

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 U.S. 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 TOTAL RETURN BOND FUND

December 31, 2012

Holdings	Security	Cost	Fair Value	% of Net Assets
MUTUAL FUND UNITS				
7 499 786	Phillips, Hager & North High Yield Bond Fund*	\$ 86 326	\$ 87 697	
TOTAL MUTUAL FUND UNITS		86 326	87 697	3.0

Par Value	Security	Coupon Rate %	Maturity	Cost	Fair Value	% of Net Assets
BONDS						
AUSTRALIA BONDS						
\$ 6 310	Brookfield Infrastructure Finance Pty Ltd. CAD	3.455	10-Oct-17	\$ 6 310	\$ 6 357	
TOTAL AUSTRALIA BONDS				6 310	6 357	0.2

CANADIAN BONDS**CORPORATE**

4 188	407 International Inc.	3.870	24-Nov-17	4 461	4 464	
4 000	407 International Inc.	5.960	03-Dec-35	5 087	5 300	
7 990	407 International Inc.	4.450	15-Nov-41	8 087	8 769	
2 425	407 International Inc.	4.190	25-Apr-42	2 470	2 553	
3 853	Access Justice Durham Ltd.	5.015	31-Aug-39	4 103	4 332	
3 495	Aéroports de Montréal	6.950	16-Apr-32	3 591	4 547	
689	Aéroports de Montréal	6.611	11-Apr-33	715	871	
1 135	Aéroports de Montréal	5.170	17-Sep-35	1 342	1 358	
460	Aéroports de Montréal	5.670	16-Oct-37	576	591	
8 060	Alliance Pipeline LP	7.181	30-Jun-23	9 872	9 811	
3 029	Alliance Pipeline LP	5.546	31-Dec-23	3 376	3 357	
2 293	Alliance Pipeline LP	6.765	31-Dec-25	2 645	2 767	
3 532	Alliance Pipeline LP	7.217	31-Dec-25	4 399	4 358	
1 455	AltaGas Ltd.	4.070	01-Jun-20	1 455	1 531	
3 920	AltaGas Ltd.	3.720	28-Sep-21	3 919	4 012	
4 300	AltaLink Investments LP	5.207	16-Dec-16	4 300	4 668	
3 231	AltaLink Investments LP	3.674	05-Jun-19	3 231	3 253	
2 440	AltaLink LP	5.381	26-Mar-40	3 129	3 057	
1 378	AltaLink LP	4.462	08-Nov-41	1 378	1 520	
1 325	AltaLink LP	3.990	30-Jun-42	1 368	1 358	
22 655	American Express Canada Credit Corp.	5.900	02-Apr-13	22 627	22 901	
10 687	Bank of Montreal	3.930	27-Apr-15	11 244	11 197	
11 100	Bank of Montreal	5.180	10-Jun-15	12 042	11 979	
18 320	Bank of Montreal	1.890	05-Oct-15	18 319	18 317	
2 985	Bank of Montreal	3.490	10-Jun-16	3 017	3 123	
6 931	Bank of Montreal	2.960	02-Aug-16	7 049	7 131	
4 275	Bank of Montreal	4.550	01-Aug-17	4 699	4 692	
4 225	Bank of Montreal	2.240	11-Dec-17	4 224	4 207	
1 465	Bank of Montreal	6.020	02-May-18	1 688	1 727	
6 765	Bank of Nova Scotia	1.418	08-Nov-13	6 765	6 766	
9 105	Bank of Nova Scotia	2.740	01-Dec-16	9 126	9 299	
2 960	Bank of Nova Scotia	2.598	27-Feb-17	2 960	3 001	
6 765	Bank of Nova Scotia	4.100	08-Jun-17	6 788	7 282	
565	Bank of Nova Scotia	4.990	27-Mar-18	562	569	
42 840	Bank of Nova Scotia	6.000	03-Oct-18	43 177	44 180	
4 005	Bank of Nova Scotia	6.650	22-Jan-21	4 351	4 508	
2 902	Bank of Nova Scotia	3.036	18-Oct-24	2 901	2 933	
5 600	BC Tel	9.650	08-Apr-22	7 564	8 201	

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

December 31, 2012

Par Value	Security	Coupon Rate %	Maturity	Cost	Fair Value	% of Net Assets
CORPORATE (cont.)						
\$ 1 130	bcIMC Realty Corp.	2.650	29-Jun-17	\$ 1 130	\$ 1 144	
3 900	bcIMC Realty Corp.	3.510	29-Jun-22	3 899	3 979	
2 125	Bell Aliant Regional Communications LP	4.950	26-Feb-14	2 034	2 194	
4 600	Bell Aliant Regional Communications LP	6.290	17-Feb-15	5 128	4 969	
4 705	Bell Canada	4.850	30-Jun-14	4 929	4 913	
2 530	Bell Canada	4.400	16-Mar-18	2 534	2 749	
7 535	Bell Canada	3.350	18-Jun-19	7 523	7 758	
3 675	Bell Canada	7.300	23-Feb-32	3 783	4 897	
4 944	Brookfield Asset Management Inc.	3.950	09-Apr-19	4 971	5 067	
1 190	Brookfield Asset Management Inc.	5.300	01-Mar-21	1 189	1 315	
4 925	Brookfield Asset Management Inc.	5.950	14-Jun-35	4 902	4 904	
4 400	Brookfield Renewable Power Inc.	6.132	30-Nov-16	4 400	4 892	
5 394	BRP Finance ULC	4.790	07-Feb-22	5 394	5 702	
8 700	Calloway Real Estate Investment Trust	5.370	12-Oct-16	8 662	9 414	
2 030	Canada Safeway Ltd.	3.000	31-Mar-14	2 044	2 041	
7 904	Canadian Imperial Bank of Commerce	1.419	28-Nov-13	7 904	7 914	
6 700	Canadian Imperial Bank of Commerce	4.750	22-Dec-14	6 891	7 089	
24 555	Canadian Imperial Bank of Commerce	3.100	02-Mar-15	25 169	25 229	
3 395	Canadian Imperial Bank of Commerce	3.400	14-Jan-16	3 420	3 533	
16 843	Canadian Imperial Bank of Commerce	2.650	08-Nov-16	16 936	17 139	
1 525	Canadian Imperial Bank of Commerce	2.350	18-Oct-17	1 531	1 527	
1 020	Canadian Pacific Railway Ltd.	6.450	17-Nov-39	1 019	1 254	
2 500	Canadian Utilities Ltd.	3.122	09-Nov-22	2 500	2 503	
790	Canadian Utilities Ltd.	9.400	01-May-23	1 219	1 212	
4 000	Capital Desjardins Inc.	5.187	05-May-20	4 000	4 560	
6 220	Capital Desjardins Inc.	3.797	23-Nov-20	6 219	6 475	
490	Caterpillar Financial Services Ltd.	2.200	01-Jun-15	492	494	
3 380	Centre Street Trust	3.690	14-Jun-21	3 380	3 373	
16 420	Citigroup Finance Canada Inc.	5.500	21-May-13	16 416	16 656	
6 000	Cogeco Cable Inc.	5.950	09-Jun-14	5 993	6 290	
4 810	CU Inc.	6.145	22-Nov-17	5 773	5 681	
6 124	CU Inc.	6.800	13-Aug-19	7 825	7 716	
2 255	CU Inc.	5.896	20-Nov-34	2 927	2 944	
5 887	CU Inc.	5.556	30-Oct-37	7 489	7 491	
4 892	CU Inc.	5.580	26-May-38	5 593	6 283	
1 265	CU Inc.	6.500	07-Mar-39	1 820	1 815	
3 805	CU Inc.	3.805	10-Sep-42	3 805	3 794	
7 515	Emera Inc.	4.100	20-Oct-14	7 770	7 785	
8 175	Emera Inc.	2.960	13-Dec-16	8 206	8 315	
4 493	Enbridge Gas Distribution Inc.	5.160	04-Dec-17	5 153	5 116	
6 333	Enbridge Inc.	5.170	19-May-16	7 069	6 958	
2 822	Enbridge Inc.	5.000	09-Aug-16	3 139	3 093	
12 925	Enbridge Inc.	4.770	02-Sep-19	13 223	14 495	
4 690	Enbridge Inc.	4.530	09-Mar-20	5 235	5 193	
3 815	Enbridge Inc.	4.260	01-Feb-21	3 813	4 159	
2 005	Enbridge Income Fund Holdings Inc.	2.920	14-Dec-17	2 005	2 000	
1 890	Enbridge Income Fund Holdings Inc.	3.940	13-Jan-23	1 890	1 881	
910	Enbridge Pipelines Inc.	4.450	06-Apr-20	1 017	1 021	
4 590	Enbridge Pipelines Inc.	8.200	15-Feb-24	6 731	6 657	
2 270	Enbridge Pipelines Inc.	5.350	10-Nov-39	2 849	2 849	
2 395	Enbridge Pipelines Inc.	5.330	06-Apr-40	2 395	2 992	
8 245	Encana Corp.	5.800	18-Jan-18	9 236	9 342	
4 380	Enersource Corp.	4.521	29-Apr-21	4 380	4 928	
570	Enersource Corp.	5.297	29-Apr-41	716	705	
770	EPCOR Utilities Inc.	6.750	22-Mar-16	911	875	

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

December 31, 2012

Par Value	Security	Coupon Rate %	Maturity	Cost	Fair Value	% of Net Assets
CORPORATE (cont.)						
\$ 1 800	EPCOR Utilities Inc.	5.800	31-Jan-18	\$ 2 070	\$ 2 079	
2 465	EPCOR Utilities Inc.	5.750	24-Nov-39	2 461	3 085	
1 975	FortisBC Energy Inc.	5.900	26-Feb-35	2 599	2 588	
900	Gaz Metropolitan Inc.	4.930	18-Jun-19	1 033	1 027	
4 390	Golden Credit Card Trust	3.824	15-May-15	4 618	4 601	
21 441	Golden Credit Card Trust	3.510	15-May-16	21 757	22 496	
971	Greater Toronto Airports Authority	7.050	12-Jun-30	1 369	1 361	
2 085	Greater Toronto Airports Authority	7.100	04-Jun-31	2 466	2 971	
2 937	Great-West Lifeco Inc.	4.650	13-Aug-20	2 951	3 262	
2 816	Horizon Holdings Inc.	3.033	25-Jul-22	2 816	2 810	
4 700	HSBC Bank Canada	3.860	21-May-15	4 705	4 915	
14 665	HSBC Bank Canada	2.572	23-Nov-15	14 665	14 899	
7 275	HSBC Bank Canada	2.901	13-Jan-17	7 275	7 448	
11 278	HSBC Bank Canada	3.558	04-Oct-17	11 278	11 874	
2 000	Hydro One Inc.	3.130	19-Nov-14	2 070	2 057	
4 365	Hydro One Inc.	4.640	03-Mar-16	4 744	4 738	
3 225	Hydro One Inc.	6.930	01-Jun-32	4 625	4 594	
1 105	Hydro One Inc.	6.350	31-Jan-34	1 513	1 507	
3 060	Hydro One Inc.	6.030	03-Mar-39	4 199	4 175	
475	Hydro One Inc.	5.490	16-Jul-40	600	609	
1 700	Inter Pipeline Fund	3.839	30-Jul-18	1 700	1 795	
1 095	Loblaw Companies Ltd.	6.450	09-Feb-28	1 167	1 251	
3 020	Loblaw Companies Ltd.	6.500	22-Jan-29	3 347	3 479	
3 740	Lower Mattagami Energy LP	2.228	23-Oct-17	3 740	3 747	
2 010	Lower Mattagami Energy LP	4.331	18-May-21	2 010	2 233	
2 734	Manitoba Telecom Services Inc.	4.590	01-Oct-18	2 734	2 959	
2 730	Maritimes & Northeast Pipeline LP	4.340	30-Nov-19	2 730	2 847	
15 670	MI Developments Inc.	6.050	22-Dec-16	15 613	16 245	
12 690	Molson Coors Capital Finance ULC	5.000	22-Sep-15	13 613	13 599	
7 990	National Bank of Canada	2.231	30-Jan-15	8 001	8 059	
1 450	National Bank of Canada	4.030	26-May-15	1 458	1 523	
5 000	National Bank of Canada	2.702	15-Dec-16	5 049	5 090	
1 105	Nova Scotia Power Inc.	8.400	23-Oct-15	1 331	1 283	
2 545	Nova Scotia Power Inc.	6.950	25-Aug-33	3 634	3 593	
3 260	Ontrea Inc.	4.619	09-Apr-18	3 260	3 552	
4 810	OPB Finance Trust	3.890	04-Jul-42	4 807	4 885	
5 515	Pembina Pipeline Corp.	3.770	24-Oct-22	5 543	5 558	
5 750	Plenary Health Hamilton LP	3.157	13-Dec-13	5 750	5 808	
880	Plenary Properties LTAP LP	6.288	31-Jan-44	931	1 151	
7 881	Rogers Communications Inc.	5.340	22-Mar-21	7 902	9 023	
5 895	Rogers Communications Inc.	6.680	04-Nov-39	6 120	7 422	
2 895	Rogers Communications Inc.	6.110	25-Aug-40	2 892	3 398	
580	Rogers Communications Inc.	6.560	22-Mar-41	724	721	
1 375	Royal Bank of Canada*	3.360	11-Jan-16	1 431	1 429	
59 660	Royal Bank of Canada*	2.680	08-Dec-16	60 175	60 784	
15 946	Royal Bank of Canada*	3.660	25-Jan-17	16 852	16 838	
21 355	Royal Bank of Canada*	2.580	13-Apr-17	21 481	21 647	
2 170	Royal Bank of Canada*	5.450	04-Nov-18	2 319	2 236	
2 100	Royal Bank of Canada*	4.350	15-Jun-20	2 212	2 215	
10 647	Royal Bank of Canada*	2.990	06-Dec-24	10 661	10 703	
9 830	Shaw Communications Inc.	6.750	09-Nov-39	10 043	10 915	
4 125	Sobeys Inc.	5.790	06-Oct-36	4 125	4 349	
1 945	Sobeys Inc.	6.640	07-Jun-40	1 970	2 287	
11 590	Sun Life Capital Trust II	5.863	31-Dec-19	11 590	12 686	
5 985	Sun Life Financial Inc.	4.950	01-Jun-36	6 107	6 328	

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

PHILLIPS, HAGER & NORTH TOTAL RETURN BOND FUND

December 31, 2012

Par Value	Security	Coupon Rate %	Maturity	Cost	Fair Value	% of Net Assets
CORPORATE (cont.)						
\$ 2 540	TELUS Corp.	4.950	15-May-14	\$ 2 655	\$ 2 647	
315	TELUS Corp.	5.950	15-Apr-15	355	343	
11 425	Teranet Holdings LP	4.807	16-Dec-20	11 830	12 706	
6 415	Teranet Holdings LP	5.754	17-Dec-40	6 360	7 248	
2 405	Teranet Holdings LP	6.100	17-Jun-41	2 789	2 854	
90	Terasen Gas Inc.	6.500	01-May-34	125	125	
785	Terasen Gas Inc.	6.000	02-Oct-37	1 056	1 059	
75	Terasen Gas Inc.	6.550	24-Feb-39	109	109	
3 785	The Standard Life Assurance Co of Canada	3.938	21-Sep-22	3 785	3 923	
10 677	Thomson Reuters Corp.	6.000	31-Mar-16	12 022	11 930	
11 058	Thomson Reuters Corp.	4.350	30-Sep-20	12 053	12 091	
1 220	Toronto Hydro Corp.	6.110	06-May-13	1 336	1 240	
10 500	Toronto Hydro Corp.	4.490	12-Nov-19	11 700	11 749	
564	Toronto Hydro Corp.	3.540	18-Nov-21	564	592	
2 600	TransAlta Corp.	6.450	29-May-14	2 829	2 719	
2 140	TransCanada PipeLines Ltd.	9.450	20-Mar-18	2 873	2 836	
75	TransCanada PipeLines Ltd.	7.900	15-Apr-27	99	108	
4 859	TransCanada PipeLines Ltd.	7.340	18-Jul-28	6 758	6 690	
2 450	TransCanada PipeLines Ltd.	8.200	15-Aug-31	3 718	3 709	
4 600	Union Gas Ltd.	11.500	28-Aug-15	6 253	5 701	
4 975	Union Gas Ltd.	4.640	30-Jun-16	5 352	5 407	
1 000	Union Gas Ltd.	5.350	27-Apr-18	1 162	1 147	
3 500	Union Gas Ltd.	8.750	03-Aug-18	4 657	4 591	
3 940	Union Gas Ltd.	8.650	10-Nov-25	5 548	6 003	
3 169	Veresen Inc.	3.950	14-Mar-17	3 167	3 267	
3 438	Veresen Inc.	4.000	22-Nov-18	3 429	3 533	
5 375	Wells Fargo Financial Canada Corp.	4.330	06-Dec-13	5 613	5 512	
3 215	Wells Fargo Financial Canada Corp.	3.970	03-Nov-14	3 366	3 339	
6 027	Wells Fargo Financial Canada Corp.	4.380	30-Jun-15	6 400	6 377	
7 565	Wells Fargo Financial Canada Corp.	2.774	09-Feb-17	7 565	7 694	
3 320	Wells Fargo Financial Canada Corp.	2.944	25-Jul-19	3 327	3 350	
6 680	Westcoast Energy Inc.	3.280	15-Jan-16	6 901	6 913	
1 245	Westcoast Energy Inc.	8.500	04-Sep-18	1 632	1 605	
2 767	Westcoast Energy Inc.	9.900	10-Jan-20	4 019	3 948	
2 670	Westcoast Energy Inc.	4.570	02-Jul-20	2 955	2 979	
2 900	Westcoast Energy Inc.	4.791	28-Oct-41	3 108	3 263	
3 314	Winnipeg Airport Authority Inc.	6.102	20-Nov-40	3 314	4 028	
				1 038 808	1 067 833	36.7
FEDERAL						
46 668	Canada Housing Trust No. 1	3.750	15-Mar-20	52 183	52 092	
12 972	Canada Housing Trust No. 1	3.800	15-Jun-21	14 546	14 595	
2 682	CBC Monetization Trust	4.688	15-May-27	2 681	3 009	
68 531	Government of Canada	1.500	01-Sep-17	68 898	68 893	
12 040	Government of Canada	3.750	01-Jun-19	13 652	13 649	
10	Government of Canada	3.500	01-Jun-20	10	11	
7	Government of Canada	2.750	01-Jun-22	7	8	
479	Government of Canada	5.750	01-Jun-29	714	712	
1 141	Government of Canada	4.000	01-Jun-41	1 537	1 525	
				154 228	154 494	5.3

PHILLIPS, HAGER & NORTH TOTAL RETURN BOND FUND

December 31, 2012

Par Value	Security	Coupon Rate %	Maturity	Cost	Fair Value	% of Net Assets
PROVINCIAL/MUNICIPAL						
\$ 4 965	Hospital for Sick Children	5.217	16-Dec-49	\$ 4 847	\$ 6 131	
1 647	Municipal Finance Authority of British Columbia	3.350	01-Jun-22	1 645	1 703	
200	Ontario Electricity Financial Corp.	8.500	26-May-25	282	309	
4 825	Ontario Electricity Financial Corp.	9.000	26-May-25	7 410	7 732	
19 336	Ontario Electricity Financial Corp.	8.250	22-Jun-26	27 525	30 036	
500	Ontario Infrastructure Projects Corp.	4.600	01-Jun-15	517	533	
4 932	Province of New Brunswick	4.800	03-Jun-41	6 059	6 064	
26 125	Province of Ontario	3.150	02-Jun-22	26 925	27 030	
11 250	Province of Ontario	9.500	13-Jul-22	15 387	17 486	
37 438	Province of Ontario	8.100	08-Sep-23	51 994	55 148	
15 910	Province of Ontario	8.500	02-Dec-25	23 557	25 016	
1 555	Province of Ontario	8.000	02-Jun-26	2 155	2 378	
200 002	Province of Ontario	7.600	02-Jun-27	274 961	302 019	
36 785	Province of Ontario	6.200	02-Jun-31	45 497	51 143	
35 939	Province of Ontario	5.850	08-Mar-33	41 938	48 813	
39 264	Province of Ontario	5.600	02-Jun-35	52 238	52 470	
11 662	Province of Ontario	4.700	02-Jun-37	12 180	14 057	
33 075	Province of Ontario	4.600	02-Jun-39	33 968	39 661	
37 462	Province of Ontario	4.650	02-Jun-41	46 051	45 902	
11 527	Province of Ontario	3.500	02-Jun-43	11 834	11 791	
61 133	Province of Quebec	3.500	01-Dec-22	64 766	64 390	
230	Province of Quebec	9.375	16-Jan-23	329	357	
59 447	Province of Quebec	6.250	01-Jun-32	72 938	82 390	
9 925	Province of Quebec	5.750	01-Dec-36	11 353	13 363	
12 534	Province of Quebec	5.000	01-Dec-41	15 609	15 824	
1 956	Province of Quebec	4.250	01-Dec-43	2 235	2 226	
8 842	TransLink	3.800	02-Nov-20	8 864	9 453	
				863 064	933 425	32.1
TOTAL CANADIAN BONDS				2 056 100	2 155 752	74.1
UNITED KINGDOM BONDS						
6 025	BAA Funding Ltd. CAD	4.000	03-Jul-19	5 987	6 271	
15 185	National Grid Electricity Transmission Plc. CAD	2.730	20-Sep-17	15 235	15 304	
7 170	National Grid Electricity Transmission Plc. CAD	2.900	26-Nov-19	7 170	7 126	
				28 392	28 701	1.0
TOTAL UNITED KINGDOM BONDS						
UNITED STATES BONDS						
5 930	Anheuser-Busch InBev Worldwide Inc. CAD	3.650	15-Jan-16	5 984	6 211	
20 000	Bank of America Corp. CAD	1.818	01-Jun-16	19 866	19 100	
4 215	Goldman Sachs Group Inc. CAD	5.200	19-Apr-22	4 121	4 250	
8 850	JPMorgan Chase & Co. CAD	2.920	19-Sep-17	8 875	8 902	
19 975	Merrill Lynch & Co. Inc. CAD	5.290	30-May-22	19 273	20 316	
5 590	Molson Coors International LP CAD	3.950	06-Oct-17	5 656	5 882	
				63 775	64 661	2.2
TOTAL UNITED STATES BONDS				2 154 577	2 255 471	77.5
TOTAL BONDS						
MORTGAGE-BACKED SECURITIES						
972	Data Centres Trust	7.233	10-Sep-14	1 077	1 010	
7 083	Equitable Trust	4.350	01-Jan-18	7 325	7 746	
2 189	Peoples Trust	4.200	01-Oct-19	2 187	2 407	
				10 589	11 163	0.4
TOTAL MORTGAGE-BACKED SECURITIES						

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

PHILLIPS, HAGER & NORTH TOTAL RETURN BOND FUND

December 31, 2012

Par Value	Security	Cost	Fair Value	% of Net Assets
MORTGAGES				
CMHC Insured				
\$ 2 960	4.930% Nov 01, 2019	\$ 3 018	\$ 3 261	
2 142	4.930% Dec 01, 2019	2 156	2 400	
1 993	4.850% Jan 01, 2020	2 011	2 250	
1 796	4.260% Nov 01, 2022	1 818	1 931	
TOTAL MORTGAGES		9 003	9 842	0.3
SHORT-TERM INVESTMENTS†				
8 800	Canadian Master Trust - Series A	8 765	8 765	
1 400	Clarity Trust	1 396	1 396	
36 850	Darwin Receivables Trust - Senior Notes	36 701	36 701	
41 500	Fusion Trust	41 375	41 375	
11 000	Government of Canada Treasury Bills	10 971	10 971	
20 000	HSBC Bank Canada	19 941	19 941	
47 400	Inter Pipeline Fund	47 251	47 251	
20 000	King Street Funding Trust	19 980	19 980	
14 550	Merit Trust - Senior Notes	14 458	14 458	
7 590	National Bank of Canada	7 587	7 587	
99 050	Prime Trust - Senior Notes	98 691	98 691	
47 700	Reliant Trust	47 500	47 500	
15 760	Ridge Trust	15 728	15 728	
14 000	TELUS Corp.	13 994	13 994	
5 000	TransCanada PipeLines Ltd.	4 986	4 986	
35 120	Union Gas Ltd.	35 112	35 112	
106 130	Zeus Receivables Trust - Senior Notes	105 795	105 795	
TOTAL SHORT-TERM INVESTMENTS		530 231	530 231	18.2
TOTAL INVESTMENTS		\$ 2 790 726	2 894 404	99.4
OTHER NET ASSETS			17 714	0.6
NET ASSETS			\$ 2 912 118	100.0

* Investment in related party (see note 7 in the generic notes).

† Short-term investments, which may be made up of treasury bills, commercial paper, term deposits and discount notes, and are grouped by issuer, earn interest at rates ranging from 0.97% to 1.31% and mature between January 2, 2013 and June 17, 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	\$ 2 894 404	\$ 2 517 194
Cash	296	579
Due from investment dealers	7 918	—
Subscriptions receivable	2 057	6 300
Unrealized gain on futures contracts	—	133
Futures contracts margin receivable	1 902	1 546
Dividends receivable, interest accrued and other assets	16 441	18 095
TOTAL ASSETS	2 923 018	2 543 847
LIABILITIES		
Due to investment dealers	8 680	—
Redemptions payable	1 294	1 355
Accounts payable and accrued expenses	926	801
TOTAL LIABILITIES	10 900	2 156
NET ASSETS	\$ 2 912 118	\$ 2 541 691
Investments at cost	\$ 2 790 726	\$ 2 413 258
NET ASSETS, END OF PERIOD		
SERIES C	\$ 253 737	\$ 218 307
ADVISOR SERIES	\$ 120 326	\$ 45 349
SERIES B*	\$ —	\$ 3 508
SERIES D	\$ 724 420	\$ 803 197
SERIES F	\$ 320 424	\$ 223 208
SERIES O	\$ 1 493 211	\$ 1 248 122
NET ASSETS PER UNIT, END OF PERIOD		
SERIES C	\$ 11.69	\$ 11.62
ADVISOR SERIES	\$ 11.69	\$ 11.62
SERIES B*	\$ —	\$ 11.72
SERIES D	\$ 11.68	\$ 11.61
SERIES F	\$ 11.70	\$ 11.62
SERIES O	\$ 11.62	\$ 11.54
NET ASSET VALUE (TRANSACTIONAL NAV) PER UNIT, END OF PERIOD (see note 3 in the generic notes)		
SERIES C	\$ 11.70	\$ 11.63
ADVISOR SERIES	\$ 11.70	\$ 11.63
SERIES B*	\$ —	\$ 11.74
SERIES D	\$ 11.69	\$ 11.62
SERIES F	\$ 11.71	\$ 11.64
SERIES O	\$ 11.63	\$ 11.56

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	\$ 100 793	\$ 98 528
Net gain (loss) from futures contracts	130	(732)
Other revenue	5 039	3 432
TOTAL INCOME (LOSS)	105 962	101 228
EXPENSES (see notes – Fund Specific Information)		
Management fees	8 554	6 989
Administration fees	884	751
Board of Governors costs	4	4
GST/HST	990	832
TOTAL EXPENSES	10 432	8 576
NET INVESTMENT INCOME (LOSS)	95 530	92 652
REALIZED AND UNREALIZED GAIN (LOSS) ON INVESTMENTS		
Capital gains received from underlying funds	1 019	—
Net realized gain (loss) on investments	14 776	37 419
Net gain (loss) on foreign currencies and other net assets	13	535
Change in unrealized gain (loss) on investments	(258)	60 981
NET GAIN (LOSS) ON INVESTMENTS	15 550	98 935
INCREASE (DECREASE) IN NET ASSETS FROM OPERATIONS		
	\$ 111 080	\$ 191 587
INCREASE (DECREASE) IN NET ASSETS FROM OPERATIONS		
SERIES C	\$ 7 966	\$ 13 891
ADVISOR SERIES	\$ 2 866	\$ 1 598
SERIES B*	\$ —	\$ 266
SERIES D	\$ 30 182	\$ 61 726
SERIES F	\$ 10 715	\$ 14 466
SERIES O	\$ 59 351	\$ 99 640
INCREASE (DECREASE) IN NET ASSETS FROM OPERATIONS PER UNIT		
SERIES C	\$ 0.38	\$ 0.82
ADVISOR SERIES	\$ 0.38	\$ 0.82
SERIES B*	\$ —	\$ 0.86
SERIES D	\$ 0.46	\$ 0.89
SERIES F	\$ 0.45	\$ 0.88
SERIES O	\$ 0.52	\$ 0.95

* 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	\$ 218 307	\$ 189 768	\$ 45 349	\$ 2 796	\$ –	\$ 3 724	\$ 806 705	\$ 825 307
INCREASE (DECREASE) FROM OPERATIONS	7 966	13 891	2 866	1 598	–	266	30 182	61 726
Early redemption fees	–	–	–	–	–	–	–	–
Proceeds from units issued	86 477	80 505	82 757	43 506	–	–	96 228	101 843
Proceeds from reinvestment of distributions	6 093	6 163	2 099	714	–	129	21 787	28 289
Payments on redemption of units	(58 399)	(65 251)	(10 105)	(2 352)	–	(479)	(205 582)	(181 458)
TOTAL UNIT TRANSACTIONS	34 171	21 417	74 751	41 868	–	(350)	(87 567)	(51 326)
Distributions from net income	(6 707)	(5 960)	(2 640)	(747)	–	(119)	(24 900)	(29 497)
Distributions from net gains	–	(809)	–	(166)	–	(13)	–	(3 013)
Distributions from capital	–	–	–	–	–	–	–	–
TOTAL DISTRIBUTIONS	(6 707)	(6 769)	(2 640)	(913)	–	(132)	(24 900)	(32 510)
TOTAL INCREASE (DECREASE) IN NET ASSETS	35 430	28 539	74 977	42 553	–	(216)	(82 285)	(22 110)
NET ASSETS – END OF PERIOD	\$ 253 737	\$ 218 307	\$ 120 326	\$ 45 349	\$ –	\$ 3 508	\$ 724 420	\$ 803 197

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	\$ 223 208	\$ 156 538	\$ 1 248 122	\$ 1 262 200	\$ 2 541 691	\$ 2 440 333
INCREASE (DECREASE) FROM OPERATIONS	10 715	14 466	59 351	99 640	111 080	191 587
Early redemption fees	–	–	–	–	–	–
Proceeds from units issued	177 043	125 111	463 583	290 621	906 088	641 586
Proceeds from reinvestment of distributions	5 317	4 746	37 877	38 477	73 173	78 518
Payments on redemption of units	(86 482)	(69 809)	(263 597)	(387 551)	(624 165)	(706 900)
TOTAL UNIT TRANSACTIONS	95 878	60 048	237 863	(58 453)	355 096	13 204
Distributions from net income	(9 377)	(7 013)	(52 125)	(50 568)	(95 749)	(93 904)
Distributions from net gains	–	(831)	–	(4 697)	–	(9 529)
Distributions from capital	–	–	–	–	–	–
TOTAL DISTRIBUTIONS	(9 377)	(7 844)	(52 125)	(55 265)	(95 749)	(103 433)
TOTAL INCREASE (DECREASE) IN NET ASSETS	97 216	66 670	245 089	(14 078)	370 427	101 358
NET ASSETS – END OF PERIOD	\$ 320 424	\$ 223 208	\$ 1 493 211	\$ 1 248 122	\$ 2 912 118	\$ 2 541 691

* 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
AAA	8.2	8.9
AA	46.9	53.6
A	27.7	22.4
BBB	14.3	14.2
BB	1.0	–
B	1.2	–
D	–	0.4
Unrated*	0.7	0.5
Total	100.0	100.0

* Mortgages, which represent 100% (December 31, 2011 – 100%) of the unrated above, are all Canada Mortgage and Housing Corporation ("CMHC") guaranteed mortgages, and therefore have the backing of an AAA rated issuer.

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
Less than 1 year	5.3	15.1
1 – 5 years	29.9	26.0
5 – 10 years	20.0	16.7
> 10 years	44.8	42.2
Total	100.0	100.0

As at December 31, 2012, had prevailing interest rates risen or lowered by 1%, with all other factors kept constant, the Fund's net assets may have decreased or increased, respectively, by approximately 6.1% (December 31, 2011 – 5.9%). In practice, actual results could differ from this sensitivity analysis and the difference could be material.

**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	87 697	–	–	87 697
Fixed-income and debt securities	–	2 276 476	–	2 276 476
Short-term investments	–	530 231	–	530 231
Derivatives – assets	–	–	–	–
Derivatives – liabilities	–	–	–	–
Total financial instruments	87 697	2 806 707	–	2 894 404
% of total portfolio	3.0	97.0	–	100.0

December 31, 2011	Level 1	Level 2	Level 3	Total
Equities	–	–	–	–
Mutual fund units	75 065	–	–	75 065
Fixed-income and debt securities	–	2 132 254	–	2 132 254
Short-term investments	–	309 875	–	309 875
Derivatives – assets	133	–	–	133
Derivatives – liabilities	–	–	–	–
Total financial instruments	75 198	2 442 129	–	2 517 327
% of total portfolio	3.0	97.0	–	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	1.00%
Advisor Series	1.00%
Series B	0.75%
Series D	0.50%
Series F	0.50%

December 31, 2012

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	0.04%
Series F	0.05%
Series O	0.02%

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	47	46
Advisor Series	94	92
Series B	–	46
Series D	48	–
Series F	48	46
Value of all units	\$ 3	\$ 3

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.

For the periods ended December 31 (see note 2 in the generic notes)	2012	2011
Series C		
Opening units	18 788	16 969
Issued number of units	7 398	7 064
Reinvested number of units	521	540
Redeemed number of units	(4 997)	(5 785)
Ending number of units	21 710	18 788
Advisor Series		
Opening units	3 903	250
Issued number of units	7 075	3 796
Reinvested number of units	180	62
Redeemed number of units	(863)	(205)
Ending number of units	10 295	3 903
Series B		
Opening units	–	330
Issued number of units	–	–
Reinvested number of units	–	11
Redeemed number of units	–	(42)
Ending number of units	–	299
Series D		
Opening units	69 509	73 803
Issued number of units	8 242	8 937
Reinvested number of units	1 867	2 487
Redeemed number of units	(17 584)	(16 017)
Ending number of units	62 034	69 210
Series F		
Opening units	19 202	13 977
Issued number of units	15 127	10 980
Reinvested number of units	455	416
Redeemed number of units	(7 390)	(6 171)
Ending number of units	27 394	19 202
Series O		
Opening units	108 130	113 481
Issued number of units	39 822	25 766
Reinvested number of units	3 262	3 399
Redeemed number of units	(22 678)	(34 516)
Ending number of units	128 536	108 130

December 31, 2012

**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 0		
RBC Select Choices Conservative Portfolio	2 190	1 810
RBC Select Choices Balanced Portfolio	2 789	1 883
RBC Select Choices Growth Portfolio	665	682
RBC Monthly Income Bond Fund	19 376	3 975
Phillips, Hager & North Total Return Bond Guaranteed Investment Fund	–	599
Total	25 020	8 949

**Other revenue and capital gains (\$000s) (see note 3
 in the generic notes)**

Other revenue and capital gains from investing in other related Investment Funds for the periods ended:

	December 31 2012	December 31 2011
Series 0		
Phillips Hager & North High Yield Bond Fund	\$ 5 039	\$ 3 432
Total other revenue	\$ 5 039	\$ 3 432
Capital gains received from underlying funds	\$ 1 019	\$ –

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.

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.