Market Commentary

First Quarter 2014

CI Investment Consulting

Portfolio Series and Portfolio Select Series

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Market performance

Stock and bond markets both started the year on a high note by delivering above-average returns for the quarter. The domestic stock markets as represented by the S&P/TSX Composite Index rallied 6.1% while the foreign markets as measured by the MSCI World Index gained 5.5% in Canadian dollar terms. Investor confidence was resilient in the face of the below-normal temperatures experienced in North America this winter and political tension in Eastern Europe. Earnings multiples, which measure the price investors pay for a dollar of future earnings, continued to rise. From a valuation standpoint, stocks in general are no longer on sale. However, as long as interest rates remain low, stocks will likely continue to be considered attractive and find support. We expect dividend and earnings growth from companies to reward investors with a long-term return in the range of 5-7%.

Investors were also relieved when the Bank of Canada hinted at the possibility of a rate cut, which led to an immediate rally in bonds. However, we do not believe a rate cut will materialize, as interest rates are already very low. Meanwhile, the Canadian dollar responded by depreciating sharply against most foreign currencies. This should, at least, improve Canada's competitiveness by making our goods cheaper internationally.

Returns in % at March 31, 2014	3 mth	1 yr	3 yr	5 yr	10 yr
S&P/TSX Composite Index	6.1	16.0	3.6	13.7	8.1
S&P 500 Index (C$)	6.0	32.6	19.8	18.0	5.6
MSCI World Index (C$)	5.5	30.3	15.8	15.9	5.6
FTSE TMX Universe Bond Index	2.8	0.8	5.0	5.0	5.1

Source: Bloomberg, PC Bond

Portfolio Series and Portfolio Select Series

All Portfolio Series and Portfolio Select Series funds earned a positive return during the first quarter. Our cash balances represented a drag on performance during the quarter with both the equity and bond markets having rallied. However, as long as we participate in the growth, cash provides valuable downside protection.

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Returns in % at March 31, 2014	3 mo	1 yr	3 yr	5 yr	10 yr	Life
Portfolio Series Income Fund	3.7	8.8	7.0	9.5	5.4	5.4 (Dec. 97)
Portfolio Series Balanced Fund	3.8	14.3	7.5	10.6	5.4	7.1 (Nov. 88)
Portfolio Series Growth Fund	4.2	19.5	8.8	12.2	4.9	4.5 (Dec. 01)
Select Income Managed	2.9	5.0	5.3	n/a	n/a	4.6 (Sept. 10)
Select 70i30e Managed Portfolio	3.1	9.9	6.7	8.7	n/a	4.0 (Nov. 06)
Select 50i50e Managed Portfolio	3.2	13.2	7.6	10.2	n/a	3.9 (Nov. 06)
Select 30i70e Managed Portfolio	3.3	16.7	8.5	11.8	n/a	3.7 (Nov. 06)

All fund returns are for Class A units/shares

Select Income Managed Corporate Class

Our decision to add government and corporate bonds during the summer of 2013 has paid off faster than we had anticipated. The yield on five-year Government of Canada bonds has fallen steadily from 2.15% to 1.5% as investors went from pricing in rate hikes to pricing in potential rate cuts. We continue to monitor and evaluate the potential trading ranges for bonds and believe that the ranges are likely to be moving up rather than down. As a result, we are cautious in making additional purchases of mid- and longer-term bonds at this time. Cash provides a yield of 1% with no volatility.

We recently doubled our allocation to short-term corporate bonds to almost 20%. These investments have very low interest rate risk as the term is extremely short (1.25 year duration). The issuers typically generate large and reliable cash flows, and include major banks, supermarkets, telephone and utility companies. We are paid a premium of 75 to 100 basis points relative to government paper for the same term.

The portfolio remains very defensively positioned. It carries very low interest rate risk, less than half that of the index in our estimation. The equity risk is manageable, with the allocation limited to 25% and diversified among countries and sectors. As we write this commentary in early April, the U.S. dollar has reversed recent trends and has traded lower relative to the Canadian dollar. We have taken advantage of this to increase our weighting in the U.S. dollar, which we believe provides both attractive return potential when below C$1.10 and a unique diversification opportunity.

Outlook and positioning

Investor confidence has continued to improve; however, we are concerned that confidence is outpacing gains in the economy. While the global economy has improved since the “Great Recession,” there are still many issues that will take time to heal, including high unemployment, high government debt, and slower emerging markets growth. Our decision to hold more cash to dampen volatility is a prudent approach to deal with uncertainty. We will invest cash when there is greater certainty and/or market valuations improve.

We diversify our equity portfolios across sectors and we favour companies that have strong balance sheets and steady cash flows. In investing today, patience and diversification are key. We would rather be patient to buy than forced to be patient if we pay too much.

The market rally that started in March 2009 has produced large returns. The S&P 500 Index, for example, has earned 18% on an annualized basis since then. We do not expect returns over the next five years to be as robust, because we are starting from a different valuation level. Simply being invested is probably not enough for the next five years. We aim to produce more attractive risk-adjusted results through active management in security selection, asset allocation and risk management.