MAWER
newsletter

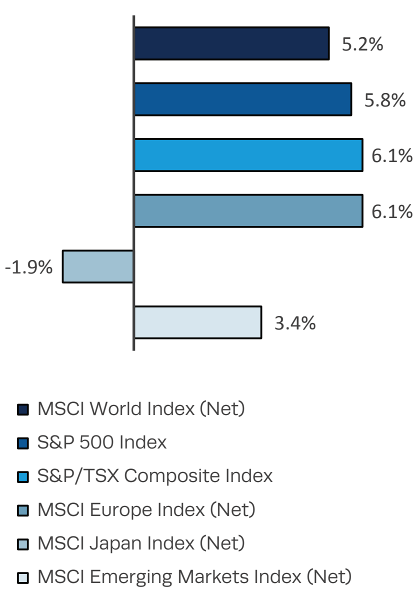
First Quarter 2014

Market Overview

Global equity markets continued to rise during the first three months of 2014. This extends their rally to five years, with only periodic interruptions. One such interruption occurred when the political standoff between Russia and Ukraine prompted some investors to assess the implications of Russia's aggression from the sidelines. The ensuing equity correction was relatively modest and short-lived, as global equity markets soon resumed their upward trajectory, with the MSCI World Index (C$) finishing the quarter with a 5.2% gain.

Unlike previous quarters, Canadian equity markets were among the frontrunners, as illustrated in Chart A. Canada's rise was fuelled by significant gains by resource companies, particularly early in the quarter. Chart A also shows the strong quarterly results achieved by equity markets in the U.S. and Europe, although it should be noted that the depreciation of the Canadian dollar relative to most major world currencies had a significant influence on the magnitude of these returns. For example, though the S&P 500 Index (C$) reported a 5.8% return, the gain in U.S. dollars was a healthy, but less pronounced rise of 1.8%.

Chart A
Q1 2014 Equity Index Performance (in C$)

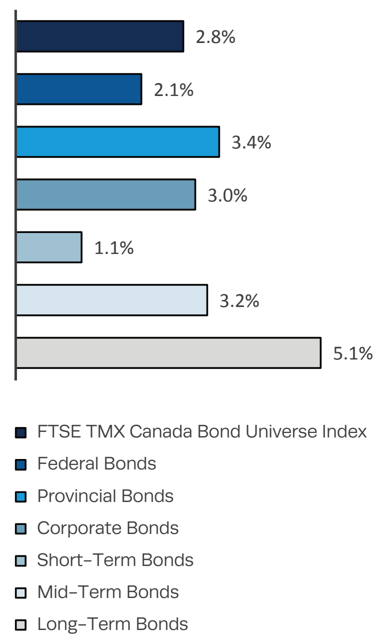


The most notable exception to the strength in global equity markets was Japan, where the MSCI Japan Index (C$) shed 1.9%. Japanese authorities have undertaken unprecedented measures to revive their economy, but an imminent hike in the sales tax, from 5% to 8%, has renewed concerns that consumption and economic growth may stagnate. Incredibly, the annualized return over the last 25 years in the MSCI Japan Index (C$) is −1.0%; a painful reminder of how unkind Japan has been to investors.

Emerging market equities once again failed to keep pace with their developed peers. The standoff in Crimea and the political turmoil and social unrest in Thailand sparked steep corrections in their respective equity markets. Meanwhile, the Chinese stock market yet again posted negative returns. Some of this underperformance among emerging market equities may be attributed to the unwinding of the carry-trade, where investors borrowed U.S. funds at low rates and redeployed this capital into higher-growth emerging markets. With the U.S. Federal Reserve continuing their exit strategy with respect to economic stimulus, and newly-appointed Fed Chairman Janet Yellen speaking openly about the timeframe to increase interest rates, the attractiveness of this carry-trade is diminishing. This may explain the sizeable flow of funds out of emerging markets and back into U.S. dollars, which has put some emerging market currencies under pressure, and seemingly their equity markets as well.

While this quarter was rewarding for equity investors, Canadian fixed income markets also delivered healthy returns with the FTSE TMX Canada Bond Universe Index gaining 2.8%. This was a welcome reprieve for fixed income investors that suffered a 1.2% decline during 2013, the first annual decline since 1999. As Chart B illustrates, performance among provincial and corporate bonds was noticeably higher than the federal sector, while mid-term and long-term securities performed particularly well:

Chart B
Q1 2014 Canadian Fixed Income Returns

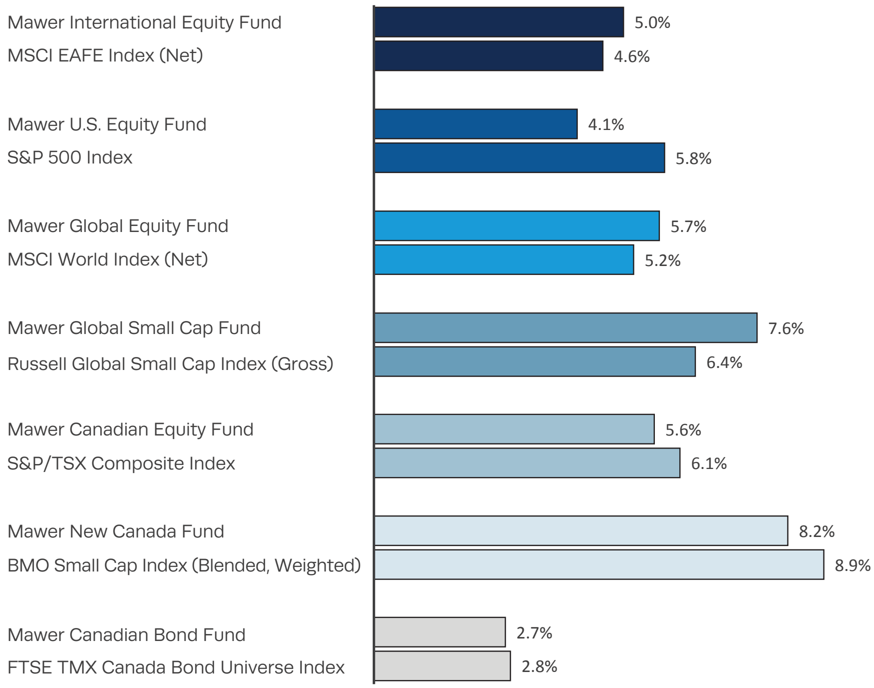


The magnitude of these gains is somewhat surprising given the muted outlook many investors held for fixed income. With the Federal Reserve gradually tapering, or reducing their monthly bond-buying program, many assumed that their waning influence would put considerable downward pressure on bond prices, and therefore, fixed income returns. But it seems that other market participants have stepped to the forefront to replace the diminishing presence of the Fed. In Canada, we've observed a healthy demand for new bond issues, further highlighting that fixed income has its place even at current yields. While investors should not expect gains of this magnitude to be a regular occurrence, it is a welcome reward for those that had the discipline to remain committed to this asset class.

Mawer Performance Overview

Mawer earned positive returns in each asset class this quarter, and subsequently our Balanced Fund delivered a quarterly return (net of fees) of 4.3%. Chart C highlights the quarterly performance (net of fees) of various Mawer Funds relative to their benchmarks.

Chart C
Q1 2014 Fund Performance relative to Index (in C$)



As Chart C depicts, most of our funds performed within a narrow range of their respective benchmarks. Generally speaking, many of the investments that lagged during 2013 enjoyed a reversal of fortune in the opening quarter of 2014. As an example, the Energy and Materials sectors were laggards during much of 2013, and our underweight position in these sectors, both in our Canadian Equity Fund and New Canada Fund, was a contributing factor to their outperformance. But in the opening quarter of 2014, these were two of the strongest performing sectors within the S&P/TSX Composite Index and BMO Small Cap Index. Fortunately, we had strong security selection within our Canadian equity portfolios to help offset the sector positioning, and this kept both the Canadian Equity Fund and New Canada Fund within striking distance of their respective benchmarks.

Our Global Equity, Global Small Cap Equity, and International Equity Funds modestly outperformed their respective benchmarks this quarter. Each of these Funds is significantly underweight Japanese equities, which helped our relative performance as Japan lagged considerably during the quarter. That said, the strong performance by companies we have limited exposure to, such as those in Italy, Spain, Portugal, and some of the other peripheral countries in Europe, worked against us. Strong security selection also played a role in our modest outperformance. Our Global Small Cap Fund, in particular, had some considerably high performers within the Industrials sector, which represents the largest sector within the Fund.

Among the asset classes noted in Chart C, the U.S. Equity Fund experienced the most significant divergence from its benchmark, posting gains of 4.1% relative to the 5.8% gain in the S&P 500 Index (C$). Our underweight position in the top-performing Utilities and Health Care sectors worked to our detriment this quarter. Our security selection within the Consumer Staples and Consumer Discretionary sectors was strong, with drug store chain Walgreen's returning approximately 20.0% this quarter and Autozone, a leading retailer and distributor of auto parts and accessories, rising approximately 16.7%. Unfortunately security selection within a number of other sectors was weaker relative to the S&P 500 Index. As an example, Exxon Mobil and Chevron returned just 1.0% and -0.2% respectively this quarter, while the overall Energy sector was up 4.7%. We observed that smaller or mid-cap companies generally outperformed their larger peers, which hampered our relative performance given our current bias to larger global companies.

The Canadian Bond Fund posted results in line with its benchmark. Overall, the allocation among Federal and Corporate sectors, combined with our security selection within these sectors, worked in the portfolio's favour this quarter. Our overweight position in the top-performing Real Estate and Infrastructure sub-sectors was particularly beneficial. The largest detractor from our relative performance was an underweight position in long-term bonds which outperformed shorter-term and mid-term bonds by a noticeable margin.

From an asset allocation perspective, we have maintained an overweight position in equities and corresponding underweight position in fixed income within our Balanced Fund. Given that each of our equity funds outperformed our bond fund this quarter, this positioning proved to be favourable. That said, our larger cash equivalent weighting and lower allocation to bonds detracted from returns, given the differential between bond returns and cash. And although our decision to de-emphasize Canadian equities and instead build greater allocations to U.S. and International equities has added considerable value in recent years, this quarter, with Canadian equities rebounding to outperform much of the world, the positioning worked against us. Fortunately, the absolute variance between the returns of our equity funds was rather narrow this quarter, indicating that our decision to overweight equities had a more significant impact to overall returns than our regional emphasis.

During the quarter, we adjusted our asset allocation strategy by reducing our exposure to smaller cap equities, both in Canada and abroad, and redeployed this capital to larger global peers. Our overweight position in equities and underweight position in fixed income remains intact.

Valuation Risk

Last quarter we wrote about the risk of speculative behavior contributing to a bubble in asset prices, including the potential of excessive equity valuations. With a rally in global equity markets to start 2014, we acknowledge that this valuation risk persists. The tools we described last quarter to combat this risk remain in place today and we continue to actively reposition our portfolios to allocate capital from companies that appear more fully valued to companies that appear more reasonably priced.

For example, Vodafone, the UK-based telecommunications leader, was a long-time holding within our International Equity mandates. The stock has appreciated significantly in recent quarters, fuelled in part by a deal formed with Verizon Communications as well as speculation of a possible takeover by AT&T. Despite being a well-run company with enduring competitive advantages, we no longer believed that Vodafone was trading at an attractive valuation, especially compared to other investment opportunities within the International equity universe. As such, we reduced our investment in Vodafone on numerous occasions during the quarter and redeployed the capital to a variety of businesses that appear more favourably valued, such as Samsung, BMW, Aberdeen (a UK-based asset management company), and Intertek (a UK-based firm providing safety inspection and testing services to customers around the world). This is just one example among many where we have proactively reduced valuation risk and enhanced resiliency within our portfolios.

Looking Ahead

Global economic expansion appears intact, and despite fears that aggressive monetary intervention in recent years might be the catalyst for higher inflation, we're observing benign inflation data, at least throughout the developed world. Deflation is likely a greater risk, with Europe's precarious recovery ever-so-dependent on the health of consumer spending in the emerging world. Despite this, Europe appears to have moved past their sovereign debt crisis. Not long ago, some circles spoke of the dissolution of the European Union. Today, yields on sovereign debt in countries such as Italy, Spain, Portugal, and Ireland are at multi-year lows; an indication of the rising confidence in the Eurozone. Japan continues to tackle structural challenges, but market participants seem to have grown accustomed to their slow progress. We will continue to watch the standoff in Crimea, but at this stage, the impact to our portfolios appears relatively insignificant. In all likelihood, this too shall pass.

We believe China presents a more serious concern, not because we have invested heavily in Chinese companies, but because most of the businesses we own rely in some part on the health of the Chinese economy. If the economic slowdown in China is worse than many expect, it will likely place substantial strain on the global economy, and especially among other emerging economies. Authorities in China face significant challenges as they transition to a slower-growth economy that is focused less on capital intensive export industries and more on domestic consumption. And while there are also potential societal strains as they urbanize on a massive scale, the tension to the financial system presents the greatest worry and the most systematic risk to the global economy. How many bad loans reside on lenders' balance sheets? How much resolve do authorities have to rescue or bail out troubled institutions?

The macro-economic themes noted above are popular topics in our discussions with clients. Ironically, we spend very little time analyzing such subjects. Not because we don't believe these issues matter, but because we don't believe we can answer any of these questions with certainty. Rather than focus on macro themes, we dedicate the vast majority of our time and effort on better understanding the individual companies used to build our portfolios. Research trips represent one way to effectively increase this understanding, and Paul Moroz, Deputy CIO, Portfolio Manager, recently completed one such trip to Thailand. As Paul's departure date in January neared, the political situation in Thailand began to rapidly deteriorate – the acting Prime Minister had passed a controversial bill that led to the dissolution of Parliament, prompting a plethora of political protests. Street demonstrators planned to effectively shut down Bangkok, right in the midst of his scheduled visit. Paul contemplated cancelling the trip, but after gaining assurance that his personal safety would not be at great risk, he went ahead as scheduled. Some readers might assume that the focus of the trip was to gain a better understanding of the political situation and how it might impact the investment outlook for Thailand. Indeed, what better opportunity to speak with economists and political strategists to gain insight about how events may unfold, than to be on the ground in the midst of political upheaval?

Instead, our objective was quite the opposite. Improving our understanding of the political nuances within Thailand had its value, but our primary goal was to search for investment opportunities amidst the uncertainty. Rather than focus on the current political drama, we were in Thailand to visit a number of different companies—both companies representing new opportunities and those that we own within our portfolios. In-person company visits can provide valuable insight into their operations, competitive advantages, and perhaps most importantly, the mindset of the management teams. So while much of the world was glued to the political uncertainty unfolding in Thailand, we skirted around the drama to visit with businesses like Bangkok Aviation Fuel Services, which provides critical fuel services to Thailand's busy airports, and Minor International, which operates various restaurants, hotels, and vacation properties in Thailand.

Although we returned from Thailand with a better understanding of the macro-economic backdrop and political climate of the country, the insight we gained from face-to-face visits with numerous businesses was far more valuable. Visiting a company's operations, touring their facilities, and speaking with managers, competitors, and customers is the informational advantage that we seek. We believe these insights lead to better portfolio decisions. While it may be more exciting to speculate on how macro-economic events will unfold, our focus remains at the micro-level.

Mawer Investment Management

Total Net Returns

For periods ending March 31, 2014†

	3-Mo	YTD	1-Yr	2-Yr	3-Yr	4-Yr	5-Yr	10-Yr
Equity Funds								
Mawer International Equity Fund	**5.0**	**5.0**	**21.4**	**18.3**	**11.7**	**11.9**	**15.7**	**7.5**
MSCI EAFE Index (Net)	4.6	4.6	27.7	20.2	11.8	10.3	13.0	4.7
Mawer U.S. Equity Fund	**4.1**	**4.1**	**30.8**	**23.3**	**19.5**	**16.1**	**15.1**	**4.9**
S&P 500 Index	5.8	5.8	32.6	24.0	19.7	17.4	18.0	5.6
Mawer Global Equity Fund	**5.7**	**5.7**	**30.6**	**23.1**	**17.7**	**16.5**	**–**	**–**
MSCI World Index (Net)	5.2	5.2	29.4	21.3	15.0	13.4	15.2	5.0
Mawer Global Small Cap Fund	**7.6**	**7.6**	**48.3**	**35.6**	**25.7**	**24.5**	**29.0**	**–**
Russell Global Small Cap Index (Gross)	6.4	6.4	28.3	21.4	12.9	14.1	18.9	7.1
Mawer Canadian Equity Fund	**5.6**	**5.6**	**23.9**	**19.2**	**11.8**	**13.9**	**18.6**	**10.6**
S&P/TSX Composite Index	6.1	6.1	16.0	10.9	3.6	7.5	13.7	8.1
Mawer New Canada Fund	**8.2**	**8.2**	**49.4**	**32.2**	**20.5**	**22.3**	**30.4**	**15.2**
BMO Small Cap Index (Blended, Weighted)	8.9	8.9	15.9	5.7	–0.2	7.4	19.8	7.2
Balanced Funds								
Mawer Global Balanced Fund*	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
Internal Global Balanced Benchmark**	4.1	4.1	17.2	13.5	10.8	9.9	11.0	5.1
Mawer Balanced Fund	**4.3**	**4.3**	**18.8**	**15.4**	**11.8**	**11.8**	**13.6**	**7.9**
Internal Balanced Benchmark ***	4.6	4.6	14.6	11.1	8.7	9.0	10.9	6.4
Mawer Tax Effective Balanced Fund	**4.4**	**4.4**	**18.8**	**15.3**	**11.7**	**11.8**	**13.8**	**7.7**
Internal Tax Effective Balanced Benchmark***	4.6	4.6	14.6	11.1	8.6	8.8	10.8	6.3
Income Funds								
Mawer Canadian Bond Fund	**2.7**	**2.7**	**–0.1**	**1.9**	**4.4**	**4.4**	**4.3**	**4.3**
FTSE TMX Canada Universe Bond Index	2.8	2.8	0.8	2.7	5.0	5.0	5.0	5.1
Mawer Canadian Money Market Fund	**0.1**	**0.1**	**0.4**	**0.4**	**0.3**	**0.3**	**0.2**	**1.3**
FTSE TMX 91 Day T-Bill Index	0.2	0.2	1.0	1.0	1.0	0.9	0.8	2.0

† Mawer Fund returns are calculated after management fees and operating expenses have been deducted. In comparison, Index returns do not incur management fees or operating expenses.

* Due to regulatory restrictions, we are unable to report performance of the Fund during its first year. The Mawer Global Balanced Fund was launched July 2, 2013.

** 5% FTSE TMX 91 Day T-Bills Index, 35% FTSE TMX Canada Universe Bond Index, 60% MSCI World Index (Net)

*** 5% FTSE TMX 91 Day T-Bills Index, 35% FTSE TMX Canada Universe Bond Index, 15% S&P/TSX Composite Index, 15% S&P 500 Index, 15% MSCI EAFE Index (Net), 7.5% BMO Small Cap Index (Blended, Weighted) and 7.5% Russell Global Small Cap Index (Gross)

Mutual funds are not guaranteed, their values change frequently, and past performance is not indicative of future performance. Commissions, trailing commissions, management fees and expenses all may be associated with mutual fund investments. (Money market fund: Mutual fund securities are not covered by the Canada Deposit Insurance Corporation or by any other government deposit insurer. There can be no assurances that the fund will be able to maintain its net asset value per share at a constant amount or that the full amount of your investment in the fund will be returned to you.) Please read the prospectus before investing.

Performance returns for the Mawer Mutual Funds are calculated by Mawer Investment Management Ltd. These returns are historical simple returns for the 3 month, YTD and 1 year periods, and annualized compounded total returns for periods after 1 year. They include changes in unit value and reinvestment of all distributions and do not take into account sales, redemption, distribution or optional charges or income taxes payable by any securityholder that would have reduced returns.

MAWER
Calgary • Toronto

t 403 262 4673
800 889 6248
e info@mawer.com
w mawer.com