

The accompanying financial statements have been prepared by RBC Global Asset Management Inc. ("RBC GAM"), as manager of the Phillips, Hager & North Investment Funds (the "Funds") and approved by the Board of Directors of RBC GAM. We are responsible for the information contained within these financial statements.

We have maintained appropriate procedures and controls to ensure that relevant and reliable financial information is produced. The financial statements have been prepared in accordance with accounting principles generally accepted in Canada (and they include certain amounts that are based on estimates and judgments). The significant accounting policies, which we believe are appropriate for the Funds, are described in Note 3 to the financial statements.

Although the Board of Directors of RBC GAM is solely responsible for approving the financial statements and overseeing management's financial reporting responsibilities, the Financial Advisory Committee of the Board of Governors provides advice to RBC GAM concerning financial reporting, the audit process and internal controls. Please see *The Role of the Board of Governors* at the end of this report.

Deloitte LLP, Independent Registered Chartered Accountants, have performed an independent audit of the financial statements in accordance with Canadian generally accepted auditing standards. Their report is set out on the next page.



Chief Executive Officer
RBC Global Asset Management Inc.



Frank Lippa, CPA, CA
Chief Financial Officer and Chief Operating Officer
RBC Global Asset Management Inc.

March 1, 2013

To the Unitholders of:

Phillips, Hager & North Canadian Money Market Fund	Phillips, Hager & North Dividend Income Fund	Phillips, Hager & North Overseas Equity Fund
Phillips, Hager & North \$U.S. Money Market Fund	Phillips, Hager & North Canadian Equity Fund	Phillips, Hager & North Currency-Hedged Overseas Equity Fund
Phillips, Hager & North Short Term Bond & Mortgage Fund	Phillips, Hager & North Community Values Canadian Equity Fund	Phillips, Hager & North Global Equity Fund
Phillips, Hager & North Bond Fund	Phillips, Hager & North Canadian Equity Value Fund	Phillips, Hager & North Community Values Global Equity Fund
Phillips, Hager & North Community Values Bond Fund	Phillips, Hager & North Canadian Equity Underlying Fund	Phillips, Hager & North LifeTime 2015 Fund
Phillips, Hager & North Total Return Bond Fund	Phillips, Hager & North Canadian Growth Fund	Phillips, Hager & North LifeTime 2020 Fund
Phillips, Hager & North Inflation-Linked Bond Fund	Phillips, Hager & North Canadian Income Fund	Phillips, Hager & North LifeTime 2025 Fund
Phillips, Hager & North High Yield Bond Fund	Phillips, Hager & North Vintage Fund	Phillips, Hager & North LifeTime 2030 Fund
Phillips, Hager & North Short Inflation-linked Bond Fund	Phillips, Hager & North U.S. Dividend Income Fund	Phillips, Hager & North LifeTime 2035 Fund
Phillips, Hager & North Long Inflation-linked Bond Fund	Phillips, Hager & North U.S. Multi-Style All-Cap Equity Fund	Phillips, Hager & North LifeTime 2040 Fund
Phillips, Hager & North Monthly Income Fund	Phillips, Hager & North U.S. Equity Fund	Phillips, Hager & North LifeTime 2045 Fund
Phillips, Hager & North Balanced Fund	Phillips, Hager & North Currency-Hedged U.S. Equity Fund	BonaVista Global Balanced Fund
Phillips, Hager & North Community Values Balanced Fund	Phillips, Hager & North U.S. Growth Fund	BonaVista Canadian Equity Value Fund (collectively referred to as the "Funds")

We have audited the accompanying financial statements of each of the Funds, which comprise the statement of investment portfolio as at December 31, 2012, the statements of net assets as at December 31, 2012 and 2011 and the statements of operations and changes in net assets for the years then ended, and a summary of significant accounting policies and other explanatory information.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of each of the Funds as at December 31, 2012 and 2011 and the results of their operations and changes in their net assets for the years then ended in accordance with Canadian generally accepted accounting principles.



Chartered Accountants, Licensed Public Accountants

March 1, 2013

Toronto, Ontario

STATEMENT OF INVESTMENT PORTFOLIO (in \$000s)

PHILLIPS, HAGER & NORTH CANADIAN MONEY MARKET FUND

December 31, 2012

Par Value	Security	Fair Value	% of Net Assets
BANKERS ACCEPTANCES AND BANK OBLIGATIONS			
\$ 122 225	Bank of Montreal	\$ 121 514	
79 150	Bank of Nova Scotia	78 780	
51 700	Canadian Imperial Bank of Commerce	51 435	
61 500	HSBC Bank Canada	61 356	
		313 085	24.9
COMMERCIAL PAPER			
51 400	Bay Street Funding Trust - Class A	51 337	
25 600	Bell Canada International Inc.	25 584	
20 550	Caisse Centrale Desjardins	20 503	
56 225	Canadian Master Trust - Series A	56 025	
49 300	Central 1 Credit Union	49 165	
47 000	Clarity Trust	46 826	
60 000	Darwin Receivables Trust - Senior Notes	59 699	
31 275	Enbridge Inc.	31 243	
56 125	Fusion Trust	55 799	
36 900	Inter Pipeline Fund	36 786	
27 815	King Street Funding Trust	27 775	
35 060	McCain Financial Canada	35 032	
56 805	Merit Trust - Senior Notes	56 513	
20 825	Nova Scotia Power Inc.	20 802	
51 060	Prime Trust - Senior Notes	50 751	
7 175	PSP Capital Inc.	7 170	
49 025	Reliant Trust	48 775	
58 000	Ridge Trust	57 720	
11 620	SAFE Trust - Series 1996-1	11 596	
45 320	SOUND Trust	45 219	
14 350	TransCanada PipeLines Ltd.	14 308	
41 750	Wells Fargo Financial Canada Corp.	41 732	
58 850	Zeus Receivables Trust - Senior Notes	58 524	
		908 884	72.3
PROVINCIAL OBLIGATIONS			
14 500	Financement-Québec	14 504	
17 500	Province of Manitoba	17 533	
		32 037	2.5
TOTAL INVESTMENTS*		1 254 006	99.7
OTHER NET ASSETS		3 803	0.3
NET ASSETS		\$ 1 257 809	100.0

* Investments, which are grouped by issuer, earn interest at rates ranging from 1.13% to 1.42% and mature between January 3, 2013 and November 28, 2013.

Statements of Net Assets (in \$000s except per unit amounts)

December 31 (see note 2 in the generic notes)	2012	2011
ASSETS		
Investments at fair value	\$ 1 254 006	\$ 1 575 481
Cash	17	41
Subscriptions receivable	7 422	4 900
Dividends receivable, interest accrued and other assets	2 336	2 263
TOTAL ASSETS	1 263 781	1 582 685
LIABILITIES		
Redemptions payable	5 779	5 457
Distributions payable	14	18
Accounts payable and accrued expenses	179	256
TOTAL LIABILITIES	5 972	5 731
NET ASSETS	\$ 1 257 809	\$ 1 576 954
Investments at cost	\$ 1 254 006	\$ 1 575 481
NET ASSETS, END OF PERIOD		
SERIES C	\$ 6 820	\$ 11 674
ADVISOR SERIES	\$ 1 412	\$ 8 497
SERIES B*	\$ –	\$ 678
SERIES D	\$ 293 820	\$ 432 080
SERIES F	\$ 7 204	\$ 8 664
SERIES O	\$ 948 553	\$ 1 115 361
NET ASSETS PER UNIT, END OF PERIOD		
SERIES C	\$ 10.00	\$ 10.00
ADVISOR SERIES	\$ 10.00	\$ 10.00
SERIES B*	\$ –	\$ 10.00
SERIES D	\$ 10.00	\$ 10.00
SERIES F	\$ 10.00	\$ 10.00
SERIES O	\$ 10.00	\$ 10.00
NET ASSET VALUE (TRANSACTIONAL NAV) PER UNIT, END OF PERIOD (see note 3 in the generic notes)		
SERIES C	\$ 10.00	\$ 10.00
ADVISOR SERIES	\$ 10.00	\$ 10.00
SERIES B*	\$ –	\$ 10.00
SERIES D	\$ 10.00	\$ 10.00
SERIES F	\$ 10.00	\$ 10.00
SERIES O	\$ 10.00	\$ 10.00

Statements of Operations (in \$000s except per unit amounts)

For the periods ended December 31 (see note 2 in the generic notes)	2012	2011
INCOME (see note 3 in the generic notes)		
Interest	\$ 18 079	\$ 17 260
TOTAL INCOME (LOSS)	18 079	17 260
EXPENSES (see notes – Fund Specific Information)		
Management fees	1 863	2 123
Administration fees	524	537
Board of Governors costs	4	4
GST/HST	280	311
TOTAL EXPENSES	2 671	2 975
NET INVESTMENT INCOME (LOSS)	15 408	14 285
INCREASE (DECREASE) IN NET ASSETS FROM OPERATIONS		
	\$ 15 408	\$ 14 285
INCREASE (DECREASE) IN NET ASSETS FROM OPERATIONS		
SERIES C	\$ 57	\$ 65
ADVISOR SERIES	\$ 24	\$ 17
SERIES B*	\$ –	\$ 6
SERIES D	\$ 2 581	\$ 2 892
SERIES F	\$ 52	\$ 54
SERIES O	\$ 12 694	\$ 11 251
INCREASE (DECREASE) IN NET ASSETS FROM OPERATIONS PER UNIT		
SERIES C	\$ 0.07	\$ 0.06
ADVISOR SERIES	\$ 0.07	\$ 0.06
SERIES B*	\$ –	\$ 0.07
SERIES D	\$ 0.07	\$ 0.06
SERIES F	\$ 0.07	\$ 0.07
SERIES O	\$ 0.12	\$ 0.11

* All outstanding Series B units were redesignated as Series D units effective July 2012.

Approved by the Board of Directors of RBC Global Asset Management Inc.



John S. Montalbano
Director



Doug Coulter
Director

The accompanying notes are an integral part of these financial statements.

Statements of Changes in Net Assets (in \$000s)

For the periods ended December 31 (see note 2 in the generic notes)	Series C		Advisor Series		Series B*		Series D	
	2012	2011	2012	2011	2012	2011	2012	2011
NET ASSETS – BEGINNING OF PERIOD	\$ 11 674	\$ 11 199	\$ 8 497	\$ 692	\$ –	\$ 1 002	\$ 432 758	\$ 459 423
INCREASE (DECREASE) FROM OPERATIONS	57	65	24	17	–	6	2 581	2 892
Early redemption fees	–	–	–	–	–	–	–	–
Proceeds from units issued	5 589	16 345	1 527	9 719	–	–	397 482	598 854
Proceeds from reinvestment of distributions	59	64	21	16	–	6	2 539	2 845
Payments on redemption of units	(10 502)	(15 934)	(8 633)	(1 931)	–	(330)	(538 959)	(629 042)
TOTAL UNIT TRANSACTIONS	(4 854)	475	(7 085)	7 804	–	(324)	(138 938)	(27 343)
Distributions from net income	(57)	(65)	(24)	(16)	–	(6)	(2 581)	(2 892)
Distributions from net gains	–	–	–	–	–	–	–	–
Distributions from capital	–	–	–	–	–	–	–	–
TOTAL DISTRIBUTIONS	(57)	(65)	(24)	(16)	–	(6)	(2 581)	(2 892)
TOTAL INCREASE (DECREASE) IN NET ASSETS	(4 854)	475	(7 085)	7 805	–	(324)	(138 938)	(27 343)
NET ASSETS – END OF PERIOD	\$ 6 820	\$ 11 674	\$ 1 412	\$ 8 497	\$ –	\$ 678	\$ 293 820	\$ 432 080

For the periods ended December 31 (see note 2 in the generic notes)	Series F		Series O		Total	
	2012	2011	2012	2011	2012	2011
NET ASSETS – BEGINNING OF PERIOD	\$ 8 664	\$ 7 607	\$ 1 115 361	\$ 903 528	\$ 1 576 954	\$ 1 383 451
INCREASE (DECREASE) FROM OPERATIONS	52	54	12 694	11 251	15 408	14 285
Early redemption fees	–	–	–	–	–	–
Proceeds from units issued	8 704	5 874	1 290 395	1 278 121	1 703 697	1 908 913
Proceeds from reinvestment of distributions	51	54	12 543	11 085	15 213	14 070
Payments on redemption of units	(10 216)	(4 871)	(1 469 746)	(1 077 373)	(2 038 056)	(1 729 481)
TOTAL UNIT TRANSACTIONS	(1 461)	1 057	(166 808)	211 833	(319 146)	193 502
Distributions from net income	(51)	(54)	(12 694)	(11 251)	(15 407)	(14 284)
Distributions from net gains	–	–	–	–	–	–
Distributions from capital	–	–	–	–	–	–
TOTAL DISTRIBUTIONS	(51)	(54)	(12 694)	(11 251)	(15 407)	(14 284)
TOTAL INCREASE (DECREASE) IN NET ASSETS	(1 460)	1 057	(166 808)	211 833	(319 145)	193 503
NET ASSETS – END OF PERIOD	\$ 7 204	\$ 8 664	\$ 948 553	\$ 1 115 361	\$ 1 257 809	\$ 1 576 954

* All outstanding Series B units were redesignated as Series D units effective July 2012.

December 31, 2012

Financial instrument risk and capital management
(see note 4 in the generic notes)**Credit risk (%)**

The table below summarizes the Fund's credit risk exposure grouped by credit ratings as at:

Rating	December 31 2012	December 31 2011
R-1 (H)	78.7	75.4
R-1 (M)	7.6	4.7
R-1 (L)	13.7	19.9
Total	100.0	100.0

Interest rate risk (%)

The table below summarizes the Fund's exposure to interest rate risk by remaining term to maturity as at:

Term to maturity	December 31 2012	December 31 2011
0 – 1 month	35.2	41.1
1 – 3 months	41.6	52.2
4 – 6 months	23.2	6.7
Total	100.0	100.0

Due to the short-term nature of the Fund's investments, the Fund has minimal sensitivity to changes in interest rates.

Fair value hierarchy (\$000s except % amounts)
(see note 3 in the generic notes)

The following is a summary of the inputs used as of December 31, 2012 and 2011 in the valuation of the Fund's financial instruments carried at fair value.

December 31, 2012	Level 1	Level 2	Level 3	Total
Equities	–	–	–	–
Mutual fund units	–	–	–	–
Fixed-income and debt securities	–	–	–	–
Short-term investments	–	1 254 006	–	1 254 006
Derivatives – assets	–	–	–	–
Derivatives – liabilities	–	–	–	–
Total financial instruments	–	1 254 006	–	1 254 006
% of total portfolio	–	100.0	–	100.0

December 31, 2011	Level 1	Level 2	Level 3	Total
Equities	–	–	–	–
Mutual fund units	–	–	–	–
Fixed-income and debt securities	–	–	–	–
Short-term investments	–	1 575 481	–	1 575 481
Derivatives – assets	–	–	–	–
Derivatives – liabilities	–	–	–	–
Total financial instruments	–	1 575 481	–	1 575 481
% of total portfolio	–	100.0	–	100.0

For the periods ended December 31, 2012 and 2011, there were no transfers of financial instruments between Level 1 and Level 2.

Management fees (see note 7 in the generic notes)

No management fees are payable by the Fund with respect to Series O units. Series O unitholders pay a negotiated fee directly to RBC GAM for investment-counselling services.

Management fees of the other series of the Fund are calculated at the following annual percentages, before GST/HST, of the daily net asset value of each series of the Fund.

Series C	up to 0.65%
Advisor Series	up to 0.65%
Series B	up to 0.60%
Series D	Note 1
Series F	up to 0.40%

Note 1: 0.50% of the Series D net asset value up to \$200 000 000 and 0.40% of the Series D net asset value of the Fund in excess of \$200 000 000.

Operating expenses (see note 7 in the generic notes)

Administration fees payable by each series of the Fund are calculated at the following annual percentages, before GST/HST, of the daily net asset value of each series of the Fund.

Series C	0.05%
Advisor Series	0.05%
Series B	0.05%
Series D	0.05%
Series F	0.05%
Series O	0.03%

December 31, 2012

Initial investments (\$000s except unit amounts)

Royal Bank of Canada, or one of its subsidiaries, held the following investments in the Fund as at:

	December 31 2012	December 31 2011
Units held		
Series C	51	50
Advisor Series	101	101
Series B	–	50
Series D	524 909	709 276
Series F	51	50
Value of all units	\$ 5 251	\$ 7 095

Taxes (\$000s) (see note 5 in the generic notes)

The Fund had no capital or non-capital losses as at December 31, 2012.

Unitholders' equity (000s)

The unitholders' equity of the Fund includes amounts representing units, undistributed net income (loss), realized gain (loss) on investments and unrealized gain (loss) on investments. There is no limitation on the number of units available for issue. Units are purchased and redeemed at the transactional NAV per unit.

	2012	2011
For the periods ended December 31 (see note 2 in the generic notes)		
Series C		
Opening units	1 167	1 120
Issued number of units	559	1 634
Reinvested number of units	6	6
Redeemed number of units	(1 050)	(1 593)
Ending number of units	682	1 167
Advisor Series		
Opening units	850	69
Issued number of units	152	972
Reinvested number of units	2	2
Redeemed number of units	(863)	(193)
Ending number of units	141	850

For the periods ended December 31
(see note 2 in the generic notes)

	2012	2011
Series B		
Opening units	–	100
Issued number of units	–	–
Reinvested number of units	–	1
Redeemed number of units	–	(33)
Ending number of units	–	68
Series D		
Opening units	43 276	45 942
Issued number of units	39 748	59 886
Reinvested number of units	254	284
Redeemed number of units	(53 896)	(62 904)
Ending number of units	29 382	43 208
Series F		
Opening units	866	761
Issued number of units	871	587
Reinvested number of units	5	5
Redeemed number of units	(1 022)	(487)
Ending number of units	720	866
Series O		
Opening units	111 536	90 353
Issued number of units	129 040	127 811
Reinvested number of units	1 254	1 109
Redeemed number of units	(146 975)	(107 737)
Ending number of units	94 855	111 536

Investments by other related Investment Funds (000s) (see note 7 in the generic notes)

The following outstanding units of the Fund were held by the following related Investment Funds as at:

	December 31 2012	December 31 2011
Series O		
Phillips, Hager & North LifeTime 2015 Fund	1	–
Phillips, Hager & North LifeTime 2020 Fund	2	1
Phillips, Hager & North LifeTime 2025 Fund	2	1
Phillips, Hager & North LifeTime 2030 Fund	1	–
Phillips, Hager & North LifeTime 2035 Fund	2	–
Phillips, Hager & North LifeTime 2040 Fund	1	1
Phillips, Hager & North LifeTime 2045 Fund	1	–
Total	10	3

December 31, 2012

1. The Funds

The mutual funds (“Fund” or “Funds”) are open-ended mutual fund trusts governed by the laws of the Province of British Columbia and governed by a Master Declaration of Trust. RBC GAM is the manager and portfolio advisor of the Funds.

The Funds may issue an unlimited number of units in some or all of Series C, Advisor Series, Series H, Series B, Series D, Series F, Series I and Series O.

Series C units are available to investors who purchase units from authorized third-party dealers.

Advisor Series units are available to all investors with an initial sales charge or low-load sales charge option. Under the initial sales charge option, investors pay a sales commission ranging from 0% to 5% of the amount invested. Under the low-load sales charge option, investors do not pay a commission.

Series H units have lower fees than Series C units and are only available to investors who invest and maintain the required minimum balance.

Series B units were previously available to investors who purchased units from authorized third-party dealers. All outstanding Series B units were redesignated as Series D units effective July 2012.

Series D units are available to all investors and may be purchased, switched or redeemed through Phillips, Hager & North Investment Funds Ltd. (“PH&N IF”) or certain other authorized dealers (primarily discount brokers).

Series F units are available to investors who have fee-based accounts with their dealer.

Series I units have lower fees than Series F units and are only available to investors who invest and maintain the required minimum balance and who have accounts with dealers who have signed a fee-based agreement with RBC GAM.

Series O units are only available to large private or institutional investors as may be determined from time to time on a case-by-case basis. Series O units may only be purchased, switched or redeemed through RBC GAM or, in certain circumstances, PH&N IF.

2. Financial year/period

The information provided in these financial statements and notes thereto is for the 12-month periods ended or as at December 31, 2012 and 2011. In the year a Fund or series is

established, “period” represents the period from inception to December 31 of that fiscal year.

3. Summary of significant accounting policies

These financial statements have been prepared in accordance with Canadian generally accepted accounting principles (“GAAP”), which include estimates and assumptions made by management that may affect the reported amounts of assets (primarily valuation of investments), liabilities, income and expenses during the reported periods. Actual results may differ from estimates. The significant accounting policies of the Funds are as follows:

Valuation of Investments The valuation methods used to calculate the daily net asset value to transact units of the Funds (“transactional NAV”), as described in the Funds’ Annual Information Form, are not identical to the GAAP valuation methods used to determine the financial statement net assets (“net assets”) described below. The primary difference between net assets and transactional NAV relates to valuation of actively traded securities at bid prices for net assets and at last sale prices for transactional NAV.

In accordance with the Canadian Institute of Chartered Accountants (“CICA”) Handbook Section 3862, *Financial Instruments – Disclosures*, the Funds’ financial instruments are measured at fair value using a three-tier hierarchy based on inputs used to value the Funds’ investments and derivatives. The hierarchy of inputs is summarized below:

Level 1 – quoted prices (unadjusted) in active markets for identical assets or liabilities;

Level 2 – inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices); and

Level 3 – inputs for the asset or liability that are not based on observable market data (unobservable inputs).

Changes in valuation methods may result in transfers into or out of an investment’s assigned level.

The three-tier hierarchy of investments and derivatives is included in “Notes to Financial Statements – Fund Specific Information.”

Investments are recorded at fair value, which is determined as follows:

Equities – Common shares, preferred shares and exchange-traded funds are valued at the closing bid price recorded by the security exchange on which the security is principally traded.

December 31, 2012

Fixed-Income and Debt Securities – Bonds, mortgage-backed securities and debentures are valued at the closing bid price quoted by major dealers in such securities.

Mortgages are valued at a principal amount, which produces a yield equivalent to the prevailing rate of return on mortgages of similar type and term.

Short-Term Investments – Short-term investments are valued at their cost including applicable foreign exchange translations. This value, together with accrued interest, approximates fair value using closing bid prices.

Options – Listed options are valued at the closing bid price on the recognized exchange on which the option is traded for the long positions and the ask price for the short positions. The premium received for written options is recorded as a credit in the Statement of Investment Portfolio and adjusted daily to the fair value of the written option.

Forward Contracts – Forward contracts are valued at the gain or loss that would arise as a result of closing the position at the valuation date. Any gain or loss at the close of business on each valuation date is recorded in the Statements of Operations. The net receivable/payable on forward contracts is recorded separately in the Statements of Net Assets. Realized gain (loss) on foreign exchange contracts is included in “Net gain (loss) on foreign currencies and other net assets” in the Statements of Operations.

Futures Contracts – Futures contracts entered into by the Funds are financial agreements to purchase or sell a financial instrument at a contracted price on a specified future date. However, the Funds do not intend to purchase or sell the financial instrument on the settlement date; rather, they intend to close out each futures contract before settlement by entering into equal, but offsetting, futures contracts. Futures contracts are valued at the gain or loss that would arise as a result of closing the position at the valuation date. Any gain or loss at the close of business on each valuation date is recorded as “Net gain (loss) from futures contracts” in the Statements of Operations. The net receivable/payable on futures contracts is recorded separately in the Statements of Net Assets.

Mutual Fund Unit Valuation – Units of Funds are valued at their respective transactional NAV per unit received from fund companies on the relevant valuation dates.

Fair Valuation of Investments (including unlisted securities) – If the valuation methods described above are not appropriate, RBC GAM will estimate the fair value of an investment using established fair valuation procedures, such as consideration of public information, broker quotes, valuation models, fundamental analysis, matrix pricing, discounts from market prices of similar securities or discounts applied due to restrictions on the disposition of securities, and external fair value service providers.

Procedures are in place to determine the fair value of foreign securities traded in countries outside North America daily, to avoid stale prices and to take into account, among other things, any significant events occurring after the close of a foreign market. This fair valuation process takes into account the last quoted price of the security and adjusts the price based on inputs such as related indices, changes in foreign markets and American Depository Receipts (“ADR”) prices. These securities are classified as Level 2.

Foreign Exchange The value of investments and other assets and liabilities in foreign currencies is translated into Canadian dollars (U.S. dollars in the case of the Phillips, Hager & North \$U.S. Money Market Fund) at the rate of exchange on each valuation date. Purchases and sales of investments, income and expenses are translated at the rate of exchange prevailing on the respective dates of such transactions. Realized foreign exchange gains/losses are included in “Net gain (loss) on foreign currencies and other net assets” in the Statements of Operations.

Valuation of Series A different net asset value is calculated for each series of units of a Fund. The net asset value of a particular series of units is computed by calculating the value of the series’ proportionate share of the assets and liabilities of the Fund common to all series less the liabilities of the Fund attributable only to that series. Expenses directly attributable to a series are charged to that series. Other expenses are allocated proportionately to each series based upon the relative net asset value of each series. Expenses are accrued daily.

Investment Transactions Investment transactions are accounted for as of the trade date. Transaction costs, such as brokerage commissions, incurred by the Funds are recorded in the Statements of Operations for the period. The period change in the difference between fair value and average cost of securities represents unrealized gains and losses. The basis of determining the cost of portfolio assets, and realized and unrealized gains and losses on investments, is average cost.

Income Recognition Dividend income is recognized on the ex-dividend date and interest income is recognized on an accrual basis. “Other income (loss)” includes income from income trusts. Distributions received from income trusts are recognized based on the nature of the underlying components, such as income, capital gains and return of capital. “Other revenue” includes income earned by a Fund from investments in underlying funds.

Increase (Decrease) in Net Assets from Operations

Per Unit Increase (decrease) in net assets from operations per unit in the Statements of Operations represents the increase (decrease) in net assets from operations by series, divided by the average units outstanding per series during the period.

Early Redemption Fees Early redemption fees (short-term trading fees) are paid directly to the Fund and are designed to deter excessive trading and its associated costs. With the exception of money market funds, a Fund may apply a fee of 2% of the current value of units if the unitholder redeems or switches out units within seven days of purchasing or previously switching into a Fund.

Foreign Currencies The following is a list of abbreviations used in the Statement of Investment Portfolio:

AUD – Australian Dollar	JPY – Japanese Yen
CAD – Canadian Dollar	NOK – Norwegian Krone
CHF – Swiss Franc	SGD – Singapore Dollar
EUR – Euro	USD – United States Dollar
GBP – Pound Sterling	

4. Financial instrument risk and capital management

RBC GAM is responsible for managing each Fund’s capital, which is its net assets and consists primarily of its financial instruments.

A Fund’s investment activities expose it to a variety of financial risks. RBC GAM seeks to minimize potential adverse effects of these risks on a Fund’s performance by employing professional, experienced portfolio advisors, daily monitoring of the Fund’s holdings and market events, diversifying its investment portfolio within the constraints of its investment objectives, and, in some cases, periodically hedging certain risk exposures through the use of derivatives. To assist in managing risks, RBC GAM also uses internal guidelines, maintains a governance structure that oversees each Fund’s investment activities and monitors compliance with the Fund’s investment strategies, internal guidelines and securities regulations.

Liquidity risk

Liquidity risk is the possibility that investments in a Fund cannot be readily converted into cash when required. A Fund is exposed to daily cash redemptions of redeemable units. Liquidity risk is managed by investing the majority of a Fund’s assets in investments that are traded in an active market and that can be readily disposed. In accordance with securities regulations, a Fund must maintain at least 90% of its assets in liquid investments. In addition, a Fund aims to retain sufficient cash and cash equivalent positions to maintain liquidity, and has the ability to borrow up to 5% of its net assets for the purpose of funding redemptions.

Credit risk

Credit risk is the risk that a loss could arise from a security issuer or counterparty not being able to meet its financial obligations. The carrying amount of investments and other assets represents the maximum credit risk exposure as disclosed in a Fund’s Statements of Net Assets. The fair value of fixed-income and debt securities includes a consideration of the credit worthiness of the debt issuer. Credit risk exposure to over-the-counter derivative instruments is based on a Fund’s unrealized gain on the contractual obligations with the counterparty. Credit risk exposure is mitigated for those Funds participating in a securities lending program (see note 6). RBC GAM monitors each Fund’s credit exposure and counterparty ratings daily.

Interest rate risk

Interest rate risk is the risk that the fair value of a Fund’s interest-bearing investments will fluctuate due to changes in market interest rates. The value of fixed-income and debt securities, such as bonds, debentures, mortgages or other income-producing securities, is affected by interest rates. Generally, the value of these securities increases if interest rates fall and decreases if interest rates rise.

Currency risk

Currency risk is the risk that the value of investments denominated in currencies, other than the functional currency of a Fund, will fluctuate due to changes in foreign exchange rates. The value of investments denominated in a currency other than Canadian dollars is affected by changes in the value of the Canadian dollar or a Fund’s functional currency, in relation to the value of the currency in which the investment is denominated. When the value of the Canadian dollar falls in relation to foreign currencies, then the value of foreign investments rises. When the value of the Canadian dollar rises, the value of foreign investments falls.

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Other price risk

Other price risk is the risk that the value of financial instruments will fluctuate as a result of changes in market prices (other than those arising from interest rate or currency risk), whether caused by factors specific to an individual investment, its issuer, or all factors affecting all instruments traded in a market or market segment.

5. Taxes

The Funds qualify as open-ended mutual fund trusts or unit trusts under the *Income Tax Act* (Canada). In general, the Funds are subject to income tax, however, no income tax is payable on net income and/or net realized capital gains which are distributed to unitholders. In addition, for mutual fund trusts, income taxes payable on net realized capital gains are refundable on a formula basis when units of the Funds are redeemed.

Capital losses are available to be carried forward indefinitely and applied against future capital gains. Non-capital losses may be carried forward to reduce future taxable income for up to 10 years, with the exception of non-capital losses realized in 2006 and later years, which may be carried forward up to 20 years.

6. Securities lending revenue

Certain of the Funds lend portfolio securities from time to time in order to earn additional income. Income from securities lending is included in the Statements of Operations of a Fund. Each such Fund will have entered into a securities lending program with its custodian, RBC Investor Services Trust ("RBC IS"). The aggregate market value of all securities loaned by a Fund cannot exceed 50% of the assets of a Fund. The Fund receives collateral, with an approved credit rating of at least A, of at least 102% of the value of securities on loan. The Fund is indemnified by RBC IS for any collateral credit or market loss. As such, the credit risk associated with securities lending is considered minimal.

7. Administrative and other related-party transactions**Manager and Registrar**

RBC GAM is an indirect wholly-owned subsidiary of Royal Bank of Canada ("Royal Bank"). RBC GAM is the manager and registrar of the Funds. RBC GAM is responsible for the Funds' day-to-day operations, provides investment advice and portfolio management services to the Funds and appoints distributors for the Funds. RBC GAM, as registrar,

also keeps records of who owns units of the Funds. RBC GAM is paid a management fee by the Funds as compensation for its services. No management fees are paid by the Funds with respect to Series O units. Series O unitholders pay a negotiated fee directly to RBC GAM for investment-counselling services.

The Funds pay a fixed administration fee to RBC GAM. RBC GAM in turn pays certain operating expenses of the Funds. These expenses include regulatory filing fees and other day-to-day operating expenses including, but not limited to, recordkeeping, accounting and fund valuation costs, custody fees, audit and legal fees, and the costs of preparing and distributing annual and semi-annual reports, prospectuses, statements and investor communications.

Notwithstanding the fixed administration fee, the Funds also pay certain operating expenses directly, including the costs related to the Board of Governors ("BoG") of the Funds and the cost of any new government or regulatory requirements introduced and any borrowing costs (collectively, *other fund costs*), and taxes (including, but not limited to, GST/HST). Other Fund costs will be allocated among each series of units of a fund in accordance with the services used. RBC GAM may, in some years and in certain cases, absorb a portion of operating expenses. The decision to absorb the operating expenses is reviewed annually and determined at the discretion of RBC GAM, without notice to unitholders.

Certain Funds may invest in units of other Funds managed by RBC GAM or its affiliates.

Affiliates of RBC GAM that provide services to the Funds in the course of their normal businesses are discussed below.

Portfolio Advisor

With the exception of the BonaVista Global Balanced Fund and the BonaVista Canadian Equity Value Fund, RBC GAM is the principal portfolio advisor of the Funds. BonaVista Asset Management Ltd. ("BonaVista"), a subsidiary of RBC GAM, is the principal portfolio advisor for the BonaVista Global Balanced Fund and the BonaVista Canadian Equity Value Fund. Sky Investment Counsel Inc. ("Sky") is the sub-advisor for the Phillips, Hager & North Overseas Equity Fund and the non-North American equity assets of the Phillips, Hager & North Balanced Fund, the Phillips, Hager & North Global Equity Fund and the Phillips, Hager & North Community Values Global Equity Fund. RBC GAM has a non-controlling interest in Sky. The fees paid to BonaVista and Sky are paid by RBC GAM and not the Funds.

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Distributors

RBC GAM, PH&N IE, Royal Mutual Funds Inc., RBC Direct Investing Inc. and RBC Dominion Securities Inc. are the principal distributors of, or distribute certain series of units of, the Funds. Dealers receive an ongoing commission based on the total value of their clients' Series C, Advisor Series, Series H, Series B or Series D units.

Brokerage

The Funds have established standard brokerage agreements at market rates with related-party dealers.

Trustee and Custodian

RBC IS is the trustee and custodian of the Funds. RBC IS is paid custodial fees for holding the assets of the Funds, and trustee fees for acting as the trustee. The fees paid to RBC IS are paid by RBC GAM and not the Funds.

Other Related-Party Transactions

Pursuant to applicable securities legislation, the Funds relied on the standing instructions from the BoG in its capacity as the Independent Review Committee with respect to one or more of the following related-party transactions:

Related-Party Trading Activities

- (a) trades in securities of Royal Bank;
- (b) investments in the securities of issuers for which a related-party dealer acted as an underwriter during the distribution of such securities and the 60-day period following the conclusion of such distribution of the underwritten securities to the public;
- (c) purchases of equity and debt securities from or sales of equity or debt securities to a related-party dealer, where it acted as principal; and

Inter-Fund Trading

- (d) purchases or sales of securities of an issuer from or to another investment fund or managed account managed by RBC GAM.

The applicable standing instructions require that Related-Party Trading Activities and Inter-Fund Trading be conducted in accordance with RBC GAM policy and that RBC GAM advise the BoG of a material breach of any standing instruction. RBC GAM policy requires that an investment decision in respect of Related-Party Trading Activities: (i) is made free from any influence of Royal Bank or its associates or affiliates and without taking into account any consideration relevant to Royal Bank or its affiliates

or associates, (ii) represents the business judgment of the portfolio manager, uninfluenced by considerations other than the best interests of the Funds, (iii) is in compliance with RBC GAM policies and procedures, and (iv) achieves a fair and reasonable result for the Funds. RBC GAM policy requires that an investment decision in respect of Inter-Fund Trading is in the best interests of each Fund.

8. Future accounting changes***International Financial Reporting Standards***

The Funds will be required to adopt the International Financial Reporting Standards ("IFRS") beginning in their fiscal 2014 year. In preparation to meet the requirements, RBC GAM has taken the following steps in managing the transition to IFRS:

- (a) established a committee for the development and implementation of a transition plan and to provide oversight of the transition to IFRS;
- (b) commenced activities to identify key issues and the likely impacts resulting from the adoption of IFRS; and
- (c) initiated analysis to reconfigure accounting systems used by the Funds.

The key elements of the plan currently include disclosure of the quantitative impact, if any, in the comparative 2013 financial statements and the preparation of the 2014 financial statements in accordance with IFRS.

Since IFRS standards are constantly evolving, the major qualitative impacts based on standards approved to date are the addition of a cash flow statement and the impact of classification of puttable instruments, the units of the Fund, as a liability or as an equity.

Regardless of the financial statement impacts, RBC GAM has presently determined that there will be no quantitative impact to the transactional NAV of each series as a result of the changeover to IFRS.

9. Comparative figures

In the Statements of Operations, "Board of Governors costs" for certain funds, which were reimbursed by the manager for the prior period, have been reflected to conform with the presentation in the current year.