

**VBA CANADIAN SMALL-CAP EQUITIES**

VBA is pleased to report that our conservative investment style and disciplined approach are again resulting in successful value-added results for our clients. VBA is known for investing in companies that have sustainable competitive advantages, that generate free cash flow, produce high returns on capital over a market cycle, that sell below intrinsic value, that have sound balance sheets and companies whose management are significant shareowners of their stock.

**CANADIAN SMALL-CAP INVESTMENT PERFORMANCE TO SEPTEMBER 30, 2011**

It is my pleasure to report more than 19 years of investment performance for VBA's Canadian Small-Cap Product, as indicated in the following table:

**VBA Canadian Small-Cap Pension Fund Composite Results**  
**Total Time Weighted Rates of Return**  
**Annualized for Periods Greater Than One Year**  
**(To September 30, 2011)**

	<b>3 Mos.</b> <b>(%)</b>	<b>YTD</b> <b>(%)</b>	<b>1 Yr.</b> <b>(%)</b>	<b>4 Yrs.</b> <b>(%)</b>	<b>7 Yrs.</b> <b>(%)</b>	<b>10 Yrs.</b> <b>(%)</b>	<b>15 Yrs.</b> <b>(%)</b>	<b>Inception</b> <b>06/30/1992</b> <b>(%)</b>
VBA Composite	-12.74	-7.04	6.29	2.87	7.40	10.17	10.10	12.46
BMO Small Cap Blended Unweighted Index	-16.67	-20.97	-5.27	0.79	6.01	10.30	5.34	7.98
BMO Small Cap Blended Weighted Index	-14.88	-18.44	-2.33	0.34	7.44	11.08	7.73	9.61
S&P/TSX Composite Blended Index	-12.02	-11.88	-3.55	-1.90	7.01	7.95	7.60	8.95
<b>Value Added</b> <b>(VBA minus BMO)</b>	<b>3.93</b>	<b>13.93</b>	<b>11.56</b>	<b>2.08</b>	<b>1.39</b>	<b>-0.13</b>	<b>4.76</b>	<b>4.48</b>

NOTE: Van Berkom and Associates Inc. [an entity registered with the Quebec, Ontario, Alberta, and British Columbia Securities Commissions as Portfolio Manager and with the Securities and Exchange Commission (United States) as Investment Advisor] claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS® standards. VBA has not been independently verified. Investment performance results are those of the VBA Cdn. Pension Fund Composite ("VBA Composite") of segregated small-cap pension fund portfolios. As at September 30, 2011, the VBA Cdn. Pension Fund Composite totalled \$0.57 billion in Canadian small-cap assets, which represented 43.1% of the firm's assets under management. The VBA Cdn. Pension Fund Composite includes eight major Canadian pension fund accounts.

**COMPARATIVE INVESTMENT PERFORMANCE VERSUS THE RUSSELL INVESTMENT GROUP UNIVERSE OF CANADIAN SMALL-CAP MANAGERS**

For the periods ended September 30, 2011, VBA's Canadian Small-Cap Pension Fund Composite Ranks:

- 40<sup>th</sup> Percentile on the Quarter Basis,
- 18<sup>th</sup> Percentile on the One-Year Basis,
- 35<sup>th</sup> Percentile on the Two-Year Basis,
- 31<sup>st</sup> Percentile on the Three-Year Basis,
- 19<sup>th</sup> Percentile on the Four-Year Basis, and
- 37<sup>th</sup> Percentile on the Five-Year Basis


I have enclosed the comparative investment performance results of the VBA Canadian Pension Fund Composite in the Russell Investment Group Universe of Canadian small-cap equity managers. Also enclosed is the Risk/Reward chart showing the VBA Canadian Pension Fund Composite versus the Russell Investment Group Universe of 33 Canadian small-cap portfolios as evaluated by *BNY Mellon Asset Servicing*.

#### **REVIEW AND OUTLOOK OF CANADIAN SMALL-CAP STOCKS**

Enclosed you will find the quarterly review and outlook for Canadian small-cap stocks for the third quarter 2011.

If you would like to learn more about VBA and our Canadian Small-Cap Equity Management Division, please visit us on our website at [www.vbassociates.com](http://www.vbassociates.com) or call me at (514) 985-5759, extension 223, or Benoît Durand, Partner, Vice-President and Senior Portfolio Manager, Canadian Small-Cap Equities, extension 226 or by e-mail at [contact@vbassociates.com](mailto:contact@vbassociates.com).

Sincerely yours,



*J. Sebastian van Berkorn*  
President and Chief Executive Officer



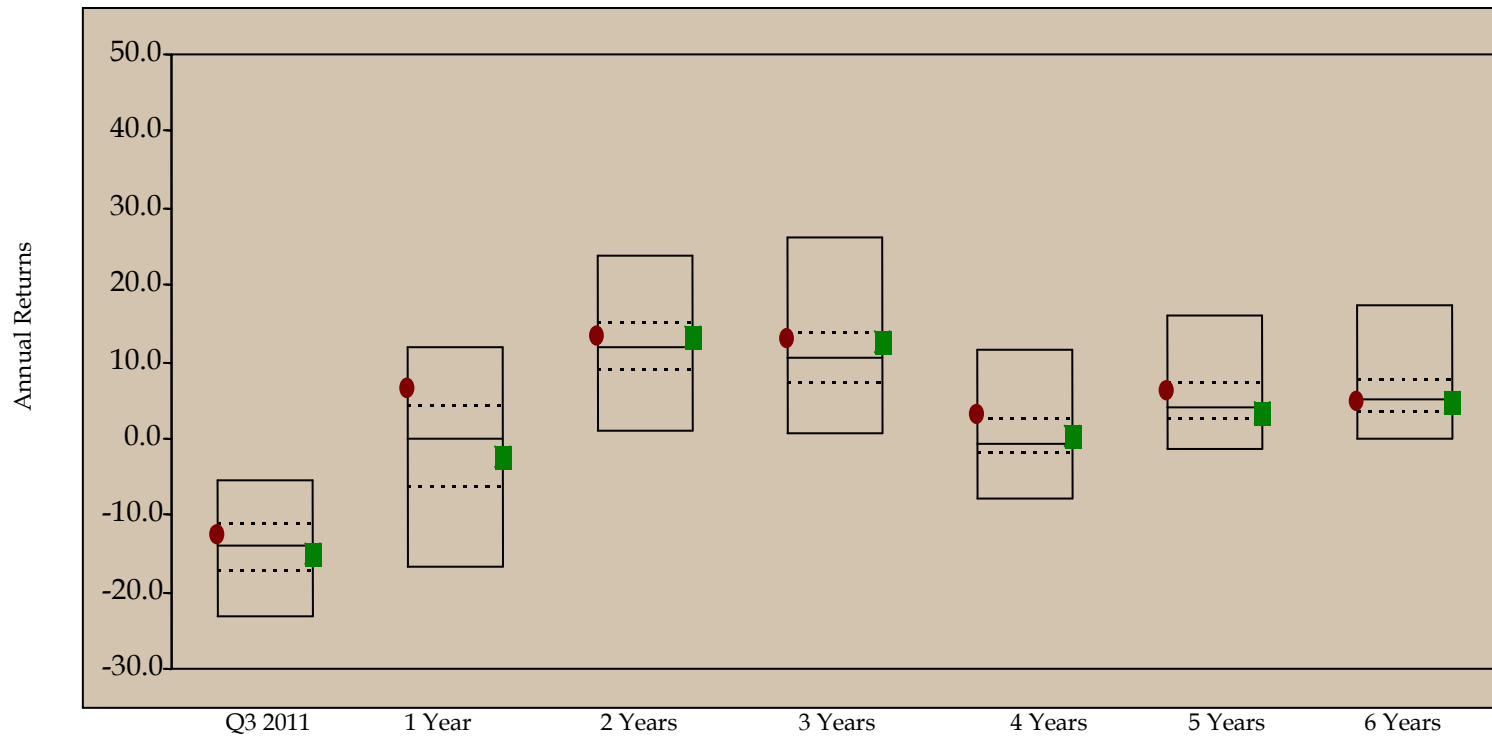
*Benoît Durand*  
Partner, Vice-President and  
Senior Portfolio Manager,  
Canadian Small-Cap Equities

# PERFORMANCE OF THE VBA CDN. PENSION FUND COMPOSITE VERSUS RUSSELL INVESTMENT GROUP



## Small-Cap Equity Universe

Rates of Return for Periods Ending September 30, 2011



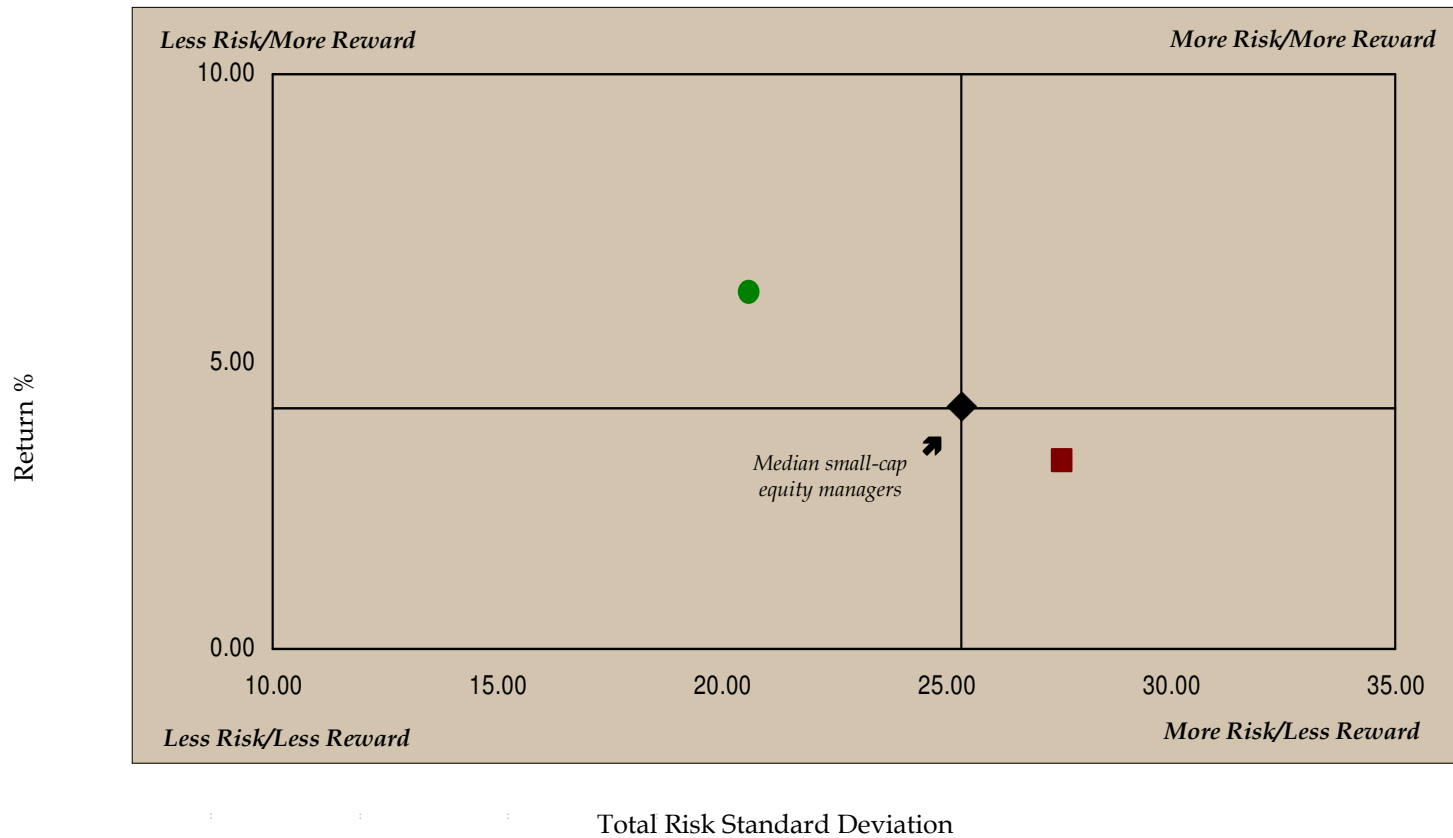
	% tile	% tile	% tile	% tile	% tile	% tile	% tile
● VBA Cdn. Composite	40	18	35	31	19	37	62
■ BMO Small Cap	56	54	34	32	37	68	63
# of Portfolios	37	37	37	36	35	33	31

Universe Source: Russell Investment Group

RISK/REWARD OF THE VBA CDN. SMALL-CAP PENSION FUND  
COMPOSITE VERSUS THE BMO SMALL CAP WEIGHTED BLENDED INDEX



**Small-Cap Equity Universe**  
5 Years Ending September 30, 2011



- VBA
- BMO Small Cap Weighted Blended Index

Universe Source: Russell Investment Group



## REVIEW AND OUTLOOK OF CANADIAN SMALL-CAP STOCKS

Global alarm concerning the economic outlook and the European debt jitters “rocked” equity markets again during the third quarter. On October 3rd, following a 372 point drop, the S&P/TSX Composite Index had officially declined by more than 20% since early April prompting frontline newspapers to claim that the “Bear is Back”. The risk trade was definitely “off” during the quarter, with world equity markets down sharply, as illustrated by the 16.5% decline of the MSCI World Index. Sovereign debt concerns impacted the German and French equity markets severely, with declines of slightly more than -25%, while the delinquent Greece market tumbled by 37.2%. Long government bonds in Canada and the U.S. did particularly well with a return of 16.1% and 31% respectively, while large-cap indices declined by 12% in Canada and by 13.9% for the S&P 500 Index. The deteriorating economic outlook led investors to dump stocks with the highest beta, the smallest market caps and the lowest ROE leading the small-cap indices to underperform large caps in both Canada and the U.S.

Using the BMO Small Cap Index as a proxy, the third quarter tends to be a tough quarter for small caps, with seven of the worst ten quarterly performances registered during that particular quarter (since 1970) and this year it was no different. The third quarter decline of -16.7% was the worst performance since fourth quarter 2008 and the September decline alone of -12.1% was the 10<sup>th</sup> worst monthly performance recorded. Weakness was broadbased in small caps as all sectors registered declines, with the Energy Sector the clear laggard. Surprisingly, while large-cap gold stocks were up during the quarter mirroring the advance of the gold price, investors’ aversion to speculative gold stocks led the BMO gold sub-index to decline by 10.4%.

All in all, the summer proved to be quite a volatile “reality check” for investors and surprised many as to the severity and duration of the economic challenges ahead. Unfortunately, investors, business leaders, as well as “Joe the Plumber”, also witnessed the lack of strong political will and the limited flexibility that monetary and fiscal authorities have on both sides of the Atlantic to deal with these pressing issues, hence, challenging their already fragile confidence level.

It is certainly during these more difficult times that our research approach, discipline and focused portfolio invested in high-quality companies allows us to add significant value. During the quarter, we outperformed our benchmark by 563 basis points, notwithstanding the record breaking level of correlations between sectors and individual stocks which, according to Bank of America Merrill Lynch, is at a 25-year high, making for a difficult stock pickers’ environment like VBA. This high level of correlation between stocks implies that all stocks, good and bad, get trashed without discrimination can be nerve-racking at times, but it allows us opportunities to buy high-quality companies at attractive prices. Therefore, again, we have been fairly pro-active during the September quarter. We eliminated our position in *The Forzani Group Ltd.*, as a result of the takeover offer by *Canadian Tire* and *Rona Inc.*, due to poor earnings performance and outlook. On the buy side, we added to our positions in *Enghouse Systems Limited*, *Peyto Exploration & Development Corp.*, *Toromont Industries Ltd.*, *Cervus Equipment Corporation*, *Savanna Energy Corporation* and *Calfrac Well Services Inc.*, as well as initiated investments in *Major Drilling Group International Inc.* and in *Orbit Garant Drilling Inc.* The latter both being entrepreneurial, well-managed and high-quality mining drilling services companies, which, because of the recent market declines, were trading at a steep discount to our measure of their intrinsic value. Please refer to these profiles from last month’s letter.

The past few months have certainly not changed our beliefs that the North American and European economies have a long recovery path in front of them. Housing and employment sectors are still weak, while the banking system is still focused on rebuilding its equity base, while, at the same time, facing fresh new fears of another major debt crisis. Added concerns recently came from the risk of China’s economy landing harder than what most economists previously expected. In such an environment, corporate profitability outlook is certainly weakening



for Canadian companies. Some mitigating factors will be the recent weakness in the Canadian dollar, as well as the decline in some input costs such as energy, but unfortunately, sell side analysts are only starting to lower their rosy earnings forecasts for 2012.

While we are not “thrilled” to report a negative absolute return for the current quarter, we are, nevertheless, comforted by the fact that your portfolio was still posting a positive return until the end of August in this volatile and difficult economic environment. We firmly believe that strong companies only get stronger, while weaker companies fall by the wayside when faced with a challenging and difficult environment, hence, in our opinion, explaining the resilience of your portfolio until August at which point investors started dumping all equities without discrimination. Furthermore, knowing that your portfolio is invested in well-managed companies, with a strong cash flow and balance sheet and trading at cheap valuation, as well as an 18.2% discount to our conservatively determined intrinsic value bodes well for its continued outperformance no matter how the economic environment unfolds.