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Buy fund companies for RRSP investments

By Shirley Won
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Gluskin, CI Financial, AGF and DundeeWealth figure in analysts' top picks

As RRSP contribution season kicks into high gear, Canadians might find some mutual fund company stocks offer more sizzle than many of the investments they sell.

January through March are key months for registered retirement savings plan sales, and can help fuel the returns of asset management companies. But industry observers suggest that some firms are better bets than others.

"You have to be selective," M Partners analyst Scott Chan says. "We estimate that the 2010 RRSP season will rebound strongly to about \$7-billion to \$8-billion in net sales from \$3.5-billion last year. That's over 100-per-cent growth, but is still less than previous RRSP seasons going back to 2004."

Over the past 10 years, the average return of shares in Canadian asset managers outpaced the S&P/TSX total return index seven times during March and eight times in April, Mr. Chan noted.

This may stem from the fact that investors wait until final sales data are released, and from analysts upgrading stocks if the numbers exceed expectations, he suggested.

This year will be a better year for fund companies because - on top of money coming in - it will come in through higher-margin equity funds. Robert Almeida, Portland Investment Counsel Inc.

Mr. Chan, who covers smaller asset managers, said that his favourite pick is Gluskin Sheff + Associates Inc. GS-T, which targets high-net worth investors. His one-year target is \$28.

"I think a franchise like Gluskin is going to surprise on the upside during RRSP season ... and you are going to get a lot more sales because of the David Rosenberg [<http://www.theglobeandmail.com/news/opinions/columnists/david-rosenberg>]effect," he said, referring to the hiring last year of the high-profile economist as its chief strategist. "And he has also been marketing to U.S. clients too."

Gluskin + Sheff also has seen strong net sales growth over the past year through a variety of investment strategies, has a clean balance sheet with no debt and trades at a significant discount to its closest peer Sprott Inc., he added.

Robert Almeida, a portfolio manager at Portland Investment Counsel Inc., said he also believes it is a good time to selectively buy fund company stocks, but suggested the sales push from RRSP season is just one of the reasons.

"Through the economic crisis, individuals have become more acutely aware of the need to save money and this should help drive sales" during the first three months, said Mr. Almeida, who co-manages the Manulife AIC Advantage Fund with its strong focus on asset managers.

CI Financial has got some of the best fundamentals in the group. It has a nice dividend yield, is typically a sales leader in the space and could be a potential takeover target by Scotiabank. Genuity Capital analyst Gabriel Dechaine

But fund company revenues are also driven by asset growth stemming from a market recovery, and more cash flowing into higher-margin, long-term mutual funds from money market funds, he said.

"This year will be a better year for fund companies because - on top of money coming in - it will come in through higher-margin equity funds," he predicted.

"Confidence is returning for investors, and interest rates are incredibly low. You can tolerate 2-per-cent returns when everything else is going down."

DundeeWealth Inc. DW-T and AGF Management Ltd. AGF.B-T should benefit because they have the highest exposure to equities among the larger firms, while DundeeWealth also has strong sales growth, he said.

"But DundeeWealth's share price has gone up more than AGF, while AGF trades at a deeper discount [versus its peers]," he said. "We think AGF may be the better buy. But DundeeWealth, just looking at the sales, is probably the best positioned to get a lift from the RRSP season."

Genuity Capital analyst Gabriel Dechaine, meanwhile, said he doesn't look at RRSP season in isolation as a reason to buy fund company stocks, but agreed the RRSP season will amplify trends in the industry.

"I think buying fund company stocks should be part of a longer-term strategy where you see positive equity markets, a gradual return to long-term investing in the retail mutual fund space versus money market funds and attractive dividends," he said. "The larger fund companies are all paying fairly attractive dividends..."

"I have a buy rating on CI Financial CIX-T, with a one-year target of \$25, and AGF, with a target of \$19," Mr. Dechaine said. "CI Financial has got some of the best fundamentals in the group. It has a nice dividend yield, is typically a sales leader in the space and could be a potential takeover target by Scotiabank."

"I like AGF because it has a nice dividend. It is the cheapest in the group terms of EV/EBITDA [enterprise value/earnings before interest, taxes, depreciation and amortization], while its issues with AGF Trust are moderating."

The whole movement by investors coming off the sidelines after last year's sharp market downturn is still in the early stages," Mr. Dechaine suggested. "Net sales in the industry have turned around, but it is still mostly in fixed-income and balanced funds."

"The real question is when equity funds are going to turn around from net redemptions. They may turn around in RRSP season, but I don't anticipate it just yet although you will see some improvement."

Fund performance

A historical view

Total net sales of mutual funds in RRSP season.

Year	Net sales excluding reinvested distributions				YoY Growth
	January	February	March	Q1 Total	
2004	1,875.4	5,555.6	4,275.8	11,706.9	n/a
2005	546.7	6,432.4	4,032.0	11,011.1	-5.9%
2006	1,715.2	6,922.0	4,440.0	13,077.3	18.8%
2007	4,046.0	7,996.7	5,388.0	17,430.7	33.3%
2008	354.5	6,233.0	3,016.0	9,603.6	-44.9%
2009	1,073.6	1,893.2	542.0	3,508.8	-63.5%
Average Last 5 Years (2005-2009)	1,547.2	5,895.5	3,483.6	10,926.3	

Sources: Investment Funds Institute of Canada, M Partners and companies. Includes CI Financial. Excludes Sprott, Gluskin Sheff & Associates and Guardian Capital

Snapshot of Canadian fund companies

Company	Symbol	Price		52-wk		Yield (%)	P/E Ratio	Market cap (\$millions)
		high	low	high	low			
Sprott Inc.	SII-T	4.82	5.10	2.95	2.1	18.5	750.0	
IGM Financial	IGM-T	41.85	45.43	24.20	4.8	21.2	11,110.8	
AGF Mgmt	AGF.B-T	16.98	17.90	6.74	5.9	45.8	1,507.7	
CI Financial	CIX-T	21.00	22.30	10.60	3.5	34	6,155.5	
DundeeWealth	DW-T	14.39	14.44	4.20	1	0	2,119.0	
Guardian Capital	GCG-T	7.90	9.97	4.30	1.8	40.5	280.0	
Gluskin Sheff	GS-T	20.74	22.50	7.49	2.4	28.8	605.9	

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