



The direction is up.

IN general, the fourth quarter was a relatively quiet period on the financial markets. Fixed income issues did well as investors sought safety through income producing assets. Although volatility lessened, the equity markets remained weak due to falling commodity prices, including gold, tax-loss selling and a pronounced pause in the Asian economies. No help to investors, the financial press remained fixated on the horrific amount of sovereign debt in southern Europe and how it could bring about the collapse of the European Union and most of the major European banks. Apparently these fears will not be realized anytime soon.

Meanwhile, corporate North America continued to show signs of greater solvency and modest growth. Assuming the Republican Party does not choose an extremist as their candidate, we foresee that most of the political gridlock in Washington will disappear after the November elections, no matter which party gains the White House. For these and a host of additional reasons, we think equities will by far be the best performing investment assets in 2012.

During the quarter, we did some tax-loss selling in **Research In Motion, Encana, and Xerox**. On a fundamental basis, RIM shares have been oversold, but

barring a takeover offer, the share price will languish until management does some major refocusing. Like so many Canadian energy stocks, Encana will require extreme patience until the glut in natural gas is absorbed. As for Xerox, we look for better investment results from **Shaw Communications** and/or our various healthcare selections.

Canadian Equities

For instance, **Canadian Medical Labs**, once again a corporation after being an income trust, finally stabilized their outlook after selling their U.S. subsidiary. We added significantly to our holdings in **Sanofi Aventis**, a leading manufacturer of vaccines and treatments for diabetes. We commenced adding **TEVA**, a leading producer of generic drugs. (*Frank Florio's update on Teva appear elsewhere in this issue*). **Centric Health Corporation** is a new name for our portfolios. The company provides a variety of health-care services at over 750 locations across Canada. Our investment has been in a unit offering consisting of five-year 6% convertible notes, plus stock and warrants. The notes are not transferable.

Shaw Communications is a leading provider of telephone, internet and television services with head-

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quarters in Calgary, Alberta. They increase their dividend regularly. The company is family controlled. If the CRTC ever allows foreign competition or consolidation in the cable business, Shaw would be a prime candidate for takeover. Of more immediate importance, Shaw serves the fastest growing areas of the Canadian economy.

Churchill Corporation, a large-project construction company, also serves the needs of Western Canada. We added to our holding of the Churchill common shares as well as the 6% convertible debentures.

Early last year we sold our positions in **Bombardier** common above \$6.50. Because the company has manufacturing facilities in Europe as well as contracts with European governments, the share price of Bombardier common has drifted below \$4.00. We saw this as a buying opportunity. We are adding to our positions in both the common and preferred shares.

For income and safety of capital, we are adding to our holdings in **Weston** and **RioCan REIT**. RioCan is Canada's largest real estate trust, focusing exclusively on retail real estate. Weston shares have a large cash component, and through subsidiary Loblaws, an undervalued portfolio of commercial real estate. We continue to add to our holding in **Metro Stores**, a food retailer whose business model is aimed at the one and two-person household units. Elsewhere in this issue colleague Evan Warsh has written a piece on **MTY Food Group**, a franchiser and operator of a variety of fast-food outlets.

In the battle for investment success, what we choose NOT to buy for our portfolios is very often more important than what we decide to purchase. During the quarter we avoided financial service companies, especially insurance companies and banks. The banks face tighter regulations and capital requirements, and the insurance company earnings are being squeezed by the persistence of low interest rates. We have also avoided most utilities because the investor "flight to safety" has pushed the prices of many utility common shares to unjustified levels. At some point (when?) interest rates will rise, squeezing the earnings of utilities just as the present low interest rate environment has squeezed the earnings of insurance companies.

U.S. Holdings

Currency volatility has made us reluctant to expand our U.S. holdings. On the other hand, the leading technology companies are traded on U.S. markets. We have maintained and sometimes added to our positions in **Intel**, **Corning** and **Cisco**. Retail sales in the U.S. have been less than we anticipated, somewhat because of the mild weather, causing the shares of **Jones Group** to languish. The fact is, retailers need snow to sell winter coats and gloves.

*Briar Foster
Frank Florio, CFA
January 15, 2012*

Teva Pharmaceutical (TEVA-NASDAQ; US\$44.55; Market Cap. US\$41.9 bln.)

Teva Pharmaceutical is an Israeli-based pharmaceutical company that develops, manufactures and markets generic and proprietary branded drugs worldwide. It has operations in 60 countries and employs over 47,000 people worldwide. After experiencing a difficult 2011 and its share price hitting a 52-week low of US\$35, Teva shares currently offer decent upside as we expect several growth drivers to propel Teva shares higher.

We last introduced Teva to most portfolios in early 2007 in the mid \$30s. We exited the position in 2008 in the low \$50s when the likelihood of increased generic competition of Teva's highly profitable branded Multiple Sclerosis ("MS")

drug became apparent. Since then, several changes have occurred. Teva's revenues and earnings have doubled, and its drug portfolio has broadened mainly through several large acquisitions including Cephalon in 2011, and ratiopharm in 2010. At the same time, several rivals are battling Teva to introduce generic versions of Copaxone, Teva's MS drug, clouding the company's outlook and sending the stock price to a 52-week low.

Although regarded by many as the "best" generic drug maker, Teva found 2011 a difficult year. The year was strewn with strong headwinds such as quality control concerns at two of its

plants, and several setbacks with clinical trials of its oral MS drug. 2012 may signal the beginning of a new chapter for Teva with some tail winds forming. Early in the year, CEO Shlomo Yanai announced his resignation. Expectations are high for incoming CEO Jeremy Levin, who is credited for the successful turnaround of Bristol Myers Squibb. Investors showed their confidence in Mr. Levin's abilities by pushing Teva's share price 10% higher since the announcement.

For 2012, Teva's revenues are expected to reach US\$22 billion, with approximately 85% being generated from North America (60%) and Europe (25%). Total sales are comprised

of generics (55% or \$12 billion), branded (37% or \$8 billion), and OTC (over-the-counter) medicines. The OTC business is a joint venture with Procter & Gamble to develop branded OTC medicine outside North America. This is a \$200 billion market opportunity and so far this small segment is growing at a faster rate than any of Teva's other businesses.

We believe there are several trends that will continue to have a favourable impact on Teva's growth. The three top trends are: 1) more people are living longer and consuming more drugs, 2) a growing trend toward healthcare reform and cost-saving initiatives to favour lower cost drugs, and 3) a growing geographic footprint due to emerging generics markets.

Other favourable catalysts include an expected increase of 20 to 30 million people with new health care coverage in US due to the Obama administration's health care reform law. The US Supreme Court will render a verdict on the constitutionality of this reform law in June 2012. A positive decision would benefit Teva as 80% of the volume from the increased covered lives would be serviced by generics.

Over the next 3 years, Teva will produce between US\$15 to 17 billion in cash flow from operations. It will continue to use 40% to 50% for share buybacks and dividends. It is also well positioned in the growing biosimilars market.

Some of the risks with holding Teva shares include: successful introduction of an oral MS

drug by its rivals and/or decline in its Copaxone franchise; a deeper recession in Europe where Teva has a leading market share; and the possibility of incoming CEO Levin not performing to expectations.

At a current price of \$44.55, Teva's shares trade at a 8 times multiple of 2012 consensus earnings of \$5.60, and 7.3 times 2013 consensus earnings of \$6.05. The dividend yield is 2%. The shares are undervalued as we don't believe Teva's current valuation fully reflects its improved outlook, opportunities and growing earnings.

Frank Florio, CFA

MTY Food Group Inc. (MTY-TSX: \$15.25 – 18.95 million shares outstanding)

MTY Food Group ("MTY") is one of Canada's largest quick service franchise companies operating over two dozen brands with over 2,200 locations. MTY operates a number of highly visible and popular brands including Yogen Fruz, Vanellis, Thai Express, Koryo Korean BBQ, Ting-Ming, and Cultures. Its most recent acquisitions are Country Style, Mr. Sub and Jugo Juice. Stanley Ma is the current CEO and has been its largest shareholder since he founded the company in 1983.

MTY has enjoyed continued growth over the last few years, not only in terms of acquisitions but also in terms of its financial performance. 2011 Q3 revenue increased 21.3% year over year to \$19.3 million and EBITDA increased 3.9% to \$7.3. EPS increased 6% to \$.23 and MTY also announced its first quarterly dividend in November of 2010 of \$.045. With no debt on its balance sheet MTY is positioned for future growth.

Historically, MTY has grown through acquisitions. Of the 27 brands operated by the company,

17 were acquired through takeovers. Both Country Style and Mr. Sub were under-performing prior to their recent purchase, however MTY added much desired brand recognition through this transaction due to the popularity of both companies. MTY's experienced management team is confident they can rebrand both companies resulting in a healthy profit. Country Style had 485 locations at the time of purchase with sales of \$94 million, while Mr. Sub had about 335 locations with sales of over \$100 million.

MTY owns and operates less than 2% of individual locations and derives its revenue from franchise fees in the remaining 98%. As a low cost operation MTY creates significant cash flow that can be used for future acquisitions.

Cash flow should continue to increase as a result of expected continued acquisitions through franchise fee payments. This will in turn help to fund future growth through acquisitions resulting in even higher cash flow to fund even further growth.

The outlook for MTY is favorable due to its strong cash flow position and the anticipated positive restructuring of Mr. Sub and Country Style. Short term risks for MTY include risks of an economic downturn and the ever present risk of an unprofitable acquisition. With an average volume of only 5,000 shares per day, MTY remains virtually unknown to investors. This constitutes a potentially positive scenario for the more long-term minded investor but is obviously a concern for those focused on short-term liquidity. Although the food service sector generally fares better than most other sectors during recessions, decreased revenues do result, as evidenced by decreased revenues for MTY during the 2008 recession.

MTY shares currently trade at \$15.25 and have a 52 week range of 17.19 and 12.63. Price to free cash flow is 17.31 which is above the sector average of 3.74. With its strong balance sheet, cash flow and gradually increasing visibility, MTY is a medium term investment with above average potential.

2011 Q4 earnings statements are scheduled to be released on February 16, 2012.

Evan Warsh



Performance Comparisons

Indices	4th quarter '11	2011	
S&P TSX Composite	2.85%	-11.07%	
DJIA	11.95%	5.71%	
S&P 500	11.15%	0.00%	
DEX Mid-Term Bond Index	1.96%	10.85%	
FPX Growth Index	2.67%	-1.71%	
US\$ per C\$	-2.95%	2.35%	

Indices	Dec. 31, '10	Sept. 30, '11	Dec. 30, '11
S&P TSX Composite	13443.22	11623.84	11995.09
DJIA	11557.51	10913.38	12217.56
S&P 500	1257.64	1131.42	1257.60
DEX Mid-Term Bond Index	827.24	899.41	917.00
FPX Growth Index	2602.26	2491.19	2557.74

Commodities (U.S.\$)	Dec. 31, '10	Sept. 30, '11	Dec. 30, '11
Gold	1421.40	1622.30	1566.00
Oil (WTI)	91.55	79.20	98.83
US\$ per C\$	1.0061	0.954	0.983

The opinions expressed in this letter are based upon our analysis and interpretation of information presented and, where applicable, are not to be construed as a solicitation or offer to buy or sell the securities mentioned herein. Certain particulars contained in this letter were obtained from sources which we believe

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