

March 8, 2013

To subscribe to our Newsletters  
[www.palosmanagement.com/register](http://www.palosmanagement.com/register)

## ■ Portfolio Management & Advisors

**Charles Marleau, CIM**  
 President & Senior Portfolio Manager

**Hubert Marleau**  
 Economist & Co-Founder

**Yarith Chhiv, CFA**  
 Senior Portfolio Manager & Risk Manager

**Adam Smalley, MBA, CPA**  
 Senior Portfolio Manager

**David Bilodeau, DMS, FCSI**  
 Sub-Advisor, Majestic Asset Management

**Denis Paquette, FRM, CAIA, DMS**  
 Sub-Advisor, Majestic Asset Management

**Robert Boisjoli, FCA**  
 Managing Director, Palos Merchant Fund

**Cameron McDonald**  
 Managing Director, Palos Merchant Fund

**George Kaneb, MBA**  
 Vice-President, Palos Merchant Fund

## ■ Contacts

**Noah Billick, BCL, LLB, MBA**  
 Vice-President, Legal Affairs

**Alexandra Kaneb**  
 Director, Sales and Marketing

**Palos Management Inc.**  
 1 Place Ville Marie, Suite 1812  
 Montreal (QC) H3B 4A9, Canada  
 T. +1 (514) 397-0188 F. +1 (514) 397-0199  
[www.palosmanagement.com](http://www.palosmanagement.com)



# Palos Weekly Commentary

## ■ Palos Income Fund

By Charles Marleau

### Opportunities from Above

MacDonald, Dettwiler and Associates Ltd. (TSX: MDA) is a global communications and information company. On November 2, 2012 it acquired SSL Palo Alto facility (SS/L) which opened many growth opportunities for MDA. SS/L, now a division of MDA, is a world leader in space systems. It has been delivering satellites and spacecraft systems for commercial and government customers around the world and currently has more geostationary commercial capacity on orbit than any other manufacturer.

MDA via SS/L provides spacecraft for a broad range of services including direct-to-home television and radio, broadband internet, television and radio distribution, and mobile communications. The company's business is fuelled by some of today's most compelling

consumer communications needs. The Company provides spacecraft to all the world's top satellite operators.

Palos sees many growth opportunities in the space systems division as demand from the U.S government is robust. Furthermore, many other countries have major satellite plans including Russia, Brazil, India and South Africa. Demand for commercial satellite from blue chip customers is also on the rise. All of this demand translates to over \$1 billion in bid.

In conclusion MDA is well positioned to diversify its business beyond the public sector and into the private sector. MDA has strategically positioned itself to take advantage of the satellite market and leverage its new U.S. operation to up-sell its other services and products. We view MDA as a growing, profitable company with a top quartile management team.

Chart 1: Palos Domestic Funds\*

	FundServ	NAVPS	5D Returns	YTD Returns
Palos Income Fund L.P.	PAL 100	CA \$9.36	1.78%	6.82%
Palos Equity Income Fund - RRSP	PAL 101	CA \$7.13	1.04%	4.58%
Palos Merchant Fund L.P. (Feb 28, 2013)	PAL 500	CA \$8.77	---	7.28%
Palos Majestic Commodity Fund L.P. (Mar 7, 2013)	PAL 600	CA \$11.19	2.70%	5.39%

Chart 2: Market Data\*

	Value	5D Returns	YTD Returns
S&P TSX Total Return Index	37,013.78	0.53%	3.69%
S&P 500 Total Return Index	2,735.67	2.22%	9.23%
S&P TSX Venture Index	1,117.85	-0.20%	-8.43%
MSCI All Countries World TR Index (CAD)	3,650.21	2.32%	9.63%
US Government 10-Year	2.04%	0.20%	0.29%
Canadian Government 10-Year	1.93%	0.13%	0.14%
Crude Oil Spot	US \$91.95	\$1.27	\$0.13
Gold Spot	US \$1,576.90	\$4.60	-\$98.90
US Gov't 10-Year/Moody BAA Corp. Spread	196 bps	-3 bps	5 bps
USD/CAD Exchange Rate Spot	US \$0.9721	-\$0.0018	-\$0.0331

\* Period ending Mar 8, 2013

**Disclaimer:** No part of this publication or its contents may be copied, downloaded, stored in a retrieval system, further transmitted, or otherwise reproduced, disseminated, transferred, in any form or by any means. This publication is proprietary to Palos Management Inc. The information and opinions contained herein have been compiled or arrived at from sources believed reliable but no representation or warranty, express or implied, is made as to their accuracy or completeness. The information contained herein is not necessarily complete and its accuracy is not guaranteed by Palos Management Inc. If you have received this communication in error, please notify us immediately by electronic mail or telephone. The overall views expressed in this report are prepared by Palos Management Inc.

March 8, 2013

To subscribe to our Newsletters  
[www.palosmanagement.com/register](http://www.palosmanagement.com/register)

## ■ Portfolio Management & Advisors

**Charles Marleau, CIM**  
 President & Senior Portfolio Manager

**Hubert Marleau**  
 Economist & Co-Founder

**Yarith Chhiv, CFA**  
 Senior Portfolio Manager & Risk Manager

**Adam Smalley, MBA, CPA**  
 Senior Portfolio Manager

**David Bilodeau, DMS, FCSI**  
 Sub-Advisor, Majestic Asset Management

**Denis Paquette, FRM, CAIA, DMS**  
 Sub-Advisor, Majestic Asset Management

**Robert Boisjoli, FCA**  
 Managing Director, Palos Merchant Fund

**Cameron McDonald**  
 Managing Director, Palos Merchant Fund

**George Kaneb, MBA**  
 Vice-President, Palos Merchant Fund

## ■ Contacts

**Noah Billick, BCL, LLB, MBA**  
 Vice-President, Legal Affairs

**Alexandra Kaneb**  
 Director, Sales and Marketing

**Palos Management Inc.**  
 1 Place Ville Marie, Suite 1812  
 Montreal (QC) H3B 4A9, Canada  
 T. +1 (514) 397-0188 F. +1 (514) 397-0199  
[www.palosmanagement.com](http://www.palosmanagement.com)

## ■ Risks, Hedges and Opportunities

By Adam Smalley

### Room to Run

The failed Italian elections and the US sequestration caused minor dips in equity markets but failed to derail its momentum. In our view, this is appropriate. There are many factors, both technical and fundamental, that will continue to drive stocks higher. JPMorgan notes that the average mutual fund is trailing its benchmark by about 100 bps so far this year. Speculation is that these managers are using market dips to get invested. Factor in some “asset rotation” into equities and the favorable technical backdrop for equities becomes clear.

More importantly, however, are fundamentals. Announced stock buybacks in the US are currently at a “buyback yield” of 8% (annualized announced buybacks over aggregate market cap). Historically, in the US, 95% of announced buybacks are executed. Companies are also returning cash via dividends. The dividend yield of the top 20% of the S&P 500 is 4.2% compared to a 3.5% yield for investment grade bonds. This spread of 123 bps is the largest it has been since 2009. Valuations and earnings tell a similar story. TEV / EBITDA multiples are currently at 9x versus 11x before the financial crisis and consensus estimates for the S&P 500 are for 10%+ growth in 2013 and 2014.

The portfolio managers at Palos have increased exposure to equities over the past few months. Fixed income (corporate bonds, convertible bonds and preferred stocks) now represent less than 5% of the funds’ exposure, down significantly from last year.

## ■ What is New on the Macro Level?

By Hubert Marleau

### Does the Dow Jones Have More Room to Run?

From the low of 6547 on March 9, 2009, the Dow Jones Industrial Average is up nearly 120%. It is a significant accomplishment that the

benchmark closed on Friday last above its historical all-time high. It may be impossible to predict how much longer this bull market will last. Yet, it is noticeable that trading, speculative and investment habits of all market participants have dramatically changed. The USD’s usual status of being a funding currency for risk averters has turned into an asset currency generally ascribed to risk takers. Over the past few months, the relationship between the USD and risk assets like stocks, real estate and junk bonds has for all purposes turned positive. The aforementioned hypothesis makes intuitive sense and can be simple to grasp since the FED decided to target the unemployment rate. On Friday last, reported labour statistics were encouraging. The US economy generated 236,000 jobs in February and the UR fell to 7.7%, the lowest level in five years, suggesting that business activity is gaining momentum. This is not about to stop. The US misery index now stands at 93 and inflation accounts for only 17.5% of the index. In our judgment, a 25% inflation composition is what is needed for a monetary policy change. Accordingly, the era of easy money is not yet over. Moreover, there are many valuation metrics that support our thesis that the bull is still in our midst:

1) The compound annual revenue growth rate for the 30 Dow companies since October 2007 is 3.7%.

2) The ratio of EV to EBITDA is about 9x versus 11x at the last peak

3) Companies have deleveraged of late and market prices-to-book are much lower than they used to be.

4) The earnings yield for stock averages 7% compared to 2.00% for ten year US treasuries.

If you have any questions about the weekly commentary, the securities that we follow, or investment ideas, please contact us at [info@palosmanagement.com](mailto:info@palosmanagement.com)

Chart 3: Palos International Fund\*\*

	Last	5D Returns	YTD Returns
Palos International Equity Income Fund PLC - CAD	CA \$5.23	1.69%	3.30%
Palos International Equity Income Fund PLC - EUR	EUR 6.85	2.04%	0.72%
Palos International Equity Income Fund PLC - USD	US \$6.49	1.67%	-0.75%
S&P TSX Composite Total Return Index - CAD	36,718.83	0.66%	2.86%
S&P TSX Composite Total Return Index - USD	35,732.61	0.65%	-0.41%

\*\* Period ending Mar 5, 2013

**Disclaimer:** No part of this publication or its contents may be copied, downloaded, stored in a retrieval system, further transmitted, or otherwise reproduced, disseminated, transferred, in any form or by any means. This publication is proprietary to Palos Management Inc. The information and opinions contained herein have been compiled or arrived at from sources believed reliable but no representation or warranty, express or implied, is made as to their accuracy or completeness. The information contained herein is not necessarily complete and its accuracy is not guaranteed by Palos Management Inc. If you have received this communication in error, please notify us immediately by electronic mail or telephone. The overall views expressed in this report are prepared by Palos Management Inc.