April 16, 2012

Russell Research / Ranks and Commentary

CONNOR, CLARK & LUNN INVESTMENT MANAGEMENT LIMITED

PRODUCT: CANADIAN EQUITY Q CORE FUND

ASSET CLASS	GEOGRAPHIC EMPHASIS	CAP TIER	DURATION RANGE
Equity	Canada	Large Cap	-
STYLE	**SUBSTYLE**	**MARKET STATUS**	
Market-Oriented	-	Developed Markets	

ACTIVITY DATE	LOCATION	ACTIVITY TYPE	PURPOSE
28Mar2012	Vancouver, BC, Canada	Research - Manager Office	Product Review

OVERALL EVALUATION

1 2 3 **4**
Hire

We recommend that clients consider this manager for new placements and additional cash flow where appropriate.

Target Excess Return: 100 bp
Target Tracking Error: 250 bp
Time Period: > 4 years
Russell Assigned Benchmark: S&P/TSX COMP

Expected Performance Pattern

The product's market-oriented portfolio structure dictates that it should perform well in a variety of market environments. We expect the product to add at least 100 basis points of value relative to the S&P/TSX Composite Index over rolling four-year periods with associated tracking error of approximately 250 basis points. Modifications to the model should help the portfolio weather extreme environments in Canada better than it has in the past.

Manager Update

Kathleen Baldwin, Kathleen Wylie and Thierry Vallée of Russell Investments met with Martin Gerber, Dion Roseman, Steven Huang, John Flintoff and Maxine Smalley of Connor, Clark and Lunn Investment Management (CC&L) on March 29, 2012 to discuss the Q-Core, Q-Value and Q-Growth products. The majority of the meeting was spent discussing their latest model enhancements associated with their North American cross border research. In March 2012, the quantitative team successfully integrated almost 3000 U.S. stocks into their universe, allowing for improved modeling of industries, improved modeling of market efficiency, increased accuracy and responsiveness as well as an increased product offering (North American portfolios). We will monitor over the next few quarters to see if these improvements have a material impact on the portfolio.

Although their research agenda appeared to be less robust than normal we are still impressed with the completion of their

LOW 1 2 3 4 5 HIGH

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North American cross border research and passion for and dedication to quantitative investing. As a result, we are maintaining the "4-Hire" rank on all three Q-products.

Performance Analysis

Q-Core performed over the short term as we would expect given the market environment in 2011. For the one-year period ending December 31, 2011, CC&L's Q-Core product added 51 basis points over the S&P/TSX Composite Index return of -8.7% and 81 basis points over the peer market-oriented manager return of -9.0%. Strong performance in the second and fourth quarter, along with market-like performance in Q3 kept this fund in the black over a difficult active management environment. Over the longer four-year period ending December 31, 2011, the Q-Core portfolio exceeded the alpha target, generating about 125 basis points of excess return over the Index and roughly 170 basis points against the peer market-oriented manager.

The style-oriented Q-products demonstrated contradicting performance to their peers, but was in line with what we would expect given their performance patterns over time. Differences in performance is mostly driven by their unique portfolio construction process and focus on pure factor investing; these features suggest that both products would be good offsets to other growth and value managers in a multi-manager fund structure. CC&L's Q-Growth product posted strong relative performance versus both the Index and peer growth manager adding approximately 285 and 500 basis points of value, respectively, over the one-year period ending December 31, 2011. In contrary, the Q-Value fund struggled over the year, losing to the benchmark and peer value manager by about 125 and 180 basis points, respectively. Both style-oriented funds performed well over the longer four-year period ending December 31, 2011 against both the Index and their peers. Q-Growth posted a modest four basis point absolute return but added about 75 basis points over the Index and 180 basis points over the peer growth manager. Q-Value returned about 55 basis points in absolute return and outperformed the benchmark and peer value manager by roughly 125 and 5 basis points, respectively.

Investment Staff ① ② ③ ④ ❺

Dion Roseman has been portfolio manager for CC&L's Canadian Equity Q-Products since May 2008 when Bill Tilford resigned from the firm. Chris Archbold is still Dion's back-up; however, they manage the portfolios more as a team than when Bill Tilford was the lead. We are confident that they possess solid quantitative skills.

Martin Gerber, the team leader for the Q-Team, was instrumental in the initial development of the Q-Products and he remains focused on them, which we view positively since we have a high conviction level in his abilities. If Martin were to leave the firm, we would reconsider this rank since we view him as critical to the process. We are monitoring his time allocation to CIO-related duties over the next couple of years as he transitions into that role.

Resources continue to be allocated to the quantitative team, which we view favorably. Steven Huang and Tate Haggins primarily focus on research. Steven leads the day-to-day research effort and we have a positive view of his abilities. The firm added support staff in 2008 and now has four research analysts, four data analysts, four systems analysts, and two traders. We have a high opinion of the quantitative team overall and believe the resources dedicated to the quantitative products are high relative to peers.

Organizational Environment ① ② ③ ❹ ⑤

CC&L is one of the largest domestic investment counselors and firm assets under management were approximately $21.1 billion at December 31, 2011. Firm-level AUM have increased in the last year but remain below the peak of $23.2 billion at

LOW ① ② ③ ④ ⑤ HIGH

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the end of 2007. They continue to have a solid revenue base, the majority of which comes from their institutional business line. CC&L continues to win business in the Q-Products (Canadian and U.S.). We have no concerns about the financial viability of the firm.

There have not been any significant departures in the team since Bill Tilford left in May 2008. There is a reasonably low likelihood of disruptive staff turnover that will impact this product. In general, we view positively the change to internally financed stock ownership from the old scheme where individuals had to secure loans from external sources. This move increased CC&L's ability to attract and retain high-quality younger professionals because the terms of share ownership will be less onerous.

Security Selection ① ② ③ ④ ❺

The Q-Core product's selection methodology is robust and diversified, including measures of Value, Momentum, Profitability, Financial Strength and Stability, and Quality, all of which have proven effective at adding value over time in the Canadian equity market. Over the years, CC&L have continuously improved the model by adding new factors or modifying existing factors and are usually ahead of peer quantitative managers in terms of innovation, which we view positively.

The Q-Core portfolio is market-oriented, with incidental bets against any key factor intentionally avoided. As a result, the portfolio is intended to outperform during periods when either the value or growth investment style is in favor. CC&L has been more forthcoming about their models compared to other quantitative-oriented firms; in Q-Core, the target model exposures are roughly equally-weighted between Momentum and Value, which are the primary sources of alpha; Quality has a lesser weight, which makes sense given the magnitude of the payoff to Quality tends to lag that to Growth and Value factors. They avoid over-fitting the model and we like this intuitive approach to model construction.

Research ① ② ③ ④ ❺

Martin Gerber is responsible for setting the research agenda for the Q-Products (while Dion Roseman and Chris Archbold are the day-to-day Portfolio Managers for the funds); we view this positively since we have a high opinion of Martin. In addition, the team now has two full-time Portfolio Researchers, Steven Huang and Tate Haggins, who are supported by four research analysts and four data analysts. Therefore, we view the level of resources as more than sufficient. We also believe that the quality of research is well above average compared to peers.

Asset Allocation ① ② ③ ④ ⑤

This component is unranked as CC&L's Q-Products are intended to be managed as fully-invested portfolios.

Sell Decision ① ② ③ ❹ ⑤

The product's sell discipline is purely a function of the optimization process and they have been trading on a daily basis since 2006. Furthermore, the purely quantitative focus of this product allows for complete emotional detachment, which allows CC&L an edge in their sell discipline over many fundamentally-focused managers.

Portfolio Construction ① ② ③ ④ ❺

The goal of CC&L's quadratic optimizer is to structure the portfolio to have better-than-market value, momentum and quality characteristics while constraining the portfolio to having market-like risk characteristics (Profitability, Financial Strength and Stability). As a result, CC&L's Q-Core portfolio is not simply a combination of their Q-Value and Q-Growth portfolios. Their portfolio construction methodology is interesting and unique (at least in Canada) because return expectations of individual

LOW ① ② ③ ④ ⑤ HIGH

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stocks are not explicitly considered.

The inclusion of a proprietary sector model to this product allows the portfolio to be overweight sectors that CC&L believes have a high probability of outperforming in the short-term. We are confident that this diversification of excess return drivers is a logical and positive extension of CC&L's processes.

CC&L has built a proprietary factor-based risk model; this new model is much simpler as it includes only six factors and it is also much better at forecasting risk. We view positively that they give as much thought to alpha as they do to risk.

Implementation ① ② ③ ④ ⑤

We believe the small size of CC&L's Q-Team should enable the results of the optimization process to be implemented quickly and efficiently. AUM is not an issue at this time as the total assets in the Canadian Equity Q-Products was $5.6 billion at December 31, 2011 and they estimate capacity of $8.0 billion.

A previous concern we had with CC&L is that they did not optimize and rebalance the portfolio often enough to efficiently capture new information; however, they moved to daily trading in 2006. As well, they continue to focus some of their research on enhancements to portfolio implementation, which we view positively.

LOW ① ② ③ ④ ⑤ HIGH

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Important Legal Information

LOW 1 2 3 4 5 HIGH