



2011 First-Quarter Portfolio Manager's Commentary

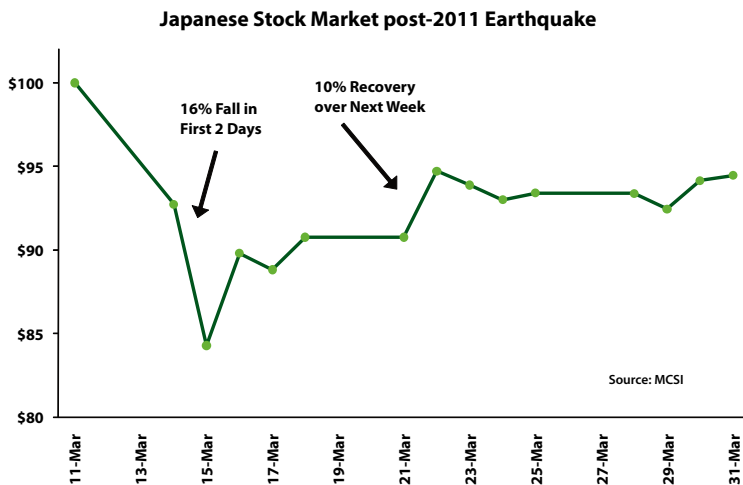
March 31, 2011

Some of the most important events of the first quarter took place outside the economic and financial arena, or at least on its periphery. The near-spontaneous eruption of democracy movements across the Middle East held out promise for tens of millions of people, but also peril for those whose governments did not heed the call for change.

This quarter also bore witness to a horrible natural disaster in Japan as an earthquake followed by a tsunami wiped out entire towns and killed over 10,000 people, with another 15,000 still missing. At this time the damaged nuclear plants in the affected region seem to be under control but even so, that a natural disaster of this magnitude can occur in one of the world's most technologically advanced countries reminds us that some of life's risks cannot be eliminated, but only managed in an attempt to minimize their damage.

Our view is that the disaster, horrible as it was in human terms, will have a negligible effect on the global economy. Japan is a huge nation of about 130 million people and the 3rd-largest economy in the world. As with every disaster since humanity's beginnings, the survivors will begin the task of rebuilding and getting on with their lives. Resources that would have otherwise been used for other purposes will instead be dedicated to the rebuilding, but the disaster will present no major interruption for the workings of the world economy.

This staid approach to the situation was not on the minds of investors in the days following the disaster. As shown below, the Japanese stock market sold off nearly 16% in the first two days but recovered two-thirds of the loss over the next week. An investor who caught the jitters and sold any time after the first day would have lost money by doing so, a cautionary tale about the dangers of short-term market-timing.

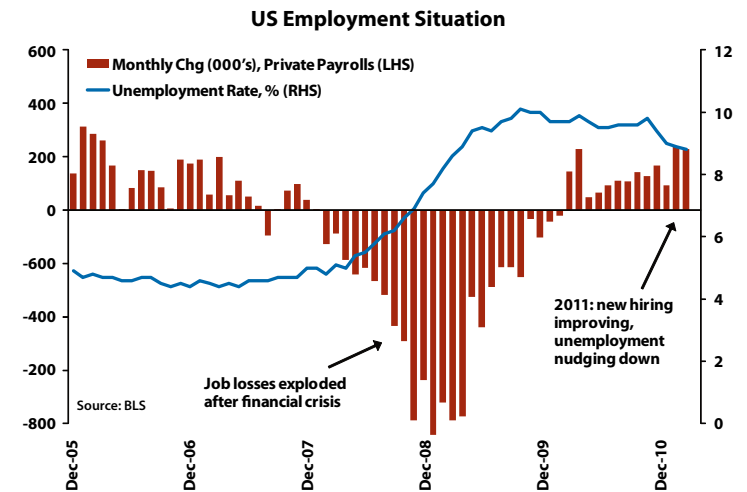


The Economy

The US economy continued to recover from the recession. Some of the good news stories from the quarter include:

- Fourth-quarter 2010 economic growth (reported in the first quarter of 2011) was a healthy 2.8% on an annualized basis
- Mortgage delinquencies continued to decline, albeit from a record-high level that reflected the reckless lending practices undertaken during the housing bubble. Bank loan losses continued to fall and bank net income was consistently positive all through 2010, which should continue to spur lending – of hopefully a more prudent nature this time around!
- Corporate profits continued to rise for non-financial companies as well. Excluding financial companies, the earnings of the S&P 500 index of large US companies are now back at their pre-recession peaks.

Perhaps most important is that the US job growth finally began to gain traction this quarter. As shown below, the unemployment rate dipped nearly 1% in the first quarter and in both February and March, over 200,000 new private sector jobs were created. While this remains slightly below the "ideal" amount of 300,000 or more new jobs each month, it is ample to start meaningfully reducing the unemployment created by the 2008 financial crisis. Moreover, the effect on the economy of an improving labor situation cannot be understated, as the uplift in moods creates its own self-reinforcing virtuous cycle.





Your Portfolio

The Compass portfolios rose between 1.5% to 4.5% in the first quarter, depending on the portfolio. Within the more conservative portfolios, government bonds lost about a half-percent as long-term interest rates rose somewhat and the resulting capital loss more than offset their interest income. The dedicated corporate bond portion of the portfolios fared better but were still flat for the quarter.

The portfolios' equity positions powered their performance. Canadian and US stocks rose about 5% in local-currency terms and while the US dollar lost some ground against the Loonie, some of this loss was mitigated by the partial currency hedge Compass uses for its US-dollar denominated investments. Overseas stock markets rose only 1% for the quarter that largely reflected the impact of Japan's 6% decline, as the other main overseas markets were more positive. Real Estate Investment Trusts (REITs), a staple of the Compass portfolios, generated returns of nearly 15% as well and provided a significant boost to the portfolios' performance.

Conclusion

The first quarter of 2011 was ultimately a good one for the Compass portfolios, but the quarter's events also provide a timely reminder of diversification's benefits. The timing and location of political upheaval, natural disasters and technological breakthroughs cannot be accurately predicted. Each may have a disproportionate impact on any one investment, but by having your investment "eggs" spread across different baskets the overall risk becomes negligible – a very desirable outcome in a world characterized by uncertainty.

Sincerely,

Sheldon Dyck

Chief Investment Officer

ATB Investment Management Inc.

Rather watch and listen?

Video of the portfolio manager's commentary is now available on-line every quarter. Find it at atb.com.

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