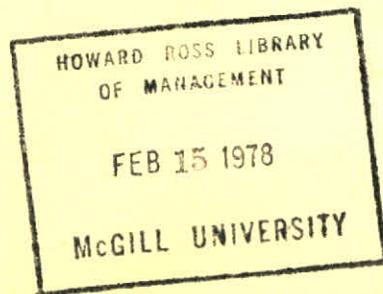


4

Fourth  
Quarter Report  
Diversified  
Investment Funds  
Oct. 1 to  
Dec. 31, 1977



## International Trust Company

International Trust Company has the same broad powers as any Canadian trust company. It has however, elected to confine its activities almost exclusively to Asset Management.

The Company provides Asset Management to institutional and individual investors. Asset Management includes investment management, trustee and custodian services and fulfillment of the fiduciary responsibilities inherent therein.

## The Diversified Investment Funds

The Diversified Investment Funds were established January 1, 1967 and are operated for the collective investment and reinvestment of tax-sheltered monies. The Funds are fully managed by International Trust Company and consist of four separate investment portfolios: the Fixed Income Fund; the Mortgage Fund; the Canadian Equity Fund; and the International Equity Fund.

Additions to, or withdrawals from, each Fund, or inter-Fund transactions, are effected on monthly valuation dates at net asset value. Income earned is distributed monthly.

This report is concerned primarily with investment composition and performance.

# The Background For Investment

## Economic Outlook

### Canada

Economic Forecast			
	1976	1977E	1978E
Real GNP % Chg.	4.9	2.5	4.0
Unemployment Rate	7.2	8.1	8.3
Housing Starts	273	240	240
Real Business Investment % Chg.	-3.1	0.8	2.0
Corporate Profits Before Tax % Chg.	-0.3	10.0	10-12
CPI	7.5	8.0	8.0
Exchange Rate on \$US (average)	1.013	.938	.90-.92

Modest improvement in real economic growth to about 4% is indicated for 1978 over the 2.5% estimated gain in 1977.

In the latest published data, the 1977 third quarter showed a gratifying ability to bounce off the slow pace of the previous period, but again in an unconvincing piecemeal fashion. Real GNP, seasonally adjusted, rose at an annual rate of 5.2% over the earlier quarter with a recovery in consumer expenditures and a material improvement in the balance of trade providing the major thrust. On the other hand business and government capital spending as well as housing remained weak.

Looking ahead there are few signs of dramatic shifts: the current pace of residential construction activity is more than adequate to satisfy the demand for housing; manufacturing capacity is still substantially underutilized; and corporate balance sheets are not much improved over the recession lows of 1975. It is, as well, agonizingly clear that with a \$9 billion federal deficit in prospect for the current fiscal year, Ottawa does not really have options open to stimulate government spending through escalation.

Growth for 1978 will then have to originate in other sectors. Recent favourable retail sales trends and personal tax reductions concentrated in January and February suggest that consumer spending will retain strength into the first quarter of 1978. Overall this sector should provide the bulk of the growth this year particularly if, as we expect, the personal savings rate is not maintained at its currently high level.

An estimated increase in pre-tax corporate profits of 20% in the fourth quarter of 1977, primarily because of the poor profit showing in 1976, would be the highest year over year rate of gain so far in this business cycle. However for the current year we are expecting an improvement of 10% to 12%.

## OECD

While the U.S. was enjoying an upward revised annual rate of growth (quarter to quarter) in third quarter real GNP of 4.7%, the major western European countries and Japan experienced a significant drop in industrial production, continuing the trend in most cases begun in the second quarter. The domestic sectors of the European and Japanese economies have been in a recessionary phase since the

## Economic Forecast

### West Germany

		U.S.	Japan	France	U.K.	West Germany
Real GNP % Chg.	1976	6.1	6.3	5.5	1.7	5.6
	1977E	4.9	6.0	3.0	1.0	3.0
	1978E	4.0	5.5	4.0	3.0	4.0
Inflation-CPI % Chg.	1976	5.7	9.3	9.6	16.6	4.5
	1977E	6.5	8.0	9.0	15.0	4.0
	1978E	6.0	7.0	8.5	8.0	4.0
Unemployment Rate	1976	7.8	2.0	4.2	5.4	4.6
	1977E	7.1	1.9	4.5	5.7	4.5
	1978E	7.0	1.9	4.4	5.5	4.4

first quarter of this year, which fully supports the U.S. viewpoint that the other major OECD countries, primarily Japan, have been living off the fat of the U.S. business uptrend. This disequilibrium in growth conditions has been a major factor in the deterioration of the U.S. balance of trade during 1977 and accordingly has helped to depress the external value of the U.S. dollar.

The relative disparity between the U.S. and other major countries' domestic economy growth will likely narrow in 1978 and perhaps even reverse late in the year, causing a favourable shift in the U.S. trade balance. This trend, together with the probable passage of energy conserving legislation, could generate a significant recovery in the U.S. dollar this year. Such a shift would reflect the impact of planned or recently implemented reflationalary moves in Japan and Western Europe which have come partly in response to U.S. complaint, but mainly because of worry about relatively high and rising unemployment.

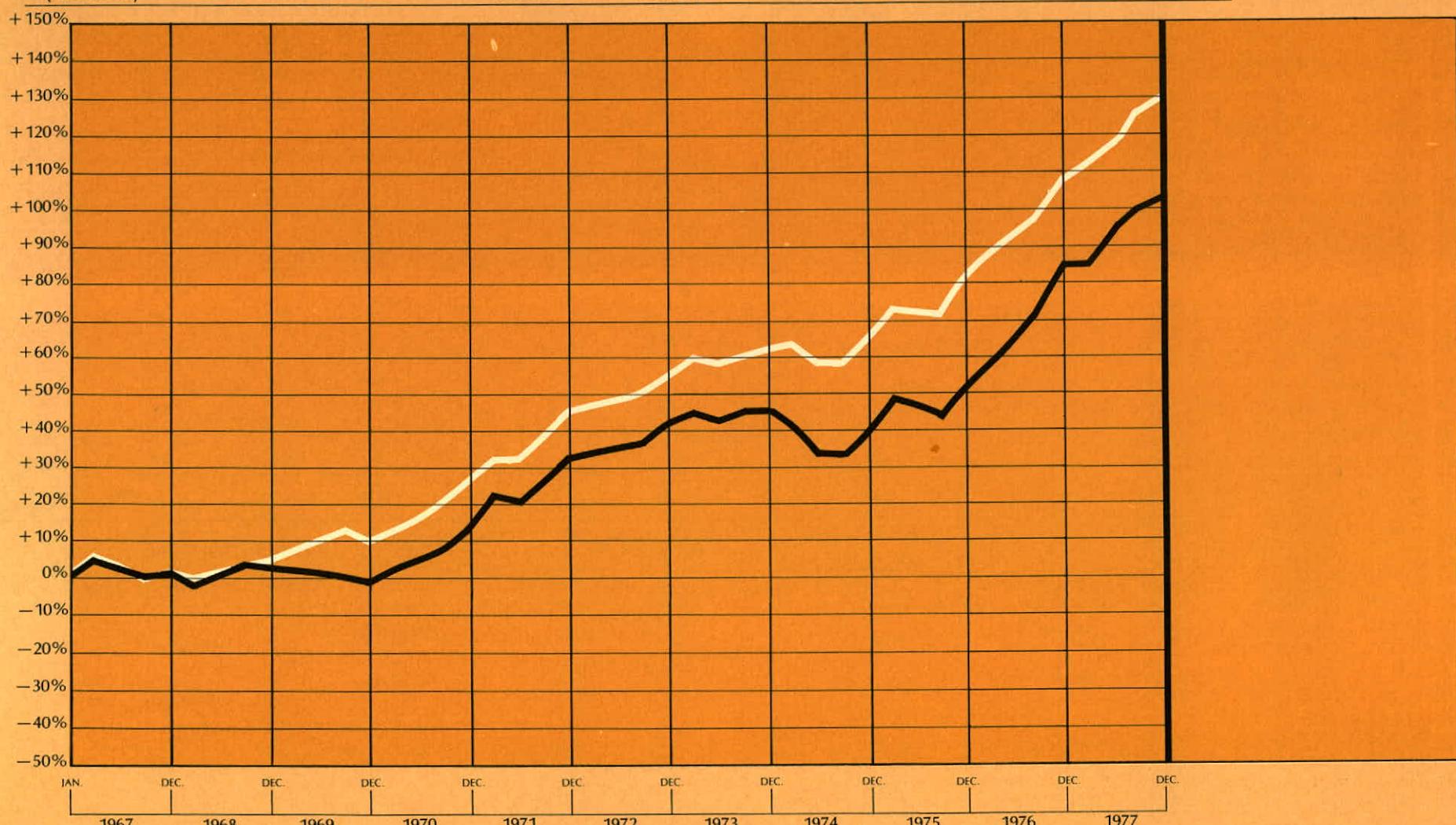
The success of these measures to stimulate demand will be helped by the fact that inflation in these countries last year subsided, in some cases dramatically.

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# Fixed Income Fund

Comparisons between	GRAPH COLOUR	VALUE DEC. 31/77	VALUE SEPT. 30/77	PERCENT CHANGE OVER QUARTER	PERCENT CHANGE YEAR-TO-DATE	COMPOUND ANNUAL RETURN SINCE INCEPTION
Fixed Income Fund		\$ 9.72	\$ 9.73	-0.1%	+0.6%	-0.3%
Fixed Income Fund (Incl. Inc.)	■	23.01	22.55	+2.0%	+9.7%	+7.9%
McLeod Young Weir 40-Bond Index		50.70	51.18	-0.9%	-0.3%	-2.4%
McLeod Young Weir 40-Bond Index (Incl. Inc.)	■	333.35	328.58	+1.5%	+9.7%	+6.6%

Average Yield to Maturity of Fund Assets  
 Sept. 30, 1977 8.91%  
 Dec. 31, 1977 9.02%



# Fixed Income Fund

## Portfolio Statement

Bonds/Convertible Bonds 96% Par Value		Market Value Dec. 31, 1977	Bonds/Convertible Bonds 96% Par Value		Market Value Dec. 31, 1977
\$ 250,000	Govt. of Canada 8% July 1/82	\$ 248,438	\$ 250,000	Hudson Bay Co. Acceptance 8-3/4% Jun. 1/91	\$ 230,000
500,000	Govt. of Canada 4-1/2% Sept. 1/83	419,375	200,000	Hudson Bay Mining & Smelting 9% Jun. 15/91	187,500
1,575,000	Govt. of Canada 9-1/4% May 15/97	1,590,750	750,000	I.A.C. 10-1/4% July 30/83	783,750
500,000	Alberta Govt. Telephone 9.90% Oct. 1/79	515,000	300,000	I.A.C. 9% Mar. 1/84	301,500
250,000	Hydro Elec. Pwr. Comm. of Ont. 9-3/4% Aug. 15/81	261,875	300,000	John Labatt 9-1/4% Sept. 1/90	297,000
1,025,000	Hydro Elec. Pwr. Comm. of Ont. 10% May 18/01	1,078,812	200,000	John Labatt 9% Mar. 15/94	192,000
450,000	Manitoba Telephone System 7-7/8% Nov. 15/91	410,062	300,000	Molson Industries 8-1/4% Nov. 1/91	273,375
325,000	Nfld. and Lab. Hydro 10% May 9/02	325,000	98,000	Niagara Realty 10-3/8% Dec. 18/84	103,390
500,000	Nova Scotia Pwr. Comm. 9-1/4% July 21/02	492,500	300,000	Niagara Realty 9-1/2% Jan. 30/84	306,000
850,000	Prov. of Ontario 9% July 1/98 Prepay July 1/83	873,375	350,000	Noranda Mines 9-1/4% Oct. 15/90	193,500
325,000	Prov. of Quebec 8-5/8% Mar. 1/99	293,719	350,000	Olympia & York Dev. 10-1/2% Oct. 31/79	242,685
300,000	Prov. of Sask. 7-3/4% Feb. 17/82	294,375	600,000	Olympia & York Dev. 9% Mar. 1/90 ret. 8-3/4% /82	300,000
250,000	Prov. of Sask. 8-1/4% Dec. 3/98	229,062	400,000	Royal Bank of Canada 9% Jun. 1/87	352,625
250,000	Prov. of Sask. 9-7/8% Nov. 3/00 Prepay Nov. 3/83	267,500	600,000	Roynat 9% Mar. 1/80	351,750
300,000	Abitibi Pulp & Paper 10-1/2% Mar. 1/95 Prepay Mar. 1/85	315,000	225,000	Seagram 9-1/2% Jun. 1/80	612,000
400,000	Alum. Co. of Canada 9-3/8% Jan. 2/91	396,500	200,000	Steel Co. Canada 9-1/4% Nov. 1/90	398,000
300,000	Ashland Oil Can. Conv. 5% Jan. 15/93	324,000		TDRI Conv. 5-1/2% Feb. 15/93	200,000
300,000	Ashland Oil Can. 10-3/8% Nov. 1/96	312,750		Tordom Corp. 8-5/8% Jun. 15/82	592,500
200,000	BM-RT 9% Apr. 1/80	201,000		TransCanada Pipe 10% Jun. 20/90	230,062
500,000	BM-RT 10-1/4% Jun. 1/81	516,250		Union Carbide 10-3/4% Jun. 15/95	213,000
200,000	BM-RT 8-3/4% Nov. 1/82	199,250			\$20,447,983
250,000	Bell Canada 9-3/4% Jun. 3/79	255,000			
400,000	Bell Canada 8-3/8% Aug. 1/93	366,000			
600,000	Bell Canada 9-7/8% Apr. 1/99	615,000			
200,000	B.C. Telephone 8-3/4% Jan. 15/81	201,040			
250,000	B.C. Telephone 9-1/4% Apr. 15/98	242,500			
400,000	Calgary Power 11-1/8% Sept. 16/79	416,000			
200,000	CP Limited 11-1/4% Nov. 15/95	218,500			
250,000	Cominco 8-1/2% Apr. 15/91	230,313			
100,000	Consumers Gas 8-3/4% Aug. 15/94	93,500			
250,000	Dominion Stores 9-1/2% Mar. 1/80	255,000			
300,000	First Canadian Investments 9-3/4% Mar. 15/81	306,000			
500,000	First Canadian Investments 10% Dec. 1/81	515,000			
500,000	General Motors Accept. 8-5/8% Feb. 9/79	504,400			
300,000	Hudson's Bay Company 9-3/4% May 1/79	304,500			
Reserve 4%					
Cash & Short Term Notes					
<b>Total Assets at Market Dec. 31, 1977</b>					
<b>\$21,296,736</b>					

### The Fourth Quarter and The Year 1977

The unit value of the Fixed Income Fund decreased by 0.1% in the final quarter of 1977 and increased by 0.6% for the year as a whole. In comparison the McLeod, Young, Weir 40-Bond Index decreased by 0.9% for the quarter and by 0.3% for the year. When income is included, the Fund's unit value increased by 2.0% for the quarter and by 9.7% for the whole year. The comparable McLeod, Young, Weir figures show increases of 1.5% and 9.7% respectively.

Interest rate changes in the fourth quarter were relatively modest but had an upward bias as shown in the following table which includes changes for all of 1977:

	Basis Points				
	31 Dec. 1976	30 Sept. 1977	31 Dec. 1977	Change 4th Q	Change 1977
Money Market	8.12%	7.25%	7.20%	— 5	— 92
Mid term Provincials	8.15	8.20	8.35	+ 15	+ 20
Mid term Corporates	9.25	8.85	8.90	+ 5	— 35
Long term Canadas	8.85	9.00	9.10	+ 10	+ 25
Long term Provincials	9.00	9.15	9.30	+ 15	+ 30
Long term Corporates	9.30	9.50	9.50	0	+ 20

Interest rate changes in the money market were relatively subdued over the quarter with variations ranging only about 25 basis points around their opening level of 7.25%. In general these rates tended to rise for the first 5 or 6 weeks of the quarter, eased down to about the 7% mark over the next few weeks, and then firmed slightly as the year ended to their closing level of about 7.20%. The rise in short rates early in the quarter continued to be the result of our tight banking system as the banks positioned themselves for their October 31st year end and caused dealer inventories to be financed at a negative carry. Another major influence over this period was also our slumping currency as our dollar weakened from its opening level of \$.9315 U.S. to a low of \$.8963 U.S. late in October. This turned out to be the low for the quarter. Also in this period U.S. short term rates were rising and resulted in an October 28th increase of 1/4% in the Re-discount Rate to 6%.

Following the end of October our banks persisted in their tight posture and the growth in monetary aggregates continued to track in the low end of their targeted range. Also the surprising success of the Canada Savings Bond campaign, which raised a net \$2.4 billion, caused some disintermediation to the system which did not ease until after mid November. Over the next 4 weeks short rates eased abruptly to about the 7% mark. The impetus stemmed from a combination of an easier banking system, which meant cheaper inventory financing, and a low level of borrower demand as the year end neared. The stability of our dollar also was a factor although this seemed to come more from the worldwide pressure on the U.S. dollar than from any strength domestically. Some talk of a possible reduction in Bank Rate was heard but this, and the decline in rates, was abruptly halted when the Bank of Canada started to sell into the market as rates showed signs of breaking below 7% as the holidays approached. For the balance of the quarter, short rates drifted higher with banking costs again producing negative carrying spreads.

In the mid-term bond markets interest rates rose modestly over the quarter although both corporate and provincial issues continued to be in good demand. The provincial sector was beset with a number of new issues that were fully priced and were initially only moderately received thereby pushing rates higher. Corporate mid-term issues in the quarter tended to be relatively fewer and more reasonably priced thus receiving better support which is the pattern this sector has shown over the whole year. Also some additional demand in this sector was evident from mortgage investors, unable to get an adequate supply.

The trend of long term interest rates in the past quarter followed that of the other sectors with the rates closing moderately higher. Trade was generally light in the secondary market, and while some year-end demand was evident, the bulk of the activity was confined to the plentiful new issue supply. The large calendar over the quarter was one factor behind the drifting markets. The U.S. market, which weakened appreciably over the period, was also a contributing factor. The weaker Canadian dollar was yet another negative influence on our long markets as were the disappointing inflation numbers received over the three months. The Finance Minister's mini budget in October lent no relief with its forecasts of still higher Federal cash deficits. At times the somewhat gloomy mood of the long markets was relieved by the unexpected success of the Canada Savings Bond sales and by the resumption of borrowings in foreign markets, but overall, the general tone of the markets remained pessimistic.

### Outlook

We expect that interest rates will continue their recent trend and rise in 1978. The magnitude of rate changes will vary by sector, but we feel that all sectors will experience higher rates. In the money market the increases could be of the magnitude of about 75 basis points with the primary causes being our expectation of higher U.S. short rates, our continuing relatively weak currency, and the resolve of our Central Bank to restrain monetary growth.

In the mid-term sector we feel that any rate increases will be quite modest as we expect demand in this area to remain relatively strong. This will be helped by traditional mortgage investors unable to find an adequate supply of product, turning to the mid-term bond market as a haven for their funds without the yield sacrifice involved in the money market.

We feel that long term interest rates will rise with an average increase amounting to about 30 basis points. The main factor behind this trend is our belief that while inflation should subside modestly in 1978, the bond market has already discounted this event and may have anticipated lower inflation numbers than will be seen this year. Also, U.S. interest rates will rise as their economic expansion continues, and borrowing demands will be higher in all of our market sectors.

### Strategy

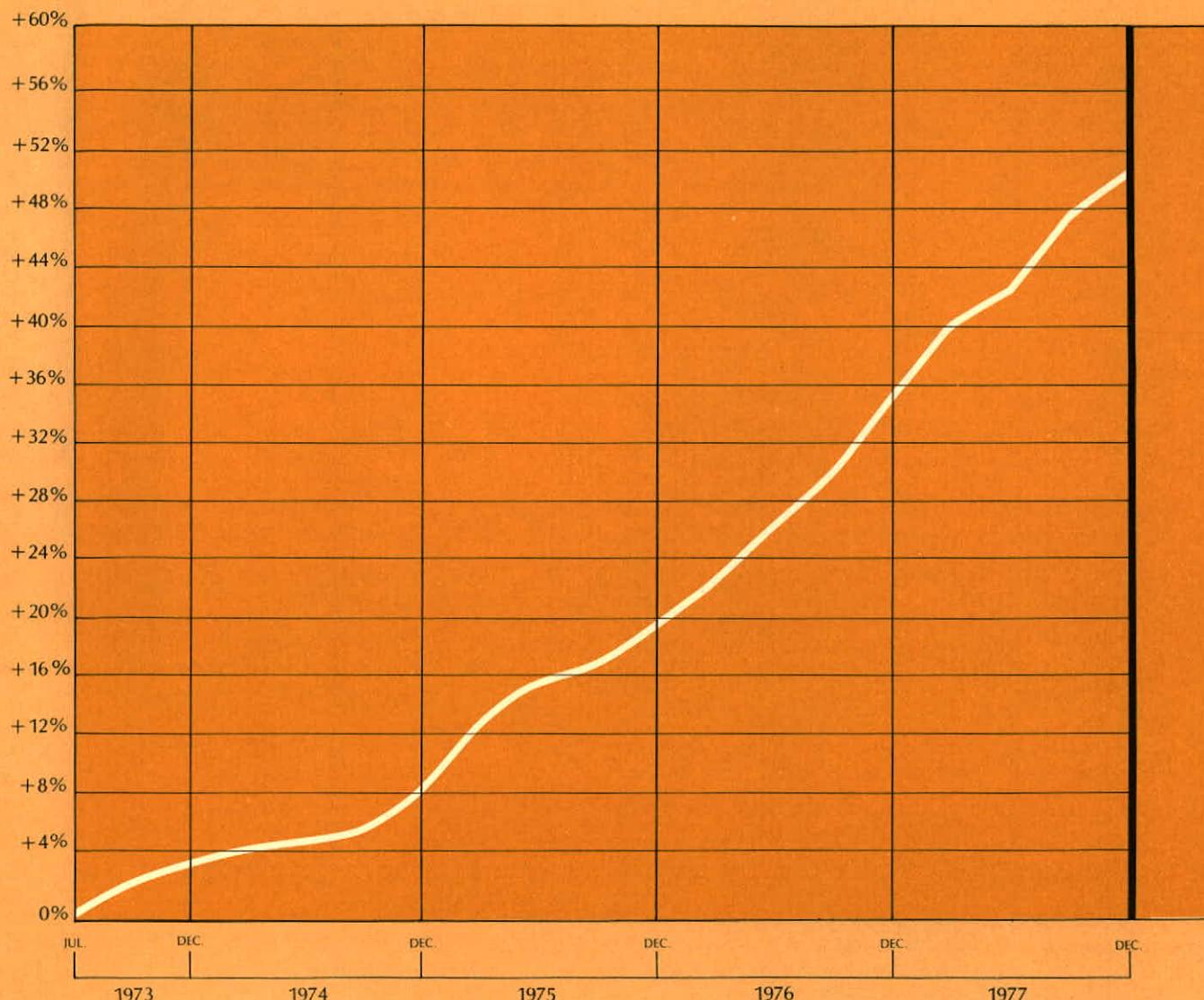
In the face of these expectations, we will be adopting a more conservative stance for the Fund. The average term of the Fund, presently about 9.6 years, will be maintained around the current level or shorter if there is no substantial yield give up involved.

### Portfolio Composition:

	Sept. 30, 1977	Dec. 31, 1977
Reserve	3%	4%
Canadas	11	11
Provincials	24	24
Corporates	60	59
Conv. Debs.	2	2
	<u>100%</u>	<u>100%</u>

# Mortgage Fund

Comparisons between	GRAPH COLOUR	VALUE DEC. 31/77	VALUE SEPT. 30/77	PERCENT CHANGE OVER QUARTER	PERCENT CHANGE YEAR-TO-DATE	COMPOUND ANNUAL RETURN SINCE INCEPTION
<b>Mortgage Fund</b>		\$ 9.96	\$ 9.96	+ 0.0%	+ 0.9%	-0.1%
<b>Mortgage Fund (Incl. Inc.)</b>	□	\$15.00	\$14.68	+ 2.2%	+10.7%	+ 9.4%



## Performance in 1977

The unit value of the Mortgage Fund was \$9.96 on December 31, 1977 (unchanged from September 30, 1977) and compares with a value of \$9.86 as of December 31, 1976. The change in the value for the year was an increase of 1.0%. Including income the unit value of the Mortgage Fund increased from \$14.68 to \$15.00, a change of 2.2% during the last quarter of the year. The value of the units including income improved from \$13.55 to \$15.00 during 1977, an increase of 10.7%.

## Mortgage Market in the Fourth Quarter

Prime residential mortgage rates continued to hold at the 10-1/4% level throughout this period. While there had been evidence of a slight firming in the third quarter with an occasional 10-1/2% rate being shown, it was reversed in the final quarter of the year. There was some downward pressure on rates, especially during the slower period in December.

Secondary mortgage rates continued to ease as the demand outstripped the available supply, especially of mortgages for settlement prior to year end. At the close, mortgages in the secondary market were being offered between 9-1/4% and 9-5/8% with only the occasional offering being above these levels. Trust company deposit rates tended to ease a little although the reduction was not widespread. Most companies remained at 9% in the five year area.

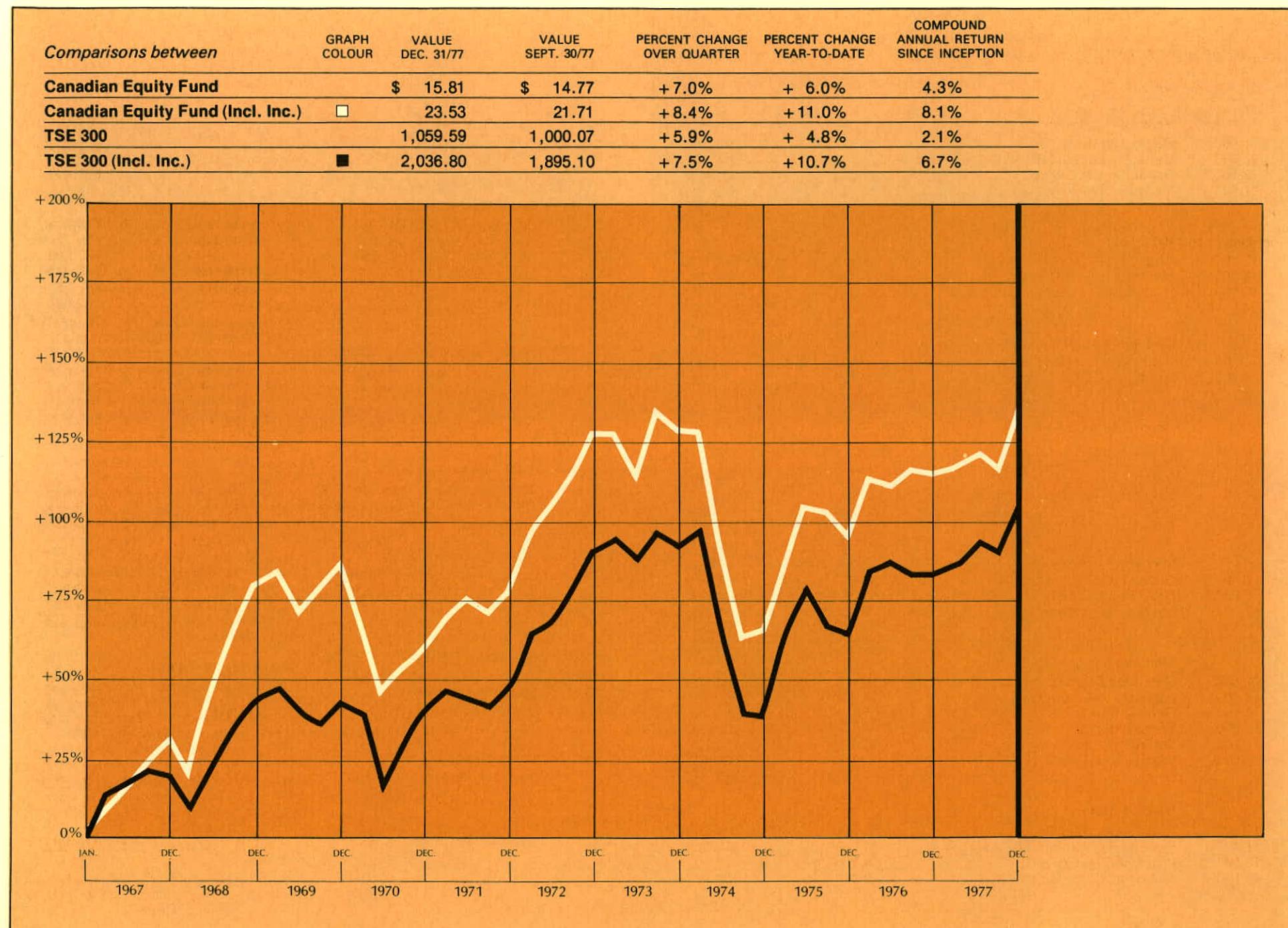
## Outlook for the Future

Mortgage rates should remain at present levels with any movement tending to slightly lower rates. Supply of funds for mortgages could outweigh the demand especially in the first quarter. As we do not expect any appreciable change in other interest rates, the possibility of a small decline in mortgage rates will depend upon the size of the supply of funds.

## Strategy

The Mortgage Fund continues to be invested in five year mortgages. Our aim is to be fully invested.

# Canadian Equity Fund



Par Value Shares	Convertible Securities or Common Stocks	Market Price	Market Value Dec. 31, 1977	Par Value Shares	Convertible Securities or Common Stocks	Market Price	Market Value Dec. 31, 1977
<b>Banks — 12.9%</b>							
28,000	Bank of Nova Scotia	19 1/2	\$ 546,000	10,000	Noranda Mines Class A	25	250,000
20,000	Canadian Imperial Bank of Commerce	25 1/8	502,500	17,000	Placer Development	22 7/8	388,875
22,000	Royal Bank of Canada	27 5/8	607,750	45,000	Sherritt Gordon Mines A	5 1/4	236,250
27,000	Toronto-Dominion Bank	17 3/8	469,125				\$ 1,934,430
			\$ 2,125,375				
<b>Beverages — 4.7%</b>							
19,800	Bright T. G. Class A	7 1/2	\$ 148,500	7,000	Canadian Superior Oil Ltd.	59 3/8	\$ 415,625
12,300	Molson Co. Ltd. Class A	15 3/4	193,725	10,000	Home Oil Co. Ltd. Class A	46 5/8	466,250
15,000	H. Walker-Goodeham & Worts A	29 3/4	446,250	10,000	Hudson Bay Oil & Gas Co.	47 3/4	477,500
			\$ 788,475	13,000	Norcen Energy Resources	18 7/8	245,375
				15,000	Pacific Petroleum Ltd.	43 3/4	656,250
				12,500	Texaco Canada Ltd.	40	500,000
							\$ 2,761,000
<b>Communications — 2.5%</b>							
38,185	Standard Broadcasting Corp.	10 1/4	\$ 391,396				
1,500	Torstar Corp. Cv. Class B	13 1/4	19,875	20,000	Pipelines — 8.3%		
			\$ 411,271	20,000	Alberta Gas Trunk Line U.A.	16 1/4	\$ 325,000
				17,000	Interprovincial Pipe Line A	14 1/8	240,125
				20,000	Trans Canada Pipe Lines	15 1/4	305,000
				15,000	Westcoast Transmission Co.	34 1/4	513,750
							\$ 1,383,875
<b>Forest Products — 8.7%</b>							
38,000	Abitibi Paper Co. Ltd.	10 3/4	\$ 408,500				
15,000	B.C. Forest Products Ltd.	21 1/4	318,750				
10,000	Domtar Limited	15 1/8	151,250	9,900	<b>Steel — 2.9%</b>		
21,000	MacMillan Bloedel Limited	18 1/4	383,250	10,000	Dominion Foundries & Steel - A	24 1/8	\$ 238,838
18,030	Price Company	10 3/8	187,061		Steel Co. of Canada Ltd. - Class A	24 1/2	245,000
			\$ 1,448,811				\$ 483,838
<b>Insurance — 6.0%</b>							
7,050	Crown Life Insurance \$1 pv	43 1/2	\$ 306,675	13,940	<b>Trust &amp; Loan — 5.8%</b>		
6,000	Great West Life \$1 pv	68	408,000	15,000	Canada Permanent Mortgage Co.	18 5/8	259,633
30,000	MICC Investments Ltd.	9 1/2	285,000	15,000	Canada Trust Co. Mortgage Co. A	29	435,000
			\$ 999,675		IAC Ltd.	18 1/4	273,750
							\$ 968,383
<b>Merchandising — 10.2%</b>							
21,500	Dominion Stores Ltd.	16 7/8	\$ 362,813	9,000	<b>Utilities — 5.9%</b>		
15,000	Hudsons Bay Company	18 1/2	277,500	20,000	Calgary Power Ltd. Class A	36	324,000
50,000	Oshawa Group Ltd. A	5 1/8	256,250	33,000	Canadian Utilities Ltd.	15 1/2	310,000
70,000	Simpsons Ltd.	4 3/4	332,500		Union Gas Ltd. Cv. A	10 3/4	354,750
10,000	Steinbergs Ltd. Class A	17 3/8	173,750				\$ 988,750
17,000	Woodward Stores Ltd. A	17 3/8	295,375				
			\$ 1,698,188				
<b>Mines &amp; Metals — 11.6%</b>							
15,000	Alcan Aluminum Ltd.	28 3/4	\$ 431,250		<b>Miscellaneous — 2.1%</b>		
17,170	Hudson Bay Mining & Smelting A	16 1/2	283,305	20,000	Canadian Pacific Ltd. \$5.00	17 3/8	\$ 347,500
10,000	Inco Ltd. Class A	18 7/8	188,750				
16,000	Mattagami Lake Mines A	9 3/4	156,000				
<b>Reserve — 1.7%</b>							
					<b>Cash &amp; Short Term Notes</b>		\$ 291,036
					<b>Total Assets at Market, December 31, 1977</b>		<b>\$16,630,607</b>

### Portfolio Balance

	Dec. 31/76	Sept. 30/77	Dec. 31/77
Common Stocks & Equivalents	97.7%	99.9%	98.3%
Reserve	2.3	0.1	1.7
	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>

### Portfolio Composition

	Dec. 31/76	Sept. 30/77	Dec. 31/77
Consumer Products & Service	38.1%	41.6%	42.1%
Cyclical	36.3	30.6	25.3
Energy	12.3	13.5	16.7
Regulated	11.0	14.2	14.2
Reserve	2.3	0.1	1.7
	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>

### Largest Common Stock Holdings as at December 31, 1977 (By Market)

	Percentage of Total Portfolio
Pacific Petroleum Ltd.	3.94%
Royal Bank of Canada	3.65%
Bank of Nova Scotia	3.28%
Westcoast Transmission Co.	3.09%
Canadian Imperial Bank of Commerce	3.02%

### Canadian Stock Market

The Canadian stock market made an heroic attempt to close the year at its high, and only failed by a few points. The close at 1059.59 for the Toronto Stock Exchange 300 Index, was less than 1% below the high of 1068.53.

General economic forecasts for 1977 turned out to be fairly close to the mark. Caution was the byword, and a year of rather modest growth was widely anticipated. The fact that corporate profits probably showed a reasonable gain, after two years of no growth, may have helped the stock market to achieve its rather modest gain of almost 5%.

The remarkable performance of the oil and gas stocks in the fall was also an important spur for general stock prices.

### Canadian Stock Market Performance in 1977

	31 Dec. 1977	Fourth Quarter	Full Year
T.S.E. 300	1059.59	+ 5.9%	+ 4.8%

The fourth quarter was the strongest of the year, and followed a weak third quarter when the Index declined 3%.

The oil and gas producers led the way with a 26% rise in the fourth quarter. Golds were up 9% and financial services were up 6%, although for the full year, they were up only 4%. Utilities (up 13% in 1977) and pipelines (up 14%) continued to be among the stronger groups as they had been in 1976. Paper and forest products and metals were among the weakest groups in 1977.

### Value In The Market

	T.S.E. 300	31 Dec. 1976	31 Dec. 1977
Price-earnings Ratio	8.99	8.24	
Dividend Yield	4.71%	4.73%	

The yield remained much the same during the year, but the price-earnings ratio declined.

Earnings per unit on the Index are estimated to have been up 14% and the dividend is up about 5.2%.

### Anticipated Return From Equities

Our most probable outcome for 1978 would provide a total return from equities of 12%. This is based on an earnings gain of 10%, a slight decline in the price-earnings ratio, and a dividend yield of 5%. Our outcome is calculated as follows:

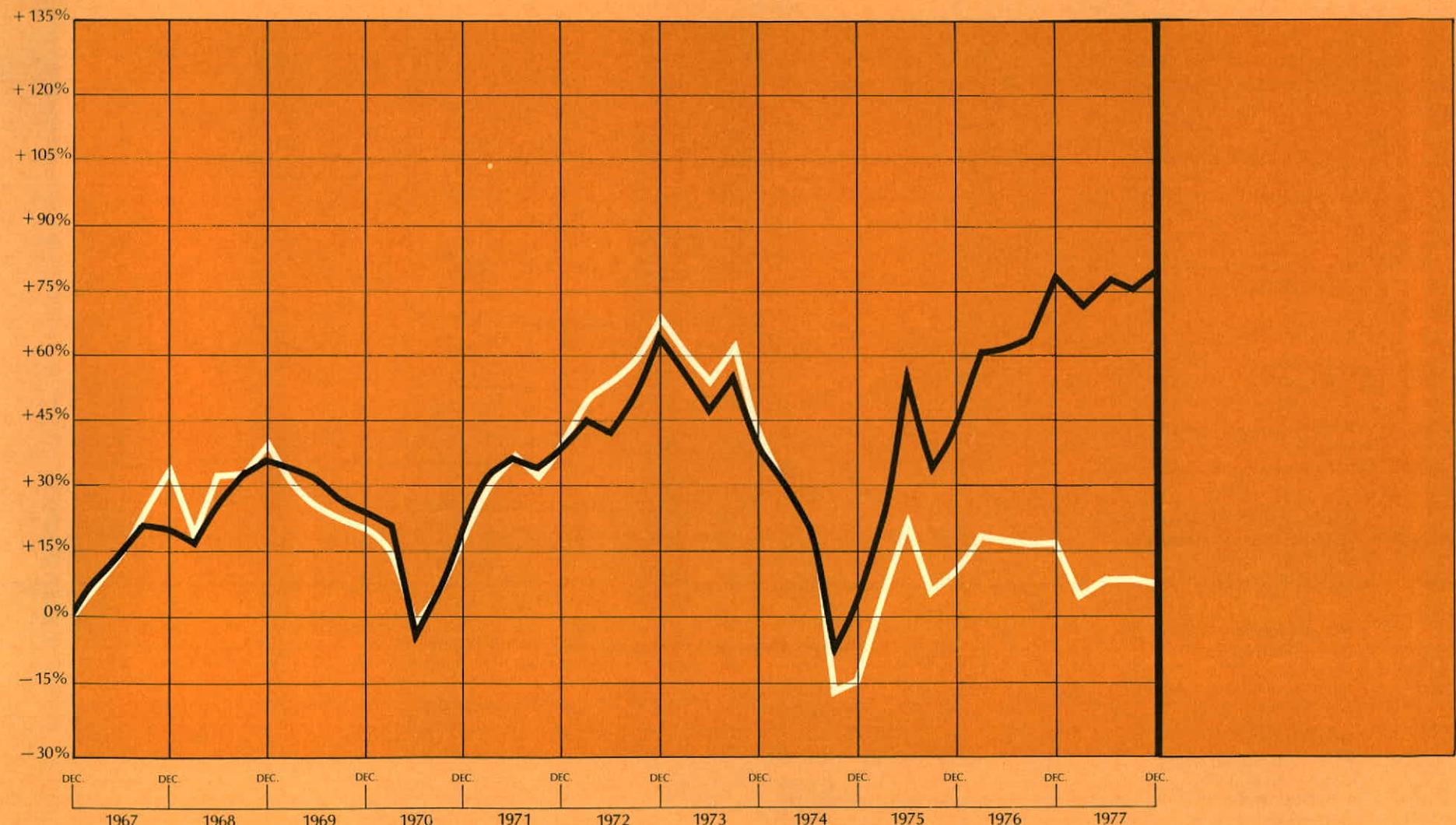
31 Dec. 1977	31 Dec. 1978	Price-Earnings Ratio Current	Estimated	Estimated TSE 300 Index 31 Dec. 1978
128.59	141.45	8.24	8	1131.60

A slightly lower price-earnings ratio is consistent with our forecast for slightly higher interest rates.

If the T.S.E. 300 Index closes 1978 around the level indicated above, it would provide a capital gain of approximately 7%. To this we add the current income yield of roughly 5% to arrive at the forecast total return of 12%.

# International Equity Fund

Comparisons between	GRAPH COLOUR	VALUE DEC. 31/77	VALUE SEPT. 30/77	PERCENT CHANGE OVER QUARTER	PERCENT CHANGE YEAR-TO-DATE	COMPOUND ANNUAL RETURN SINCE INCEPTION
<b>International Equity Fund</b>		\$ 8.22	\$ 8.38	-1.9%	-11.5%	-1.8%
<b>International Equity Fund (Incl. Inc.)</b>	■	10.59	10.72	-1.2%	-9.2%	+0.5%
<b>*S &amp; P 500</b>		104.08	103.62	+0.4%	-4.0%	-0.1%
<b>*S &amp; P 500 (Incl. Inc.)</b>	■	2,146.50	2,107.71	+1.8%	-0.7%	+0.1%



Par Value Shares	Convertible Securities or Common Stocks	U.S. Market Price	Canadian Market Value Dec. 31, 1977	Par Value Shares	Convertible Securities or Common Stocks	U.S. Market Price	Canadian Market Value Dec. 31, 1977
<b>Banks — 4.1%</b>							
10,000	Bankamerica Corp.	22 7/8	\$ 250,344	5,000	Personal Care — 2.9%	33 5/8	\$ 183,996
4,600	J.P. Morgan & Co. Inc.	43	216,472	6,000	Bristol Myers Co.	22 1/4	146,102
			<u>\$ 466,816</u>		Chesebrough-Ponds Inc.		<u>\$ 330,098</u>
<b>Chemicals — 2.2%</b>							
8,800	Dow Chemical Co.	26 3/4	<u>\$ 257,622</u>	4,100	Consumer Products — 8.5%	61 7/8	\$ 277,636
<b>Drugs — 3.1%</b>							
7,700	American Home Products	27 3/4	\$ 233,846	5,200	Philip Morris, Inc.	19 3/4	112,395
2,100	Merck Co.	55 1/2	127,552	3,400	Jewel Co., Inc.	59 1/4	220,467
			<u>\$ 361,398</u>	8,000	R. J. Reynolds Industries	20 7/8	182,765
<b>Electronics — 6.8%</b>							
6,000	General Electric Co.	49 7/8	\$ 327,499	9,700	U.A.L. Inc.	17 1/4	183,120
2,600	Hewlett Packard Co.	73 1/4	208,428		Goodyear Tire & Rubber		
3,000	Texas Instruments Inc.	73 1/2	241,315				<u>\$ 976,383</u>
			<u>\$ 777,242</u>	8,100	<b>Retail Trade — 4.1%</b>	27 3/8	\$ 242,670
<b>Forest Products — 2.0%</b>							
7,800	Weyerhaeuser Co.	27 3/8	<u>\$ 233,682</u>	2,900	K. Mart Corp.	13 1/2	42,846
<b>Foods &amp; Beverages — 4.9%</b>							
7,400	Coca Cola Co.	37 1/4	\$ 301,671	4,300	Safeway Stores, Inc.	41 3/8	<u>194,708</u>
4,700	McDonalds Corp.	51 1/2	264,900				<u>\$ 480,224</u>
			<u>\$ 566,571</u>	5,000	<b>Utilities — 6.4%</b>	60 1/2	\$ 331,056
<b>Hospital Supply — 2.5%</b>							
5,900	Medtronic Inc.	19	\$ 122,682	6,200	American Tel. & Tel.	31 1/8	211,192
2,000	Johnson & Johnson Inc.	76 3/4	167,990	6,800	General Tel. & Electronics	26 3/8	196,281
			<u>\$ 290,672</u>		Southern California Edison		
<b>Information Processing — 8.5%</b>							
4,100	Automatic Data Processing	28 7/8	\$ 129,564	4,700	<b>Communications — 1/8%</b>	40 1/8	<u>\$ 206,390</u>
5,000	Digital Equipment	46 1/4	253,080		American Broadcasting Co.		
2,000	Int'l. Business Machines	273 1/2	598,637	11,300	<b>Automotive — 3.9%</b>	12 5/8	\$ 156,130
			<u>\$ 981,281</u>	5,900	Chrysler Corporation	45 3/4	295,406
<b>Miscellaneous — 5.2%</b>							
5,000	Caterpillar Tractor	54 7/8	\$ 300,276	1,500	<b>Manufacturing-Processing — 9.1%</b>	38 3/4	\$ 63,612
6,100	Masco Corp.	20 3/8	136,021	6,500	American Cyanamid Co.	26 3/4	190,289
3,000	Minnesota Mining & Manufacturing	48 1/2	159,235	5,400	Continental Group Inc.	34	200,932
			<u>\$ 595,532</u>	3,400	Great Northern Nekoosa Corp.	27 1/4	101,396
<b>Oils — 10.4%</b>							
5,100	Atlantic Richfield Co.	51 3/8	\$ 286,746	7,900	Phelps Dodge Corp.	21 1/2	185,884
7,700	Continental Oil Co.	30	252,806	9,000	Scott Paper Co.	14	137,894
5,000	Standard Oil Co. Indiana	49 1/2	270,864	7,900	Williams Companies	18 1/2	159,947
7,000	Exxon Corp.	48 1/8	368,676				<u>\$ 1,039,954</u>
1,000	Reserve Oils & Minerals	13 1/8	14,364	5,000	<b>Trust Companies — 1.5%</b>	32 3/8	<u>\$ 177,156</u>
			<u>\$ 1,193,456</u>		Manufacturers Hanover		
<b>Reserve — 11.2%</b>							
				4,800	<b>Capital Goods — 0.9%</b>	19 5/8	<u>\$ 103,092</u>
					National Semiconductor Corp.		
					<b>Cash and Short Term Notes</b>		<u>\$ 1,282,237</u>
					<b>Total Assets at Market, December 31, 1977</b>		<u>\$11,509,871</u>

### Portfolio Balance

	Dec. 31/76	Sept. 30/77	Dec. 31/77
Common Stock & Equivalents	95.0%	99.8%	88.8%
Reserve	5.0	0.2	11.2
	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>

### Portfolio Composition

	Dec. 31/76	Sept. 30/77	Dec. 31/77
Consumer Products & Service	39.7%	39.0%	37.3%
Cyclical	10.6	12.2	18.0
Energy	5.8	16.1	10.4
Technology	38.9	32.5	16.7
Regulated	—	—	6.4
Reserve	5.0	0.2	11.2
	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>

### Largest Common Stock Holdings as at December 31, 1977 (By Market)

	Percentage of Total Portfolio
International Business Machines	5.20%
Exxon Corp.	3.20%
American Tel. & Tel.	2.88%
General Electric Co.	2.85%
Coca Cola Co.	2.62%

### FOREIGN STOCK MARKETS

#### United States

For the first time since 1974, the U.S. stock market did significantly worse during the year than the Canadian. In fact, the 1977 performance was more striking since the Canadian market was positive by almost 5% whereas the U.S. market was negative by varying amounts from 9% to 17%, depending on which Index you prefer to use.

### U.S. Stock Market — 1977 Results

	31 Dec. 1976	31 Dec. 1977	Change
Dow Jones Industrials	1004.65	831.17	(17.3)
Standard & Poor 500	107.45	95.10	(11.5)
N.Y.S.E. Composite	57.88	52.50	( 9.3)

As a point of interest for stock market antiquarians, the Dow Jones Industrial Index finished the year below its book value, which is only the third time in modern history that this has occurred. The last was in 1974 which to the pessimists may mean occurrences are becoming more frequent, while the optimists can point to the 50% plus advance which took place within six months of the 1974 close.

#### Internal Features

There was quite a divergence among various industrial groups with the utilities providing a stable performance. The Dow Jones Utility Average was up 2.7% and the Transportation Average was down 8.4%.

General Motors, an important bellwether stock, hit a low of \$61 1/8 on 21 December, a significant day in the calendar, and according to the GM theory the stock must remain above this low for four months before an uptrend can be signalled. Unfortunately, early in January, it was recording new lows below its 1977 low.

Of the large so-called glamour stocks, IBM was a stable performer, being down only 2%. The others improved after the first quarter, but that was sufficiently bad to give a weak overall result.

### U.S. Stock Indexes — Earnings & Dividends

	Est. 1978 Earnings	P.E. Ratio	Dividend	Yield
Standard & Poor 500	11.90	8.0	4.50	4.7%
Dow Jones Industrials	114.00	7.3	46.00	5.5

Our forecast for the U.S. stock market is approximately the same as for the Canadian, that is, a total return of 12% for 1978.

#### Other Stock Markets

	31 Dec. 1976	31 Dec. 1977	Change
London (F.T. Industrials)	354.7	485.4	36.8%
Tokyo (Nikkei Dow)	4,990.85	4,865.60	— 2.5
Frankfurt (Commerzbank Index)	727.4		

The U.K. market had the strongest year of any of the world's major markets, and this followed a small gain in 1976, and a very large rise in 1974. The Japanese market was surprisingly little changed.

# Unit Values of Diversified Investment Funds Since Inception

	Fixed Income Fund			Mortgage Fund			Canadian Equity Fund			International Equity Fund		
	UNIT VALUE	INCOME YR./QTR./MO.	VALUE INCL. INC.	UNIT VALUE	INCOME YR./QTR./MO.	VALUE INCL. INC.	UNIT VALUE	INCOME YR./QTR./MO.	VALUE INCL. INC.	UNIT VALUE	INCOME YR./QTR./MO.	VALUE INCL. INC.
1966 Dec. 31	\$10.00		\$10.00				\$10.00		\$10.00	\$10.00		\$10.00
1967 Dec. 31	9.52	\$62366	10.14				12.65	\$33967	13.02	13.28	\$22027	13.54
1968 Dec. 31	9.45	.60514	10.73				17.06	.36222	18.00	13.67	.27420	14.24
1969 Dec. 31	9.05	.71799	11.09				16.99	.59274	18.57	11.40	.38707	12.27
1970 Dec. 31	9.64	.74717	12.80				14.03	.58790	15.98	10.62	.34250	11.82
1971 Mar. 31	9.84	.19593	13.33				15.03	.12995	17.28	11.84	.05244	13.24
June 30	9.64	.18892	13.31				15.04	.12842	17.44	12.30	.04849	13.81
Sept. 30	9.90	.20070	13.96				14.59	.11095	17.05	11.79	.05142	13.30
Dec. 31	10.06	.19743	14.46				15.19	.10311	17.87	12.32	.05237	13.96
1972 Mar. 31	10.00	.18497	14.64				16.60	.11675	19.67	13.30	.06550	15.14
June 30	9.93	.18826	14.81				16.95	.11314	20.21	13.46	.04167	15.37
Sept. 30	9.97	.18887	15.16				17.78	.09474	21.32	13.92	.05572	15.96
Dec. 31	10.16	.18626	15.73				18.95	.12469	22.88	14.87	.04958	17.11
1973 Mar. 31	10.13	.18029	15.96				18.87	.09384	22.90	13.94	.06410	16.11
June 30	9.88	.17908	15.85				17.50	.12377	21.38	13.22	.05627	15.36
Sept. 30	9.77	.19265	15.99	9.92	.13906	10.07	19.24	.10939	23.64	13.98	.06974	16.32
Dec. 31	9.71	.19317	16.21	9.92	.20852	10.28	18.32	.16836	22.73	12.11	.05223	14.19
1974 Mar. 31	9.61	.19337	16.36	9.86	.22438	10.45	18.24	.12509	22.77	11.14	.04991	13.11
June 30	9.07	.19501	15.77	9.69	.21141	10.49	15.18	.19720	19.19	10.22	.05406	12.10
Sept. 30	8.91	.20719	15.86	9.50	.23806	10.54	12.53	.16598	16.05	6.68	.05505	7.96
Dec. 31	9.13	.21338	16.64	9.57	.23663	10.89	12.54	.20532	16.32	7.10	.04961	8.51
1975 Mar. 31	9.46	.19206	17.60	9.79	.20778	11.37	14.46	.18013	19.05	9.07	.04728	10.94
June 30	9.26	.19967	17.59	9.72	.22361	11.55	15.73	.13351	20.90	10.33	.07126	12.55
Sept. 30	9.03	.20160	17.54	9.53	.22903	11.60	15.04	.19163	20.23	8.42	.05070	10.29
Dec. 31	9.10	.19367	18.05	9.58	.22931	11.94	14.49	.16139	19.72	8.83	.05527	10.85
1976 Mar. 31	9.18	.20326	18.62	9.60	.23375	12.26	15.92	.15653	21.86	9.61	.05271	11.88
June 30	9.25	.20240	19.18	9.64	.23232	12.61	15.64	.15509	21.71	9.40	.04859	11.68
Sept. 30	9.33	.21144	19.79	9.69	.23378	12.99	15.45	.15367	21.66	9.30	.05021	11.62
Dec. 31	9.66	.22550	20.98	9.86	.23682	13.55	14.91	.19877	21.19	9.28	.05092	11.67
1977 Jan. 31	9.67	.06992	21.15	9.88	.07969	13.67	14.70	.02356	20.93	8.44	.00812	10.61
Feb. 28	9.63	.06845	21.21	9.95	.08046	13.88	14.82	.06150	21.18	8.34	.01941	10.52
Mar. 31	9.60	.07096	21.29	9.96	.07269	13.99	14.89	.07381	21.39	8.26	.01696	10.43
April 30	9.61	.06820	21.45	9.91	.08485	14.04	14.70	.02794	21.15	7.97	.00737	10.08
May 31	9.66	.07050	21.73	9.93	.07733	14.19	14.39	.04354	20.78	7.84	.02317	9.95
June 30	9.69	.06863	21.97	9.93	.07148	14.29	15.05	.10956	21.90	8.41	.01664	10.69
July 31	9.71	.07238	22.17	9.93	.08370	14.41	15.24	.02442	22.20	8.34	.00570	10.62
Aug. 31	9.73	.07444	22.37	9.93	.07577	14.52	14.77	.04591	21.59	8.44	.02625	10.77
Sept. 30	9.73	.06988	22.55	9.96	.07321	14.68	14.77	.08777	21.71	8.38	.01758	10.72
Oct. 31	9.71	.07209	22.66	9.95	.07273	14.78	14.36	.03050	21.16	8.18	.00602	10.47
Nov. 30	9.71	.07152	22.82	9.93	.07159	14.85	15.07	.05268	22.28	8.34	.02123	10.70
Dec. 31	9.72	.07369	23.01	9.96	.06885	15.00	15.81	.10159	23.53	8.22	.03050	10.59



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**INTERNATIONAL TRUST COMPANY**

**TORONTO  
ONE FIRST CANADIAN PLACE**

**MONTREAL  
1155 SHERBROOKE STREET WEST**