

# OB REPORT



## OB Model Portfolio Different Makes a Difference

OCTOBER 2012

### INSIDE THIS ISSUE

#### OB Model Portfolio

*Different Makes a Difference*

→ Page 1

#### Charitable Donations –

Cash vs. Shares

→ Page 4

#### Odlum Brown Limited

Suite 1100 – 250 Howe Street  
Vancouver BC Canada V6C 3S9  
Tel 604 669 1600  
Fax 604 681 8310  
Toll Free 1 888 886 3586

information@odlumbrown.com  
odlumbrown.com

Kelowna 250 861 5700  
Victoria 250 952 7777  
Chilliwack 604 858 2455  
Courtenay 250 703 0637  
Campbell River 250 286 3151

Member-Canadian Investor Protection Fund



### OB MODEL PORTFOLIO HITS NEW HIGH



<sup>1</sup> As of September 15, 2012.

**EVERY ONCE IN A WHILE THE INVESTMENT** stars align and we achieve performance of which we are proud. We are at one of those junctures. Looking back, the performance of the Odlum Brown Model Portfolio is respectable over most horizons.

The Model is up 13.7 per cent for the year through to September 15, 2012 and 19.1 per cent compared to a year ago. The 3-year and 10-year compound annual growth numbers are decent too, at 10.6 per cent and 11.6 per cent, respectively. Only the 5-year figure, at 3.7 per cent, is uninspiring.

We feel good about the Model's security holdings, diversification, and foreign exposure. Despite the troubles in the world, we still believe that it is possible for the Model to achieve growth averaging eight to 10 per cent over the long-term. Our optimism is driven by our expectation that the economic recovery will continue, albeit at a modest pace, and by the fact that there are many high quality companies trading at attractive prices. Indeed, the overall quality of the stocks in the portfolio has never been better.

Still, it is important to remember that the stock market is a risky, volatile place that will continue to produce unpredictable bumps along the way. Moreover, there will be times when our returns are poor relative to our benchmark and when investors will wonder if we have lost our marbles.

Over the course of the Model's almost 18-year history there were two occasions that really tried our clients' patience. The first was during the final blow-off stage of the technology mania in late 1999 and early 2000. Unable to justify the valuations in the technology sector, and unwilling to own Nortel Networks in particular, the Model did not keep pace with the broad market averages in the final months of the mania. At worst, the Model's year-over-year return trailed the Canadian equity benchmark by 24 percentage points in February 2000 (23 per cent vs. 47 per cent). Fortunately, our relative performance and reputation snapped back quickly once the bubble burst.

More recently, the Model significantly underperformed relative to its benchmark the year prior to the 2008/09 financial crisis. Commodity stocks

### COMPOUND ANNUAL RETURNS<sup>1</sup> (INCLUDING REINVESTED DIVIDENDS, AS OF SEPTEMBER 15, 2012)

	YTD	1 YEAR	3 YEAR	5 YEAR	10 YEAR	15 YEAR	INCEPTION <sup>2</sup>
Odlum Brown Model Portfolio	13.7%	19.1%	10.6%	3.7%	11.6%	12.7%	14.9%
S&P/TSX Total Return Index	6.7%	3.6%	5.7%	0.9%	9.4%	6.4%	8.8%
S&P 500 Total Return (\$CDN)	13.0%	22.0%	10.2%	0.8%	2.1%	2.5%	6.6%

<sup>1</sup> Except for year-to-date. <sup>2</sup> December 15, 1994.

CONTINUED ON NEXT PAGE

CONTINUED FROM PAGE 1

## OB Model Portfolio

### Different Makes a Difference

#### LOOKING BACK CAN BE DANGEROUS

Performance  
by Decade<sup>1</sup>



1990s	172%	565%
2000s	72%	-34%
2010s <sup>2</sup>	14%	28%

<sup>1</sup> Measured in Canadian Dollars; <sup>2</sup> As of September 15, 2012

“ U.S. STOCKS PRODUCED A TOTAL RETURN OF 565 PER CENT IN THE 1990S, MEASURED IN CANADIAN DOLLARS, WHICH IS THREE TIMES WHAT WAS ACHIEVED BY CANADIAN STOCKS. CONSEQUENTLY, MANY CANADIANS USED DEPRESSED CANADIAN DOLLARS TO DIVERSIFY INTO U.S. STOCKS AT THE TURN OF THE CENTURY, JUST IN TIME FOR A DECADE OF HORRIBLE PERFORMANCE FROM U.S. STOCKS. ”

*The Odlum Brown Model Portfolio was established on December 15, 1994 with a hypothetical investment of \$250,000. The Model provides a basis with which to measure the quality of our advice. It also facilitates an understanding of how we believe individual security recommendations could be used within the context of a client portfolio. Trades are made using the closing price on the day a change is announced. Performance figures do not include any allowance for fees. Past performance is not indicative of future performance.*

were hot and we did not own enough. Rather than having a resource concentrated portfolio similar to the makeup of the S&P/TSX Index, we instead had a portfolio that was diversified across sectors and geographies. Having diversification ultimately cushioned the blow during the market crash and yielded better growth in the long-term; however, much patience was required.

We highlight periods of poor relative performance because they should be expected. One has to be prepared to be different and underperform over the short-term in order to achieve above-average results over the long-term.

We did not change our strategy when our relative performance was poor. We maintained our discipline, focused on business fundamentals and continued to ensure that we owned the securities with the best combination of quality and price.

It is important to note that the foundation for the Model's recent good performance was set as far back as 2005. That was the year we meaningfully diversified outside of Canada, as many high quality U.S. multinationals started to meet our “value” criteria. Businesses like Coca-Cola had almost always traded at valuation multiples that caused value-minded investors to cringe, but as investors lost interest in the shares of great U.S. companies, we built positions.

For the first 10 years of the Model's existence, the Canadian dollar was depressed and there was great value in Canada, so we kept most of our money at home. As the Canadian dollar appreciated and U.S. stocks started to look more attractive relative to opportunities in Canada, we increased the foreign content to the 45-50 per cent range in 2005 and 2006. Since then, it has stayed at that level.

The willingness to be different, yet sensible, has allowed us to assemble a portfolio that has characteristics that we believe are far superior to the Canadian benchmark index. Not only is the OB Model Portfolio considerably more balanced across sectors than the S&P/TSX Index, but it also has a very different focus within some of the big sectors.

Within the Financial Services sector, for example, we have a much lower weighting in Canadian Banks, as we believe their growth prospects are muted compared to other opportunities. Instead of big Canadian Bank holdings, we have large

positions in Brookfield Asset Management, JPMorgan, Onex, Howard Hughes Corporation and Intact Financial.

Investors are nervous and frustrated with equity investing, which is somewhat understandable given the extreme volatility in recent years. Nonetheless, with the benchmark Canadian equity index achieving a compound annual return of 9.4 per cent over the last 10 years, it makes one wonder why investors are disillusioned. It is probably because many investors achieved sub-par results by chasing what worked in the last cycle rather than focusing on the fundamentals and forward-looking odds.

U.S. stocks produced a total return of 565 per cent in the 1990s, measured in Canadian dollars, which is three times what was achieved by Canadian stocks. Consequently, many Canadians used depressed Canadian dollars to diversify into U.S. stocks at the turn of the century, just in time for a decade of horrible performance from U.S. stocks. In the 2000s, Canadian stocks appreciated by 72 per cent whereas U.S. stocks dropped by 34 per cent. Disgusted with poor U.S. returns and pessimistic regarding the U.S. economic outlook, it became common for Canadians to sell U.S. stocks and bring money back home. Once again, that proved to be the wrong tactical decision. Since the end of 2009, U.S. stocks have produced a total return of 28 per cent, which is double what the Canadian equity benchmark has achieved.

U.S. stocks are performing better than their Canadian counterparts because the outlook is better south of the border. Following a devastating financial crisis and recession, the U.S. is recovering whereas Canada's economy is only now starting to cool. We own a lot of U.S. stocks in the Model because we are looking forward, not backward.

We are not sure how the Canadian benchmark index will perform in a slow-growth world, but we are confident that the businesses we own will grow and appreciate in value over time. Our approach is different and we are hopeful that it will continue to make a difference. 

**MURRAY LEITH, CFA**  
VICE PRESIDENT AND DIRECTOR,  
INVESTMENT RESEARCH

## ODLUM BROWN MODEL PORTFOLIO

	S&P/TSX Weight	Sep 15/12 Price	Shares	Cost	Market Value	Portfolio Weight	Dividend Yield	Target Price	Total Return Potential
<b>FINANCIALS</b>	<b>30.5%</b>					<b>28.9%</b>			
Toronto-Dominion Bank (TD)		\$81.80	1,600	\$71,826	\$130,880	4.4%	3.8%	\$92.00	16%
Brookfield Asset Management Inc. (BAM.A) <sup>1</sup>		\$34.73	3,700	\$89,816	\$128,501	4.3%	1.6%	\$40.00	17%
JPMorgan Chase & Co. (JPM)*		\$41.57	3,000	\$112,931	\$121,174	4.1%	2.9%	\$55.00	35%
Onex Corp. (OCX)		\$39.73	2,700	\$49,293	\$107,271	3.6%	0.3%	\$48.00	21%
The Howard Hughes Corp. (HHC)*		\$73.52	1,300	\$63,704	\$92,866	3.1%	0.0%	\$100.00	36%
Intact Financial Corp. (IFC)		\$58.60	1,200	\$43,380	\$70,320	2.4%	2.7%	\$72.00	26%
Manulife Financial Corp. (MFC)		\$12.64	5,500	\$104,447	\$69,520	2.3%	1.0%	\$16.00	28%
Berkshire Hathaway Inc. (BRK.B) <sup>2</sup>		\$88.70	600	\$49,545	\$51,711	1.7%	0.0%	\$120.00	35%
Bank of Montreal (BMO)		\$58.35	750	\$43,613	\$43,763	1.5%	4.9%	\$65.00	16%
Bank of Nova Scotia (BNS)		\$53.58	750	\$15,713	\$40,185	1.4%	4.3%	\$57.00	11%
<b>MATERIALS</b>	<b>20.4%</b>					<b>7.9%</b>			
Agrium Inc. (AGU)		\$100.74	900	\$43,227	\$90,666	3.1%	1.0%	\$125.00	25%
Barrick Gold Corp. (ABX)		\$41.19	1,900	\$90,915	\$78,261	2.6%	1.9%	\$45.00	11%
Potash Corporation (POT)		\$41.37	1,550	\$64,434	\$64,124	2.2%	1.9%	\$62.00	52%
<b>ENERGY</b>	<b>26.8%</b>					<b>17.9%</b>			
Royal Dutch Shell PLC ADR (RDS.B) <sup>3</sup>		\$75.00	1,500	\$90,034	\$109,311	3.7%	4.6%	\$90.00	25%
Enovus Energy Inc. (CVE)		\$35.72	2,800	\$95,717	\$100,016	3.4%	2.5%	\$47.00	34%
Trinidad Drilling Ltd. (TDG)		\$7.25	12,800	\$100,685	\$92,800	3.1%	2.8%	\$12.00	68%
Peyto Exploration & Development Corp. (PEY)		\$21.75	3,300	\$57,090	\$71,775	2.4%	3.2%	\$27.00	27%
TransCanada Corp. (TRP)		\$45.30	1,400	\$21,550	\$63,420	2.1%	3.9%	\$47.00	8%
Bonavista Energy Corp. (BNP)		\$16.61	2,800	\$57,232	\$46,508	1.6%	8.6%	\$21.00	35%
Encana Corp. (ECA)		\$22.69	2,000	\$66,178	\$45,380	1.5%	3.6%	UR	UR
<b>INDUSTRIALS</b>	<b>5.7%</b>					<b>10.6%</b>			
Canadian National Railway Co. (CNR)		\$90.97	800	\$42,264	\$72,776	2.5%	1.6%	\$92.00	3%
3M Co. (MMM)*		\$93.98	650	\$56,003	\$59,355	2.0%	2.5%	\$105.00	14%
General Electric Co. (GE)*		\$22.11	2,600	\$50,404	\$55,856	1.9%	3.0%	\$25.00	16%
United Parcel Service Inc. (UPS)*		\$73.68	650	\$50,735	\$46,534	1.6%	3.1%	\$90.00	25%
Canadian Pacific Railway Limited (CP)		\$85.22	500	\$35,955	\$42,610	1.4%	1.7%	\$88.00	5%
Ritchie Bros. Auctioneers Inc. (RBA)		\$19.12	2,000	\$41,880	\$38,240	1.3%	2.6%	\$23.50	25%
<b>CONSUMER DISCRETIONARY</b>	<b>4.3%</b>					<b>4.4%</b>			
Lowe's Companies Inc. (LOW)*		\$29.40	2,500	\$58,391	\$71,416	2.4%	2.2%	\$34.00	18%
Starbucks Corp. (SBUX)*		\$50.46	1,200	\$27,941	\$58,835	2.0%	1.4%	\$63.00	26%
<b>INFO TECH</b>	<b>1.3%</b>					<b>11.1%</b>			
Syntel Inc. (SYNT)*		\$62.25	1,850	\$45,902	\$111,898	3.8%	0.4%	\$74.00	19%
Apple (AAPL)*		\$691.28	120	\$39,079	\$80,602	2.7%	1.5%	\$750.00	10%
Cisco Systems Inc. (CSCO)*		\$19.49	3,400	\$53,270	\$64,387	2.2%	2.9%	\$23.00	21%
Google (GOOG)*		\$709.68	75	\$38,148	\$51,717	1.7%	0.0%	\$800.00	13%
STMicroelectronics NV (STM)*		\$6.74	3,000	\$31,490	\$19,647	0.7%	6.4%	\$8.00	25%
<b>CONSUMER STAPLES</b>	<b>2.8%</b>					<b>8.1%</b>			
Diageo PLC ADR (DEO)*		\$108.72	700	\$48,931	\$73,946	2.5%	3.1%	\$120.00	13%
The Coca-Cola Company (KO)*		\$38.12	2,000	\$49,982	\$74,079	2.5%	2.6%	\$44.00	18%
Colgate-Palmolive Co. (CL)*		\$103.75	550	\$45,094	\$55,445	1.9%	2.3%	\$118.00	16%
Sysco Corp. (SYY)*		\$30.35	1,200	\$42,458	\$35,387	1.2%	3.5%	\$36.00	22%
<b>TELECOM SERVICES</b>	<b>4.9%</b>					<b>2.9%</b>			
BCE Inc. (BCE)		\$42.56	2,000	\$69,350	\$85,120	2.9%	5.3%	\$44.00	9%
<b>UTILITIES</b>	<b>1.9%</b>					<b>2.8%</b>			
Fortis Inc. (FTS)		\$33.00	2,500	\$58,375	\$82,500	2.8%	3.6%	\$35.00	10%
<b>HEALTH CARE</b>	<b>1.5%</b>					<b>4.6%</b>			
Stryker Corp. (SYK)*		\$56.01	1,400	\$75,744	\$76,191	2.6%	1.5%	\$65.00	18%
Novartis AG ADR (NVS)*		\$59.86	1,050	\$57,696	\$61,071	2.1%	4.1%	\$64.00	11%
<b>SUB TOTAL</b>				<b>\$2,350,423</b>	<b>\$2,936,065</b>	<b>99.1%</b>			
<b>SHORT-TERM INVESTMENTS</b>					<b>\$25,534</b>	<b>0.9%</b>			
<b>PORTFOLIO TOTAL</b>					<b>\$2,961,599</b>	<b>100%</b>			

\* = Prices in U.S. dollars UR = Under Review U.S. Exchange (\$US/\$CDN) \$1.0292 Foreign Weight 45.8%

<sup>1</sup> Class A shares elect one-half of the company's Board of Directors.

<sup>2</sup> A share of Class B common stock has the rights of 1/1,500<sup>th</sup> of a share of Class A common stock except that a Class B share has 1/10,000<sup>th</sup> of the voting rights of a Class A share.

<sup>3</sup> Class A shares have a Dutch source for tax purposes, and the Class B shares have a UK source.



## In the Community

Odlum Brown Chilliwack is proud to partner with the Chilliwack School of Performing Arts (CSOPA) as a Gold Sponsor for the 2012/13 Season.

CSOPA is the only non-profit youth theatre company in Chilliwack for children ages 3-18 that provides learning and performance opportunities through a variety of workshops and classes taught by professional artists, directors and instructors.

Each year, CSOPA hosts a variety of productions and presentations to showcase the talented work and artistic skills of its students, including the school's Spring Festival, and the *annual* production, which takes the stage at the Chilliwack Cultural Centre every January.

For more information, visit [csopa.ca](http://csopa.ca)

## Charitable Donations – Cash vs. Shares

### PLEASE READ OUR ODLUM BROWN LIMITED DISCLAIMER & DISCLOSURE / IT IS IMPORTANT

Odlum Brown Limited is an independent, full-service investment firm focused on providing professional investment advice and objective research. We respect your right to be informed of relationships with the issuers or strategies referred to in this report which might reasonably be expected to indicate potential conflicts of interest with respect to the securities or any investment strategies discussed or recommended in this report. We do not act as a market maker in any securities and do not provide investment banking or advisory services to, or hold significant positions in, the issuers covered by our research. Analysts and their associates may, from time to time, hold securities of issuers discussed or recommended in this report because they personally have the conviction to follow their own research, but we have implemented internal policies that impose restrictions on when and how an Analyst may buy or sell securities they cover and any such interest will be disclosed in our report in accordance with regulatory policy. Our Analysts receive no direct compensation based on revenue from investment banking services. We describe our research policies in greater detail, including a description of our rating system and how we disseminate our research, on the Odlum Brown Limited website at [odlumbrown.com](http://odlumbrown.com).

This report has been prepared by Odlum Brown Limited and is intended only for persons resident and located in all the provinces and territories of Canada, where Odlum Brown Limited's services and products may lawfully be offered for sale, and therein only to clients of Odlum Brown Limited. This report is not intended for distribution to, or use by, any person or entity in any jurisdiction or country including the United States, where such distribution or use would be contrary to law or regulation or which would subject Odlum Brown Limited to any registration requirement within such jurisdiction or country. As no regard has been made as to the specific investment objectives, financial situation, and other particular circumstances of any person who may receive this report, clients should seek the advice of a registered investment advisor and other professional advisors, as applicable, regarding the appropriateness of investing in any securities or any investment strategies discussed or recommended in this report.

This report is for information purposes only and is neither a solicitation for the purchase of securities nor an offer of securities. The information contained in this report has been compiled from sources we believe to be reliable, however, we make no guarantee, representation or warranty, expressed or implied, as to such information's accuracy or completeness. All opinions and estimates contained in this report, whether or not our own, are based on assumptions we believe to be reasonable as of the date of the report and are subject to change without notice.

Please note that, as at the date of this report, the Research Analyst responsible for the recommendations herein, associates of such Analyst and/or other individuals directly involved in the preparation of this report hold securities of the issuer(s) referred to directly or through derivatives.

No part of this publication may be reproduced without the express written consent of Odlum Brown Limited. Odlum Brown Limited is a Member-Canadian Investor Protection Fund.

Odlum Brown Limited respects your time and your privacy. If you no longer wish us to retain and use your personal information preferring to have your name removed from our mailing list, please let us know. For more information on our Privacy Policy please visit our website at [odlumbrown.com](http://odlumbrown.com).

**CANADA HAS LONG PROVIDED GENEROUS TAX INCENTIVES FOR CANADIANS** who donate to charitable organizations by means of a two-tiered tax credit. Since 2006, an additional incentive has allowed Canadians to donate publicly-traded securities with unrealized gains.

The following overview outlines the tax benefits of donating shares, in lieu of cash, to a registered charity.

### THE BASICS

On the first \$200 of charitable donations claimed in a year, a BC taxpayer would receive a tax credit of \$40 (20.06 per cent). The credit on donations in excess of \$200 is worth 43.7 per cent. For example, a \$5,000 donation would result in a tax credit worth \$2,138 [ $\$40 + (\$4,800 \times 43.7 \text{ per cent})$ ].

The maximum donation amount that can be claimed for a tax credit in a given year is 75 per cent of your net income. Any donations not claimed in the year they are made can be claimed in any of the following five years. The annual limit for donations that can be claimed in the year of death or the year preceding death is 100 per cent of your net income.

### PUBLICLY-TRADED SECURITIES<sup>1</sup>

In addition to the existing donation tax credit that is based on the fair market value of the shares or other securities donated, since 2006, any capital gains triggered on donations of publicly-traded securities to a registered charity are not taxable.

### EXAMPLE

Suppose you have shares of XYZ Co. worth \$5,000 that you originally purchased for \$3,000. If you sell the shares and donate the proceeds to a registered charity, you can expect \$437 in capital gains taxes (assuming a marginal tax rate of 43.7 per cent). However, since you would receive a tax credit of \$2,138, the total economic cost to you would be \$3,299 (see table below).

On the other hand, if you choose to donate the shares directly to a charity, you would not only receive a tax credit of \$2,138, as stated above, but you would also save the \$437 in capital gains taxes. Under this scenario, the total economic cost for your \$5,000 donation would be \$2,862 (see table below).

		SELL SHARES & DONATE CASH	DONATE SHARES DIRECTLY
<b>a</b>	<b>Value of Donation</b>	<b>\$5,000</b>	<b>\$5,000</b>
	Original Cost of Shares	(3,000)	(3,000)
	Capital Gain	2,000	2,000
	Taxable Capital Gain (50% or NIL)	1,000	-
<b>b</b>	<b>Income Tax @ 43.7% (Before Credit)</b>	<b>437</b>	<b>-</b>
<b>c</b>	<b>Donation Tax Credit (\$200 x 20.06%) + (\$4,800 x 43.7%)</b>	<b>2,138</b>	<b>2,138</b>
<b>a+b-c</b>	<b>Economic Cost of Donation to You</b>	<b>\$3,299</b>	<b>\$2,862</b>

As illustrated above, if you are considering making a charitable donation, it can be advantageous to donate securities that have appreciated in value. Before making a donation of publicly-traded securities or other non-cash assets to a charitable organization, it is advisable to contact the recipient charity to verify that they are able to process your intended donation.

To learn more about tax incentives for donations to registered charitable organizations or for more information about the products and services offered by Odlum Brown Financial Services Limited, please contact us through your Odlum Brown Investment Advisor or Portfolio Manager.

**MICHAEL EREZ, CGA, CFP, BA**

FINANCIAL AND TAX PLANNER, ODLUM BROWN FINANCIAL SERVICES LIMITED

<sup>1</sup> Flow-through shares are subject to more restrictive rules and are beyond the scope of this article.

ODLUM BROWN FINANCIAL SERVICES LIMITED IS A WHOLLY-OWNED SUBSIDIARY OF ODLUM BROWN LIMITED, OFFERING LIFE INSURANCE PRODUCTS, RETIREMENT, ESTATE AND FINANCIAL PLANNING EXCLUSIVELY TO ODLUM BROWN CLIENTS.