

## Acuity High Income Fund Update

### Recent Performance

After a strong first half for the capital markets, recent turmoil related to the U.S. housing slow down and the ensuing credit crunch has curtailed returns. The Acuity High Income Fund has not been immune: following a solid start, the Fund has been adversely affected by these events. The core foundation of the Fund, its well diversified asset mix, remains sound. In fact, asset allocation decisions have been exceptional, both over the long term and this year. The Fund has maintained an overweight exposure to stocks (approximately 62% of the Fund), which have outperformed bonds (approximately 25% weight) and trusts (approximately 13% weight). Nevertheless, on a year to date basis, 2007 marks the first time in eight years that the Fund has materially underperformed its peers. A number of issues have affected year to date performance:

1. Dividend-paying equities, as measured by the Dow Jones Select Canadian Dividend Index, have underperformed the S&P/TSX Composite Index by 5.3% through Oct. 12. Unlike most balanced funds, the Acuity High Income Fund is constrained to investing in stocks with a dividend. As a result, stocks such as Research in Motion Inc., which we own in our other balanced funds and which has contributed 2.1% to index returns so far this year, are ineligible for the Fund;
2. Certain value-oriented securities have performed well this year due to significant takeover premiums after nearly a decade of negligible returns (e.g., BCE Inc. and Alcan Inc. have contributed 1.6% to TSX Index returns year to date), crimping results for growth-oriented investors such as Acuity;
3. Large cap securities, as measured by the S&P/TSX 60 Index, have outperformed small caps, as measured by the S&P/TSX Small Cap Index, by 4.9% year to date as of Oct. 12. The Fund has always included small and mid cap equities and trusts to complement its large cap holdings;
4. The Fund's investments in international securities have resulted in a foreign currency loss of approximately 2.5% year to date;
5. Excellent companies (and core Fund holdings) such as Canadian National Railway Co., Goldcorp Inc. and Suncor Energy Inc. have been range bound this year despite stalwart earnings and cash flow growth;
6. The Fund's investments in sectors like natural gas-related energy services trusts and U.S. consumer discretionary stocks have held back results.

### Current Strategy

We are continually reevaluating and where necessary adjusting the Fund's holdings in order to address issues like the six points raised above:

1. Because of its emphasis on income generation, dividend equities remain a core focus of the Fund, especially since growth-oriented dividend paying equities have traditionally outperformed over the long term;
2. The value investing style has outperformed growth for the past seven years. The market typically fluctuates through cycles favouring first one style and then another, and after such a long period during which investors have preferred value, we believe the prospects for growth-oriented investing are increasingly attractive. Acuity remains true to our growth philosophy, which we believe positions the Fund as an excellent complement to the value-dominated style of our peers;
3. We have gradually moved the portfolio toward larger cap securities, both to improve liquidity and to take advantage of the fact that large caps offer better relative value after having underperformed small caps for most of the decade;
4. We remain committed to the Fund's foreign holdings, despite the appreciation of the Canadian dollar, since we believe that the dollar is unlikely to rise by anywhere near as much in the next few years as it has in the past five years. In addition, we believe these global investments offer strong growth potential and diversification benefits not available in Canada;

5. We continue to emphasize a number of key themes, such as global infrastructure spending, which we have favoured for years. In our view, this theme is likely to keep bolstering the growth of companies in the industrial, materials and energy sectors;
6. While we remain optimistic about resources, the commodity sectors have grown to represent over 40% of the TSX. Accordingly, we have prudently sought other avenues to broaden the Fund's diversification, such as blue chip technology. After seven years of underperformance following the crash, dividend paying tech stocks with superb cash flow, strong franchises and cheaper valuations than the S&P 500 Index are showing signs of resurgence.

### A Recipe for Long Term Success

The multi-asset class approach that has been a hallmark of the Fund's success remains a key component of our strategy. We believe that equities continue to offer the best long term prospects of the major asset classes, and accordingly have maintained an overweight position in stocks. A current snapshot of key fundamental characteristics for the stocks in the Fund illustrates its exceptional value, as the following chart shows\*:

Equities	High Income Fund	S&P/TSX Index	Difference
Debt to Equity	0.5	0.6	0.1
Forward Price/Earnings	12.2x	14.3x	2.1x
Forward EPS Growth	10.0%	9.0%	1.0%
ROE ('07E)	21.4%	19.2%	2.2%

In aggregate, the Fund's securities have stronger balance sheets, more attractive valuations, better growth prospects, and higher profitability than the index. Historically, this mix has always resulted in superior long term returns for unit holders, and we believe that the current situation will prove to be no different. In addition, the Fund retains its focus on securities generating cash yields regardless of asset class. The secular trend of companies increasing cash payouts is likely to continue unabated despite the move to curtail income trusts. An expanding focus on yield makes sense as dividends have become more tax effective\*\*, and investors' desire for yield remains undiminished. The Acuity High Income Fund is particularly well positioned to capitalize on this trend given its historical and very successful emphasis on income generating investments. Overall, we remain highly confident about all the securities in the Fund, which we believe provide a conservative mix of high quality, attractive yields, and superior growth prospects.

In closing, it is critical to note that even the best funds have periods of underperformance. However, the Fund's long term track record is unrivalled: over the past decade and a half, the Fund has delivered positive results every year but one, and has outperformed its peers for virtually the entire 15 year period. More importantly, the same management team that has generated the Fund's outstanding results is in place today, and we continue to rigorously employ the consistent, disciplined, growth-oriented philosophy and diversified, multi-asset class mix that produced these superior long term returns. Finally, **we believe that the way to succeed in investing is by buying good funds like the Acuity High Income Fund that are on sale, or by adding to solid investments like the Fund that have temporarily languished.** Indeed, in our view, the attributes tabled above are precisely the characteristics an investor should aspire to own in a fund, and reflect our commitment to the long term success of the unit holders in the Acuity High Income Fund.

\* All figures based on CPMS (Computerized Portfolio Management Services).

\*\* The combined dividend tax rate of 59% in 2005 has declined to 52% in 2007 and is projected to decrease to 47.6% in 2011 (consistent with income trusts) for the highest marginal tax bracket.

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