

# 2016

## ANNUAL MANAGEMENT REPORT OF FUND PERFORMANCE

For the year ended December 31, 2016

Offered by Educators Financial Group  
Portfolio Adviser: Foresters Asset Management Inc., Toronto, Ontario

**Educators North American Diversified Fund**



This annual management report of fund performance contains financial highlights but does not contain the complete annual financial statements of the investment fund. You can get a copy of the annual financial statements at your request, and at no cost, by calling 1.800.263.9541, by writing to us at Educators Financial Group, 2225 Sheppard Ave. East, Suite 1105, Toronto, Ontario, M2J 5C2, or by visiting our website at [www.educatorsfinancialgroup.ca](http://www.educatorsfinancialgroup.ca) or SEDAR at [www.sedar.com](http://www.sedar.com).

Securityholders may also contact us using one of these methods to request a copy of the investment fund's interim financial report, proxy voting policies and procedures, proxy voting disclosure record, or quarterly portfolio disclosure.

## MANAGEMENT DISCUSSION OF FUND PERFORMANCE

### Investment Objectives and Strategies

The investment objective of the Educators North American Diversified Fund (the "Fund") is to provide long-term capital growth by investing primarily in common shares of established Canadian corporations and other equity securities. The Fund's holdings will normally be at least 65% in large cap stocks, and non-Canadian securities are limited to no more than 49% of the Fund's assets. Foreign currency exposure may or may not be hedged.

### Risk

The risks of investing in the Fund remain as discussed in the Simplified Prospectus. No changes affecting the overall level of risk of investing in the Fund were made to the Fund in the one-year period ending December 31, 2016.

### Results of Operations

For the twelve-month period ending December 31, 2016, the Fund provided a return of 8.73%, versus a Benchmark return of 17.40%. The Benchmark comprises 55% S&P/TSX Composite Total Return Index, 40% S&P 500 Total Return Index (U.S.\$) and 5% MSCI 1750 U.S. Small Cap Index (the "Benchmark"). Note that investors cannot invest in the Benchmark without incurring fees, expenses and commissions which are not reflected in Benchmark returns.

The Fund's net assets increased by 1.5% to \$95.9 million at the end of December 2016, down from \$94.5 million at the end of December 2015.

The Fund underperformed the Benchmark over the period, primarily due to its positioning in the Materials and Energy sectors, which generally benefitted from the rebound in commodity prices. However lower-quality, high-beta stocks, many of which do not meet the Fund's investment criteria, was the best performers. As a result, the Fund was underexposed to these securities, when compared to the Benchmark.

At the end of the fourth quarter, the Fund was positioned with 57.6% in Canadian equities, 40.7% in U.S. equities (including 2.5% in U.S. small-cap equities), and 1.7% in cash. In response to improving fundamentals in Energy and other resource-oriented sectors, the weight of these sectors was increased during the year. As a result, the Fund's U.S. equity allocation was reduced to a slight underweight position relative to its Benchmark, as these sectors are better represented in the Canadian market.

The Fund seeks to minimize its exposure to currency fluctuations between U.S. and Canadian dollars. To accomplish this, the Fund has held a forward contract to hedge its foreign currency exposure to movements in the U.S. dollar since early 2013. Following three years of significant appreciation against the Canadian dollar, the U.S. dollar stabilized during 2016, and weakened by 3.2% against the Canadian dollar during the year. As a result, the value of the currency forward contract increased in value over the course of the year, consistent with its function to offset exchange rate fluctuations.

Following a period of significant volatility in early 2016, the Canadian and U.S. equity markets delivered strong returns for the year, as a result of rising commodity prices, solid economic data, and improving corporate earnings. In addition, interest rates and high-beta cyclical stocks appreciated strongly following the U.S. presidential election, due to expectations that potentially significant fiscal stimulus and other pro-business policies would be implemented with the incoming administration.

Globally, the S&P/TSX Composite Index was one of the best performing equity indices during 2016, with an impressive 21.1% total return for the year, led by strong advances in the Materials, Energy, Industrials, and Financials sectors. The relatively small Health Care sector was the only negative performer over the year.

After five years of consistently outperforming Canada, the U.S. stock market underperformed during 2016, with

the S&P 500 Total Return Index advancing by 12.0%, in U.S. dollar terms and 8.8% in Canadian dollar terms. As in Canada, U.S. equities benefited from strong performance in the more cyclically-oriented Energy, Financials, Industrials and Materials sectors. Health Care was the only sector with a modest negative return for the year.

For added diversification, the Fund includes an allocation of the Vanguard U.S. Small-Cap Exchange Traded Fund (VB), which returned 18.3% in U.S. dollars, over the period.

Among the Canadian and U.S. large cap holdings, the Fund was selectively overweight in the Information Technology, Consumer Staples, Consumer Discretionary, and Health Care sectors, while more neutrally positioned towards Energy, Industrials, Utilities and Real Estate. The Fund remained underweight in the highly volatile Materials sector, as well as the Telecommunications and Financials sectors, due to their respective subdued growth outlook and challenging regulatory environments in both Canada and the U.S.

In 2016, the Fund benefitted from good stock selection within the Health Care sector, which helped offset the negative impact from the Fund's overweight position in the sector, which was a weak performer in 2016. Overall, sector returns reflected a string of negative headlines during the U.S. presidential campaign, due to heightened uncertainty surrounding potential changes to policies and regulations. In addition, as commodity prices rebounded, market participants reallocated away from defensive sectors such as Health Care, towards more cyclically-oriented, high-beta sectors such as Materials. The portfolio manager continues to view the growth outlook, cash generation potential and stock valuations of the Fund's Health Care selections as compelling, resulting in an attractive prospective upside going forward.

The Fund also benefited from good stock selection in the Consumer Discretionary sector, where one of the Fund's holdings was acquired by a competitor at a significant premium, while several of the holdings in the Media, Retail and Restaurant sector delivered strong growth momentum and stock performance throughout the year.

The Fund was negatively impacted by its underweight position in Materials, as well as unfavourable stock selection in both the Energy and Materials sectors. These sectors were two of the strongest performers for the year, as a result of a significant rebound in the price of oil, coal, base metals and other commodities. However, the gains were primarily led by lower-quality,

high-beta stocks, which typically do not meet the Fund's investment criteria. Given the portfolio manager's expectations of further volatility in these sectors going forward, the Fund remains focused on high-quality companies with strong fundamentals. As improved conditions across commodity markets translate into stronger profitability, cash flows, and balance sheets, the portfolio manager will continue to look for attractive opportunities to add exposure.

The Financials sector was another significant detractor, as the Fund was underweight in banks and life insurers in both Canada and the U.S., a conscious decision based on expectations of a continued benign interest rate environment and onerous regulations following a potential Hillary Clinton presidential win. However, the surprising Republican sweep led by Donald Trump resulted in a rapid reset of market expectations towards significantly reduced regulations and corporate taxes, as well as rising interest rates. As a result, North American financials performed well following the U.S. election, to end the year as one of the best performing sectors. As U.S. policy direction becomes clearer, the Fund will continue to selectively add to its Financials exposure based on the sector's improved outlook

### **Recent Developments**

Despite a volatile start for 2016, equity markets in both Canada and the U.S. posted strong positive returns for the year, supported by a significant rebound in commodity prices. While global growth was slower than expected, the portfolio manager expects growth to remain positive, led by the U.S. economy. However, political uncertainty has increased, as a result of the recent Brexit vote, as well as significant changes that potentially may be introduced by the newly elected Trump administration.

Supported by the consistently strong U.S. job market and other economic data, combined with a recent increase in inflation expectations, the Federal Open Market Committee (FOMC) announced its widely anticipated second interest rate hike in December 2016. In addition, there is an increased probability of between two and four additional FOMC rate hikes in 2017, particularly if the U.S. economy demonstrates further strength. Globally, central banks have maintained highly accommodative monetary policies, which reduce the probability of a widespread recession. The rising acceptance of increased fiscal spending in a number of countries may provide further support to global economic growth.

The portfolio manager believes that, given macro-economic factors, North American markets will continue

to experience significant volatility during 2017. These challenging conditions underscore the importance of an appropriately diversified and actively managed portfolio to help navigate through the current environment.

Relative to the Benchmark, the Fund has reduced its exposure to U.S. equities, while establishing a slightly overweight position in Canadian equities, which provide a better selection of resource-oriented names. At the same time, its exposure to U.S. equities enables the Fund to reap the benefits of potential higher growth and better diversification from sectors that the portfolio manager believes are under-represented in the Canadian marketplace. Across both the Canadian and U.S. holdings, the primary focus of the Fund remains the active management of large cap equities, with a blend of growth and dividend income oriented companies. The portfolio manager continues to pursue investment opportunities in sectors with high-quality companies demonstrating above-average growth prospects, strong balance sheets and reasonable valuations.

#### **Caution Regarding Forward-looking Statements**

This report may contain forward-looking statements about the Fund, including its strategy, expected performance and condition. Forward-looking statements include statements that are predictive in nature, that depend upon or refer to future events or conditions, or that include words such as “expects”, “anticipates”, “intends”, “plans”, “believes”, “estimates” or negative versions thereof and similar expressions.

In addition, any statement that may be made concerning future performance, strategies or prospects, and possible future Fund action is also a forward-looking statement. Forward-looking statements are based on current expectations and projections about future events and are inherently subject to, among other things, risks, uncertainties and assumptions about the Fund and economic factors.

Forward-looking statements are not guarantees of future performance, and actual events and results could differ materially from those expressed or implied in any forward-looking statements made by the Fund. Any number of important factors could contribute to these digressions, including, but not limited to, general economic, political and market factors in North America and internationally, interest and foreign exchange rates, global equity and capital markets, business competition, technological change, changes in government regulations, unexpected judicial or regulatory proceedings, and catastrophic events.

It should be stressed that the above-mentioned list of factors is not exhaustive. You are encouraged to consider these and other factors carefully before making any investment decisions and you are urged to avoid placing undue reliance on forward-looking statements. Further, you should be aware of the fact that the Fund has no specific intention of updating any forward-looking statements, whether as a result of new information, future events or otherwise, prior to the release of the next Management Report of Fund Performance.

#### **Related Party Transactions**

On May 14, 2016, Foresters Financial, through Foresters Life Insurance Company, acquired 100 percent of the shares of Aegon Capital Management Inc.) and was renamed Foresters Asset Management Inc. (“FAM”)., FAM the Fund’s Portfolio Adviser, is an indirect wholly-owned subsidiary of The Independent Order of Foresters, which is not a publicly listed company.

In 2016 Educators Financial Group did not refer any conflict of interest matters to the Fund’s Independent Review Committee (IRC) and accordingly did not rely upon any recommendation of the IRC in respect of any related party transactions.

Educators Financial Group is the Manager and Trustee of the Fund. Educators Financial Group is a wholly-owned subsidiary of the Ontario Secondary School Teachers’ Federation (“OSSTF”). OSSTF may from time to time invest in units of the Fund.

## FINANCIAL HIGHLIGHTS

The following tables show selected key financial information about the Fund and are intended to help you understand the Fund's financial performance for each year ended December 31 for the past five years.

### The Fund's Net Assets per Unit <sup>(1)</sup>

	Year ended December 31				
	2016	2015	2014	2013	2012
Net Assets, beginning of year	\$18.56	\$19.13	\$17.81	\$15.04	\$14.45
<b>Increase (decrease) from operations:</b>					
Total revenue	\$0.40	\$0.43	\$0.43	\$0.38	\$0.38
Total expenses, including transaction costs [excluding distributions]	\$(0.41)	\$(0.42)	\$(0.41)	\$(0.34)	\$(0.29)
Realized gains (losses) for the period	\$0.94	\$0.12	\$1.20	\$1.42	\$(0.07)
Unrealized gains (losses) for the period	\$0.67	\$(0.68)	\$0.09	\$1.32	\$0.56
<b>Total increase (decrease) from operations <sup>(2)</sup></b>	<b>\$1.60</b>	<b>\$(0.55)</b>	<b>\$1.31</b>	<b>\$2.78</b>	<b>\$0.58</b>
<b>Distributions:</b>					
From net investment income (excluding dividends)	\$--	\$--	\$--	\$--	\$--
From dividends	\$--	\$--	\$--	\$0.01	\$--
From capital gains	\$--	\$--	\$--	\$--	\$--
Return of capital	\$--	\$--	\$--	\$--	\$--
<b>Total Annual Distributions <sup>(3)</sup></b>	<b>\$--</b>	<b>\$--</b>	<b>\$--</b>	<b>\$0.01</b>	<b>\$--</b>
<b>Net Assets , end of year</b>	<b>\$20.18</b>	<b>\$18.56</b>	<b>\$19.13</b>	<b>\$17.81</b>	<b>\$15.03</b>

<sup>(1)</sup> This information is derived from the Fund's audited annual financial statements. For the financial year beginning after January 1, 2014, the financial highlights were derived from the Fund's financial statements prepared in accordance with International Financial Reporting Standards ("IFRS"). For the financial year ended December 31, 2013, the financial highlights numbers were restated to comply with IFRS reporting. For financial years beginning before January 1, 2013, the financial highlights were derived from the Fund's financial statements prepared in accordance with Canadian GAAP. For financial years beginning after January 1, 2013, all references to "Net Assets" or "Net Assets per Unit" in these financial highlights are references to net assets attributable to holders of redeemable units determined in accordance with IFRS as presented in the financial statements of the Fund.

<sup>(2)</sup> Net assets and distributions are based on the actual number of units outstanding at the relevant time. The increase/decrease from operations is based on the weighted average number of units outstanding over the financial period. This table is not intended to be a reconciliation of beginning to ending net assets per unit.

<sup>(3)</sup> Distributions were either paid in cash or reinvested in additional units of the Fund.

### Ratios and Supplemental Data (based on Net Asset Value)

	Year ended December 31				
	2016	2015	2014	2013	2012
Total Net Asset Value (000's) <sup>(1)</sup>	\$95,876	\$94,454	\$101,688	\$93,476	\$79,742
Number of units outstanding <sup>(1)</sup>	4,750,945	5,089,059	5,316,626	5,249,793	5,302,458
Management expense ratio <sup>(2)</sup>	1.93%	1.93%	1.93%	1.90%	1.90%
Management expense ratio before waivers or absorptions <sup>(3)</sup>	1.98%	1.98%	1.98%	1.98%	1.98%
Trading expense ratio <sup>(4)</sup>	0.11%	0.15%	0.15%	0.21%	0.09%
Portfolio turnover rate <sup>(5)</sup>	70.96%	64.04%	97.70%	135.21%	41.21%
Net Asset Value per unit	\$20.18	\$18.56	\$19.13	\$17.81	\$15.04

<sup>(1)</sup> This information is provided as at December 31 of the year shown.

<sup>(2)</sup> Management expense ratio is based on total expenses (excluding [distributions], commissions and other portfolio transaction costs) for the stated period and is expressed as an annualized percentage of daily average net asset value during the period.

- (3) The management expense ratio before waivers or absorptions shows what the management expense ratio of the Fund would have been if Educators Financial Group had not charged a lesser amount for its management fee.
- (4) The trading expense ratio represents total commissions and other portfolio transaction costs expressed as an annualized percentage of daily average net asset value during the period.
- (5) The Fund's portfolio turnover rate indicates how actively the Fund's portfolio adviser manages its portfolio investments. A portfolio turnover rate of 100% is equivalent to the Fund buying and selling all of the securities in its portfolio once in the course of the year. The higher a fund's portfolio turnover rates in a year, the greater the trading costs payable by the fund in the year, and the greater the chance of an investor receiving taxable capital gains in the year. There is not necessarily a relationship between a high turnover rate and the performance of a fund.

## Management Fees

Educators Financial Group is the Manager-Trustee, promoter and principal distributor of the Fund, and is responsible for the day-to-day management and administration of the Fund.

The Manager-Trustee monitors and evaluates the performance of the Fund, and pays for the investment management services of the portfolio adviser, as well as all administrative services required by the Fund. As compensation for these services, Educators Financial Group is entitled to receive a fee, payable monthly and calculated daily, based on the Net Asset Value of the Fund, at the annual rate of 1.75%.

The Fund is responsible for paying any applicable tax owing on its management fee.

Approximately 9.8% of the management fees were used to pay for portfolio management services, with the remainder of the fees allocated to custodial services, marketing, technology and Manager-Trustee operating expenses.

## PAST PERFORMANCE

### General

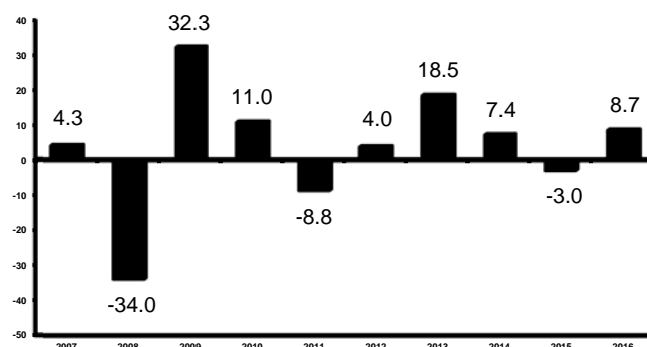
The Fund's performance information shown assumes that all distributions made by the Fund in the periods shown were reinvested in additional units of the Fund.

The performance information does not take into account sales, redemption, distribution or other optional charges that would have reduced returns or performance. Please remember that how the Fund has performed in the past does not necessarily indicate how it will perform in the future.

### Year-by-Year Returns

The bar chart shows the Fund's performance for each of its past 10 financial years and illustrates how the Fund's performance has changed for each 12-month period ending December 31. The chart shows, in percentage terms, how much an investment made on the first day of

each financial period would have grown or decreased by the last day of each financial period.



## Annual Compound Returns

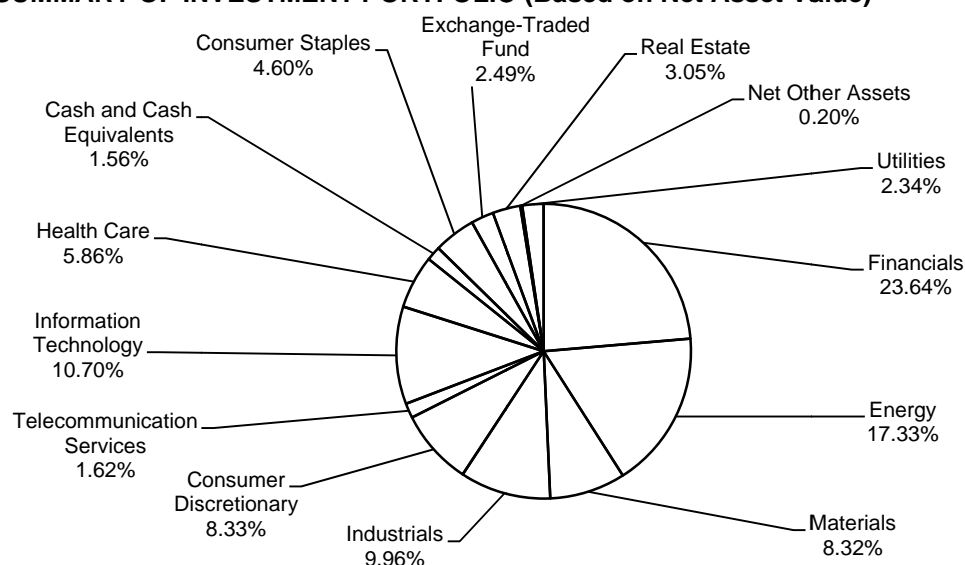
The following table compares the historical annual compound returns of the Fund with the performance of the blended Benchmark index comprised as follows: 55% S&P/TSX Composite Total Return Index (S&P/TSX Index), a capitalization-weighted index designed to measure the market activity of some of the largest float adjusted stocks listed on the Toronto Stock Exchange, 40% S&P500 Total Return Index (U.S.\$), a stock market index based on the market capitalizations of 500 large companies having common stock listed on the New York Stock Exchange and 5% MSCI 1750 U.S. Small Cap Index (MSCI Index), made up of a universe of small capitalization companies in the U.S. equity market.

	Educators Diversified Fund (%)	S&P/ TSX Index (%)	S&P500 Index (U.S.\$) (%)	MSCI Index (%)	Blended Index (%)
Past 10 years	2.54	4.72	8.47	9.76	5.50
Past 5 years	6.90	8.25	21.21	21.56	11.57
Past 3 years	4.26	7.06	17.67	15.65	7.89
Past year	8.73	21.08	8.62	16.25	17.40

The Benchmark returns do not include any costs of investing. See Management Discussion of Fund Performance for a discussion of performance relative to the Benchmark.



## SUMMARY OF INVESTMENT PORTFOLIO (Based on Net Asset Value)



## Top 25 Holdings

Security Name	Percentage of Net Asset Value
Royal Bank of Canada	3.84%
Toronto-Dominion Bank	3.53%
Bank of Nova Scotia	2.65%
Suncor Energy Inc.	2.54%
Vanguard Small-Cap ETF	2.49%
JPMorgan Chase & Co.	1.98%
Canadian National Railway Co.	1.97%
Canadian Natural Resources Ltd.	1.78%
Agnico Eagle Mines Ltd.	1.77%
Enbridge Inc.	1.74%
Bank of Montreal	1.72%
TransCanada Corp.	1.70%
Canadian Pacific Railway Ltd.	1.46%
CGI Group Inc., Class A	1.45%
Alphabet Inc.	1.33%
Brookfield Asset Management Inc.	1.30%
Apple Inc.	1.25%
Manulife Financial Corp.	1.14%
Pembina Pipeline Corp.	1.12%
Intercontinental Exchange Inc.	1.10%
BCE Inc.	1.07%
BlackRock Inc.	1.07%
Simon Property Group Inc.	1.07%
Amazon.com Inc.	1.05%
Franco-Nevada Corp.	1.05%
<b>Total Net Assets (000's)</b>	<b>\$95,876</b>

The top 25 holdings represent approximately 43.17% of the total net assets of the Fund.

The summary of investment portfolio of the Fund is as at December 31, 2016 and may change due to the Fund's ongoing portfolio transactions. Updates are available quarterly.

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