CANADA WEEKLY PORTFOLIO MANAGER'S SUMMARY
August 18, 2012

Interesting ideas for this week

For Required Non-U.S. Analyst and Conflicts Disclosures, please see Required Disclosures section at the end of each comment.

Macro Musings

Canadian Equity Strategy (Bi-weekly); by Myles Zyblock, August 15

Roughly 80% of companies in the TSX have reported, with earnings for these reporting companies contracting at an 18% y-o-y clip. Non-bank Financials, Energy, and Materials have been the major weights on earnings delivery.
Soft global economic growth has been a key factor in the poor results (via its commodity price impact) and this condition might persist for a few more quarters. The Euro-zone and China have been important growth drags, while the U.S. outlook remains highly uncertain given a tenuous domestic policy backdrop.
Taking a closer look at China, in light of the incoming data and recent insight from our Emerging Markets team, we conclude:

- **The Chinese economy is weak.** China's GDP growth is running at its slowest pace since Q1 2009. Higher frequency data such as industrial production and general government revenues, alongside leading indicators, suggest that this soft patch might persist for a few more months.
- **Forthcoming Chinese stimulus might prove less aggressive than investors currently demand.** Food prices are rising, energy prices are rising, and real estate prices remain elevated. The country could choose to sacrifice a bit of near-term growth in order to lower the risk of pipeline inflation, similar to India's recent message. Our Emerging Markets team argues that Chinese policymakers will ultimately attempt to deliver just the right balance of stimulus for a moderate pace of growth.

With TSX earnings likely to remain under pressure, we continue to argue in favor of a portfolio biased toward dividend growth. This group has been outperforming over the past year and displays a rewarding long-term performance track record.
Canadian Equity Strategy (Bi-weekly)

Strategic Investment Ideas

Small Cap Conviction Ideas Q3 2012; Mid-Quarter Performance Update by Canada RBCCM Equity Small Caps, August 16

- Our inaugural list of Canadian Small Cap Conviction Ideas (introduced on June 27, 2012) has increased 4.5% on a total return basis through the first half of the quarter, which compares to returns of key indices including the S&P TSX Composite (+2.9%), Completion (+3.5%) and Small Cap (+3.8%). The goal of our Small Cap Conviction Ideas is to deliver superior absolute returns.
- **RBC Capital Markets has equity research coverage of more than 190 Canadian-listed small cap names** (defined as less than $1 billion market cap). With this series of publications, we aim to highlight our Research analysts' top money-making ideas within the Canadian small-cap market place over a 3–6+ month horizon. High conviction levels from the analyst(s) are particularly important.

Small Cap Conviction Ideas Q3 2012

Featured Stock Idea

Agrium Inc. (AGU) - Retail Worth More, but Split May not be Needed to Realize Upside; by Adam Schatzker, August 15

- On August 13, 2012, a story was published in the Wall Street Journal indicating Jana Partners LLC is requesting that Agrium split its company in two, namely Wholesale and Retail. The rationale for this split is that the Retail segment is undervalued and would be worth more on a stand-alone basis.
- Agrium has highlighted comparable companies in past communications, but these companies have very little overlap and significant operating differences that lead to different inventory turnover/requirements, seasonality, and margins. We believe that resulting metrics comparing Agrium's Retail business to its "peers" or historical multiples are of limited utility.
- We estimate the market is currently discounting a Retail EV/EBITDA multiple of approximately seven times. believe this is a reasonable assumption given the company's ability to: realize synergies within the Retail segment; reduce working capital requirements; and, acquire the Viterra retail assets as planned.
- Although some investors may be tempted by the short-term potential of a split-up, we believe that management is determined to continue its current strategy which we think will generate significant returns to shareholders. We reiterate our Outperform, Average Risk rating.

Retail Worth More, but Split May not be Needed to Realize Upside

Brookfield Asset Management Inc. (BAM) - Q2/12 Results; Time Is Working in BAM's Favour; by Neil Downey, August 13

- **Low Hydrology Hurts –** Q2/12 FFO of $244MM ($0.34/share) was -21% from Q2/11's $309MM ($0.45/share). Our forecast was for $273MM ($0.39/share). A major piece of the YoY decline was Q2/11's $60MM (~$0.10/share) private equity monetization related to the Longview recap. Versus forecast: **i)** Renewable Power FFO was weak (~$45MM or $0.07/share, below LTA, due to weak hydrology); and **ii)** Investment Income was -$18MM YoY, due largely to $21MM in negative marks in Q2/12.
- **Ramping Up Investing; It All Takes Time, Which Is on BAM's Side –** Thematically, BAM's investing activity has really begun to ramp up this year. Having spent years cultivating relationships and building its track record, now global uncertainties, excess leverage and the passage of time are bringing an ever greater number of opportunities.
- **TNAV Gets Hit by the Brazilian Real and Declining Yields –** Q2/12 Tangible NAV declined by $317MM to $35.35/share from Q1/12's $35.89. Q2/12 strength in the US$, notably versus the Real, hit TNAV by $516MM ($0.78/share), while declining bond yields resulted in a $124MM ($0.19/share) negative valuation mark on interest rate contracts.
- **Corporate Liquidity Declines to $1.8B –** Our records suggest this is the lowest level of the past 6 quarters.
- **Asset Management Platform: Q2/12 Fee Growth Demonstrates Positive Leverage –** We see the accelerating investing activity as a precursor to base fee and longer-term performance fee growth. Base AM fees are now running at ~$225MM annualized.
- **Target Increased to $40 from $37; Outperform Reiterated**

Q2/12 Results; Time Is Working in BAM's Favour

Genworth MI Canada (MIC) - Downside Risk Analysis Under a Bearish Housing Scenario; by Geoffrey Kwan, August 16

- **Our analysis suggests MIC would have approximately $20/share to absorb additional losses after taking into account our bearish housing scenario, which we believe could provide some valuation support for MIC's share price.** Some key assumptions in our analysis: (1) 30% home price decline; (2) delinquency rates rise from 0.34% currently to 5.00%; (3) 40% severity ratios for the 2012 vintage.
- **Maintaining 12-month target of $22.00/share, Sector Perform rating.** Our Sector Perform rating reflects our view that despite trading at a discount to the mortgage companies and below book value, we believe there is reduced earnings visibility that may constrain valuation in the near-term.
- **We believe investors with a longer-term investment horizon might find the current share price attractive** given the discount valuation and attractive dividend yield (6.1%, and we are forecasting a 3.5% dividend increase when MIC reports Q3/11 results).

Downside Risk Analysis Under a Bearish Housing Scenario

Stella-Jones Inc. (SJ) - Growth Story Continues; Raising Price Target to $70 on Valuation Roll Forward; by Elaine Lae, August 10

- SJ reported a Q2 EPS beat; we are raising price target to $70 from $66 on roll forward of valuation.
- **SJ Reported Q2 Beat on EBITDA margin** of 17.2% up 60bps YoY and above our est of 15.7%, driven by railway ties which saw sales up 15% organically. Mgmt maintains 2012 target EBITDA margin of 15.5-16%. Despite a H1/12 pull-forward in demand, company continues to see strong Q3, typically seasonally strong.
- **Still Solid Tuck-In Acquisition Pipeline.** Although dependent on timing of sellers, mgmt notes there are still tuck-in opportunities (we believe likely in the fragmented US pole market).
- **Still See Future Organic Growth Opportunities:** 1) CN announced today that it secured support from mining companies in northern QC to initiate a feasibility study for a Plan Nord proposed rail line. We view SJ as well-positioned to be a primary railway tie supplier given their geographic presence and supply capacity. 2) Similar to utility pole peers, SJ is also seeing a trend of utilities increasing investments in multi year projects to expand and replace pole infrastructure.
- **Raising Price Target to $70 from $66** on 14x (unchanged) on rolled-forward increased F13/F14 EPS estimates or ~9x on F13/F14 average EBITDA ests. We continue to like SJ's defensive & high-barrier to entry business model with ROE of ~20% and ~15% ROIC. With a 19% all-in return to our $70 target price, we rate SJ Outperform, Above Average Risk.

Growth Story Continues; Raising Price Target to $70 on Valuation Roll Forward

Bi-Modal Stock Picks: Quant + Technical; by Chad McAlpine, August 17

A two-discipline look at CAE, DII/B, and TCL/A. Removing SNC. Stopped out on AEM.

Bi-Modal Stock Picks: Quant + Technical

The Week Ahead

The Canadian Week Ahead; August 20-24, 2012 by RBCCM Global Research , August 16

CGI Group's Acquisition of Logica Expected to Close - Aug 20th

- The acquisition is immediately accretive and offers a very complementary strategic fit. We estimate $0.44 to $0.56 accretion to F13 EPS (25-30%), with possible further long-term upside on additional cost and revenue synergies.
- Beyond near-term EPS accretion and cost synergies, the acquisition strengthens CGI's global IT services positioning. Long-term revenue synergies may include expanded global wallet share at existing customers, new European outsourcing wins, and software/IP cross-selling.

Glencore International Reports H1/12 Results - Aug 21st

- Our H1/12 EPS estimate stands at US$0.20/sh, in line with consensus. In addition, we expect Glencore to remain moderately free cash flow positive at the H1/12 stage as we believe operating cash inflows will more than offset capex spend & dividend for the period.
- We also expect Glencore to give an update on progress made (if any) with China's Ministry of Commerce (MOFCOM) after the Ministry moved to a second phase review of the Viterra transaction. In addition, Glencore may provide an update regarding progress, approvals and terms for the proposed XTA/GLEN merger, ahead of the Xstrata shareholder vote which is scheduled for September 7th.

BHP Billiton Reports FY12 Earnings - Aug 22nd

- We are forecasting revenues of US$70.8bn vs. consensus at $71.8bn, EBITDA of $32.6bn vs. consensus at $33.5bn and EBIT of $26.4bn vs. consensus at $26.9bn.
- We could also see an update on the proposed disposal of the diamonds business, but we expect the themes to remain consistent with RIO and AAL: falling prices and rising costs.

Home Capital Group Marketing with RBC - Aug 22nd

- Martin Reid, President, and Bob Blowes, CFO, will join RBC in Montreal to meet with investors. Discussions are expected to focus on insights into the latest housing data and trends in the prime and non-prime mortgage market.

RBC Attends NovaGold Resources Site Tour - Aug 23/24th

- RBC will attend a site tour of the Donlin Gold project in Alaska, hosted by NovaGold Resources. The site is a 50/50 joint venture between NovaGold and Barrick Gold, and is one of the world's largest undeveloped gold resources with 34 MMoz 2P Reserves and 45 MMoz of total resource.
- The site tour will give RBC an opportunity to evaluate the existing infrastructure in the area, review the ongoing exploration activity at the site, and hear updates on the permitting process.

The Canadian Week Ahead

Initiations

Discovery Metals Limited (DML) - Emerging Copper Producer in Botswana Shaping up Well; by Geoff Breen, August 16

We initiate coverage of Discovery Metals, an A$600m Botswana emerging copper-silver producer, with a **Sector Perform rating and A$1.30/share target.** Its new US$250m Boseto open-pit mine in the Kalahari Copper Belt began commissioning in June 2012 with planned annual output of 36kt copper and ~1moz silver. Once the company navigates through the challenges of mine commissioning and production ramp up, we see upside potential to A$1.60/share. The biggest risk, in our opinion, is the commissioning phase and production ramp up to a stable operating regime. Copper price risk is partially mitigated by ~40% of production hedged at ~US$4/lb into FY15. **During the commissioning phase we would expect the shares to trade at a discount to peers. However, the upside potential should result in an uplift in our target multiples to the ASX sector average of ~8x CFM and 0.9x P/NAV.**

Emerging Copper Producer in Botswana Shaping up Well

Durata Therapeutics, Inc. (DRTX) - Dalbavancin, The First Long-Acting Antibiotic Targeting Severe Infections; by Adnan Butt, August 12

- We believe risk/reward is favorable ahead of pivotal Phase III readouts for Durata's proprietary long-acting antibiotic, dalbavancin, for patients with acute bacterial skin and skin structure infections (abSSSI). Our positive view is based on dalbavancin's differentiated profile, short time-lines to Phase III data, prior Phase III results, sufficient funding into regulatory approvals and 100% ownership. The well developed, blockbuster antibiotic market and dalbavancin's clinical and regulatory history lower clinical, regulatory and commercial risk by providing greater transparency than typical for a Phase III drug. We are initiating with an Outperform, Speculative Risk rating and $15 price target.

Dalbavancin, The First Long-Acting Antibiotic Targeting Severe Infections

Rating Revisions

Ainsworth Lumber Co. Ltd. (ANS) - Western Canada OSB Prices Have Been Going Vertical - Upgrading to Outperform; by Paul Quinn, August 15

- **Upgrading to Outperform as Higher Prices Reduce the Re-financing Risks –** While we were previously hesitant on the story given the ~US$527MM of debt Ainsworth has coming due in H214/H215, higher prices significantly reduce the re-financing risks and improves the likelihood that Ainsworth will be able to realize value from its unfinished/idled capacity
- **Increasing Our WC OSB Price Deck for H2 –** Western Canada OSB prices ended last week at US$310/msf, well above the YTD average of US$228/msf. To reflect stronger-than-expected mkt conditions since we last adjusted our deck, we increase FY12 from US$223/msf to US$240/msf (with Q3 at $275 and Q4 at $250). Under the current operating platform, a US$10/msf annual change in North American OSB prices represents $15MM in EBITDA.
- **Long-Term OSB Industry Fundamentals Compelling –** We like the fundamentals of the NA panel sector due to its ownership concentration (top 5 producers were 82% of 2011 production) and lack of import competition. While others may point to the significant idled capacity (which we estimate at 6.7 Bsf, of which 5.5 Bsf returns) as a constraint on pricing, we don't expect significant mill restarts until US housing starts are 850K+.

Western Canada OSB Prices Have Been Going Vertical - Upgrading to Outperform

Antrim Energy Inc. (AEN) - Positive steps at Causeway; by James Hosie, August 13

We believe Antrim has the potential to deliver positive operational momentum through H2/12, most notably first oil from Causeway in late Q3 and the Cyclone exploration well in Q4. Trading below our core NAV of C$0.76/share (48p) we believe the stock is fairly valued and have upgraded our recommendation to Sector Perform from Underperform with a revised C$0.75 (47p) Price Target, up from C$0.70.

Positive steps at Causeway

Great Basin Gold Ltd. (GBG) - Q2 - Hard Times on the High Veld; by Jonathan Guy, August 15

Great Basin Gold has reported its results for Q2 2012. Both operating and financial results were poor.

- Following another challenging quarter GBG's CEO, Ferdi Dippenaar, has resigned and has been replaced by the CFO, Lou Van Vuuren. The company has set up a board committee with the objective of raising at least US$60 million either through equity or asset sales. Management believes that as of 30th June the company had a working capital deficit of US$23 million including US$17 million of cash. We believe that the company needs to raise at least US$109 million based on less optimistic production forecasts.
- GBG produced 6.39 koz at Burnstone during the period, well below both our estimate of 9.74 koz and guidance of 17.79 koz. This poor performance was attributed to ongoing water management and underground infrastructure issues.
- GBG's EPS during the period was -4 cps compared to RBC at -1cps. The under-performance was due to lower than expected production levels at Burnstone and higher costs. The company finished the period with a cash position of US$17 million and with debt of US$293 million.
- We have reduced our price target to C$0.26/shares (from C$0.94/share) based on 2013E NAVx of 0.55x (unchanged) and 5.0x 2013E CFPS (from 8.0x). We move to an Underperform Rating from Sector Perform due to the financial uncertainty facing the company. We retain our Speculative Risk qualifier.

Q2 - Hard Times on the High Veld

Paladin Energy Ltd (PDN) - Pulls a Rabbit Out of Its Hat; $200M Prepaid Contract Solves Financial Issues; by

Adam Schatzker, August 15

- On August 14, Paladin announced that it has entered into a long-term off-take contract with a utility whereby the company will sell 13.73 million pounds between 2019 and 2024 and receive $200 million as a pre-payment. The pre-payment will be used to repay the remaining portion of the March 2013 convertible debenture (US$134 million) and the remainder will be used to strengthen the balance sheet.
- We applaud the company for this highly creative solution to a lingering balance sheet problem and we believe shareholders have been provided with a non-dilutive means to solve the perceived debt overhang.
- We think this transaction will cause many to take notice. We think the purchaser is highlighting the potential market tightness in the 2019–2024 time-frame.
- Given the significant financial risk reduction this deal provides Paladin, we are upgrading the shares to Outperform and maintaining our Above Average risk qualifier and A$2.00 price target.

Pulls a Rabbit Out of Its Hat; $200M Prepaid Contract Solves Financial Issues

Multimedia link for Regis Resources

Regis Resources (RRL) - Site visit to Moolart Well & Garden Well, Western Australia by Steuart McIntyre, August 17

- Top Pick-rated gold stock
- Consistent production profile, high quality management
- Cash Flow self-sufficient, 6% dividend yield
- This multimedia recording highlights a recent site tour, Western Australia

Regis Resources Multimedia

Upcoming RBC Conferences/Events

Global Industrials Conference
September 11-12, 2012
Las Vegas, Nevada

International Oil & Gas
October 9, 2012
London, UK

Gold Conference
November 8, 2012
London, UK

MLP Conference
November 15-16, 2012
Dallas, Texas

Consumer & Retail Investor Day
December 6, 2012
New York, New York

Healthcare Investor Day
December 6, 2012
Denver, Colorado

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