

Update Report

March 18, 2008

POWER FINANCIAL CORP.

(PWF-TSX \$32.95)

Recommendation

Buy

Risk

Low

Target Price

\$46.00

Price

\$32.95

52-Week Range

\$32.06 - \$42.69

% Below High

-22.8%

% Above Low

2.7%

Shares O/S

705 million

Market Cap

\$23 billion

Average Daily Volume

873,100

Year-End

December 31

C\$	EPS	& Mult
2007a	\$2.84	11.6x
2008e	\$3.15	10.5x
2009e	\$3.35	9.8x
NAV	\$35.75	-7.8%

	Amount	Yield
Dividend	\$1.25	3.8%

Analysts

Robin Cornwell



Data Source: www.BigCharts.com

Q4/07 EARNINGS LOWER THAN EXPECTED LARGELY DUE TO CURRENCY IMPACT CONTINUES TO BE A TOP CHOICE IN FINANCIAL SECTOR

CONCLUSION: BUY - 12 MONTH TARGET LOWERED TO \$46.00

Power Financial reported Q4/07 operating EPS (fd) of \$0.72. Adjusted operating EPS was \$0.68 (up 6% Y/Y) when \$0.04 per share of non-operating earnings from Great-West Lifeco are excluded. The adjusted earnings were lower than expected. The results also saw slower earnings from IGM (up 5% Y/Y) but better earnings at Pargesa (+33% Y/Y). The stronger C\$ vs US\$ had a negative impact of an estimated \$0.02 per PWF share. ROE was 17.3% down from 18.4% last quarter. For the full year cash earnings were \$2.84 up 16% from \$2.44 in 2006.

We are lowering our 2008 EPS estimate for PWF to \$3.15 from \$3.22 and have also introduced our 2009 EPS estimate at \$3.35. Our 12 month share price target for PWF has been lowered to \$46.00 from \$48.50 to reflect the lower target prices set for Great-West Lifeco and IGM. We continue to rate the shares as a BUY and believe PWF continues to be one of the best positioned financial service companies in Canada particularly in the wealth management sector.

PWF Trades At An 8.0% Discount To Net Asset Value

PWF had a book value of \$16.26 per share as at December 31, 2007, however this is not representative of current market value of its subsidiaries. Actual Net Asset Value (NAV) for PWF is \$35.75 per share which more appropriately reflects the current public market value of all investments. PWF at present trades a discount of 8.0% to this current NAV. Our 12-month projected NAV is \$48.50 per PWF share based on our 12 month revised share price targets of \$58.00 for IGM (previously \$63.00) and \$40.00 target for GWO (previously \$41.50).

Valuation - PWF Should Support A Share Price Closer To NAV

We expect PWF's share price to trade closer to its forward NAV and therefore we have lowered our 12 month share price target to \$46.00 from \$48.50 which implies a discount of closer to 5% to our 12 month target NAV of \$48.50 per share. If financial service sector consolidation becomes a possibility then we would expect the discount to disappear and see PWF's share price trade closer to its targeted NAV and possibly support a premium.

Great-West Lifeco – BUY - 12 Month Target Lowered To \$40.00

We have lowered our 12 month target share price for GWO to \$40.00 from \$41.50 based on the modestly slower earnings outlook. We believe GWO represents a solid, low risk, global growth opportunity using an “add-on” acquisition strategy focused on the wealth management sector. In addition to the Putnam transaction, GWO has made five other add-on acquisitions which collectively we expect to be significantly accretive to 2008 EPS. More significant is our expectation that GWO may make several more of these add-on acquisitions over the next 12 months and further enhance EPS in 2008 and 2009. We continue to highly endorse this strategy. Our valuation also recognizes the good constant currency underlying earnings growth at GWO.

- **Great-West Lifeco (GWO) Reported Q4/07 EPS** (fd) of \$0.60 up 9% Y/Y and \$0.03 below our expectations. The currency impact was significant such that on a constant currency basis EPS would have been \$0.64 up 17% Y/Y. The quarter included 3 months of Putnam with the contribution to GWO's earnings slightly lower than expected with net redemptions higher than expected. Adjusted ROE decreased modestly to 21.9% in the quarter.
- **Dividend Per Share Increased** to \$1.17 annually from \$1.10 up 6%.
- **For Year-ended 2007** - as a whole GWO reported adjusted EPS (fd) of \$2.42 per share up from \$2.11 in 2006, a gain of 15%. However on a constant currency basis net income would have been \$0.03 per share higher and the earnings growth would have been closer to 16% for the year. ROE for 2007 was 21.6% up from 20.1% in 2006.
- **Recent Acquisitions** - GWO also recently announced the acquisition of another add-on U.K. payout annuity block from Standard Life. We expect this business to be accretive to 2008 EPS by an estimated \$0.04. In addition, the pending sale of the Health Care unit announced previously is considered a positive move for GWO as it has been struggling for scale and profitability. This deal completes the financing for Putnam with no need for equity financing. However, and far more significant, is that we expect the growth potential from Putnam will be greater than that which would have been generated from the stagnant Health Care unit. We see this deal as reinforcing managements focus on the wealth management (retirement) sector in the U.S.
- **Earnings Outlook** - We are lowering our 2008 EPS estimate for GWO to \$2.70 from \$2.77 due to weaker equity markets, our lower expected AUM forecast and the stronger \$C currency. We have also introduced our 2009 estimate at \$2.95, a 9% increase over 2008. ROE is expected to remain strong at near 20%.
- **Dividend Outlook Remains Good** - We expect a trailing dividend payout ratio of 47% to 50% which would suggest further dividend increases over the next 12 months to the \$1.30 level for an increase of 11%.
- **Putnam Update** – First Full Quarter Putnam contributed net earnings of US\$27 million or \$0.03 per GWO share for the quarter. On a standalone basis excluding restructuring charges Putnam reported net income of US\$50 million and US\$81 million before tax and non-controlling interest. The gross margin was 25.4%. This included about US\$5 million of seasonal adjustments including performance fees. Management is working towards eliminating more administrative expenses as well as increasing its institutional book of business which looks very promising. Both should allow for an improvement in margins closer to the 30% level. The retail turnaround will take longer as we expected.

- **U.S. health care division to be sold to CIGNA Corp.** GWO has agreed on a price of US\$2.25 billion with after-tax cash proceeds of US\$1.6 billion. Management indicated that it will use the proceeds to repay financing associated with the Putnam purchase. The transaction is expected to close in mid-2008.
- **U.K. Payout Annuity Block From Standard Life** - Accretive to 2008 EPS by an estimated \$0.04. GWO announce on February 14, 2008 that it signed an agreement with Standard Life Assurance Limited in the U.K. to assume by way of indemnity reinsurance, a large block of U.K. payout annuities. The business will be acquired by its wholly owned UK subsidiary Canada Life Limited. This transaction will increase policyholder liabilities by approximately C\$13 billion. We estimate that this acquisition will bring the total annuity block managed by Canada Life to almost C\$35 billion.
- **Canada**, Q4/07 net income was \$246 million up 10% Y/Y. Operating expenses were down 2% Y/Y providing positive operating leverage.
- **U.S. Division** was weaker than expected and reported a 4% increase in \$US net income excluding Putnam and a 10% increase including a full quarter of Putnam.
- **Europe** reported weaker Q4/07 net income of \$150 million or flat Y/Y. On a constant currency basis net income rose 10%. Sales in the U.K. were down 42% Y/Y while sales in Germany & Ireland decreased 5% Y/Y. The lower U.K. sales in the quarter resulted from a decline in single premium bonds sales in reaction to proposed U.K. budget changes. The acquisition of the Standard Life annuity payout block should be a positive in 2008 as will rolling over of Equitable Life block.
- **Subprime Exposure:** Management stated that GWO has approximately US\$1.5 billion of 'AAA' rated home equity subprime investments in various pools representing 1.5% of its total invested assets. Most of the loans (65%) were originated prior to 2006 and all are fixed rate in nature. Management indicated that there was equity of about 30% below GWO's investments. None of the investments have been subject to credit rating downgrades.
- **Monoline Exposure:** GWO has \$3.5 billion in Monoline exposure largely wrapping bonds that are government and utility related. Geographically the exposure is Canada (6%), U.S. (36%), Europe (58%). Monoline insurers are Ambac (35%), MBIA (32%), FSA (16%), FGIC (15%), XL (2%). Management expects little impact from the default of any of these insurers.

IGM Financial – BUY - 12 Month Target Lowered To \$58.00 – Outlook Weaker

We consider IGM as the premier asset management company in Canada and well positioned in its distribution channels with Investors Group. We believe IGM is deserving of a premium EBITDA multiple based on its superior positioning and good profit margin. The outlook for AUM growth in fiscal 2008 has turned decidedly more negative recently and we have lowered our earnings outlook. Accordingly, we have lowered our 12-month target price for IGM to \$58.00 from \$63.00 which represents a multiple of 8.5x our 2008 EBITDA forecast.

- **IGM reported Q4/07 Results** - about 3% weaker than expected. EBITDA per share increased by 5% Y/Y to \$1.56 but were lower than last quarter at \$1.60. EPS (fd) was reported at \$0.82, a 9% Y/Y gain. ROE was marginally lower at 21.2%. The Y/Y increase in EBITDA was largely due to an increase in average mutual fund AUM of 10% Y/Y. Total AUM as at the end of the quarter amounted to \$123 billion up 3% Y/Y but down flat from the previous quarter.
- **Dividend Per Share Increased** by 6% to \$1.95 annually from \$1.84.
- **EPS for fiscal 2007** was reported at \$3.23 (excluding the tax benefit) up from \$2.90 or 11% reported in fiscal 2006. EBITDA in fiscal 2007 was reported at \$6.29 per share up from \$5.68 per share last year, a Y/Y gain of 11%. Total revenues increased 11% Y/Y.

- **Lower AUM Growth** - We expect market volatility to continue for some time and we have lowered our AUM growth expectations for fiscal 2008. Accordingly, we have lowered our 2008 EBITDA per share estimate to \$6.70 from \$6.90 and have introduced our 2009 EBITDA per share estimate at \$7.25 a gain of 8%. Our EPS estimate for 2008 has been lowered to \$3.45 from \$3.62. Our 2009 EPS estimate has been set at \$3.70.
- **Dividend Outlook** - We expect a dividend payout ratio in closer to the 60% of EPS in 2008 which would imply a dividend in 12 months time of about \$2.05 to \$2.10 per share or an increase of 6% to 8%.
- **Total Mutual Fund AUM for IGM** as at the end the quarter increased to \$107 billion down marginally from \$109 billion as at the end of last quarter and up 2% Y/Y. Gross mutual fund sales in the quarter were \$4.6 billion with net sales of \$534 million. Total AUM increased to \$123 billion, a Y/Y increase of 3%.
- **IG** had gross long term fund sales of \$1.6 billion in Q4/07 with net sales of \$386 million, a relatively good quarter considering the market environment. Total mutual fund AUM as at the end of the quarter was \$60.2 billion up 3% Y/Y.
- **Mackenzie** experienced gross long term fund sales of \$1.4 billion in the quarter with net long term redemptions of \$0.3 billion. Total mutual fund gross sales were \$3.0 billion with net sales of \$0.2 billion. Total mutual fund AUM as at quarter end was \$46.6 billion flat Y/Y. Mackenzie had net sales of \$46 million its money market funds. Total AUM including institutional AUM and the Cundill AUM increased to \$63.3 billion up 3% Y/Y.
- **Counsel Fund Management** had net redemptions of \$1 million (gross sales of \$66 million) in Q4/07, a decent quarter given the market volatility. AUM increased by 3% Y/Y to \$2.3 billion.

Parjointco-Pargesa

- Pargesa (through Parjointco, the holding company owning the interest in Pargesa) contributed \$40 million to net income in Q4/07 up from \$30 million in the prior quarter and the same quarter last year.

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