

MALACHITE AGGRESSIVE PREFERRED FUND

Monthly Report, April 2002

It was a good, solid month for MAPF, with a total return before fees of 1.22% in a month during which preferred shares as a class had a return of essentially zero. Trading activity during the month was higher than usual, reflecting the implementation of a revised analytical methodology which extensive back-testing has shown should result in improved performance over the long term.

Month	MAPF Total Return*	NB-50 Total Return	<i>The "NB-50" is an index of preferred shares proprietary to BMO Nesbitt Burns. It is composed of 50 issues having good liquidity and credit quality.</i>
May 2001	-0.20%	-0.66%	
June	+2.56%	-0.62%	
July	+1.40%	+0.48%	
August	+1.74%	+1.13%	
September	+4.20%	+0.51%	
October	+1.25%	-0.06%	
November	-0.81%	+0.98%	
December, 2001	-2.54%	-0.14%	
January, 2002	+5.43%	+2.01%	
February	+1.16%	+0.17%	
March	-0.08%	-2.16%	
April, 2002	+1.22%	-0.63%	
Last 12 Months	+16.17%	+0.95%	
<i>*MAPF total returns include reinvestment of dividends and are after fund expenses but prior to management fees. They are shown for illustrative purposes only and future returns are not assured.</i>			

New issues of shares during the month included Weston 5.15% (WN.PR.B), retractible into a set market value of common shares commencing in April, 2009; Canadian Imperial Bank of Commerce 6.0% redeemable perpetuals (CM.PR.C), and Brascan redeemable preferred securities, 8.30%, maturing in 2051 (BNN.PR.T). It is fascinating to note that Weston was able to issue its shares with such a low dividend, but the following comparison of "curve prices" helps explain matters:

TSE Ticker Symbol	Bid Price, 2002-04-30	Curve Price, 2002-04-30*
CM.PR.C	24.85	25.45
WN.PR.A	24.55	23.85
WN.PR.B	25.20	25.37
<i>*Calculated for investor in Ontario's highest marginal tax bracket. The "curve price" applies the self-consistent yield curve to all expected cash flows from the instrument, after accounting for the effects of options and yield spreads.</i>		

The yield curve was relatively quiet during April, shifting upwards in a more-or-less parallel fashion. While credit spreads widened this change was mild and accounts for the relatively narrow spread of total returns posted by individual issues during the month. The increase in the prime rate occurring in mid-month did not have a great effect; floating-rate issues outperformed slightly but also became a touch more expensive relative to the yield curve.

Curve Attribute	March 28, 2002 (After Tax Figures)	April 30, 2002 (After Tax Figures)
Base Rate	3.29%	3.42%
Short Term Premium	-3.60%	-3.60%
Short Term Decay Time	4.1 Years	4.5 Years
Long Term Premium	1.44%	1.44%
Long Term Decay Time	23.6 Years	21.4 Years
Interest Income Spread	0.65%	0.62%
Cumulative Div. Spread	-0.23%	-0.25%
Split-Share Spread	0.27%	0.35%
Retractability Spread	-0.50%	-0.50%
Floating Rate Spread	-1.50%	-1.59%
2 nd Tier Credit Spread	0.43%	0.50%
3 rd Tier Credit Spread	0.95%	1.01%
“High” Credit Spread	-0.29%	-0.28%
“Low” Credit Spread	0.00%	0.00%
<i>Note: Figures for March have changed somewhat from the previous report. This is due to additions of data.</i>		

All these various specifications of the structure of the yield curve are used in

calculation of the “Curve Price” for each instrument by discounting expected cash flows at appropriate rates. A comparison of the “Curve Price” to the actual market price of the instrument then serves as an indicator of whether the particular instrument should be considered “rich” or “cheap” in comparison with its peers.

Curve Price is also used in a reiterative fashion when determining the projected level of floating rate dividends to be paid by instruments which pay dividends at some proportion of the prime rate, that proportion being determined by the average market price of the instrument over some period. As an example of this, consider the rather complicated issue BCE.PR.Y, which is not susceptible to simple analysis. Briefly, the terms of this issue as disclosed in the prospectus dated December 10, 1997 are:

- Dividends will be paid at an annual rate of \$1.15 per share, quarterly until December 1, 2002.
- From December 1, 2002, the dividend rate will float, commencing with a rate equal to 80% of the Canadian Prime Rate.
- This proportion, initially 80%, will be adjusted monthly: upwards if the Calculated Trading Price (CTP) is less or equal to \$24.875; downwards if the CTP is greater than or equal to \$25.125, subject to...
- The maximum monthly adjustment is $\pm 4.00\%$ of prime; the maximum rate after adjustment is 100% of prime; the minimum rate after adjustment is 50% of prime.

Clearly, the intent of the issuer is to provide some assurance to the purchaser of these shares that the market price of the shares will always be reasonably close to their par-value; which is much the same as saying that the proportion of prime paid will always be reasonably competitive with new issues of floating rate preferreds.

This reasoning can break down when the yield curve is extraordinarily steep, as is the case now (BCE.PR.Y finished the month quoted at \$23.50-75) ... but how may an investor determine analytically what the expected dividend payments will be?

Hymas Investment Management calculates the “Curve Price” of BCE.PR.Y daily, using a dividend rate obtained from the previous day’s analysis (the initial rate is based on the “fixed” rate paid for the first five years). The current proportion is adjusted by an amount dependant upon the difference between “Curve Price” and par, subject to the minimum and maximum – it is assumed that the Prime Rate will not change in the future. Having calculated the expected amounts of all future dividend payments, analysis may proceed similarly to the analysis of other instruments.

Risk Factor	Returns for “True” (Pre-Tax)	Returns for “False” (Pre-Tax)
Retractable	0.16%±1.35%	-0.45%±2.94%
Split Share Corp	0.13%±1.15%	-0.12%±2.28%
Cumulative Dividends	0.07%±1.65%	-0.30%±2.71%
Payments are Dividends	-0.09%±2.23%	-0.01%±1.21%
Floating Rate	0.03%±3.70%	-0.12%±1.44%
Credit Class 2	-0.10%±1.50%	-0.07%±2.67%
Credit Class 3	0.35%±2.13%	-0.14%±2.15%
Credit Class Modifier “High”	-0.06%±2.14%	-0.09%±2.16%
Credit Class Modifier “Low”	0.02%±1.38%	-0.22%±2.84%

April was a relatively quiet month for differences between the various risk groups. Retractable issues outperformed significantly, as did the weaker credits comprising “Class Three”.

TSE Ticker Symbol	Total Return, April 2002	Remarks (Valuation commentary based on Ontario’s highest marginal tax rate)
NTL.PR.G*	-17.12%	Nortel downgraded yet again by DBRS, now is 5 th tier credit
BT.PR.E	-4.25%	Very low volume, credit class 3
GT.PR.A	-3.18%	Credit class 3, split share: hit by telecom weakness
BCE.PR.A	-3.10%	Fixed floater (floats in 2007), credit class 2; attractive at \$23.45-75
NSI.PR.D	-2.76%	Credit class 2; reasonably priced at \$25.67-00.
...
BBD.PR.B	+2.72%	Floating rate, credit class 2
CM.PR.N	+2.98%	Credit class 1, retractable into common.
BC.PR.B*	+3.80%	Floating rate, credit class 2
TFC.PR.C	+3.88%	Floating rate, credit class 3, low volume; quite expensive at \$18.45-60
NSI.PR.C	+4.76%	Credit class 2, low volume, expensive at \$25.77-00

*indicates that the issue was also on last month’s best/worst performers table

James Hymas
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BCE.PR.Y Period (inclusive) from 2000-12-29 to 2002-04-30

Tax Identifier: 7

X-Axis: Date

Ratchet Yield : Spot Rate

Y-Axis: Yield as Fraction

This graph shows the floating dividend rate presumed in the analysis.

