SENTRY

Oil and gas update

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OIL

Supply and demand

- Oil discoveries have dropped significantly since 1930.
- Oil is now being found in frontiers – deep water, the Arctic or non-conventional sources such as heavy oil and oil shales.
- These barrels are a lot more expensive than the oil we are used to getting from the Middle East and North Africa because of higher production costs.
- The world is very much focused on US demand for oil.
- Even though the US is the biggest consumer of oil, the incremental barrel is going to be consumed in emerging markets.
- We believe any drop in oil demand from slowing European and American economies will be picked up by energy-hungry emerging markets whose residents are buying cars with new-found wealth.
- In developed markets, oil demand increased by 200,000 barrels a day in the first quarter (Q1) of this year, compared to Q1 of 2010.
- Despite higher prices, consumption was up 2 million barrels in emerging markets over the same period.

Production

- We think the civil war in Libya will last the rest of the year since NATO and the rebels have failed to oust Gaddafi.
- Spare capacity runs at about 4.5 million barrels a day if Libya produces its full 1.6 million barrels.
- Libya currently has 1.3 to 1.5 million barrels offline, so the effective spare capacity is just over 3 million barrels a day.
- Over 80% of the spare capacity lies in Saudi Arabia alone.
- Production in Saudi has been rising to just under 9 million barrels a day.
- The peak in Saudi oil production was at 9.7 million barrels in the summer of 2008.
- The official production capacity for Saudi is 12.5 million barrels per day but we don’t think it can produce more than 10 million.
- Even if the Saudis can actually produce 12.5 million barrels a day, and Libya can produce 1.6 million barrels a day, then spare capacity in 2012 would still drop below levels seen in 2005 to 2006.
- Real spare capacity could be less than 1 million barrels, so the market is tight.

Costs and pricing

- From 2002 to 2008, production costs were up 50% to 100%.
- We’re still seeing cost inflation, especially in the oil sands.
- Currently, we believe the world cannot handle $150 oil.
- The US consumer is starting to suffer at $4.20 a gallon for gasoline, or the equivalent of about $115 for oil.
- US household incomes have been largely flat since 2001, yet the cost of food and gasoline has doubled during that time.

- This year, we think West Texas Intermediate (WTI) will be capped at $115 per barrel.
- Before the Libyan civil war, WTI was trading at about $85 per barrel.
- Our downside target is approximately $90 per barrel since over a million barrels of light, sweet crude have been taken off the market.
- Once the market realizes how tight supply is, oil prices could spike to $150 per barrel in 2012 to 2013.

GAS

Supply and demand

- The International Energy Agency expects a significant increase in gas demand, particularly from China and the Middle East.
- Canada doesn't currently participate in the global gas market, but we're getting there.
- One to three liquefied natural gas (LNG) terminals are expected to be built on the west coast of Canada.
- Our biggest concern is the increase in supply. This growth is slowing with less drilling to hold land and companies reallocating capital to "oilier" plays.
- Gas is the only commodity that has not been repriced by China.
- We expect Nymex gas prices to approach world prices when we start exporting gas from North America in four to five years.
- Long term, we are bullish on gas prices.

Costs and pricing

- Oil and gas are far cheaper than alternative forms of energy.
- Gas companies such as Encana and Chesapeake are chasing growth at any price just to retain land.
- As companies have chased production growth, returns have declined.
- Fossil fuels still generate 90% of our energy needs and none of the renewables has the scale or cost structure to be competitive.
- Because of increasing costs, it can be difficult to make money in energy.

SENTRY ENERGY GROWTH AND INCOME FUND

- We're a specialist energy management team, travelling to oil fields around the world to conduct our due diligence.
- We're index agnostic, meaning that we don't try to replicate index-like strategies.
- We focus on opportunities, not the index, so exposure to index volatility is limited.

Our approach

- We look at the internal growth of the business, the soundness of its balance sheet and the cash flow it delivers, especially in a flat commodity price environment.
- We look deeper at wealth creation, asset quality, risk management and our assessment of the total return potential of the investment.
- Wealth creation yield stems from the cash flow generated in excess of the amount of capital an oil and gas company requires to sustain its business and overcome base declines.
- We look at risk related to geology and the operating jurisdiction, since many international jurisdictions will warrant a much higher risk premium.
- Our capability allows us to analyze the geology and technical aspects of a producer's assets, as well as to comb through the footnotes of financial statements.
- We avoid what we call in our example company "Chronic Capital Destroyer" – a real company with the name changed that doesn't pay a dividend and is very highly leveraged to natural gas, which accounts for over 80% of its production.
- "Chronic Capital Destroyer" has typically been a serial issuer of equity and convertible debentures to fund its own unprofitable capital expenditures.

- Unlucky investors in "Chronic Capital Destroyer" have been rewarded with declining per share metrics and successive dilutive financings.
- In general, the highest-quality stocks that exhibit the highest return potential end up in our portfolio.

Holdings

- The Fund generally aims to be about 75% invested in income-oriented energy securities like dividend-paying oil and gas producers.
- Weightings are determined by our view of broad equity markets as well as the relative return expectation for the various subsets in the energy universe.
- Our general expectation is that the three quarters or so of the portfolio that is income oriented will have a minimum expected return of 10% to 15%.
- One quarter of the portfolio augments this "anchor" and is populated by the very best capital appreciation "opportunities," where we expect a return of 25% or more.
- This forms our mandate of income and growth, with a singular, disciplined approach to stock selection.

Performance

- The Fund provides superior risk-adjusted returns and positive, after-tax income.
- The Fund's yield as at May 31st was 5.7%.
- That yield is over twice that of the Energy ETF at just 2.3%.
- Over a two-year period ending May 31st, the Fund has outperformed the S&P TSX Capped Energy Index by 51%.
- Since its inception (March 16, 2009), the Fund has captured substantially all of the upside of the Index during months when the Index was up.
- More importantly, the Fund has typically generated positive returns during months when the Index was down.
- Only one other fund in the peer group (a universe of 20 mutual funds) provides a regular monthly distribution.
- Sentry Energy Growth and Income Fund has outperformed that fund by 21% since inception.

Sentry Energy Growth and Income Fund

AVERAGE ANNUAL COMPOUND RETURNS (SERIES A)

1 YEAR	2 YEAR	3 YEAR	S.I.
38.2%	34.1%	n/a	44.5%

As at May 31, 2011