Kilgour Advisory Group

Portfolio Manager Report

UWO Liquidating Trust – Quarter ending 30 June 2011

Preamble

The University of Western Ontario Liquidating Trust ('UWO LT') holds a portfolio of Restructured Asset Backed Notes ('AB Notes') that resulted from the restructuring of the Non-Bank Asset Backed Commercial Paper ('ABCP') market that was completed in January 2009. Kilgour Advisory Group (KAG) is a specialist risk management firm retained by UWO LT to provide portfolio valuation, risk management and reporting, and market liaison. KAG reports quarterly with commentary on credit markets, description of the margin triggers and reference indices, discussion of events affecting UWO LT's holdings, summary of secondary markets, and valuation of the portfolio.

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Credit Markets

North American credit markets continued their strengthening trend through the first half of Q2 with further tightening of both bond yields and credit default swap spreads. At mid-May, however, the trend reversed as the markets reacted to worsening conditions in Europe and an emerging US debt limit crisis. While the North American markets had previously shrugged off negative news regarding European sovereigns and Greece specifically, in the latter part of the quarter there was growing concern about contagion spreading more broadly among European sovereigns and the potential knock-on effect on the global economic recovery.

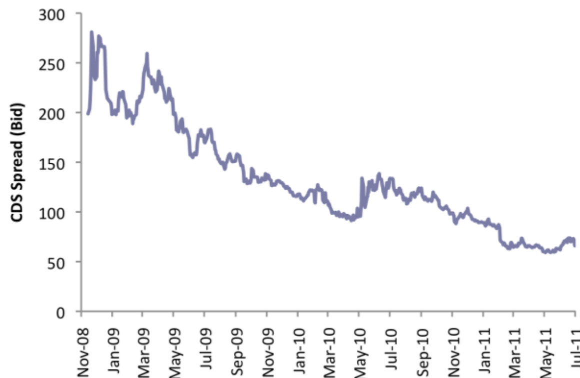
The movements in credit default swap premiums and bond yields over time and during the second quarter of 2011 are tracked in the charts below. The upper charts show the Credit Default Swap Index for Investment Grade rated US corporations ('CDX IG')[1]. The lower charts track corporate bond yields by S&P ratings cohorts.

The trend within the credit default index demonstrates the pricing developments described above. Namely, that the CDX index has tightened significantly over the last year (see upper left chart) but that this tightening trend was reversed somewhat in mid-May of 2011 (upper right). Whereas the markets were able to shrug off concerns about Greece and other European sovereigns in Q1, the re-emergence of these concerns in Q2 concurrent with the apparent reality that the US economic recovery has been weaker than initially anticipated combined to add volatility and wider spreads in the CDX.

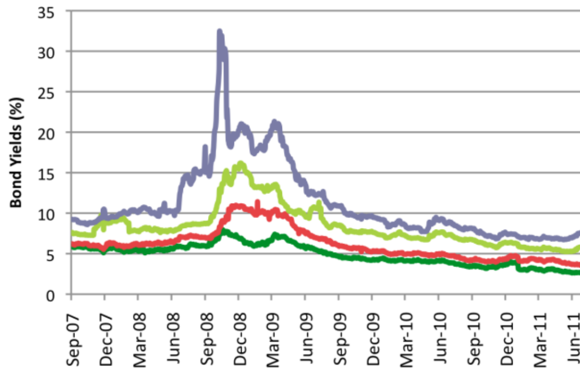
[1] Series 11 is shown as this was the on-the-run (i.e. current) index at the time of the ABCP restructuring.

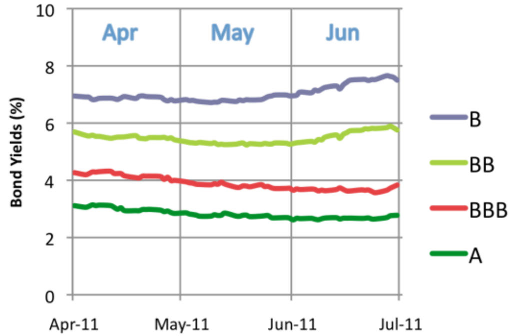
Bond yields also trended lower over the first part of 2011 (see lower left chart). This trend changed in mid-May and there was increased volatility and a widening in yields in the latter half of Q2 (see lower right chart). There was a bit of a divergence of yield between High Yield rated bonds (viz. B and BB) and the High Grade ones, which is typical when credit markets begin to get nervous.

CDX IG Series 11 (5Y)



S&P Bond Cohorts





Source: Advantage Data

Looking forward, it is noted that the MAV2 Notes are not directly exposed to European sovereign risk, however there are some concerns about 'contagion' effecting the global economic recovery and therefore North America corporations. Additionally, since credit markets currently expect a successful resolution to the US debt ceiling matter, any failure to resolve this matter could have a negative effect on secondary trading prices and liquidity of the MAV notes.

Risk Assessment

KAG's risk assessment framework tracks credit risk, margin trigger risk, collateral risk, and structuring risk.

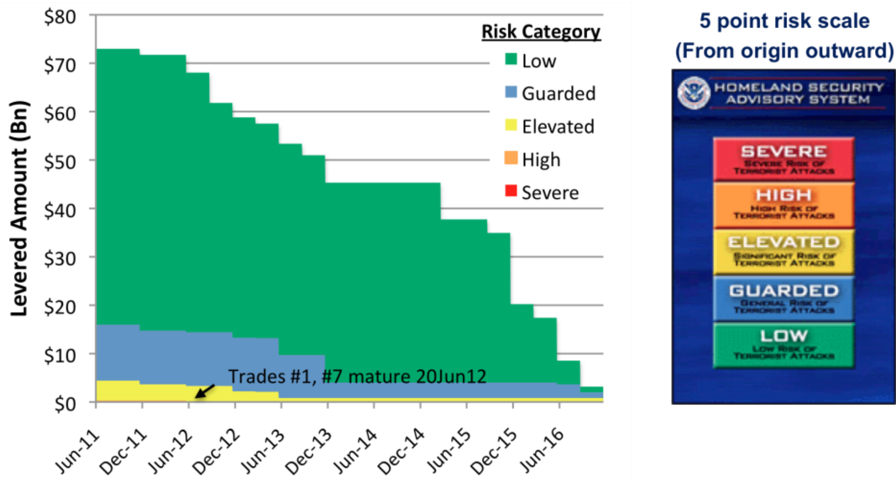
Credit Risk

The assessment of credit risk focuses on the potential for losses within the portfolio of Leveraged Super Senior ('LSS') credit default swaps that underlie the MAV2 Pool.[2] The volatility in the broad credit markets gives a high level indication that credit risk in the Pool has somewhat increased and this is marginally negative to the value of the MAV2 Pooled notes.

In addition to considering the general state of the credit markets, it is necessary to consider the risk of each individual LSS deal when assessing overall credit risk. And for the LSS deals that are closest to incurring losses, the MAV2 Pooled notes are exposed to the idiosyncratic risk of the individual corporate names in those portfolios.

The chart below tracks the maturity of the Pool of LSS trades from today until final maturity in January 2017. Two LSS trades – Trades #1 and #7 – continue to be the only ones that are highlighted as presenting 'Severe' risk and none that are identified as 'High' risk. There are a small number of trades that are classified in the 'Elevated' risk category; the remainder is 'Guarded' or 'Low' risk. It is also notable that the majority of the highest risk trades, those in the Severe and Elevated categories will mature in the next ~24 months. By June-2013, both the size of the risk pool will be reduced but also – more importantly – the bulk of the riskiest assets will be gone. This de-levering and 'de-risking' will be an important beneficial feature for the MAV2 Pooled notes.

LSS Pool Risk Segmentation

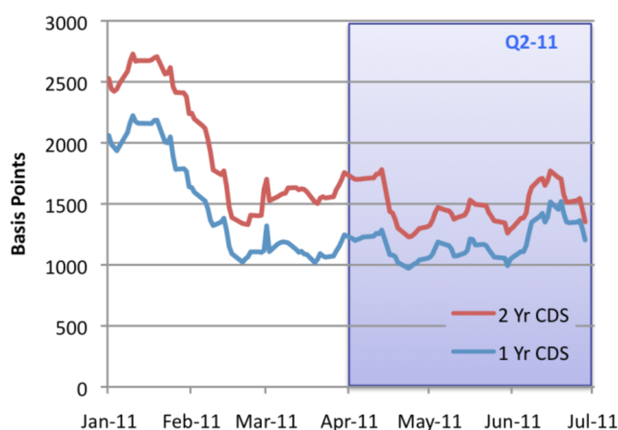


During the second quarter of 2011, there was one default of a reference entity in one of the credit default swap portfolios underlying the AB Notes. The defaulting entity was Allied Irish

[2] When the original non-bank asset-backed commercial paper was restructured, all eligible LSS trades and their collateral were pooled. Currently, there are 69 LSS trades with a total notional value at risk of $73 Bn; these are collateralized by the $9.8 Bn of assets in the collateral pool.

Bank. The portfolio in question, Trade 24, has an attachment point ('deductible') of 8.56% and a detachment point of 100%. Because the attachment point remains quite high and the tranche thickness is very wide, this single loss will not cause any changes to risk categorization of this or any LSS trade in the KAG risk segmentation[3] of the LSS pool. However, this trade also has significant exposure to various European financial institutions that are at risk, including two which have defaulted in the start of Q3[4]. Accordingly, it is expected that Trade 24 will be classified as a higher risk trade by next quarter. However, while the potential for losses in this portfolio is becoming greater, the potential severity of losses remains relatively low given the modest size of the trade ($327mm) and the wide tranche thickness.

Therefore, Trades #1 and #7[5] continue to be the most immediate source of credit risk for the MAV2 Pooled notes and the focus of our credit risk assessment. The outcome of Trades #1 and #7 will largely be determined by the performance of one individual reference entity, MBIA Insurance Corp. This position is overweight within the portfolio and represents 2.45% of the portfolio. MBIA Insurance is a US 'monoline' insurer of residential mortgage backed securities. which was badly affected by the sub-prime crisis and its fallout on the US real estate market. It is now in a "run-off mode" whereby it is not writing any new insurance and is balancing its assets versus current and future liabilities. It is engaged in litigation and negotiations with mortgage originators disputing whether the bonds that they insured were properly made in context of their mortgage origination policies. At the same time, the parent company, MBIA Inc., is being countersued by the same banks who allege that MBIA made a "fraudulent conveyance" when it divided into separate legal entities for the mortgage insurance (MBIA Insurance) and muni-bond insurance (National Public Finance Guarantee).



The credit default swap spread on MBIA Insurance was volatile and tightened somewhat during the quarter (see left). The CDS is a focus of trading and is largely influenced by day-to-day news related to the status of its legal wrangling. For holders of the MAV2 Pooled Notes, perhaps the more relevant measure is the decreasing time-to-maturity on Trades #1 and #7: there is some comfort that these trades will mature before MBIA can default.

[3] KAG maintains a segmentation of the LSS pool whereby each individual trade is categorized as Severe, High, Elevated, Guarded, or Low risk.

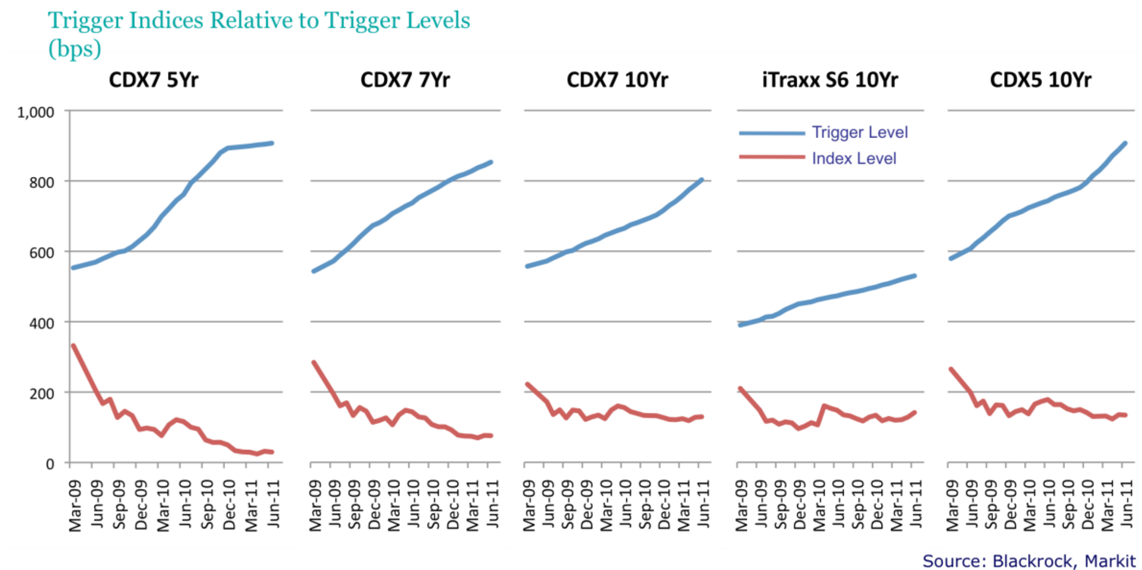
[4] Irish Life & Permanent plc and Governor and Company of the Bank of Ireland both defaulted in July 2011 and both are in Trade 24.

[5] To recap: trades #1 and #7 are two Leveraged Super Senior trades with Deutsche Bank as the asset provider. They contain portfolios that are identical in composition and allocation and have the same leverage (2.5X). Trades #1 and Trade #7 together have levered amounts at risk of $324 million. In combination, these trades represent about 3% of the MAV2 Pool. If Trade #1 and #7 begin to experience losses, those losses will first affect the value of the MAV2 Class C notes. If #1 and #7 were to lose all value – namely $324 million – then the Class C notes will lose all value and the maximum value at redemption of the Class B notes would be reduced to ~$0.80 per dollar of par value. The Class A-2 and A-1 notes that comprise the bulk of the LP's exposure to the Pooled Notes cannot be affected by a default of Trades #1 and #7 alone. Trades #1 and #7 have a maturity date of 20 June 2012 therefore we are only concerned with their performance for the next ~11 months, after which they will present no risk to the LP's notes.

Margin Trigger Risk

Margin trigger risk is still extremely remote in spite of the recent volatility in credit markets. There were no new defaults during Q2/11 in any of the reference indices for the MAV2 Spread-Loss margin triggers[6]. Credit markets have greatly improved since the time of the restructuring notwithstanding that certain reference indexes widened over the quarter. The reduction in time to maturity also reduces margin trigger risk by raising the trigger levels. There continues to be a very large divergence between the falling reference indices (red lines below) and their trigger levels (blue lines). (Note that a trigger breach would occur if, at any time, a red line crosses above a blue one.)

As at the end of June 2011, indices on average were 14.0% of their trigger level; put another way, credit indices would have to blow out to levels over seven times wider to trigger. At the end of Q1, the indices were somewhat tighter and were 13.5% of trigger levels.



Collateral Risk

The Leveraged Super Senior pool is supported by $9.8 Bn of collateral. These assets are available to the LSS counterparties in the case that an LSS trade defaults. At the maturity of the notes, the remaining collateral will be released and distributed to the noteholders as return of

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[6] The margin triggers for the Pooled Notes take the form of 'spread-loss' triggers whereby a limit is defined in terms of the market spread of a reference index (e.g. CDX IG7) and determined within a matrix of actual loss and remaining time to maturity. Losses within the reference indices have the impact of lowering the 'margin trigger' spread limit, thereby increasing the risk of margin calls. The passage of time – and resulting decrease in time to maturity – has the effect of increasing the spread limit and, all else being equal, reduces the risk of a margin call. The margin triggers are important because if the market spread on the reference index exceeds the trigger level, MAV2 must draw upon its margin funding facility to post margin. If credit markets deteriorate significantly, there is a possibility that the margin funding facility will not be large enough to post sufficient margin. This would result in the underlying assets in MAV2 defaulting and would entail significant losses to the LP.

principal. Therefore, it is important to monitor the quality of the collateral pool itself in order to be assured that funds will be available to investors at maturity.

The collateral pool is generally composed of high-quality, low-risk assets. One notable exception is the three CDO-squared assets that have been highlighted by DBRS and others as potentially risky. These assets have been stable and realized no additional losses in Q2/11. KAG continues to monitor the disclosures from BlackRock, the asset administrator, regarding these assets.

Structuring Risk

KAG monitors for adverse affects of 'structuring risk', which is a hold-all category for errors in drafting or application of legal documents, changes in regulatory environment, etc. At this point, structuring risk is seen as minimal.

DBRS placed its ratings of the MAV2 A-1 and A-2 notes 'under review with positive implications' on 1-Jun-2011. While the bond rating does not impact the intrinsic value of the notes, this positive outlook by DBRS does provide a third-party validation of the improving risk of the senior MAV2 Pooled notes.

Additionally, there has been some ongoing litigation concerning the QSPE-XCD mortgage securitization program in which the MAV2 pooled notes and certain tracking notes are invested. This suit has been ongoing for about 1 year and is nearing a negotiated settlement which should have no material impact on UWO LT's holdings.

Risk Assessment – MAV2 Class 13s

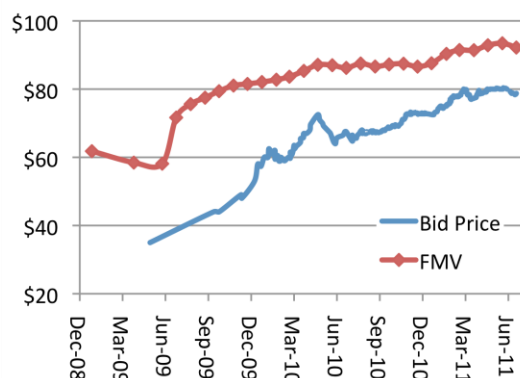
While the vast majority of UWO LT's portfolio consists of MAV2 Pooled notes, it also has about 3.5% of its holdings (~$650,000) in the MAV2 Class 13 Ineligible Asset Tracking note. This note has a US$96 million credit exposure to a portfolio of Credit Default Swaps which matures in March 2013. There were no additional defaults in this portfolio in Q2/11, so the attachment point of the transaction remains unchanged at 6.19%.

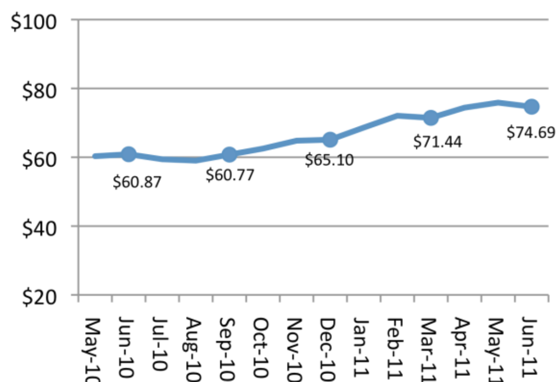
The collateral for the CDS was originally a US$96 million 'TABS note' which was the senior note of a credit structure with exposure to US sub-prime mortgages. The current par value of this note is US$37.7 million (US$38.9 million last quarter) as there has been $58.4 million ($57.3 million last quarter) repaid on the note. The $58.4 million cash is still being held as collateral on the CDS. The remaining portion of the TABS note is likely to realize some losses. It is rated CC/Ca and it has a mark to market value less than 10% of par.

With less than two years to maturity and an attachment point exceeding 6%, KAG continues to be of the view that it is likely that the CDS will mature without losses. If the attachment point is not breached prior to the CDS maturing, the remaining collateral will be returned to note holders. The collateral, which now consists of approximately 60% cash and 40% distressed bond would therefore have a minimum payout of approximately 60% of par and possibly (although not likely) higher in the event that the TABS note enjoys some greater level of recovery.

AB Notes Secondary Market

Secondary market indicative bid prices rose again during Q2/11. The indicative bids for the 'full strip' (namely, the MAV2 A-1, A-2, B and C notes in the proportion that they were issued) rose from $0.714 as at 31 March 2011 to $0.747 as at 30 June 2011. In a reflection of the performance of broader credit risk markets, prices peaked at higher rates in mid-May before falling off somewhat to the end of June. Trading continues to be focused on the MAV2 Pooled Notes. There are very few buyers of Tracking Notes.





The potential for an 'optional early redemption' continues to buoy secondary market prices but it appears that current pricing levels are such that the investment yield to the hedge fund investors is becoming less compelling. There were no new public disclosures during the quarter from the conglomerate of US hedge funds who are driving this initiative. KAG continues to monitor the situation and new developments closely.

Portfolio Valuation

The Fair Market Value ('FMV') of the Portfolio as at 30 June 2011 was $14.11 million, up from $13.55 million as at 31 March 2011 and $12.41 million at 31 December 2010. The Weighted Average Price of the Portfolio at end of Q2 was 74.58%, up from 71.57% one quarter prior. The full portfolio and note-by-note pricing for the last 3 quarters is listed in the table below.

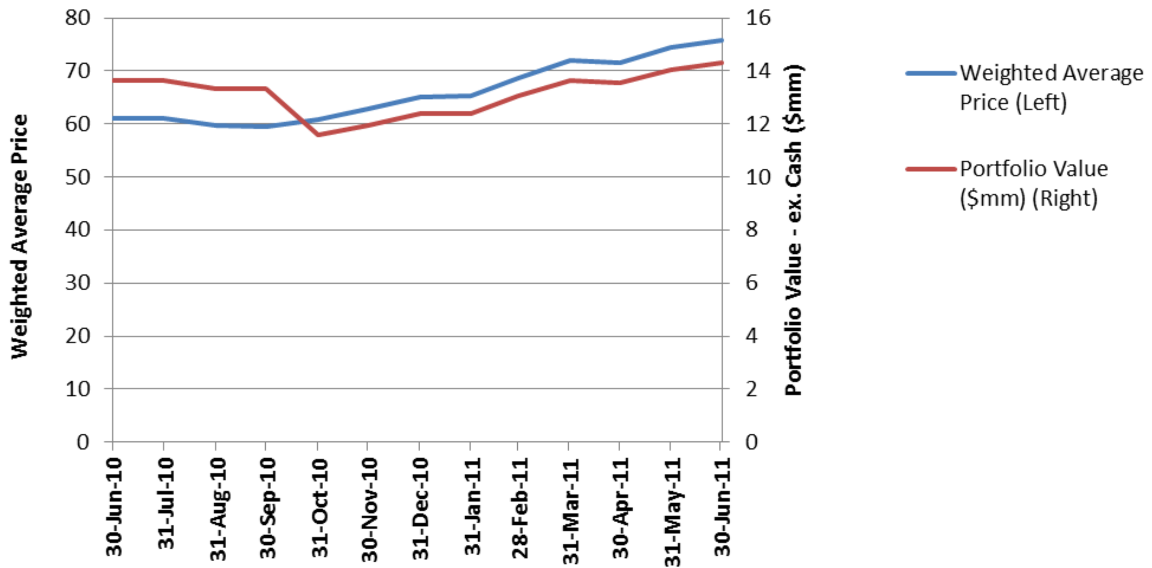
UWO Liquidating Trust

Re-Structured Asset Backed Notes

Valuation as of:	**31-Dec-10**			**31-Mar-11**			**30-Jun-11**		
			CAD:USD			CAD:USD			CAD:USD
			0.99365			0.97275			0.96510
Notes	**Par Value (Local currency)**	**Price (Local currency)**	**Market Value (CAD)**	**Par Value (Local currency)**	**Price (Local currency)**	**Market Value (CAD)**	**Par Value (Local currency)**	**Price (Local currency)**	**Market Value (CAD)**
Class A-1	8,997,474	72.44	6,517,590	8,997,474	77.38	6,961,796	8,997,474	78.92	7,100,507
Class A-2	5,919,516	63.94	3,784,820	5,919,516	70.10	4,149,581	5,919,516	73.92	4,375,509
Class B	1,074,551	41.81	449,302	1,074,551	55.50	596,376	1,074,551	64.73	695,548
Class C	495,472	9.81	48,621	495,472	25.30	125,354	495,472	35.98	178,246
IA Tracking Note Class 13	316,001	48.00	151,680	316,001	54.33	171,694	316,001	57.50	181,701
Class A-1 (USD)	1,799,382	72.44	1,295,160	1,799,382	77.38	1,354,332	1,799,382	78.92	1,370,454
Class C (USD)	55,836	9.81	5,444	55,836	25.30	13,742	55,836	35.98	19,386
IA Tracking Note Class 13 (USD)	333,292	48.00	158,964	333,292	54.33	176,154	333,292	57.50	184,955
Total (Local currency)	$18,991,524			$18,991,524			$18,991,524		
Total (CAD)	$18,977,627		$12,411,582	$18,931,887		$13,549,028	$18,915,145		$14,106,304
Wtd Average (CAD)		65.40			71.57			74.58	

Over the last 12 months the portfolio has steadily appreciated in value, particularly since September 2010, when numerous new buyers came into the market and as well as the initial concept for the potential optional redemption began to circulate in the market.

Portfolio Value over Last 12 Months



Throughout the quarter, almost all of the change in value was due to price increases in the secondary market, while there was a slight negative impact due to exchange rate fluctuations. These changes are shown below.

Quarter over Quarter Changes (C$mm)

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In summary, Q2 2011 saw volatility and some widening in North American credit markets in reaction to global events and to the flat US economic recovery. In spite of this, secondary market prices continued their climb and narrowed the gap to intrinsic fair market value. The portfolio value was also increased due to improved outlook for some of the Tracking notes. KAG continues to believe that the LP's strategy of holding these notes rather than liquidating at current prices is financially prudent.

Kilgour Advisory Group
29 July 2011

GLOSSARY OF TERMS

Asset-Backed Notes or 'AB Notes'	Notes created through the restructuring of the former non-bank asset-backed commercial paper (ABCP) purchased by the LP in July 2008. The AB Notes are comprised of: 'Pooled Notes', 'Ineligible Asset Tracking Notes' and 'Traditional Asset Tracking Notes'.
Credit Default Swapor 'CDS'	Contract where Counterparty A pays financial consideration to a Counterparty B to assume the risk of default by a specific third party company. Analogous to insurance, where A pays a premium to B in return for a lump-sum payment should the specified third-party company go bankrupt or otherwise default. Credit default swaps can be done on an 'unfunded' basis since there is no requirement for either party to own the referenced credit. A CDS premium is quoted in terms of basis points (one-hundredths of a percent) of the notional value 'insured'. Portfolios of CDSs typically underlie 'Leveraged Super Senior' trades.
Credit Default Index e.g. 'CDX' or 'iTraxx'	A quoted market index of the Credit Default Swap premiums on one hundred representative corporate credits. The indices are renewed semi-annually; the vintage most relevant to the AB Notes is the CDX Investment Grade Series 7, which was issued in Sep-06. Indices also are quoted in terms of term to maturity – e.g. the CDX IG7 '5 Year' is based on prices for 5-year credit insurance. The CDX indices are comprised of North American companies; the iTraxx indices reference European credits.
Ineligible Asset ('IA') Tracking Notes	Notes created from the restructuring of ABCP assets that had exposure to US subprime mortgage securities. The Ineligible Assets were quarantined from the Pooled Notes and the IA Tracking Notes will directly track the financial performance of the underlying assets on a one-note-per-asset basis.
Leveraged Super-Senior or 'LSS'	A trade of a portfolio of Credit Default Swaps where the seller of the insurance/buyer of the risk receives a small premium in return for insuring the losses on the portfolio only above a certain amount, for example, the insurance might be for any losses above 30%. Thus, 'super senior'. LSS is partially funded in that the seller of insurance posts collateral ('Margin') for only a portion of the total amount of risk insured. In this way, the small premium is levered to provide a higher return on investment.There are many LSS trades underlying the MAV2 Pooled Notes whereby the MAV is the seller of credit insurance on a levered basis.

Margin	A reserve of cash or near-cash securities pledged as collateral to the insurance purchaser (swap counterparty) under an LSS trade. If the portfolio of CDS experiences losses or the market price of the CDS premiums increase, the counterparty may have the right to call for additional collateral to be posted (a 'margin call').
Margin Funding Facility or 'MFF'	A lending facility established by the federal government, Canadian banks, and some international banks to provide Margin funding should the Spread-Loss Triggers be breached. By making this additional collateral available, the MFF reduces the risk that the AB Notes will be terminated early and incur massive losses to investors.
Master Asset Vehicle or 'MAV'	The so-called Master Asset Vehicles are the issuers of the restructured AB Notes. Essentially, they are the legal entities holding the assets and issuing the Notes, receiving income on the assets and paying expenses and interest to the Noteholders. MAV1 is the vehicle for issuing Notes to the self-margin investors (e.g. the Caisse de Depot) and is not relevant to the ABCP LP. MAV2 issues the Pooled Notes and IA Tracking Notes held by the LP. MAV3 is the issuer of the Traditional Asset Tracking Notes.
Net Asset Value or 'NAV'	The value of a security or fund; equal to the market value of assets minus liabilities.
Pooled Notes	AB Notes created from the restructuring of ABCP containing both cash assets (loans, non-US residential mortgage backed securities, commercial mortgage backed-securities, etc.) and Leveraged Super Senior assets. These notes are comprised of classes A-1, A-2, B, and C, in order of seniority. These notes are supported by the Margin Funding Facility.
Spread-Loss Trigger	A 'margin trigger' is the metric by which it is judge whether an AB Note must provide additional collateral. A 'Spread-Loss' trigger provides a limit for a pre-determined CDX index's market price (the 'spread') above which additional margin must be posted (e.g. "if spreads on the CDX IG7 5Year exceed 550 basis points, then the note triggers."). The Spread-Loss Triggers are given within a matrix of the level of losses on the Index and the remaining term to maturity on the note. When the AB Notes were restructured, the triggers where changed from market price triggers to Spread-Loss Triggers and the overall levels of the triggers were raised; this reduces the likelihood of margin calls relative to current market conditions.
Traditional Asset ('TA') Tracking Notes	Notes created from the restructuring of ABCP assets that had exposure ONLY to cash assets (loans, non-US residential mortgage backed securities, commercial mortgage backed-securities, etc.). These notes will directly track the performance of the underlying assets on a one-note-per-asset basis.