyst expectations, surprising by over 5% on average.

3. Great corporate balance sheets with high cash levels, record high margins and strong cash flow

The much-improved financial position of most corporations has been well covered by the media. Companies remain in a great position to spend excess capital on inventory, equipment or new hires once sentiment improves. Alternatively, companies simply initiating or increasing dividends and/or pursuing stock buybacks could be a significant catalyst to drive equities higher.

4. Improving relative performance of U.S. equities

U.S. equities rank among the world's top performers for 2011. The S&P 500 Index was up 2.1% in 2011 while the Dow Jones Industrial Average rose 8.3%. While U.S. small caps as measured by the Russell 2000 Index fared worse, down 4.2%, they handily outperformed the S&P/TSX Composite Index (down 8.7%) and the BMO Small Cap Weighted Equity Only Index (down 16.9%). Among the worst performing equity markets last year was China, whose 20%-plus declines even exceeded those of many battered European markets. After a decade of underperformance, an increasing number of market pundits believe the U.S. will remain among the world's best equity markets for years to come.

5. Largest investable universe with plenty of options outside of resources

The main reason for Canadian equities underperformance this year was their high leverage to the commodity cycle, with close to half of their market capitalization comprised of Energy and Materials. Commodity prices have been under pressure since April over concerns about construction bubbles and a Chinese hard landing. In stark contrast, the U.S. equity indices have less than

15% of their composition in resource sectors. They also offer many more defensive options in sectors such as Health Care, Consumer Staples, Telecom Services and Utilities.

6. Accommodative fiscal and monetary policy

Central banks continue to keep interest rates low and governments have been careful not to withdraw stimulus from the economy too quickly. The U.S. FOMC recently reiterated that interest rates would stay near zero through at least mid-2013 and the possibility of a new round of asset purchases is becoming increasingly likely in the first half of 2012. Even China is in a better position to begin lowering interest rates with headline inflation easing lately. Governments and central banks willing and ready to act as economic conditions warrant should limit the downside risk in equities next year.

7. Potential for increasing M&A activity

A decelerating global economy increases the challenge of growing the top line, especially for larger sized companies with an already big revenue base. Fortunately, most of these companies are in excellent financial shape and have large cash balances to make necessary investments to grow. While companies will continue strategies to grow organically such as introducing new products and services or by expanding into new regions, many will choose to grow through acquisitions. And declining equity prices and valuations for many small caps are making the case for M&A even more compelling.

8. Valuations are very attractive

While there are always risks in investing, what matters from a potential return standpoint is whether those risks are reflected in stock prices. In other words, do the equity valuations discount the risks and uncertainties in the market? With the S&P 500 trading at an 11x forward P/E multiple and U.S. small caps trading at large discounts to their 10-year average multiples, we believe it is an attractive entry point to add positions in U.S. equities. In the Norrep US Class, we've managed to construct a portfolio that trades in-line with larger caps at 10.6x forward P/E, but offers much better growth prospects and should be a bigger beneficiary of increasing M&A activity.

9. Value investing style should begin to outperform

Participants in the equity markets are well aware that style biases can have significant impacts on relative performance, especially for time horizons up to three years. The most memorable example of style driving performance was the massive outperformance of growth managers during the years leading up to the tech bubble and the subsequent outperformance of value managers as that bubble deflated over the next several years.

Growth investing has performed relatively better lately with three consecutive calendar years of outperformance within the Russell 2000 U.S. small cap universe. This has only occurred one other time in the last 30 years, between 1989 and 1991. What followed that period was value outperforming growth by over 30% in the subsequent three years. Our Fund's focus on value investing should be rewarded as we move forward.

10. Sentiment is depressed and consensus is cautious about 2012

Contrarian investors believe that you can't make money by simply following the crowd. With the financial media and investors so focused on the negative headlines, we believe the risks are priced into the stock market. In fact, the market is in a better position to be surprised on the upside given lowered expectations. As legendary investor John Templeton wrote - "Bull markets are born on pessimism, grow on skepticism, mature on optimism and die on euphoria".

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U.S. EQUITIES: A CONTRARIAN INVESTING OPPORTUNITY

Kamran Khan, CFA

October 2010

According to EPFR Global, there has been a stampede out of US stock funds this year with outflows totaling $51 billion. With such an overwhelming sense of pessimism, a laundry list of concerns and a general lack of investor interest, U.S. equities may just offer the next big contrarian investing opportunity.

In finance, a contrarian is one who attempts to profit by investing in a manner that differs from the conventional wisdom. Essentially, a contrarian investor goes against the crowd. A contrarian might believe that widespread pessimism surrounding U.S. equities have driven prices so low that they overstate the market's risks and understate the prospects for improving profitability.

The decision to abandon U.S. equities in favour of fixed income or emerging markets is usually supported by a variety of investor worries. After years of listening to various market participants, I believe those concerns can be narrowed down to five key areas: debt levels, a weak consumer, lower economic growth, poor historical performance and a weakening currency.

The important questions for the contrarian investor are whether these risks are overstated and whether the market has already discounted these risks in current stock prices. To answer these questions, let's dig deeper into those five areas of investor concern.

Debt Levels

U.S. government debt currently hovers around $13 trillion. Debt levels have experienced rapid increases since the onset of the global financial crisis.

Most countries have seen significant increases in government debt levels due to higher stimulus-related spending combined with falling tax receipts. While U.S. debt is quite high relative to many emerging economies, it is actually in-line with the larger developed markets. In fact, only Canada has a lower net debt to GDP ratio than the U.S. within the G7 nations.

Nevertheless, elevated debt levels require close scrutiny by all levels of government. On the bright side, viable options are available to improve upon the current situation. Through a combination of spending cuts and increased revenues, the U.S. can outline a plan to reduce deficits and reign in government debt.

The good thing about reigning in costs in the world's largest economy is that there is lots of fat available to trim. While there are many places to cut costs, key areas of focus will include reforming entitlement programs, such as Medicare and Social Security and reversing recent increases in military spending.

While the recent passage of health care reform came with a slew of reimbursement cuts for industry participants, many politicians argue that more can be done to control the rising cost of health care. Thus, it is very likely that the highly-debated, nationalized, single-payer system will be revisited in the years to come along with many other options for dealing with escalating health care costs.

Military spending is already in the crosshairs according to comments from Defense Secretary Robert Gates. The Pentagon must hold down its spending and make choices that will anger "powerful people" in an era of economic strain, Secretary Gates said in a recent speech.

With a $535 billion budget expected for 2010, the Department of Defense base budget equals the entire national debt of Canada. Items contributing to a swelling military budget include a top-heavy uniformed and civilian management force, big-ticket weapons systems and increasing health care costs. Not to mention the wars in Iraq and Afghanistan. As polls show rising public opposition to both wars and as President Obama strives to fulfill campaign pledges, we should see a continued decline in military spending.

Aside from spending cuts, the other side of solving the debt problem will come from higher revenues. Among the items being debated are higher estate taxes, higher marginal income-tax rates and even the possibility of a value-added tax.

Many options are available for tackling the U.S. debt – they just require the political will to proceed. With this in mind, President Obama created the bi-partisan National Commission on Fiscal Responsibility and Reform earlier this year. It's main objective – reigning in the soaring federal debt. The panel's recommendations, due out later this year, should provide further clarity towards solving this problem.

Weak Consumer

Another commonly used argument against U.S. equities follows quite logically. The consumer is 70% of the U.S. economy and the consumer is weak, therefore avoid U.S. equities. This argument is deceptively simple and starts to break down under closer scrutiny.

The problem is most people associate consumer spending with iPods, Ugg boots and fancy dinners. While personal consumption does make up 70% of U.S. GDP, 75% of that household spending is non-discretionary in nature. That would include items such as housing, healthcare, energy, groceries and other household staples.

Only 25% of personal consumption is discretionary spending, which equates to less than 20% of U.S. GDP. While discretionary spending is still important to the U.S. economy, it's not nearly as relevant as the scary headlines might suggest.

Lower Expected Growth

Why invest in U.S. and other developed markets when China, India and other emerging markets are expected to grow faster? If only it was that simple.

The expectation of slower economic growth from the U.S. and Europe versus China, India and other emerging nations is not a new phenomenon. Developed markets have typically exhibited lower growth than emerging markets – it's probably why they're called developed markets to begin with.

More importantly, despite a long history of higher economic growth, emerging markets have underperformed developed markets over the long term. In fact, between 1975 and 2009, emerging markets provided an annualized return of 9.5% while developed markets provided an annualized return of 10.6%. That equates to more than 1% underperformance annually over 35 years.

The significance of this performance differential is even more surprising when we consider the major economic and financial events that transpired in these markets. Within the developed markets, we witnessed two lost decades of economic performance from Japan, a decade of flat equity market returns in the U.S. and most recently, a financial crisis across Europe. Meanwhile, within the emerging markets, we saw China enter the World Trade Organization and quickly become an economic superpower while India experienced robust growth in its middle class of 300 million citizens. Yet, despite all this, emerging markets underperformed developed markets.

Research from three authors at London Business School sheds some light on these surprising performance figures. Looking at 83 countries over 110 years, Dimson et al found no evidence that investing in growth economies produced superior returns. Instead, they found that stock markets incorporate predictions of future economic growth into current valuations, often leading to disappointments relative to expectations. "Historically, the total return from buying stocks in the low-growth countries has equaled or exceeded the return from buying stocks in the high-growth economies."

More important than long-term growth prospects, which are difficult to accurately predict and subject to a barrage of unexpected events, is valuation. On this measure, U.S. equities appear very attractive, trading at 12x expected earnings.

Poor historical performance

U.S. equity performance has been awful for the last 10 years, with the S&P 500 providing negative returns of 1.8% annually. While the average investor would likely shun U.S. equities based on this track record, a contrarian investor would view this favorably for the return prospects over the next decade.

After all, the poor decade's performance is largely due to a starting date that begins in the year 2000, at the most lofty index levels of the technology bubble. In fact, for the 10-year period ending August 31, 2000, the S&P 500 returned a staggering 19.5% annually. We should have known performance like this simply isn't sustainable over the long term. What we've experienced in U.S. equities since then is a period of dramatically reduced earnings expectations, significant compression in valuation multiples and a normalization of returns.

Academics refer to this phenomenon as mean reversion, the tendency of a variable to converge towards its long-run average value over time. In layman's terms, what goes up tends to come down and vice versa.

Mean reversion occurs in nature and many economic indicators including GDP growth, exchange rates, interest rates and not surprisingly - stock prices.

Let's look at another example of mean reversion. Think back to the year 2000 when you were debating which investment funds to contribute to in your retirement account. Perhaps you glanced at the best and worst performers over the prior decade. Remember all the science & technology funds making the top performers list? It wasn't too hard with the S&P 500 Information Technology Index annualizing 31.5% for the 10-year period ending August 31, 2000. And certainly you noticed the awful performance of all those precious metals funds. It was tough to deliver positive returns with the S&P/TSX Gold Index down 4.2% annually over the same time period.

Fast forward to present day and have a look at this month's best and worst performers over the most recent decade. The tables have certainly turned. If you're looking for those high-flying technology funds, you'll need to glance over to the worst performers list. It's very hard to deliver positive performance when the S&P 500 Information Technology Index declined 8.8% annually over the latest 10-year period ending August 31, 2010. Meanwhile, many of the gold bugs who bailed out in 2000 aren't too pleased with their market timing ability. Over the same time period, the S&P/TSX Gold Index returned an average of 13.5% annually. Can you count how many times you see "Precious Metals" in the names of the top performing funds?

The bottom line is pay attention to the fine print in your investment prospectus. "Past performance may not be indicative of future results and returns." As legendary investor Jeremy Siegel showed in his book Stocks for the Long Run, which examined over 100 years of stock returns, strong future returns have often followed poor historical results.

In reality, when forecasting returns, valuations matter much more than historical performance. And today, U.S. equities aren't sitting at astronomical valuation multiples based on ridiculously optimistic forecasts. They trade at some of the lowest valuation multiples of the past 50 years.

Weak Currency

With the USD-CAD exchange rate of 1.066 at August 31, the greenback has declined 34% against the loonie since peaking at 1.614 in early 2002. The large decline of the USD combined with bouts of high volatility added to the sense of frustration for any Canadian holding an unhedged U.S. equity position by further hampering investment returns. The consensus view is that the Canadian dollar will continue to appreciate versus the U.S. dollar, supported by a stronger Canadian economy, higher commodity prices and our nation's fiscal prudence relative to the U.S.

While it's tough to make a bull case for the U.S. dollar, it's important to remember that a big reason for its devaluation has been the weaker relative performance of its economy and stock markets over the last few years. Just like economies and stock markets move in cycles and experience periods of mean reversion, currencies are subject to the same forces over long periods. This mean-reverting tendency over the long term is one of the reasons why many institutional investors prefer not to hedge their currency exposure.

If you prefer not to be subjected to the day-to-day currency fluctuations there are a wide variety of hedged investment options available to you. These strategies employ futures or some other hedging vehicle to substantially reduce the currency volatility. Of course, the hedging doesn't come free. Dan Hallett, an independent mutual fund analyst estimates that hedging costs can add up to 0.4 to 0.5 of a point to the cost of owning a mutual fund.

On the Brighter Side

While investing always entails some caution, it's important to put your concerns in perspective and assess the significance of those risks. High U.S. debt levels are a relevant risk but solutions are available to address this concern. A weak consumer is also an issue but the risk is often overstated in the headlines. Lower economic growth would seem to imply lower equity market returns, but the historical research would argue otherwise.

A poor historical track record may actually be viewed as a positive for future prospects. And if you can't handle those currency swings, there is a large and growing universe of hedged investment options available to you. And of course, let's balance the risks with the positives and examine everything in the context of current valuations. U.S. equities offer the largest potential universe of investment options with over 5,000 stocks to choose from in just about any market niche you can imagine.

For Canadians, they provide prudent diversification away from banks and resources into sectors not well represented north of the border, such as health care, consumer discretionary and information technology. They offer access to the brightest entrepreneurs in the world who practice in one of the most supportive political and regulatory landscapes. The U.S. economy offers a pure-play on free market capitalism – "the best path to prosperity" as Larry Kudlow reminds us each evening on CNBC.

With equity valuations closer to 50-year lows, I'd say the risks are well discounted in current prices, while the many positives offer significant upside for the contrarian investor.

CONTACT US

Phone 403.531.2650

Client Services 1.877.531.9355

Sales & General 1.877.431.1407

info@norrep.com

www.norrep.com

Calgary

Barclay Centre

Suite 1100, 606 - 4 Street SW

Calgary, Alberta T2P 1T1

Toronto

TD North Tower

Suite 4330, 77 King Street West

Toronto, Ontario M5K 1H6

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