

Capital International – U.S. Equity

Quarterly portfolio review and commentary

Executive summary

- U.S. stocks fell sharply in the second quarter, following a year of impressive gains.
- Series A units of the Capital International – U.S. Equity portfolio ended the quarter with a decline of 7.28%, roughly in line with the Standard & Poor's 500 Composite Index decline of 7.23% in Canadian dollars.
- The Canadian dollar weakened slightly against the U.S. dollar.

U.S. equities rose through April, then headed sharply lower. The downturn was sparked by a myriad of investor concerns that began in the euro zone and spread around the globe. Although the U.S. dollar gained ground against the Canadian dollar over the period, the positive effect of currency translation for Canadian investors wasn't enough to reverse declines in U.S. stocks.

What helped

A number of individual holdings did well, but these standouts, as well as a relatively high cash position, were not strong enough to overcome the general decline in equities. Portfolio holdings that made positive contributions to returns included:

- American Tower, an operator of towers that provide coverage for rapidly expanding wireless communications in the U.S., Brazil, Mexico, India and Southeast Asia
- General Mills, one of the world's largest food companies, which sells products in more than 100 countries and has offices or manufacturing facilities in more than 30 countries
- Apple, which introduced a new iPhone and the iPad, a tablet computer that has garnered rave reviews and millions of unit sales

What hurt

In such a weak market environment, nearly every major sector was down.

- Shares of Baxter International, which develops and manufactures products for the treatment of complex medical conditions, dropped after the company reported margins had fallen more than expected. Portfolio managers subsequently sold all holdings of Baxter, as it appeared the trend would continue.
- Shares of entertainment company DreamWorks SKG also hurt results, after the latest Shrek film disappointed at the box office.
- While Google reported solid earnings during the quarter, the company's tepid outlook caused concern among investors.

Long-term perspective

Portfolio managers are using periods of heightened volatility to selectively make subtle changes to the portfolio. Shares of Johnson & Johnson were eliminated due to concerns about the company's future growth, while Weatherford International, one of the world's largest oil field service companies, was added to the portfolio after its stock price dropped in the wake of the Gulf oil spill. Despite worries about a new slowdown in the U.S. economy, managers are focused on finding opportunities for growth. For example, as U.S. discretionary sales have rebounded considerably from the depressed levels of

2009, portfolio managers are finding that certain companies with a clear niche, smart merchandising, geographic diversity and careful hands-on management are doing quite well. Two examples from the portfolio are Coach, a maker of luxury handbags and accessories, and Urban Outfitters, an apparel and furniture retailer with global ambitions.

Portfolio description

Capital International – U.S. Equity is a core portfolio, and is complementary to other style-specific mandates (i.e., growth or value mandates, etc.).

Investment objective

The objective of the portfolio is long-term growth of capital through investments in a portfolio comprised primarily of equity securities of large U.S. issuers and securities whose principal markets are in the U.S. (including ADRs and other U.S.-registered foreign securities).

Other portfolio characteristics

- Built from bottom-up stock selection by each portfolio manager and/or research analyst.
- May buy currency forwards to manage risk and implement investment strategies.
- Permitted to hold cash, cash equivalents and debt securities when desirable.

Portfolio managers

	Years in profession	Years with Capital
William H. Hurt	58	37
Todd S. James	24	24
Shelby Notkin	45	16
Theodore R. Samuels	30	28

A portion of assets is managed by 19 research analysts, who average 15 years of industry experience.

As of December 31, 2009.

Top 25 equity holdings	
	% of net assets
IBM	2.0%
Target	2.0
Cerner	2.0
Lowe's	2.0
Royal Dutch Shell	1.9
JPMorgan Chase	1.8
Allegheny Technologies	1.8
American Water	1.7
Schlumberger	1.7
Cisco Systems	1.7
Monsanto	1.6
General Mills	1.5
Allergan	1.5
PepsiCo	1.5
Microsoft	1.5
Emerson Electric	1.5
Barrick Gold	1.5
Charles Schwab	1.5
Iron Mountain	1.4
Danaher	1.4
Illinois Tool Works	1.4
Merck	1.4
Google	1.4
Shire	1.4
Procter & Gamble	1.3

Portfolio characteristics	
Assets (\$ mil) ¹	\$16.12
Number of holdings	118
Dividend yield	1.94%
Portfolio turnover rate	38.35%
Trading expense ratio ²	0.06%
Average market cap (\$ bil):	
Capital International – U.S. Equity	\$51.01
S&P 500 Index	\$77.36
Price to earnings:	
Capital International – U.S. Equity	16.51
S&P 500 Index	14.72
Price to book:	
Capital International – U.S. Equity	2.21
S&P 500 Index	1.92

Sector diversification	
	% of net assets
Information technology	16.5%
Industrials	13.7
Consumer discretionary	11.7
Materials	10.6
Financials	9.1
Health care	8.8
Energy	7.6
Consumer staples	7.2
Utilities	2.8
Telecommunication services	1.3
Cash and cash equivalents & other assets less liabilities ³	10.7
Total investments	100.0%

¹For combined series. ²As of December 31, 2009. ³Cash and cash equivalents include short-term investments.

Total returns (%) as of June 30, 2010													
Series	Cumulative		Annualized					Calendar year					
	3 mo	YTD	1 yr	2 yr	3 yr	4 yr	5 yr	Since inception*	2009	2008	2007	2006	2005
A	-7.28	-7.32	0.89	-7.31	-13.35	-8.58	-7.16	-3.30	9.00	-24.71	-18.04	9.36	0.96
B	-7.31	-7.39	0.73	-7.39	-13.34	-8.68	—	-9.53	8.79	-24.70	-18.16	—	—
D	-7.16	-7.09	1.39	-6.90	-12.96	-8.15	-6.72	-2.85	9.51	-24.40	-17.64	9.92	1.47
F	-7.05	-6.86	1.93	-6.48	-12.54	-7.71	-6.27	-2.36	10.09	-24.13	-17.21	10.46	1.98
H	-6.99	-6.76	2.13	-6.20	-12.31	-7.48	-6.04	-5.68	10.31	-23.82	-17.04	10.68	2.20

*Series A: November 1, 2002; Series B: March 31, 2006; Series D: November 1, 2002; Series F: November 1, 2002; Series H: May 3, 2004

Attribution analysis

Q2 2010	Companies	Sectors
Major contributors	Barrick Gold American Tower General Mills	Materials Consumer staples
Major detractors	DreamWorks Animation SKG Monsanto Charles Schwab	Consumer discretionary Information technology Financials

Sector changes

Since June 30, 2009	% of net assets
Largest increase:	
Cash and cash equivalents	7.0%
Consumer discretionary	0.9
Utilities	0.8
Largest decrease:	
Information technology	-3.6%
Health care	-2.9
Telecommunication services	-1.7

Holdings changes

Since March 31, 2010
New:
Coach
Halliburton
Weatherford International
Eliminated:
Johnson & Johnson
Baxter International
Transocean Ltd.

Commissions, service fees, management fees and expenses all may be associated with mutual fund investments. Please read the prospectus before investing. The indicated rates of return are the historical annual compounded total returns including changes in unit value and reinvestment of all distributions and do not take into account sales, redemption, distribution or optional charges or income taxes payable by any securityholder that would have reduced returns. Mutual funds are not guaranteed, their values change frequently and past performance may not be repeated.

Unless otherwise indicated, data as of June 30, 2010.

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