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### BUILDING WEALTH The Internet Wealth Builder

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## THE PH&N TAKEOVER

My first reaction on hearing the news that Royal Bank is buying Vancouver-based Phillips, Hager & North was disappointment. I have been an admirer of PH&N for many years for several reasons, the most important being the consistent high level of integrity of the firm. Management has changed over time and the founding partners are gone (although Rudy North has set up his own shop across the street). But the fundamental principles of the company have never wavered. PH&N, in my view, is one of the few money management firms that genuinely cares about the well-being of its clients.

Now that it is poised to become part of the RBC empire, I wonder how long that personal touch can be maintained. Yes, it is gratifying to hear that PH&N will continue as an autonomous operating division and that most (but, significantly, not all) of its fund managers have signed five-year non-compete clauses. But the reality is that president John Montalbano and his team will now answer to a higher authority, one which may not always take the same view of the world.

For example, one of the great attractions of PH&N is its low cost structure, as expressed through the management expense ratios (MERs) of its funds. The annual costs charged against the company's original A units are among the lowest in the fund industry. The MERs of similar RBC fund units are higher.

To illustrate, let's compare the A units of the PH&N Dividend Income Fund, which has been on our Recommended List since 2001, with the RBC Canadian Dividend Fund. The PH&N fund has a management fee of 1% and an MER of 1.13%. The RBC fund has a 1.5% management fee and a 1.73% MER. That's very reasonable by industry standards but it is obviously a lot higher than the costs associated with the PH&N fund. (The RBC fund's D units have a management fee of only 1% but they can only be purchased by clients of Royal Direct Investing.)

A fund's MER comes right off the bottom line when calculating net return to an investor. So, all things being equal, the PH&N fund's A unit have a 0.6% edge over the A units of the RBC Canadian Dividend Fund right out of the starting gate. Interestingly, over the 10 years to Jan. 31 PH&N Dividend Income posted an average annual compound rate of return of 10.8% while RBC Canadian Dividend gained an average of 10.37% for a differential of 0.43 percentage points. Were it not for the extra cost burden of the higher MER, the RBC fund would have come out slightly ahead. (In fact, it has outperformed the PH&N fund recently, despite the MER disadvantage.)

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**Takeover - continued from page 1...**

The PH&N fund has almost \$2.8 billion in assets under management. Raising the management fee of the A units by a quarter point would add about \$7 million to the company's bottom line while still leaving the MER below that of its RBC counterpart. Spread that across PH&N's total fund assets of \$19.5 billion and there is the potential for a lift of almost \$50 million to RBC's profits without doing anything else.

Of course, everyone involved will deny that any such action is contemplated and at this stage that's probably true. In fact, RBC has stated its commitment to PH&N's low-fee model. But once the deal closes and the integration is complete, the bottom-line thinkers at RBC are going to be looking at ways to make this acquisition more accretive to their shareholders. Grabbing PH&N's pension and institutional business, worth about \$55 billion (\$36 billion in pensions), will be a major plus – RBC currently is not a big player in the pension market. But the potential profit add-ons from the mutual funds business won't go unnoticed.

John Montalbano, who will be the head honcho of the RBC/PH&N asset management business after the closing, was quoted in the media on Friday as saying that he believes his company's clients will react positively to the announcement once they see why it is in their best interests. PH&N vice-president Chris Dotson identified some of the benefits as being access to additional front-line managerial talent, such as RBC's chief investment officer Dan Chornous, research expertise in areas where PH&N is weak (e.g. U.S. high-yield bonds and emerging markets debt instruments), and greater international credibility in recruiting top-flight talent.

I hope it works out that way and that PH&N is able to retain its unique character despite being part of a mega-bank. But I'm sceptical. I see the obvious benefits of this deal at the corporate level but my immediate reaction is that PH&N customers will be fortunate if at the end of the day there is a continuation of the status quo from a cost and client relations perspective and some improvement in returns on the equity funds side. – G.P.

## **PENN WEST** **RELEASES RESULTS**

### **Penn West Energy Trust** **(TSX: PWT.UN, NYSE: PWE)**

*Originally recommended by Gordon Pape on Feb. 18/08 (IWB #2807) at C\$28.44, US\$28.22. Closed Friday at C\$28.81, US\$28.56.*

Penn West released fourth-quarter and year-end results on Friday and they were pretty much in line with my expectations. Especially important was the trust's commitment to maintain the current monthly distribution of 34c a unit for at least the next three months.

For the last three months of 2007, the trust reported a 17% year-over-year improvement in funds flow per unit at \$1.43, fully diluted. Distributions were \$1.02 per unit for a payout ratio of 71%.

Since I wrote about Penn West last week, I have received e-mails from some members commenting that the trust's earnings are well below its distributions. For example, in the fourth quarter, earnings per share (EPS) were only 52c, fully diluted. For the full year, EPS came in at 73c, down 78% from 2006.

EPS are usually a reliable indicator of the strength of a company. However, in a few industries, such as energy and real estate, they can be misleading. In the case of trusts, that effect is magnified.

When you look closely at Penn West's results, you'll see that in the second quarter, the trust booked \$325 million against future liabilities relating to the new distribution tax. Of course, that tax does not take effect until 2011 and with the tax pools at its disposal Penn West should be able to minimize its impact for several years after that, so this is really an accounting entry. Another \$200 million was booked as an "unrealized loss against risk management activities". Add back those numbers and Penn West's net income would have been slightly better than the previous year.

With energy trusts, cash flow related to distributions and capital expenditures is the main criterion to look at. Penn West's cash flow was dampened through most of 2007 by weak natural gas prices. However, with gas prices now firming up and oil prices still flirting with the \$100 a barrel level, the first half of 2008 looks good to me.

**Action now:** Buy. – G.P.

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## **LIFE SETTLEMENT DEALS ATTRACT INTEREST**

Last week I received an e-mail from a member asking about the bona fides of one of those “too-good-to-be-true” offers. It read as follows:

“I’ve recently heard about an investment opportunity in an area called Life Settlement. I’m unfamiliar with this concept. The company claims dividend returns of 8% and a projected equity growth of 15%-20% per year. The returns sound overly optimistic and I can’t help thinking about similar claims made by Eron Mortgage Corp. What do you know of the company and the investment concept?” – Dave R.

Our reader provided a link to the company. I am not including it here as I do not want to appear to recommend this investment for reasons that I will explain.

Coincidentally, the e-mail arrived the day after I had watched an episode of the television series Boston Legal. One of the story lines dealt with a man who had been diagnosed with AIDS and given only a short time to live. Believing he was about to die, he sold his life insurance policy to a company at a discount to face value. In return, they promised to pay for the medication he needed to ease his final days. As it turned out, medical research developed new therapies that extended his life expectancy for many years. However, the company that bought his insurance contract refused to keep buying the drugs he required on the grounds he did not die on schedule. He sued.

The technical term for the deal at the core of the Boston Legal plot is “viatical settlement”. This was a business that exploded out of nowhere in the 1970s and 1980s when AIDS began to emerge as a major problem. The business model was to purchase insurance contracts from terminally ill people at a discount. When the person died, the buyer collected and made a big profit. For example, consider the case of someone who had a whole life policy for \$500,000. He was diagnosed with AIDS and told he had a year to live. He decided to sell the policy for \$250,000 to raise cash for drugs. When he died on schedule, the buyer collected the proceeds and made a profit of 100%, less any premiums, on a one-year investment. As a bonus, the money is tax-free since insurance payments are not taxable. It’s a pretty good business, if it doesn’t leave you with a sense of moral outrage.

Over time, however, all sorts of problems began to emerge, not the least of which was the one dramatized on Boston Legal – medical advances prolonging the life spans of people who supposedly were under a death

sentence. Viatical settlements no longer were can’t-miss investments and the fledgling industry went into eclipse.

Life settlements are the reincarnation of the idea. In this case, the policy holder (who must be at least 65 to qualify in most cases) may not be terminally ill but may suffer from a serious health problem, such as heart disease, which shortens his or her life expectancy. Since death is not imminent, the discounted value of the insurance policy is less but may still represent an attractive pay day to someone in need of money.

Companies have been set up that buy these insurance policies, bundle them into large packages, and sell shares to investors. That brings us back to our reader’s query. In this case, the company appears to be Canadian. It sells shares in “a corporation that becomes the irrevocable beneficiary of a portfolio (sic) of life insurance policies”. All the policies originate in the U.S.; the company says it has no intention of buying Canadian policies. Their product is sold under offering memorandum which means a high initial investment is required, at least \$25,000. “Our securities are RRSP and RESP eligible (sic), provide an 8% dividend return and offer potential equity growth of a projected 15-20% per year,” the website says. Sounds attractive. But the fact they can’t spell makes me wonder about their numbers skills as well.

Life settlements have become big business. According to Conning Research of Hartford, Connecticut, they had a total value of US\$5.5 billion in 2005 and are the fastest-growing segment of the life insurance industry with a staggering potential of US\$160 billion. There are newsletters devoted to the subject. There is a Life Insurance Settlement Association (LISA). Deloitte Consulting has produced an in-depth report about the actuarial implications of the business ([http://www.quatloos.com/uconn\\_deloitte\\_life\\_settlements.pdf](http://www.quatloos.com/uconn_deloitte_life_settlements.pdf)). This is a legitimate and growing industry. But should you invest in it?

The first issue is a moral one. This is an investment in other people’s misery. These folks are in ill-health and seemingly desperate for cash – so much so that they are selling their insurance policies for an average of 20c on each \$1 of face value, according to the Deloitte study. Their reasons for wanting money up-front will vary but at least some will likely spend part or all of it on quack cures. So the first question you have to answer is whether you want to be a party to this.

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**Life Settlements – continued from page 3...**

If the answer is yes (and judging by the rapid growth of the business that's what many are saying) then you have to look at the potential returns and the risks. That's where things get murky. The Canadian company I looked at purports to offer good cash flow (8%) plus capital gains. However, there is no public performance record to support this and given the nature of this business it is unlikely that you'll find any. I prefer investing in securities that are transparent – you know exactly what's happening and how well (or badly) they are performing at all times.

Moreover, you won't find anything on this company's website about risks. For that you would have to read the offering memorandum and to get a copy you need to contact one of their sales representatives who will undoubtedly want to meet with you and give you a well-rehearsed (and very plausible sounding) sales pitch.

Not having subjected myself to this ordeal, I have not seen the offering memorandum. But I can tell you some of the questions to ask. To begin with, find out if there is an exit option. Are you locked in forever, or is there a way to withdraw your capital if needed? Second, see if the 8% dividends are guaranteed and if so for how long. If there is a guarantee, is the money held in an escrow account? Next, ask how you collect the projected capital gains, should they materialize. Find out how much you are paying in fees, both up-front and on-going. Inquire about the tax implications. See if the company has the capital to continue to pay the premiums on the policies until the insured people die. Ask to see evidence of past performance. In short, do your homework.

As I said, this is a legitimate business but high projected returns should always be regarded as a red flag. No one gives something for nothing. – G.P.

## **GLENN ROGERS'S UPDATES**

### **Heineken N.V. (OTC: HINKY, AMS: HEIA)**

*Originally recommended by Glenn Rogers on July 9/07 (IWB #2725) at US\$28.60, €41.83. Closed Friday at US\$27.40, €36.94.*

Heineken shares fell sharply after the Dutch brewer released fourth-quarter and year-end results on Wednesday. Net profit came in at €807 million, down 33.4% from the year before. However, most of the drop resulted from a €219 million fine assessed against the company by the European Union last spring for price fixing. Net revenue increased 6.2% and the company will propose a 17% dividend increase to €0.7 per share (about C\$1.04) at the annual meeting in April.

Investors seemed to be most concerned about the lack of specific financial guidance for 2008. In a statement accompanying the financial results, Heineken said that it "expects 2008 to be another year of positive organic growth in net profit, based on a further improvement in sales mix, better prices, higher beer volumes and savings in fixed costs." But there were no hard numbers attached to this rosy outlook and in the next paragraph the company added this disconcerting comment: "As a result of worldwide input cost inflation, Heineken expects a 15% price increase in its raw material and packaging costs. The company expects that it will be able to fully pass on the impact of the increased input and energy costs in most of its markets. Due to the uncertainties around the possible impact of worldwide consumer price inflation and the effect of weakening economies on consumer spending and beer consumption, it is too early to make a reliable estimate of volume levels for 2008."

In January, the company announced it was successful in its bid to acquire British brewer Scottish and Newcastle in conjunction with Carlsberg. Heineken will take over the operations in the U.S., Britain and most of Europe leaving France, Greece, Eastern Europe, China, and Vietnam to Carlsberg. The deal is expected to close in the second quarter of this year.

I still like this stock and the sell-off provides an opportunity to enter at an attractive price.

**Action now:** Buy. – G.R.

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## **TOM SLEE: INSURANCE STOCKS ARE GOOD VALUE**

**Contributing editor Tom Slee is back this week to look at the battered financial sector. He is still wary of the banks but the insurance companies look solid from his perspective and he has a new pick for us. Tom managed pension fund money for many years and holds CGA and CFA certifications. Here is his report.**

Tom Slee writes:

Ever since I can remember, financial stocks have been a safe haven during business downturns. It was always a no-brainer. If the economy sputtered, you rotated into the banks, protected your capital, earned a decent dividend, and slept nights. This time, though, it's different. This time the banks themselves are a major part of the problem. Having helped to finance the U.S. housing bubble, they are now paying the price. Bank stocks are taking the worst beating in ten years. How the mighty have fallen!

This is a significant change in the investment landscape and it raises some difficult questions. Almost everybody in Canada owns bank stocks in one way or another, either directly or indirectly through mutual funds or pension plans. Moreover, financial stocks constitute 28% of the S&P/TSX Composite Index. They are the counterweight to our huge resource sector and to a large extent set the market tone. So it's not just a matter of finding alternative defensive stocks such as pipelines and utilities. We have to decide whether the banks and insurance companies are just temporarily eclipsed. If they remain out of favour, the TSX is likely to underperform this year. There is also the question of whether the financials are oversold. Is it time to jump in and snap up some bargains?

The key, I think, is what lies beyond "subprime". We have to stop focusing on commercial paper losses and take a look at the broader picture. It's not pretty. Consumer spending is down, U.S. unemployment is climbing, and we are tottering on the edge of a recession. That is going to make it difficult for the banks to rebound from their recent setbacks. There is no rising tide. The life insurance companies, however, are much better positioned and could do surprisingly well over the next year or so. Almost recession-proof, they tend to flourish in an economic downturn.

Let's start by taking a look at the Canadian banks. First of all, we have to keep in mind that they are immensely strong and that the subprime mess will pass. Bond insurers, such as

giant MBIA Inc., which carry a great deal of the risk, are raising capital and remain confident that they can meet their obligations. My concern, though, is that the CEOs, having been mauled, are now going to hunker down and become much more defensive. That is going to dampen earnings growth, especially if there is an American recession and loan demand dries up. The stocks could mark time.

Even worse, many analysts now believe that the banks' 2008 guidance is far too optimistic, not because of lingering subprime charges but because of insufficient business and non-residential loan loss provisions. The feeling is that the banks may have to increase these costs by as much as \$1 billion between now and 2010. Moreover, revenue growth projections appear to be optimistic. The boom times are coming to an end, at least for a while. Bank CEOs, however, perhaps spoiled by five years of prosperity, seem to have made little allowance for a rough patch. Don't take my word for it. BMO Nesbitt Burns (owned by a bank, no less) has reduced its 2008 industry revenues forecast by \$2.5 billion. We also have to assume that it's going to be a difficult couple of years for the banks' traders and wealth managers.

None of this is real cause for concern; it's just a reflection of the normal banking cycle. The banks are going to continue doing relatively well; they always do. It's just that we are going into a down period with lower earnings growth, only modest dividend increases, and reduced share buyback programs. So I am a little reluctant to leap into the bank stocks right now, even though some of them look depressed. Any rebound may be short-lived if 2008 earnings are a disappointment. If you do want to add a bank to your portfolio, my choice would still be TD Bank (see updates).

When we come to insurance companies, though, the overall picture is much brighter and I would be more inclined to start overweighting in these stocks. Manulife (TSX, NYSE: MFC) is trading at \$39, down 12% from its 52-week high. Sun Life (TSX, NYSE: SLF) is trading around \$48, down 15% from its high. Both are both excellent value (see detailed updates elsewhere in this issue).

This highly conservative industry is in good shape and none of the major companies were ever seriously exposed to the asset backed securities mess. Balance sheets are solid, credit experience remains good, and, most important, new business is strong. Yet investors, worried about financial institutions in general, have shied away from the stocks. I think that spells opportunity.

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**Insurance stocks - continued from page 5...**

Looking ahead, the strong loonie makes foreign acquisitions much cheaper and Manulife and Sun in particular are expected to expand even further into the vast U.S. markets. Credit control remains tight. In fact, the industry has only 0.7% of its entire assets in third party asset backed commercial paper, mostly through their money funds, and these are superior grade. Thanks to large in-house resources, the life insurance companies carry out their own credit analysis when investing and then take out bond insurance as well, a sort of belt and suspenders approach. At the same time, strong cash flows should underwrite active buyback programs and dividend increases.

**Buy Industrial Alliance (TSX: IAG, OTC: IDLLF)**

One insurance company that I particularly like right now is Industrial Alliance. Canada's fifth-largest life insurer is often overlooked because of its Quebec base but the company is generating solid earnings growth, expanding across the country, and improving an already lucrative sales mix. Trading at \$36, only 12 times 2007 earnings of \$2.99 a share, the stock is cheap and offers capital gains potential as well as downside protection if the market tanks in 2008.

Founded in 1892, Industrial Alliance provides a wide range of life and health insurance products along with an array of money management services. Unlike most of its competitors, the company is focused on Canada and collects approximately 97% of its premiums and other income in this country, although IAG does have some operations in the western United States. With 1,500 exclusive agents and about 12,000 brokers, the company has more than \$50 billion of assets under management and earns a respectable 15.2% return on equity (ROE). Market capital amounts to more than \$3.3 billion.

For a long time, IAG was primarily a writer of individual insurance, which contributed over 50% of the company's earnings. In 2006, however, its acquisition of Clarington Corporation, an independent fund manager with \$4 billion of assets, signaled a new thrust into wealth management. IAG now ranks number 15 in the Canadian retail fund market. As a result, overall income is going to be better balanced and the higher-margin wealth management business will boost the company's ROE.

Not that everything is sweetness and light. IAG, like all other fund managers, inevitably had some exposure to the asset backed commercial paper (ABCP) market and last August assured clients that it would repurchase these investments at 100% of purchase price plus accrued interest. That eventually translated into a \$104 million exposure to ABCP and the company has signed on to the Montreal Accord, a group of financial institutions attempting to create an orderly commercial paper market. Management subsequently wrote down its exposure by 15% and took a \$15.6 million charge in the third quarter. Based on arm's-length transactions now taking place, this should account for most of the problem and the company confirmed that in a statement contained in the fourth-quarter/year-end report.

For fiscal 2007, IAG reported net income of \$242.2 million (\$2.99 a share, fully diluted), up 9% from the previous year. It also announced a dividend increase of 12.5% to 22.5c per quarter (90c a year). Management said that it is maintaining its target of a 28% dividend payout ratio. At the current price, the shares yield 2.5%.

Looking ahead, Industrial is well positioned to generate solid earnings growth in its traditional insurance lines and with almost no U.S. exposure will remain sheltered from foreign exchange fluctuations. However, we could see a hiccup in 2008. The company's guidance said that "under normal circumstances" earnings per share would be expected to increase by 10% to 13% annually. However, management issued this caution: "Given the volatility of the stock markets at the beginning of 2008, the company estimates that a sudden 10% drop in the stock markets at the beginning of the year, followed by stock market growth according to forecasts for the year, would lead to a \$18.6 million (23c per common share) decrease in the net income available to common shareholders." The share price held steady on that news, suggesting the market has already priced in this potential drop in EPS.

U.S. members should note that although Industrial Alliance trades in the Grey Market (symbol IDLLF), volume is extremely light and the stock may go several days or even weeks with no trades. The last reported quote was from Jan. 23 at a price of \$35.01. If you cannot execute a trade through the TSX, I advise steering clear of this one.

**Action now:** Buy Industrial Alliance at \$36 with a \$44 target. I will revisit the stock if it dips to \$32.

## TOM SLEE'S UPDATES

### **Sun Life Financial (TSX, NYSE: SLF)**

*Originally recommended on Oct. 23/00 (IWB #2038) at C\$29.85. Closed Friday at C\$47.95, US\$47.36.*

Sun Life Financial disappointed analysts with its fourth-quarter and year-end results and the stock price dropped as a result. However, the numbers weren't really that bad and a dividend increase of 2c per quarter reflected that.

Net income for the quarter came in at \$555 million (97c a share, fully diluted), up only slightly from \$545 million (94c a share) in the same quarter last year. Management said that earnings were reduced by \$41 million as a result of the strong loonie. For the full year, Sun Life reported net income of \$2.2 billion (\$3.85 a share) compared to slightly less than \$2.1 billion (\$3.58 a share) in 2006.

Asian sales continued to be strong while U.S. earnings jumped 62% in the fourth quarter and were ahead 40% for the full year. The balance sheet is solid and shows excess capital of between \$1 and \$1.5 billion. Subprime mortgage investments of \$516 million comprise a miniscule 0.5% of invested assets. Most important, the return on equity continues to progress and is now at a respectable 14.3%, although that leaves a lot of room for improvement. Great-West Life, for example, has a 21.1% ROE.

As always, there is talk of Sun making another U.S. acquisition but even if nothing happens on that front 2008 should be a good year for the company. New business costs ("strain" as they are known) are expected to decline and profit margins at MFS, a U.S. mutual fund subsidiary company, continue to widen.

(One of the reasons why life insurance companies are so strong is that they write off almost all the costs of new business immediately, even though the premium income continues for years. This front-end loading makes new policies extremely expensive and is a major problem for small companies. The faster you expand, the greater the loss. Major insurers are able to draw down their surplus and when doing so refer to it as "new business strain". In fact companies and analysts constantly base projections on the expected strain.)

Sun's overall earnings should increase to \$4.35 a share this year and then to almost \$5 in 2009.

**Action now:** Buy Sun Life with a target of \$60. I have set a \$42 revisit level.

### **Manulife Financial (TSX, NYSE: MFC)**

*Originally recommended on Aug. 21/00 (IWB #2031) at C\$14.20 (split-adjusted). Closed Friday at C\$39, US\$38.57.*

Manulife Financial is on track and the company's manageable \$860 million exposure to ABCPs is less than 0.5% of general assets. It's not a serious problem and, as if to reassure investors, Moody's recently upgraded MFC's subsidiaries, citing predictable earnings and financial flexibility. Strong sales results are laying a firm foundation for future earnings.

On Feb. 14, Manulife released fourth-quarter and year-end results and they were excellent. Quarterly earnings were a record \$1.14 billion (75c a share, fully diluted). That was up 4% from 2006 in dollar terms and 7% in per share terms. For the full year, Manulife reported net income of \$4.3 billion, an increase of 8% over 2006. Fully diluted earnings per share were \$2.78, an increase of 11% compared to the \$2.51 reported a year ago. Those results were achieved despite a currency hit of \$163 million in the fourth quarter due to the strong loonie. Return on equity (ROE) was a record 18.4% for 2007, up from 16.8% in 2006. Fourth-quarter ROE improved to 20.5% compared to 18% last year.

With a strong loonie and an estimated \$3 billion of excess capital, MFC could hit the acquisition trail at any time. The company, however, is so strong and cash rich that even a major deal would not hamper its aggressive buyback program or expected dividend increases. Manulife should make \$3 a share this year and \$3.40 in 2009.

**Action now:** Buy Manulife at \$39 with a target of \$48. I will revisit the stock if it drops to \$32.

### **Altria Group (NYSE: MO)**

*Originally recommended on Dec. 4/06 (IWB #2643) at \$63.04. Closed Friday at \$73.60 (all figures in U.S. dollars).*

Altria Group continues to perform well, racking up steady earnings growth regardless of the economic turmoil. No doubt about it, tobacco is a recession-proof industry.

The company made an operating profit of \$4.33 in 2007, up from \$4.05 in 2006, helped by higher U.S. and international cigarette prices. Management had already celebrated by raising the dividend 8.7% to \$3 annually

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**Updates – continued from page 7...**

after the third quarter. Incidentally, that means the shares now yield 4.76% on our original recommended price of \$63.04. That sort of return should support the stock if I am wrong and the market collapses this year.

Most encouraging, however, is that Altria continues to grab market share in the U.S. and now has a record 51%. Flagship Marlboro is gaining further acceptance. Philip Morris International is also making strides and reported a 19% increase in profits despite tax hikes on tobacco in several European countries. In China, a half-hearted smoking ban in public places (it relies on persuasion) is failing to stick and Altria has benefited from lower costs and favourable pricing.

Overall, the outlook for tobacco is now much better, mainly because of reduced litigation risk and positive pricing trends. Deep discounting is less of a threat and industry leaders are campaigning against excise taxes. It's also interesting to note that the gradual reduction in North American consumption of one to two percent per annum is being offset by cost savings. All of this bodes well for Altria in 2008.

The big news here, however, is that on Jan. 30 the company announced that it will spin off Philip Morris International (PMI) effective March 28. Shareholders as of that date are to receive one common share of PMI for every share of Altria that they own. Dividends in aggregate on the two stocks will remain at \$3 per annum. The company has also announced a \$20.5 billion buyback program for both Altria and PMI over the next two years. More guidance as well as plans for the

two companies will be unveiled at an investor meeting on March 11. I shall of course keep you posted.

Incidentally, as a result of the spin-off Altria is being removed from the Dow 30 Industrials Average. It's no reflection on the company, however. This index is restricted to companies that have meaningful influence over the economy and Dow Jones feels that Altria, having shed Kraft Foods and now Philip Morris International, has become a smaller and more focused company.

**Action now:** Buy Altria at \$73.60 with a target of \$85. I will revisit the stock if it dips to \$68.

**Toronto Dominion Bank (TSX, NYSE: TD)**

*Originally recommended on Feb. 12/07 (IWB #2031) at C\$69.85, US\$59.59. Closed Friday at C\$67.18, US\$66.41.*

TD, the Canadian bank least affected by the subprime mortgage and structured products debacle, had a strong fourth quarter. Earnings came in at \$1.40 a share, up from \$1.20 the year before. All the major divisions showed improvement and TD's Tier 1 equity ratio is now 10.3%. Management has a tight rein on costs and credit controls; other banks please copy. Earnings for this year should be about \$5.75 a share and we could see as much as \$6.25 in 2009.

**Action now:** Buy TD Bank at \$67.18 with a target of \$77. I have set a \$63 revisit level.

- end Tom Slee

**Glenn Rogers's updates – continued from page 4...****Sony Corp. (NDQ: SONY)**

*Originally recommended by Glenn Rogers on Jan. 21/08 (IWB #2803) at \$51.44. Closed Friday at \$46.77 (all figures in U.S. dollars).*

When I recommended Sony in January, I said it appeared that the company had won the battle for control of the high definition DVD market. Last week it became official when Toshiba officially waved the white flag and announced it would no longer produce its competitive (and non-compatible) HD DVD players.

Right after my January call, Sony shares sold off in the big market correction, falling as low as \$42.74 in intraday trading at one point. The news of Toshiba's surrender gave the stock a boost, however, and it finished the week at \$46.77. That's still below my original entry price which makes Sony an even better buy in my view at this level. If you didn't act before, now is the time.

**Action now:** Buy. – G.R.