

Recommendation

Buy

Target Price

\$48.50

Risk

Low

Average Daily Volume

20da:742,500/150da:577,900

Quick Facts

Recent Price \$39.75
Symbol PWF-TSX
Shares O/S 705 million
Market Cap. \$28.4 billion
52 Wk. Range \$25.81-\$42.69
Year End December 31

	<u>EPS</u>	<u>Multiple</u>
2006a	\$2.44	16.3x
2007e	\$2.89	13.7x
2008e	\$3.22	12.3x
NAV	\$43.40	-8.4%

	<u>Rate</u>	<u>Yield</u>
Dividend	\$1.25	3.2%

Power Financial Corp.



Data Source: BigCharts.com

Power Financial Corp. is a holding and management company. Its operations provide a range of individual and corporate financial and fiduciary services in North America and Europe. Subsidiaries include Great-West Lifeco, IGM Financial, London Insurance Group, Canada Life Financial, Investors Group, and Mackenzie Financial, and major affiliate Pargesa Holding SA of Switzerland.

CONCLUSION: BUY - 12 MONTH TARGET MAINTAINED AT \$48.50

Power Financial reported Q3/07 adjusted operating EPS (fd) of \$0.73 up 22% Y/Y. Earnings excluded a \$74 million after tax charge (\$0.11 per share) relating to a Canadian pension retirement plans provision at GWO. The adjusted earnings were \$0.01 better than our expectations and \$0.02 better than consensus. The earnings were driven by solid earnings from both GWO (up 16% Y/Y) and IGM (up 14% Y/Y) but as well, better earnings from Pargesa (up 150% Y/Y). ROE was 18.4% down from 20.1% last quarter and 19.0% in Q3/06. Dividend was increased to \$1.25 annually from \$1.16 representing an increase of 7.8%.

We are increasing our 2007 EPS estimate for PWF to \$2.89 from \$2.87 and have also increased our 2008 EPS estimate to \$3.22 from \$3.20. Our 12 month share price target for PWF has been increased to \$48.50. 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 8.4% Discount To Net Asset Value Of \$43.40 Per Share

PWF had a book value of \$15.58 per share as at September 30, 2007, however this is not representative of current market value of its subsidiaries. Actual Net Asset Value (NAV) for PWF is \$43.40 per share which more appropriately reflects the current public market value of all investments. PWF at present trades a discount of 8.4% to this current NAV. Our 12-month projected NAV, based on our 12 month revised share price targets of \$63.00 for IGM (previously \$61.00) and \$41.50 target for GWO (previously \$40.50) is \$51.00 per PWF share.

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 increased our 12 month

share price target to \$48.50 from \$48.00 which implies a discount of closer to 5% to our 12 month target NAV of \$51.00 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. Total 12 month return is forecast at 25.0%.

PWF Quarterly Highlights

- PWF reported Q3/07 operating earnings of \$457 million vs \$795 million in Q3/06. However after adjusting for the \$74 million after tax charge (\$0.11 per share) relating to a Canadian pension retirement plans provision at GWO in Q3/07 and the \$356 million (\$0.50 per share) gain from the sale of PWF interest in Bertelsmann in Q3/06, the adjusted earnings for Q3/07 were \$531 million or \$0.73 per share up 22% Y/Y over an adjusted \$439 million or \$0.60 per share in Q3/06.
- NAV (Net Asset Value) currently stands at \$43.40 per share well above the Company's stated book value.

Great-West Lifeco – BUY - 12 Month Target Increased To \$41.50

- Great-West Lifeco (GWO) reported Q3/07 EPS (fd) of \$0.625 up 16% Y/Y in line with our expectations and about \$0.01 ahead of consensus. These results exclude a one-time \$95 million after-tax or \$0.11 per share reserve provision relating to Canadian pension retirement plans. The quarter included 2 months of Putnam with the contribution to GWO's earnings better than expected. In addition the quarter was helped by strong earnings in both the U.S. and Europe as the add-on acquisitions continue to show positive results.
- We are maintaining our 2007 and 2008 EPS estimates for GWO of \$2.46 and 2.77 respectively. ROE is expected to remain strong at near 22%.
- We have increased our 12 month target share price for GWO to \$41.50 from \$40.50 based on what we believe is 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 four 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.
- The recent strength of the CDN\$ relative to the US\$ (approximately 27% of GWO's earnings are sourced in the U.S.), and assuming the CDN\$ stays closer to the \$1.05 level versus the \$0.95 level that we had previously expected, the impact on GWO could be negative by some 2% on 2008 EPS (\$0.03 to \$0.04 per share) rather than the neutral impact previously expected. However we believe an offset will be higher earnings benefits from Europe as payout annuity assets are reinvested at higher rates and a better than expected contribution from Putnam.
- We expect a trailing dividend payout ratio of 47% to 50% which would suggest further dividend increases over the next 18 months to the \$1.35 to \$1.40 level (annualized at about 18%).
- Our valuation also recognizes the good constant currency underlying earnings growth at GWO and the significantly higher yield of 3.0%. Our total expected return over the next 12 months for GWO is 16.5%.

- Putnam contributed earnings of \$16 million after-tax (and financing costs) or \$0.017 per GWO share for 2 months of the quarter which would imply \$0.025 per share for Q4/07 assuming no additional cost benefits. This is about \$0.01 better than expected for 2007 and implies a contribution of \$0.10 per share for 2008 or about \$0.04 per share better than expected. Putnam reported net redemptions in the period of US\$966 million which although still negative, the outflow is down sharply from US\$3.1 billion in the same period last year. As at the end of the quarter total AUM was US\$191 billion of which US\$113 billion were long-term AUM, US\$4.1 billion short-term and the balance institutional.
- In Canada, Q3/07 net income was \$245 million up 14% Y/Y. Excluding a write-down on BCE bonds net income would have been 17% higher Y/Y. Total life insurance sales were up 10% Y/Y lead by strong Universal life sales. Individual Retirement sales were up 27% due to strong segregated fund and mutual fund sales. Operating expenses were up 2% Y/Y.
- U.S. division reported stronger net income, including Putnam, of \$150 million up 23% Y/Y (up 30% on a constant currency basis). Excluding Putnam net income would have been up 16% Y/Y. Sales of 401k plans were up 192% Y/Y due to the recent acquisitions of 401k business blocks from MetLife and US Bancorp and as well the acquisition of two new large case accounts. GWO could see faster growth in 401k accounts as management focuses its strategy on the acquisition of larger cases. Fee income on AUA was up 60% Y/Y also driven by the 401k assets recently acquired. Healthcare net income was reported at \$44 million flat on a Y/Y but however sales fell and there were 149 net case outflows. Many of the lost cases were however smaller in size and not profitable.
- Europe reported a very strong Q3/07 net income of \$161 million up 25% Y/Y. Sales in the UK were up 6% Y/Y while sales in Germany & Ireland increased 58% Y/Y. Less than 50% of the \$3.0 billion of the payout annuity block of business purchased from Equitable Life has been reinvested under the yield enhancement strategy initiated when the block was acquired. Although reinvestment is happening at a slower rate than expected, the good news is that the recent credit problems seem to be widening potential spreads going forward from the 70bp pick-up in spread achieved to date to the 100bp to 125pb level. We expect further benefits to accrue as the balance is gradually reinvested in higher yielding securities.

IGM Financial – BUY - 12 Month Target Increased To \$63.00

- IGM reported solid Q3/07 results in line with our expectations and consensus. EBITDA per share increased to \$1.60 up from \$1.57 last quarter and up 12% Y/Y. EPS (fd) was reported at \$0.82, a 14% Y/Y gain. ROE was stable at 21.5%. The Y/Y increase in EBITDA was largely due to an increase in average mutual fund AUM of 12% Y/Y and positive overall operating leverage.
- We are maintaining our 2007 and 2008 EBITDA per share estimates at \$6.35 and \$6.90 respectively as well as our 2007 and 2008 EPS estimates at \$3.25 and \$3.62 respectively. ROE for 2008 is expected to be stable at the 21.5% level.
- We consider IGM as the premier asset management company in Canada and well positioned in its distribution channels with Investors Group (strong & growing captive sales force), Mackenzie (independent sale channel) and IPC (Financial Planning + Counsel Fund Management). We believe IGM is deserving of a premium

EBITDA multiple based on its superior positioning and good profit margins (impressive expense controls) which will enable it to successfully compete in what is becoming an increasingly competitive environment. We have increased our 12-month target price for IGM to \$63.00 from \$61.00 which represents a multiple of 9.1x our 2008 EBITDA forecast.

- We expect a dividend payout ratio in closer to the 58% 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 14% to 16%. We expect a 12-month total return of 20.0%.
- Total mutual fund AUM for IGM as at the end the quarter increased to \$111 billion down marginally from \$112 billion as at the end of last quarter and up 12% Y/Y. Gross mutual fund sales in the quarter were \$4.3 billion with net sales of \$192 million. Total AUM increased to \$124.2 billion, a Y/Y increase of 13%.
- IG had gross long term fund sales of \$1.3 billion in Q3/07 with net sales of \$253 million, a relatively slow quarter. Total mutual fund AUM as at the end of the quarter was \$61.2 billion up 13% Y/Y.
- Mackenzie experienced gross long term fund sales of \$1.4 billion in the quarter with net long term redemptions of \$0.1 billion. All mutual fund gross sales were \$1.8 billion with net redemptions of \$0.2 billion. Total mutual fund AUM as at quarter end was \$47.8 billion up 11% Y/Y. Mackenzie had net redemptions of \$131 million in its money market funds (attributed to concerns over the 3rd party ABCP issues) and net redemptions of \$261 million in its institutional business. Total AUM including institutional AUM and the Cundill AUM increased to \$63.5 billion up 12% Y/Y.
- Counsel Fund Management had net sales of \$34 million (gross sales of \$80 million) in Q3/07, another decent quarter. AUM increased by 15% Y/Y to \$2.3 billion.

Parjointco-Pargesa

- Pargesa (through Parjointco, the holding company owning the interest in Pargesa) contributed \$30 million to net income in Q3/07 over double the \$12 million reported in Q3/06 (excluding the \$356 million gain from the sale of PWF interest in Bertelsmann) but down from \$80 million last quarter.

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