

Canada Core Pick List

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The Canadian Core Buy List couldn't keep up the blistering pace of outperformance posted in June, and fell 0.5% in July. This is well below the positive 0.5% total return generated by the S&P/TSX 60 index. Thankfully, the overall returns since inception (Jan. 1, 2009) remain quite strong, with the Core Buy List posting a 67.9% total return, cumulatively, versus 44.2% for the benchmark index.

The primary culprit this past month was **Bombardier BBD.B**, which fell 10.1% during July. **Thomson Reuters TRI**, **IGM**

Financial IGM, and **Cenovus CVE** were all also in the red, but to a lesser extent. The best-returning stock of the bunch was **Rogers Communications RCI.B**, but its 6.5% gain was not nearly enough to offset the losses elsewhere.

Our model is recommending a couple of changes this month. First, we are adding **Potash Corp POT** back to the Buy list, and it is taking the place of Rogers Communications following Rogers' solid appreciation since last issue. Moreover, we are moving **Enbridge ENB** from the Sell portion of the

The Morningstar Canada Core Pick List Strategy
The Morningstar Canada Core Pick List features our most attractively valued names among larger Canadian companies with sustainable competitive advantages (what we refer to as "economic moats"). These best ideas are further refined into a Consider Buy and a Consider Hold list.

Canada Core Picks

Company	Ticker	Sector	Morningstar Rating	Current Price (CAD)	Fair Value (CAD)	Economic Moat™	Uncertainty Rating	Market Cap (CAD Mil)	Dividend Yield (%)
Consider Buying									
Canadian Natural Resources Ltd	CNQ	Energy	★★★★★	27.35	51.00	Narrow	Medium	30,060.57	1.54
Suncor Energy Inc	SU	Energy	★★★★★	30.66	52.00	Narrow	Medium	47,387.66	1.70
Bombardier Inc	BBD.B	Industrial Materials	★★★★★	3.61	7.00	Narrow	High	6,333.05	2.77
Thomson Reuters Corporation	TRI	Business Services	★★★★	28.44	39.00	Narrow	Medium	23,582.03	4.58
Cenovus Energy, Inc.	CVE	Energy	★★★★	30.65	42.00	Narrow	Medium	23,162.21	2.87
IGM Financial Inc.	IGM	Financial Services	★★★★	39.29	48.00	Wide	Medium	10,048.64	5.47
Valeant Pharmaceuticals International Inc	VRX	Healthcare Services	★★★★	47.80	64.00	Narrow	High	14,624.07	N/A
↑ Potash Corporation of Saskatchewan, Inc.	POT	Industrial Materials	★★★★	44.40	57.00	Wide	High	38,142.75	1.29
Consider Holding									
↑ Enbridge, Inc.	ENB	Energy	★★★★	41.03	46.00	Wide	Low	32,615.54	2.75
↓ Rogers Communications, Inc. Class B	RCI.B	Media	★★★★	39.31	45.00	Narrow	Medium	20,254.28	4.02
Shaw Communications, Inc. Class B	SJR.B	Media	★★★★	19.57	22.00	Narrow	Medium	8,651.97	4.96
Power Corporation Of Canada	POW	Financial Services	★★★★	23.04	28.00	Narrow	High	9,471.52	5.03
Power Financial	PWF	Financial Services	★★★★	24.72	30.00	Narrow	High	17,506.05	5.66
Bank of Montreal	BMO	Financial Services	★★★	57.44	65.00	Narrow	High	37,141.71	4.87
Royal Bank of Canada	RY	Financial Services	★★★	51.38	55.00	Narrow	Medium	74,204.50	4.44
Great-West Lifeco Inc.	GWO	Financial Services	★★★	21.68	23.00	Narrow	High	20,592.11	5.67
Canadian Imperial Bank of Commerce	CM	Financial Services	★★★	73.35	76.00	Narrow	High	29,713.51	4.91
BCE Inc	BCE	Telecommunications	★★★	42.68	43.00	Narrow	Medium	33,028.59	5.08
ARC Resources Ltd.	ARX	Energy	★★★	25.03	23.00	Narrow	High	7,296.63	4.79
TransCanada Corp	TRP	Energy	★★★	45.67	44.00	Narrow	Low	32,172.74	3.85
Canadian National Railway Co	CNR	Business Services	★★★	88.47	80.00	Narrow	Medium	38,466.76	1.70
Consider Selling									
Encana Corp	ECA	Energy	★★	22.34	18.00	Narrow	High	16,448.94	3.59
↓ Canadian Pacific Railway Ltd	CP	Business Services	★★	81.51	70.00	Narrow	Medium	13,993.76	1.72
Talisman Energy Inc	TLM	Energy	UR	12.40	UR	None	High	12,959.82	2.23

All prices as of July 31, 2012. | ↑ = Upgrade, ↓ = Downgrade, * = New Addition

list back up to the Hold portion, following an increase in the company's fair value estimate to \$46 per share from \$37, as well as an upgrade in the economic moat rating to wide. Finally, we are moving **Canadian Pacific CP** down to the Sell portion of the list, thanks to the stock rising to a point where it trades at a greater than 15% premium to its \$70 fair value estimate.

Economic Moat

Morningstar's proprietary measure of the quantifiable, sustainable competitive advantage a company enjoys. All things held equal, we would expect a wide-moat firm to sustain relatively high returns on invested capital for longer than a narrow-moat firm and a narrow-moat firm to sustain relatively high returns on invested capital for longer than a no-moat company.

Uncertainty Rating

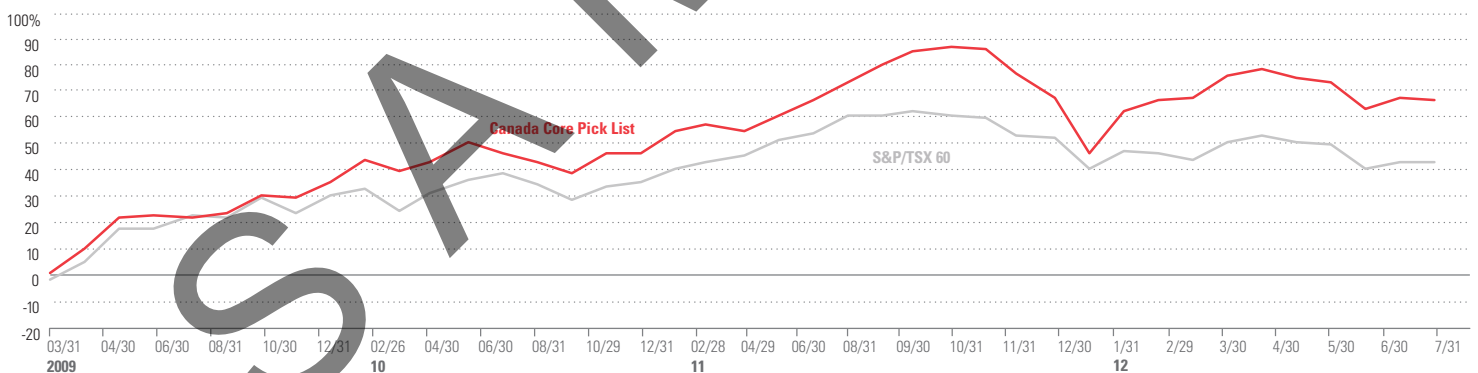
Morningstar's proprietary measure of the degree to which the economic value of a company is uncertain. Three factors go into the uncertainty rating: revenue variability, operational leverage, and financial leverage. The greater each of these measures, the greater the difficulty in bounding the ranges of a fair value for the firm.

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Performance vs. S&P/TSX 60 (%)	This Month	Trailing 12 Months	2009	2010	2011	Since Inception
Core Cons. Buying List	-0.47	-5.7	44.6	12.0	4.2	67.9
S&P/TSX 60	0.50	-6.6	33.9	13.9	-4.9	44.2

Inception: 1 Jan 2009

Total Return: Canada Core Pick List vs. S&P/TSX 60 (%)



A Recap of the Stocks on This Month's Buying List

Canadian Natural Resources remains on the list from last month, and our \$51 fair value estimate is unchanged.

Suncor rose 4% in July, but it remains on the list from last month, thanks to the large discount it trades to our \$52 fair value estimate.

Bombardier was the worst-performing stock in July, down 10.1%. Despite the volatility in the stock price derived from the company's perceived economic sensitivity, our fair value estimate remains \$7, and the company remains on the Core Buy List.

Thomson Reuters remains on the list from last month, and our \$39 fair value estimate is unchanged.

Genovus fell slightly in July, and our fair value estimate is unchanged at \$42 per share. As such, the company remains on the list from last month.

IGM Financial's stock fell slightly in July relative to a steady \$48 fair value estimate. As such, IGM remains on the list from last month.

Valeant Pharmaceuticals remains on the list from last month, and our \$64 fair value estimate remains unchanged.

Potash Corp has been added back to the Consider Buying portion of the list, replacing Rogers Communications. Our fair value estimate for Potash remains \$57.

Rogers Communications appreciated the most on the Consider Buying portion of the list last month. Because of the now-smaller discount to its \$45 fair value estimate, Rogers has been downgraded to the Hold portion of this list.

An Overview of the Canada Core Pick List

The purpose of having a Consider Buy list and a Consider Hold list is to continually surface our best ideas in the Consider Buy list, while allowing users to track what's happened to former Consider Buy picks in the Consider Hold list. A Consider Buy list name "graduates" to the Consider Hold list once it is no longer among the top eight names based on our selection criteria, or once other fundamental factors have necessitated a change in our view of the company.

The Core Consider Buy list only includes Canadian companies with: A market capitalization of greater than CAD 5 billion; Narrow or wide economic moats; A fair value uncertainty that is not very High or extreme.

We keep sector exposure for the Consider Buy list capped at 38%. Because we use an absolute rather than a relative approach to a valuation, there will be times that some sectors have greater representation in the Consider Buy list than others. This is especially true for Canadian stocks, which tend to be concentrated among a few major sectors like financials, energy, and basic materials.

The Morningstar Methodology

The central tenet of the Morningstar approach to equity research is to buy strong businesses at appropriate margins of safety to what they're worth. This is what drives the star rating you'll find in each company report. A 5-star company is one we'd consider undervalued, meaning that its stock price is trading at a discount to its true worth that is greater than the margin of safety we'd need to consider buying it. A 1-star stock is, conversely, overvalued.

Performance Tracking

Morningstar tracks the performance of the Core Consider Buy and the Income Consider Buy lists on a trailing month, year-to-date, and trailing year basis. As more time passes, we'll be able to add longer terms of measurement. To track performance, we began with a fictional \$100,000 invested equally in each stock on the buy lists. At the end of each month, we reinvest the value of the lists (including dividends) back into the new buy list, again with equal weighting.

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