CGOV ASSET MANAGEMENT

21 Bedford Road
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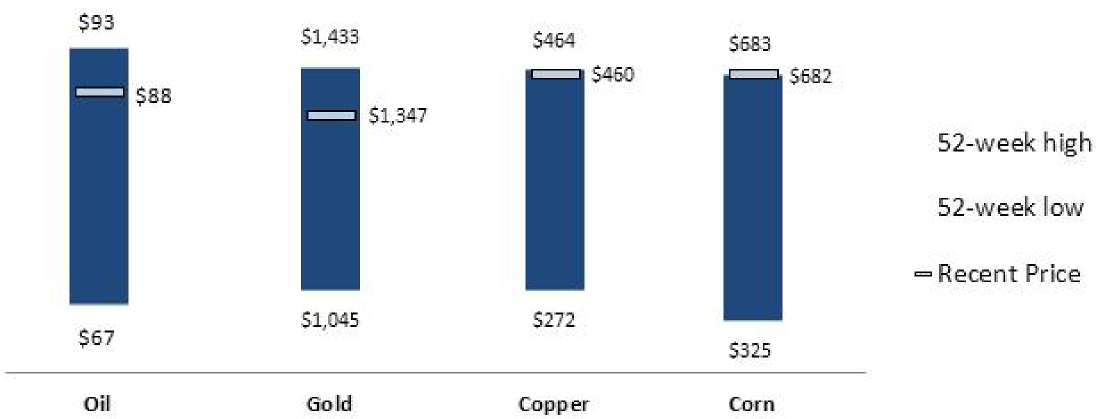
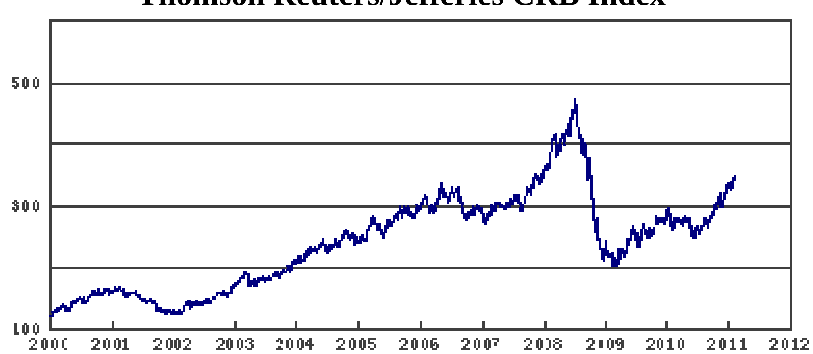
Equity Strategy

The effect of rising commodity prices on our businesses

Commodity prices are rising dramatically across the board. Some of our businesses will benefit while others will feel the pinch. The portfolio has a healthy dose of commodity producers (*Potash Corp, Compass Minerals, Kinross, Suncor, Crescent Point and Birchcliff*) that are prime beneficiaries of this trend. Instead of focusing on the obvious winners, we'll look at which companies can pass-through these increases and which companies will likely suffer.



Thomson Reuters/Jefferies CRB Index [1]



While commodity inflation is not as extreme as it was in 2008, the magnitude and speed that it is increasing is significant. This trend is expected to continue in 2011.

[1] The **Thomson Reuters/Jefferies CRB Index** is designed to provide an accurate representation of a broadly diversified investment in commodities.

Unilever reported a lower gross margin in the fourth quarter primarily due to increased commodity costs in the second half of 2010. Unilever was able to increase prices to recover some of these costs. Unilever is sensitive to increases in palm oil, sunflower oil and crude oil. Unilever is coping with higher raw material costs by squeezing out inefficiencies in its supply chain. Given the size and scope of its operations, Unilever has considerable bargaining power with its suppliers. Unilever recently established a *commodity risk management team* to mitigate some of the volatility they are experiencing.

Asia Pacific Breweries' profitability is affected by increases in the cost of raw materials and energy used in their operations. Most of the key ingredients used in alcohol production (*grains*) are subject to price volatility arising from changes in global supply and demand along with weather conditions and agricultural production. APB is also susceptible to changes in the price of glass and other packaging materials. Rising energy prices affect APB in terms of transportation costs to ship its products and operating expenses at the brewery level. While APB can increase prices, doing so could result in reduced sales volumes as consumers may switch to less costly brands.

In contrast to the prior three quarters of growth, **Nalco** saw its margins contract in each of its business segments during the fourth quarter resulting from rising commodity prices and material shortages. Nalco's water services division was hit the hardest. This coincides with multiple price increase announcements the company released during December and January to relieve some of this pressure. The company is increasing prices for customers across Europe, Africa and the Middle East by 5% to 15%. Nalco should be able to recoup these higher raw materials costs in the first half of this year barring no more significant price increases in 2011.

Given that **Lincoln Electric** is in the welding business, it is susceptible to increases in copper, silver, steel, brass, aluminum, electricity and natural gas prices. Lincoln's operating margins are dependent on their ability to manage the impact of the volatility of these costs. Lincoln tries to hedge their commodity risk with derivative financial instruments.

Pason Systems is a beneficiary of rising oil prices as demand for its services is directly related to its customers' capital expenditure programs. In an environment of high and stable energy prices, oil and gas exploration companies are willing to increase their capital expenditures and drilling activities. When energy prices are weak or very uncertain these companies tend to reduce their expenditures and base their capital decisions on more conservative outlooks.

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Conclusion

With approximately 25% of the portfolio allocated to commodity producers (*ex: Suncor and Potash*) and several companies that can pass-through these cost to their customers (*ex: Unilever and Nalco*), the **CGOV Equity Portfolio** is well positioned to withstand an environment of rising commodity prices.

Should you have any questions please feel free to contact me at any time.

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About CGOV

Established in 1995, CGOV Asset Management oversees in excess of $1 billion on behalf of high net-worth individuals and families, charitable organizations and institutions.

Our mission is to preserve and enhance our clients' capital while providing peace of mind. We do this by utilizing a disciplined and repeatable investment process that allows us to deliver superior long term results.

Mandates that we offer clients are: Canadian equity, Global equity, Global dividend equity and Balanced (includes fixed income)

CGOV Investment Committee


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Gord O'Reilly


Roy Hewson


Ted Ecclestone


Sheila Norman


Jim Green


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