

Beutel, Goodman
Investment Manager Review
October 10, 2012

EXECUTIVE SUMMARY

- On October 10, 2012 Martin Bélanger met with the following Beutel, Goodman professionals from 9:30 a.m. to 12:00 p.m. at their Toronto office:
 - Peter Clarke, Managing Director, Client Service
 - Mark Thomson, Managing Director, Canadian Equities
 - Steve Arpin, Portfolio Manager, Canadian Equities
 - Bill Otton, Portfolio Manager, Canadian Equities
 - Pat Palozzi, Portfolio Manager, Canadian Equities
 - James Black, Vice President, Canadian Equities
- Ranked “Retain” by Russell.
- Beutel, Goodman manages 10% of the Diversified Equity Fund and 33 1/3% of the Canadian Equity Fund.
- The UWO Retirement Plans had \$69.2 million with Beutel, Goodman as of September 30, 2012 and annualized investment management fees are 0.21% at that asset level; the Operating & Endowment Fund had \$58.4 million.
- Beutel, Goodman’s investment style is bottom-up, value.
- Beutel, Goodman was hired by Western Retirement Plans on August 28, 2009.
- The Retirement Plans invest in a separately managed account with Beutel, Goodman.
- There have been no changes to Beutel, Goodman’s corporate structure since our last review.
- Peter Clarke, who succeeded William Ashby as President, announced that he would retire in three years.
- The Canadian equity mandate managed by Beutel, Goodman posted a return of 6.43% year-to-date for 2012, outperforming the S&P/TSX Index by 1.05%. Since inception in August 2009 the fund has underperformed the index by 0.70%.
- There have been no changes to key individuals on our portfolio. Mark Thomson is still the lead portfolio manager on the strategy.
- Beutel, Goodman’s investment process has not changed since we’ve hired them.
- Their research process considers environmental, social or governance factors when they present a financial liability.
- The Canadian Large Cap Equity strategy has \$10.4 billion in assets under management and will be closed to new business as of October 31, 2012. This doesn’t impact the Western Retirement Plans as we’re an existing client.
- Beutel, Goodman doesn’t have any major compliance issues. The company, its funds or its personnel are not facing any major litigation, no material issue was raised following their most recent regulatory review, the firm is not aware of any conflict of interest involving its personnel. Overall their compliance processes are adequate.
- The firm has an adequate code of ethics.

- Beutel, Goodman has an adequate business continuity plan.

RECOMMENDATION

- Beutel, Goodman has outperformed its benchmark by 1.05% year-to-date in 2012 but has underperformed by 0.70% annualized since inception in August 2009.
- There have been no changes to their investment process, which is very thorough and disciplined.
- There have been no personnel changes on our mandate.
- The firm doesn't have any compliance issues.
- Given the above and Russell's "Retain" recommendation, I don't recommend making any changes to our relationship with Beutel, Goodman & Company Ltd.

ORGANIZATION

- The firm had \$29 billion in assets under management as of June 30, 2012, including \$10.4 billion in Canadian equities, the strategy the UWO Retirement Plans invest in.
- They are planning to close the strategy to new clients on October 31, 2012.
- Since the beginning of 2012 Beutel, Goodman has gained 18 new accounts, for a total of \$1,543 million. They have lost 4 accounts for \$337 million.
- The UWO Retirement Plans had \$69.2 million with Beutel, Goodman as of September 30, 2010 and the Operating & Endowment Fund had \$58.4 million.
- The firm is 51% owned by 40 Beutel, Goodman employees and 49% by Affiliated Managers Group. Affiliated Managers Group is a global asset management company with equity investments in boutique investment management firms.
- There have been no changes to Beutel, Goodman ownership structure since we hired them in August 2009.
- There have been no changes to the management structure of the firm that Peter Clarke implemented when he took over from William Ashby, the previous President. However, Peter Clarke has announced that he will retire in three years.
- The management committee makes decisions using a simple majority rule.
- Beutel, Goodman had 26 investment professionals as of September 30, 2012.
- Since the beginning of the year the only significant personnel change has been the hiring of Colin Ramkissoon who covers Financials.
- Beutel, Goodman has an adequate business continuity plan. The firm has engaged SS&C Technologies of Mississauga to provide dedicated hosting and business continuity. The disaster recovery centre is located in the Toronto core. They test the plan on an annual basis.

CANADIAN EQUITY MANDATE

	3-Mth	YTD	1-Yr	2-Yr	3-Yr	Since Inception
Beutel, Goodman Cdn Equity	4.42%	6.43%	12.55%	3.95%	5.77%	6.39%
S&P/TSX	7.02%	5.38%	9.17%	2.61%	5.52%	7.09%
<i>Value Added</i>	<i>-2.60%</i>	<i>1.05%</i>	<i>3.38%</i>	<i>1.34%</i>	<i>0.25%</i>	<i>-0.70%</i>

- The target value added for this mandate is 200 bps over 4-year rolling periods.
- The fund has 34 names (as of August 31, 2010); the Fund will typically hold between 30 and 50 stocks.
- Beutel, Goodman outperformed its benchmark by 105 bps since the beginning of 2012, as of September 30, 2012, although they underperformed by 260 bps during the third quarter of 2012.
- The underperformance in the third quarter of 2012 was due to Beutel Goodman's lack of exposure to gold companies and its underweight in the Energy sector.
- Over the first nine months of 2012, sector allocation in Materials, Energy and Consumer Discretionary have added value, while stock selection in Consumer Discretionary and Consumer Staples have detracted. The top three contributors to performance year-to-date are TD Bank, Royal Bank and Agrium. The top three detractors have been Inmet Mining, Baytex Energy and Canadian Natural Resources.
- Portfolio turnover is typically 20% to 30%.
- Their portfolio positioning is currently as follows:
 - Remain fully invested, cash targeted at less than 2%.
 - Invest in companies with strong free cash flows and high dividend yield.
 - Maintain exposure to improving North American economy through high quality financials, railways, infrastructure auto parts, retailers and information technology stocks.
 - They are focused on resource opportunities valued on fundamentals rather than investment demand.
 - No exposure to large cap gold stocks.
 - The portfolio's dividend yield of 2.9% is near market yield of 3.0% despite a lack of exposure to utilities and REITs.
 - They have recently added new positions in SNC-Lavalin and Open Text.
 - SNC has a wide offering of products and services, they have competitive advantages and a significant concession portfolio.
 - They have sold out of Altagas.
 - They have added to their position in Canadian Natural Resources, Potash, Agrium, Scotiabank and Onex, while they have trimmed their exposure to Baytex, CN, Canadian Pacific, Finning, Metro, Molson Coors and Shoppers Drug Mart.

- They like the dynamics of the Telecommunication industry. It is a controlled market with a limited number of players.

Investment Personnel

- There have been no changes to the lead portfolio manager on our strategy.
- Mark Thomson, Managing Director, Canadian Equities is still the lead portfolio manager; he's supported by 4 portfolio managers / equity analysts on the Canadian equity team.
- All stocks are covered by their global research platform, except Canadian financials which are covered from a Canadian point of view only.
- We reviewed the investment thesis for Research in Motion with James Black and SNC-Lavalin with Pat Palozzi. They both demonstrated good insights in their analyses.
- Portfolio managers / analysts must prepare a detailed research on each of their investment ideas. The reported is vetted by Mark Thomson and another team member and then presented to the entire team for debate.

Investment Process

- Process hasn't changed: bottom-up value.
- Beutel Goodman uses a bottom-up value process to select securities. Its philosophy is based on four principles:
 - Preservation of capital is paramount.
 - Business value is determined by the present value of sustainable free cash flow; they define free cash flow as: Net Earnings + Depreciation + Amortization – Maintenance Capital Expenditures.
 - Low valuations outperform high valuations.
 - Purchase of companies below business value.
- Beutel Goodman focuses on a firm's ability to create long-term shareholder value through free cash flow generation. They believe that long-term shareholder value is created by: management skill, competitive advantage, strategic positioning, industry structure, profitability and financial strength.
- For non-cyclical companies they require a 33% discount to intrinsic value in order to purchase the stock. For cyclical companies, the discount must be at least 50%. Furthermore, they believe that a company's ability to generate free cash flow provides the following benefits: independence, financial flexibility, ability to make acquisitions, organic growth, capacity to repurchase shares, capability to pay dividends. They estimate value three years into the future using a discounted cash flow model.
- For non-cyclical companies, their sell discipline involves selling 1/3 of their position when their target price is reached. They then review the business value through additional research. If the business value has increased, they hold on to their position, otherwise they sell the remainder of their position. For cyclical companies, they also sell 1/3 of their position when their target price is reached, but they will sell the rest of their position when the stock price reaches the peak historical multiple.

- They will also sell for the following reasons: change in senior management or corporate strategy, major asset acquisition or disposal, material increase in financial leverage or the business value becomes impossible to determine.
- Environmental, Social and Governance Factors (ESG):
 - Any potential liability, such as an environmental issue, is taken into consideration when they analyze a company.
 - They include a margin of safety when they value a stock.
 - They focus on companies with management that is a good steward of capital.
 - Issues are industry specific. For example, railroads have made major investments to improve safety.
 - They manage a fund for The Ethical Fund Company and very few companies are screened out of their universe, which indicates that their process tends to select companies with strong ESG characteristics.
- The size of an active position is based on the following considerations:
 - The minimum position size is 1%.
 - The position size is based on liquidity and the market capitalization of a company is a good proxy for liquidity.
 - The conviction in the stock will also influence the size of the position.

Risk Management

- Beutel Goodman controls portfolio risk by doing a thorough analysis of each stock.
- Risk control guidelines are broad; there's no minimum for any sector and the maximum is equal to the S&P/TSX weight plus 10%.
- The minimum number of stocks is 30 and the maximum per stock is 10%.

Capacity

- They currently manage \$10.4 billion in Canadian equity mandates.
- They feel that they can handle about \$11 billion in Canadian equities. As a result, they will close the Canadian Equity Large Cap strategy on October 31, 2012.
- They feel at above 1% of total market capitalization it becomes harder for a portfolio to add value.

COMPLIANCE

- Compliance was reviewed with Peter Clarke.
- Michael Gibson, Managing Director of Operations is the Chief Compliance Officer; he is assisted by Cynthia Rogers, the firm's legal counsel.
- We reviewed some of Beutel, Goodman's compliance processes. They have recently implemented a pre-trade compliance process.
- The Ontario Securities Commission did an audit of Beutel, Goodman's pooled funds in the spring of 2012. The OSC had no issues to report.
- Beutel, Goodman, its funds or its personnel are not facing any other litigation.
- No material issue was raised following their most recent regulatory review.

- Beutel, Goodman is not aware of any conflict of interest involving its personnel.
- The firm has an adequate code of ethics.
- Everyone has to pre-clear personal transactions.
- The funds managed on behalf of UWO are in compliance with the letter of appointment dated August 18, 2009.
- Ernst & Young does an audit of Beutel, Goodman's process, but they don't produce a Section 5970 Report.
- Ernst & Young is also the firm's auditor.
- Overall Beutel, Goodman has adequate compliance processes in place.

**THE UNIVERSITY OF WESTERN ONTARIO
RETIREMENT PLANS and OPERATING & ENDOWMENT FUND
Beutel, Goodman & Company Ltd.
Meeting Agenda**

Date: October 10, 2012

Meeting time: 9:30 AM to 12:00 PM

Location: 20, Eglinton Ave West, Suite 2000, Toronto, Ontario

UWO Attendee:

Martin Bélanger, Director, Investments

ORGANIZATION (15 min):

- Introduction – relationship review
- Discuss any meaningful change to your corporate structure since the last review
- Overview of new products and future plans for the firm
- Review changes in assets under management
- Discuss clients gained and lost
- Overview of your business continuity plan

INVESTMENT PERSONNEL (10 min):

- Introduction to key personnel on our mandates
- Discuss personnel turnover

REVIEW OF UWO PORTFOLIOS (Retirement Plans and Operating & Endowment Fund) (75 min):

- Overview of investment process and changes to investment philosophy, if any; please provide examples of stocks added that meet your investment criteria
- Performance overview
- Attribution analysis (sector and security selection effects)
- Detractors/contributors to performance (individual stocks)
- Portfolio characteristics
- Discuss changes made to the portfolios
- Discuss current portfolio positioning
- Describe how you measure and control portfolio investment risk
- Address how you handle capacity issues
- Report how you integrate environmental, social and governance factors in your investment process and the impact on your portfolio and investment strategy

INVESTMENT RESEARCH (30 min):

- Review global research platform
- Review approach to research
- Discuss research reports with portfolio managers/analysts

COMPLIANCE (15 min):

- Provide an overview of your compliance processes
- Confirm that all investments managed by Beutel, Goodman & Company on behalf of UWO are in compliance with the terms and conditions of the Letter of Appointment and the Investment Manager Mandate and Performance Standards and in compliance with all applicable laws
- Describe any material litigation to which your firm, key personnel or the funds have been party over the past year
- Describe any material issue raised as a result of recent regulatory reviews
- Confirm that your key investment personnel complies with an appropriate code of ethics
- Confirm that any conflict of interest or potential conflict of interest involving Beutel, Goodman & Company or key investment personnel has been disclosed

OTHER (5 min):

- Office tour