VANCITYINSIGHT

RESPONSIBLE INVESTING NEWSLETTER 2011

Business and Human Rights

Companies we invest in are expected to demonstrate a commitment to honour and respect basic human rights, including freedom from racial, religious or gender discrimination, and freedom of association - the right to join a union. The foundation for our analysis is the UN Universal Declaration of Human Rights. As originally conceived, the Declaration was designed to apply to states and government. Over the ensuing 60 + years, government willingness to regulate has been declining while the corporate sphere of influence has expanded. For perspective, the 100 largest economies in the world include at least 38 corporations. To illustrate: in 2009 Dell Inc., the computer manufacturer, had $52,902,000,000 in revenue, placing it at number 99, while Luxembourg's 2009 GDP at $52,449,075,701 is in 100th place. Through their growing economic activity, influence and power, corporations, like governments, are capable of being either a positive or negative force for promoting human rights.

On June 16, 2011, the UN Human Rights Council endorsed the Guiding Principles on Business and Human Rights. The Guidelines were developed, through extensive consultation with business and other stakeholders, as a framework to enhance and define corporate policies and procedures on human rights. The development of this framework is the culmination of a six year project led by John Ruggie, the Special Representative for Business and Human Rights to the Secretary General of the United Nations.

The Guidelines are based on a number of internationally recognized rights derived from core documents including the UN Declaration and the International Labour Organization (ILO) conventions on rights in the workplace. The Guidelines cover three inter-related topics:

1. Role of the state to protect against human rights abuses
2. Responsibility of corporations to respect human rights
3. Need for communities and individuals to have access to judicial and non-judicial remedies

Our focus, as socially responsible investors, is on the human rights policies, practices, commitments, and vulnerabilities of companies held in our portfolio. When implemented by companies, the Guidelines will allow shareholders who use environmental, social and governance analysis to more fully evaluate human rights risks. The Guidelines state that business enterprises should have in policies and processes covering a commitment to respect human rights, a due diligence process to identify, prevent, mitigate and account for how human rights impacts are addressed, and processes to remediate any adverse impacts. With regard to having a human rights policy, it should be approved at the most senior level of the enterprise, stipulate expectations of business partners, and be reflected in operational polices and procedures. In terms of due diligence, the policy should cover impacts of the business and activities by its business relationships that may be directly linked to its operations, products or services. Expansive due diligence addresses the concern that other businesses connected to a company (e.g. upstream suppliers, third party security providers, or downstream clients) can each have a significant impact on human rights, without involving company personnel or assets.

We've called on eight companies in our portfolio to undertake a Board level review of existing human rights polices and procedures using the UN Guidelines as a framework. Such a review will provide shareholders with the assurance that company policies are consistent with emerging developments in human rights, and that operations are occurring in a manner that respects communities, individuals and their representative institutions. We have made this request to the Chairs of CIBC, Agnico-Eagle, IAM GOLD, Suncor Energy, Enbridge, Potash Corporation, Vodafone and Telenor Group. By operationalizing the Guidelines, these companies have an opportunity to demonstrate leadership in corporate responsibility and encourage greater adoption of human rights policies at other corporations.

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Economic and Market Commentary Q3 - 2011

Failed Political Leadership

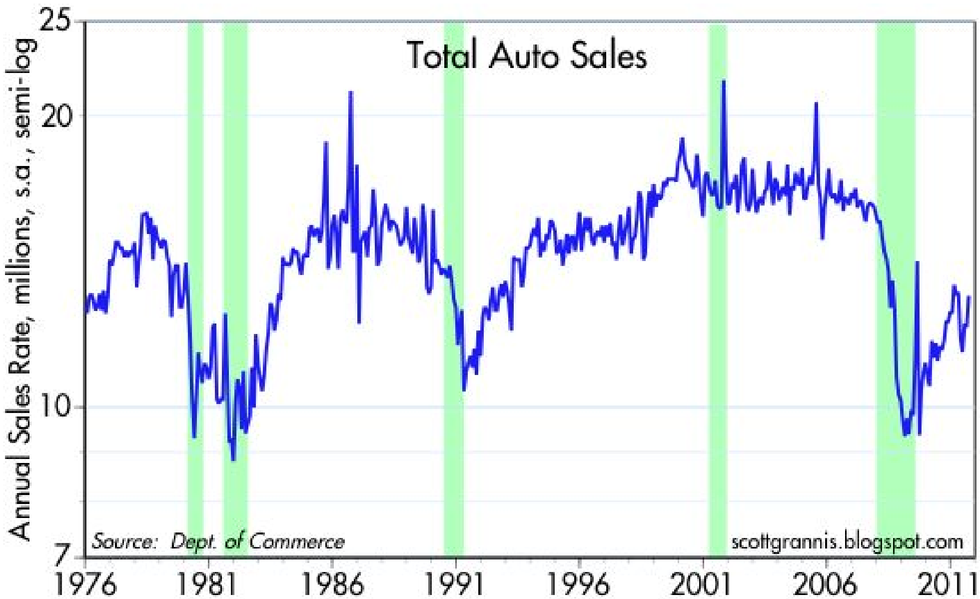
It has been a dramatic summer for markets to say the least! Equity markets tumbled as investor confidence in political and economic leadership on both sides of the Atlantic evaporated. First was the rancorous brinkmanship in the US Congress over the otherwise innocuous issue of raising the debt ceiling. Next was the vapid response by European leaders and disinclination of to deal with their spreading Euro debt crisis in August. On both counts, unnerved investors did not take kindly to the gigantic game of chicken politicians of all stripes played with markets to gain political points. If this were not enough, media predictions of the imminent demise of the Euro or the disintegration of the European Union fueled the anxiety. As investors fled equities, demand for the "safe" assets, short-term bonds, soared, driving their already low yields even lower. At least investors in balanced products were cushioned somewhat from equity market volatility.

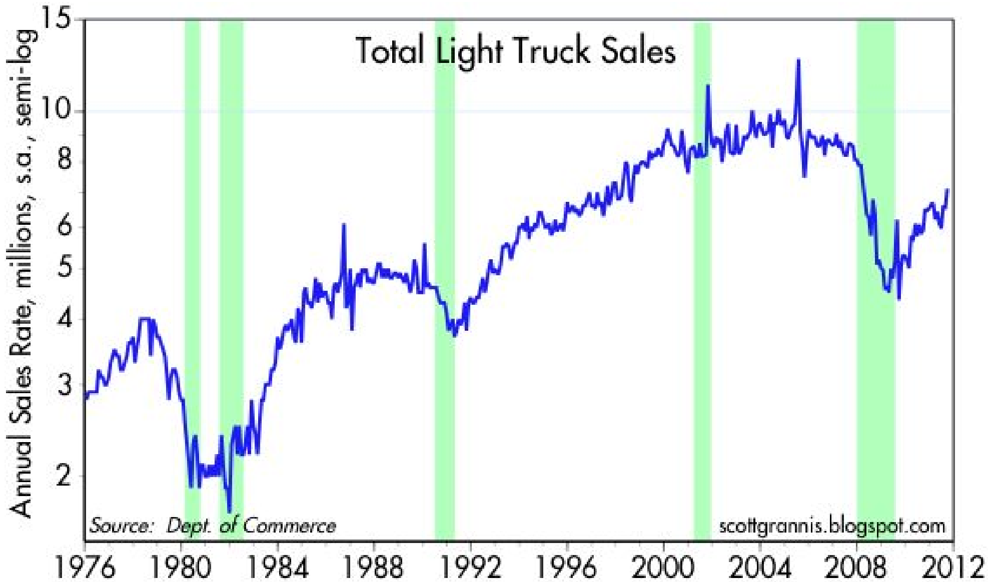
Watching and Waiting on Europe

At the start of the fourth quarter, the spotlight is squarely on the mounting disorder in Europe. Investors have become extremely frustrated by empty rhetoric. Positive utterances from one official one day, fuelling a market rally, are denied or altered by another the next day, causing markets to plunge. However, the recent imminent bankruptcy of the French-Belgian bank Dexia (its second time no less!), and funding stresses among other larger banks have clearly caught the attention of the politicos. Governments technically have limitless resources to survive; unfunded banks have none. The spectre of a Lehman moment is haunting. With pressure from everywhere, there seems to be a new-found urgency to come up with concrete policies to put funding for Europe's sovereigns and banks on secure footing. Indeed, we have just been promised a "comprehensive solution" to be presented to the G20 meeting on November 3-4. While the recapitalization of the banks is of course vital, the longer-term solution for Europe must also include more aggressive measures on the part of the ECB, credible measures to curtail government spending, and some form of controlled default or restructuring of Greek debt. Progress on these steps may likely prove slow. A silver bullet "grand bargain" would seem well nigh impossible in the absence of a sudden, catastrophic shock given the cumbersome/tortuous ratification processes within the EU and their tendency towards incrementalism. But even gradual removal of uncertainty and substantive progress will effectively limit downside risk and remove the "nightmare scenario", clearly benefiting depressed markets. We believe the Euro leaders have seen the light and expect more positive outcomes over time, nonetheless many challenges remain. Upcoming meetings will be closely watched which will either set Europe on a proper course and calm markets or disappoint, once again roiling markets. As managers unaccustomed to handicapping unprecedented political/macro events and having witnessed many twists and turns on the tortuous road to a resolution of the Euro mess, we are resigned to watching and waiting but with an overall expectation of a positive outcome.

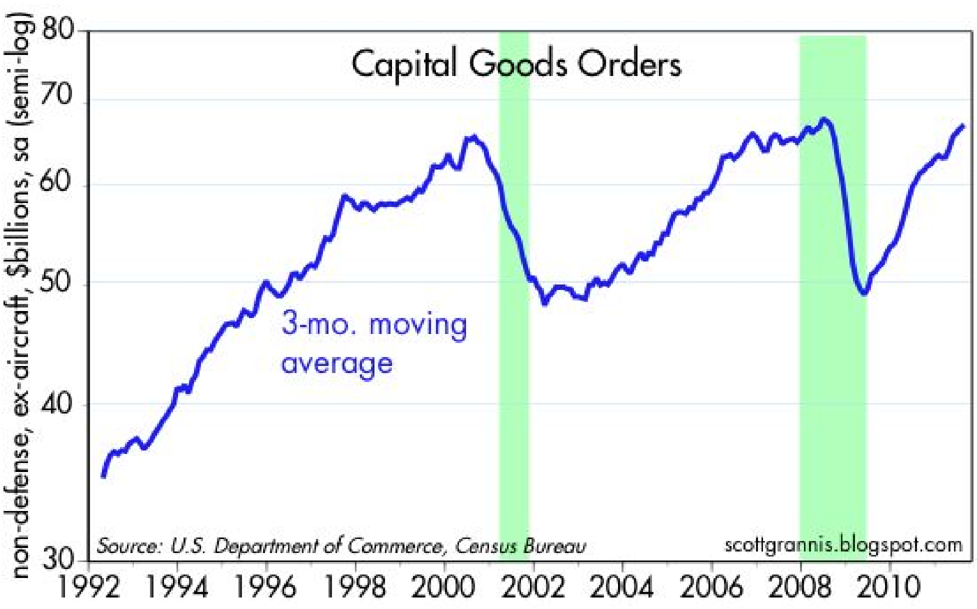
And now for some better news?

While the volatility of markets has undoubtedly weighed negatively on consumer and corporate confidence, and indeed, the equity market sell-off suggests investors are discounting a rising risk of recession, surprisingly, recent economic data releases have generally been better than expected. In our view, they point to continued slow growth in the global economy rather than a slide into recession. True recessions are characterized by a retrenchment in the consumer and corporate sectors. A consumer retrenchment would be evident in reduced spending on big ticket discretionary items like motor vehicles. In fact, recently reported total US September vehicle sales, pictured below, blew past expectations and continue to rise strongly from the June low and from a year ago. Light truck sales, illustrated in the following graph, which account for just over half of vehicle sales, have recovered even more strongly. Definitely no signs of recession here!

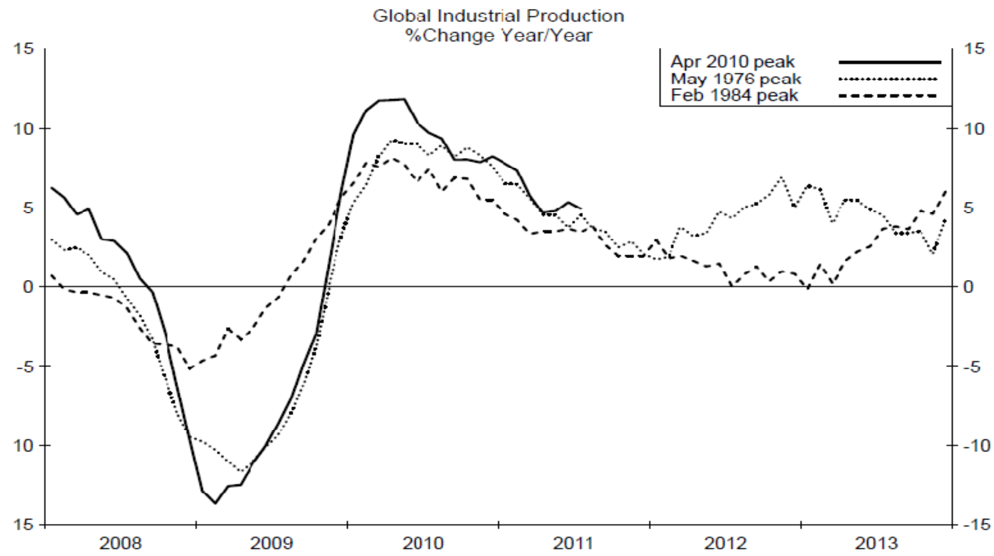




On the corporate side, a retrenchment would be evident in declining orders for capital goods as business became less confident in the economic outlook. The durable goods data recently reported featured a surprisingly strong rise in August and a positive prior revision. The sustained strength in capital goods orders, as pictured below, is an encouraging forward looking indicator suggesting declining business confidence has not translated into a retrenchment in planned business spending. Again, no recession here!



While this data is encouraging and should allay fears of an outright recession, it does not suggest an imminent strong surge from the typical mid-cycle slowdown which has been on-going for some time in the global economy. As illustrated below, the rate of change of global industrial production (IP) has been gently decelerating since mid-2010, following the typical trajectories of other economic cycles of similar amplitude. The close fit suggests IP should not re-accelerate until well into 2012. This would be consistent with the well-documented, on-going sluggish recovery in the US and accumulating signs that the European economy has now slowed abruptly. While growth expectations should therefore remain muted, they are at least positive and while positive policy actions evolve, we can expect confidence to rise and with it a gradual resumption of stronger economic growth.



Source: TD Securities

Challenging Times!

We can fully sympathize with unitholders who once again find the investing "climate" rather stormy and fearful. No less than the front cover of a recent edition of The Economist magazine pictures a vortex sucking up the universe into a black hole with two words "Be afraid" in the middle of the hole! Much better advice is to be *sensible.* No policy-maker wants to watch our highly integrated global financial system implode, especially when mechanisms are in place and liquidity measures are readily at hand to avert disaster. Rationality will prevail and as successful outcomes to past crises prove, positive solutions evolve and markets recover. Meanwhile, left to their own devices, global economies are growing, not receding. The current challenging times once again highlight the merit of asset diversification. Balance matters! While stock markets have weakened, fixed income investments have strengthened, helping to mitigate volatility. Furthermore, there is a strikingly positive paradox to the current environment-while so-called safe assets yield virtually 0%, strong corporations provide an enormous yield advantage on both their debt and equity. A focus on receipt of income and compounding over time as well as timely portfolio re-balancing will be much more beneficial to financial health than worrying about the next pronouncement out of Europe and other fear-mongering in the media. Stay the course…be *not* afraid!

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