

London Life Balanced Fund (\$14)

Q2 2010

Investor profile: Suited to the investor whose objectives are income and growth over the medium to long term.

Objective: The fund's objective is to provide a balance between long-term capital growth and current income by investing in Canadian and foreign equities and Canadian fixed-income securities.

Investment strategy: Laketon's is responsible for the ongoing asset mix decisions for the fund. In addition, they are responsible for the Canadian equity and fixed income components of the portfolio. The foreign equity component of the portfolio is delegated to specialty managers. Setanta Asset Management, a Dublin-based manager and London Capital Management, manage the non-Canadian equity components of our balanced mandates. Both managers use a GARP-like approach to equity management.

Investment performance

	Annualized rates of return (%)					
	Quarter	YTD	1 Year	2 Years	3 Years	5 Years
London Life Balanced	-3.5	-1.6	6.8	-1.6	-0.6	3.9
Benchmark	-3.1	-1.5	6.9	-2.8	-1.5	3.4
Value Added	-0.4	-0.1	-0.1	1.2	0.9	0.5

All returns are gross of fees. Prior to October 1, 2004, the Canada Life Fund equivalent was used.

Portfolio management team

Gary Morris, CFA (Fixed Income)
 Daphne Dodig, CFA (Canadian Equity)
 Ben Fawcett, CFA (Canadian Equity)
 Susan Spence, CFA (Canadian Equity)
 Setanta Asset Management (EAFE)
 London Capital Management (U.S. Equity)

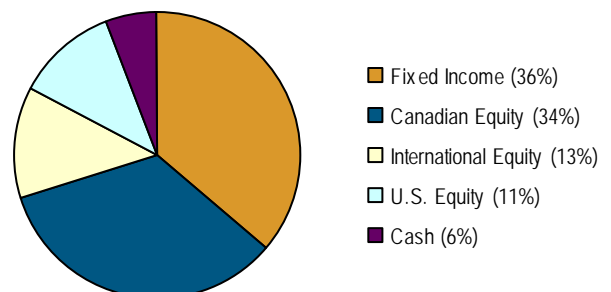
Portfolio information

Assets: \$120.8 million
 Benchmark: "Blended" benchmark as follows:
 35% S&P/TSX Composite
 35% DEX Universe Bond
 12.5% S&P 500
 12.5% MSCI EAFE
 5% DEX 91 Day T-Bill

Top 10 holdings

	Portfolio (%)
Govt of Canada 3.75% 06-01-19	4.8
Govt of Canada - Disc 09-02-10 02-SEP-10	4.3
Prov of Ontario 6.5% 03-08-29	3.2
Barrick Gold Corp	2.6
Canada Housing Trust 3.55% 09-15-13	2.3
Royal Bank of Canada	2.2
Canada Housing Trust 4.10% 12-15-18	2.2
Toronto-Dominion Bank	2.1
Government of Canada 3.50% 06-01-13	1.9
Canadian Natural Resources Ltd	1.8
Total	27.5

Asset class diversification



Fund performance attribution

Positive performance factors in the second quarter

Asset Mix

- A slight over weight position in fixed income added modestly to performance.

Security Selection

- The fixed income fund from a longer than benchmark duration over much of the quarter.

Negative performance factors in the second quarter

Asset Mix

- A slight over weight to international and US equities detracted from performance.

Security Selection

- International stock selection was slightly negative for the quarter.

Outlook & strategy

- The global economic recovery is proceeding to varying degrees across different countries, with continued momentum in emerging markets and Canada and with recent signs of stabilization in the U.S. The outlook for Europe, however, remains uncertain, and a double dip in that region is a real possibility. Spurred by worries over the European sovereign debt crisis, China property tightening and the strength of the U.S. consumer, the markets are currently characterized by a heightened degree of risk aversion. To date, spillover risks to Canada have been limited to a fall in commodity prices and some tightening of financial conditions.
- It is clear that the world economies remain highly dependent on monetary and fiscal stimulus, as evidenced by the key takeaways from the recent G20 summit in Toronto. There is a pressing need to carefully begin to remove excesses that have kept our system afloat, so as to prevent a future crisis. In our analysis, there are two positives to be derived from this situation: (1) the U.S. and Canadian governing authorities and central banks recognize the risk of premature fiscal and monetary over-tightening – which clearly is supportive of markets and should be enough to sustain the cyclical uptrend in stocks, and (2) the flight to the safe haven U.S. Treasuries and Canadian bonds has caused yields to drop – and with lower interest rates, consumers get a "break" servicing their heavy debt loads.
- With credit spreads gapping out, equity valuations have fallen and are once again relatively attractive. Furthermore, enabled by strong corporate balance sheets and improving corporate profitability, our thesis calls for a revival in capital expenditures. We continue to be largely sector neutral, providing us decent opportunity to gain alpha through stock selection. Names we highlight as being attractive are Gildan Activewear Inc., Cenovus Energy Inc. and Telus Corp. Gildan is well positioned to continue to gain share in the wholesale basic apparel market and simultaneously pursue new growth initiatives. Cenovus provides the best in class oil sands exposure – although natural gas is currently favoured by the market from a seasonality perspective, our bias is toward oil as we see global (especially emerging market) demand growth. And finally, with an improved competitive position (especially in wireless), we expect Telus to deliver improved operating metrics and better earnings momentum.
- Following May's rally, the duration of the portfolio was brought back to neutral on May 31st. Although yields rose, it was only temporary, and now bond yields are back at their lowest for the year. We believe longer term yields are at the lower end of a trading range, but will continue to manage the portfolio's duration from a neutral to long position.
- Our take on the Bank of Canada, is that it has embarked on a tightening cycle that will be very much dependent upon current information. In the bank's spring Monetary Policy Report we thought the Bank was on a clear path to normalising rates, which we interpreted as a series of hikes to about 2%. In our view, recent events have caused the Bank to shorten its projection horizon, creating more policy uncertainty over the medium term. Consequently, we expect short term rates to be more volatile.
- The concentration in 10-year bonds, has given the portfolio more running yield, reasonable positioning in the recent flattening, and good performance in the second quarter rally. We expect the 10-year part of the yield curve to stay out of trouble, and hence we will retain the portfolio's overweight in that part of the yield curve.
- The recent underperformance of corporate and provincial bonds has presented an opportunity to increase the portfolio's running yield at attractive yield spreads. We have begun this process and will continue to look for further opportunities. We expect credit spreads to remain at heightened levels, until there is further clarity on the PHIIGS situation.

Opinions expressed herein are the sole views of Laketon Investment management and are subject to change without notice. Securities mentioned herein are not to be construed as recommendations to buy, hold or sell. Past performance is no guarantee of future results.