

AGF MANAGEMENT LIMITED

(TSX: AGF.B)

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eResearch Corporation is pleased to provide a **Catalyst** report on:
AGF MANAGEMENT LIMITED.

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Managing Director, Research Services, **eResearch Corporation**

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(AGF.B – TSX \$19.60)

Recommendation: HOLD
Target Price (1 Year): C\$20.00
Prior: C\$19.00
Total Return (1 Year): 7.3%
Risk: Medium-Low

Market Data

Current Price \$19.60
 52-Wk Range \$13.36-19.99
 Mkt. Cap. (mm) \$1,850
 Dividend \$1.04
 Yield 5.3%

Financial Data

Fiscal Y/E November 30
 Shares O/S (mm) 94.4
 Total AUM (bill) \$52.5
 Mkt. Cap. as % AUM 3.5%
 Mutual Fund AUM (bill) \$26.8
 Mkt. Cap. as % MF-AUM 6.9%

Estimates (f.d.)

Year	2010A	2011E	2012E
EPS	\$1.30	\$1.48	\$1.63
EBITDA/Shr.	\$2.85	\$3.20	\$3.50
Prior EBITDA/Shr.	-	\$3.20	\$3.40

Valuations

Year	2010A	2011E	2012E
P/E Mult.	15.1x	13.2x	12.0x
P/EBITDA Mult.	6.9x	6.1x	5.6x

AGF Management Limited



Chart Courtesy Big Charts

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Notes:
 All figures in Canadian dollars, unless otherwise specified.
 * Under Review

Please see the final pages of this document for important disclosure information.

Q1/11 Earnings Slightly Better Than Expectations Mutual Fund Net Redemptions Continue to Hamper Asset Growth Acuity Acquisition Adds 15% to AUM But Uncertain For Earnings

Conclusion: HOLD – Target Increased to \$20.00

AGF Management (AGF) reported Q1/11 earnings about 10% above expectations. EBITDA was reported at \$0.69 per share, however, excluding a \$5.3 million acquisition charge for Acuity and a \$1.0 million regulatory charge at Smith & Williamson, operating EBITDA was more in the order of \$0.76 per share, up 3% Y/Y. The better earnings were driven by higher management fees due in part by the Acuity acquisition. Assets Under Management (AUM) increased 20% Y/Y to 52.5 billion. Excluding the Acuity acquisition, AUM increased 3% Y/Y. AGF Trust EBITDA declined 22% Y/Y and 5% sequentially or about 15% below expectations driven by a 13% Y/Y decline in loans outstanding. Q1/11 EPS was reported at \$0.35 excluding the one-time items referred to above.

For fiscal 2011, higher earnings should result from an increase in average AUM including the AUM from the Acuity acquisition. Integration of Acuity has begun which should surface some cost savings. However, we expect little in the way of earnings accretion from the acquisition in fiscal 2011. The decline in loans outstanding at AGF Trust is expected to result in a negative Y/Y change in its EBITDA. Our fiscal 2011 EBITDA per share forecast for AGF has been maintained at \$3.20 and our EPS forecast has been increased marginally to \$1.48 from \$1.45.

For fiscal 2012, our EBITDA per share forecast has been increased to \$3.50 from our preliminary estimate of \$3.40, largely due to cost controls and some accretion from the Acuity acquisition. Our fiscal 2012 EPS forecast has been increased to \$1.63 from \$1.55.

Valuation & Recommendation

Our 12-month target price has been increased to \$20.00 from \$19.00. This valuation reflects the average AUM increase of 25% largely driven by the Acuity acquisition and the additions to AGF's product lines and the attractive dividend yield offset by the continued rather substantial shortfall in loan collateral coverage of \$200 million in AGF Trust (\$2.00 per share) and a higher than expected level of mutual fund redemptions.

In our view, AGF continues to warrant an overall valuation discount to its peers. Our target price values AGF at about 5.7 times our 2012 EBITDA forecast versus IGM and CIX at about 8.0 times. AGF currently trades at almost 4.0% of AUM versus 9.8% for CIX and IGM. The lower valuation for AGF also reflects (i) the fact that almost 50% of AGF's assets are institutional in nature, the latter of which are generally valued significantly less than retail assets and, (ii) the estimated \$2.00 per shortfall in loan collateral value. Furthermore, AGF's management has indicated that they will pursue the institutional business more aggressively which, in our view, will lower margins further. Our Hold recommendation is maintained.

AUM Lower by 4% Y/Y – Mutual Funds Still in Net Redemption

AGF experienced net redemptions in the quarter of \$398 million versus \$414 million in the prior quarter. Market performance was a positive \$1,188 million versus a negative \$331 million in the same quarter last year. Total mutual fund AUM decreased 17% Y/Y to \$25.9 billion while total AUM, including institutional and high-net-worth, increased by 20% Y/Y to \$52.5 billion. Most of the increase was due to the Acuity acquisition.

Investment Management

Investment management operations (fund management) revenues were higher by 7% Y/Y and sequentially. The revenues included only one month of Acuity. Management and advisory fees increased 7% Y/Y. Operating expenses in the quarter increased 1% Y/Y due to lower fund absorption and IT related expense. EBITDA was \$60.0 million (excluding one-time expenses), up from \$56.3 million last quarter and 10% Y/Y. The EBITDA margin (EBITDA as a % of management and advisor fees) increased to 45% from 44% in the same period last year.

AGF Trust Operations Going Sideways

The trust operations were below expectations reporting EBITDA of \$8.6 million, down from \$11.1 million last year and \$9.1 million last quarter. Loan losses were \$3.5 million, down 10% Y/Y and 16% sequentially.

This quarter saw an increase in interest margins to 2.73% from 2.62% last quarter and from 2.44% in the same period last year. Total loans decreased by 13% Y/Y to \$3.0 billion driven by a 20% decrease in mortgage loans.

AGF Trust has dramatically reduced its lending base, and we continue to question why AGF remains in this business. We expect total loans outstanding will shrink further over the near-term. AGF's mortgage loans comprise about 35% of all loans with Home Equity loans, secured investment loans and RSP loans making up the balance. The latter are expected to continue to hamper earnings growth as management struggles with loan losses.

About \$1.6 billion of the loan portfolio is comprised of investment loans (excluding RSP loans). The underlying value of the securities supporting these loans is about \$1.4 billion for a shortfall of \$200 million (\$2.00 per AGF share). Gross Impaired Loans (GIL) decreased to \$33.4 million versus \$35.7 million in the prior quarter. We have lowered our PCL estimate to \$15 million for fiscal 2011 from \$16.0 million. At best, we expect PCL to flatten out in fiscal 2012.

Our 2011 EBITDA estimate for AGF Trust has been lowered to \$40 million from \$42 million which is about 2% lower versus last year. For fiscal 2012, we expect only a marginal improvement in EBITDA.

Acquisition of Acuity – Not a Bargain But a Nice Addition

- On February 1, 2011, AGF completed the acquisition of Acuity Asset Management for a consideration of \$325 million, 60% cash and 40% AGF Class B shares. \$223 million paid at closing with \$102 million subject to deferral to be paid over 3 years. Purchase price to be adjusted based on client growth or contraction in Acuity's institutional book of AUM.
- \$7.4 billion of institutional, mutual fund and high net worth AUM.
- Increases AGF's institutional AUM by 20% – adds \$3.6 billion of institutional AUM.
- Increases AGF's mutual fund AUM by 12% – adds \$2.7 billion of mutual fund AUM.
- Increases AGF's high net worth AUM by 29% – adds \$1.0 billion of high net worth AUM.
- Accretive to cash EPS in fiscal 2011 according to management.
- We estimate that AGF paid 4.4% of AUM overall. This would breakdown to 1.5% of institutional, 5% of High Net Worth and slightly over 8% of the mutual fund AUM. Overall, Acuity was fully priced.

Definition of Risk Rankings

Low: Low financial and operational risk, high predictability of financial results with stronger than average balance sheet and strong free cash flows. Company may pay substantial dividends or have an active share repurchase program.

Medium: Moderate financial and operational risk, moderate predictability of financial results, positive free cash flows and may or may not pay a dividend.

High: High financial and/or operational risk, low predictability of financial results. Limited financial history, negative free cash flows, adequate working capital and no dividends.

Definition of Research Ratings

The Catalyst research recommendation structure consists of the following categories:

Buy: The stock's total return, including dividends paid, is expected to exceed a minimum of 15% on a risk-adjusted basis, over the next 12 months.

Hold: The stock's total return, including dividends paid, is expected to be between 0% and 15%, on a risk-adjusted basis, over the next 12 months.

Sell: The stock's total return, including dividends paid, is expected to be negative over the next 12 months.

Speculative: The stock's total return is expected to exceed 30% over the next 12 months; however, there is material event risk associated with the investment that could result in significant loss.

Note: Analysts have discretion within 500 basis points of the upper and lower limit of each rating to maintain the recommendation.

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