

U.S. EQUITY FUND

**PHILLIPS, HAGER & NORTH
U.S. EQUITY FUND**

December 31, 2012

Portfolio Manager *RBC Global Asset Management Inc. ("RBC GAM")*

The Board of Directors of RBC Global Asset Management Inc. approved this annual management report of fund performance on March 1, 2013.

A Note on Forward-looking Statements

This report may contain forward-looking statements about the Fund, its future performance, strategies or prospects, and possible future Fund action. The words "may," "could," "should," "would," "suspect," "outlook," "believe," "plan," "anticipate," "estimate," "expect," "intend," "forecast," "objective" and similar expressions are intended to identify forward-looking statements.

Forward-looking statements are not guarantees of future performance. Forward-looking statements involve inherent risks and uncertainties, both about the Fund and general economic factors, so it is possible that predictions, forecasts, projections and other forward-looking statements will not be achieved. We caution you not to place undue reliance on these statements as a number of important factors could cause actual events or results to differ materially from those expressed or implied in any forward-looking statement made in relation to the Fund. These factors include, but are not limited to, general economic, political and market factors in Canada, the United States and internationally, interest and foreign exchange rates, global equity and capital markets, business competition, technological changes, changes in laws and regulations, judicial or regulatory judgments, legal proceedings and catastrophic events.

The above list of important factors that may affect future results is not exhaustive. Before making any investment decisions, we encourage you to consider these and other factors carefully. All opinions contained in forward-looking statements are subject to change without notice and are provided in good faith but without legal responsibility.

This annual management report of fund performance ("MRFP") contains financial highlights but does not contain the complete annual financial statements of the Fund. You can get a copy of the financial statements at your request, and at no cost, by calling 1-800-661-6141, by writing to us at RBC Global Asset Management Inc., Phillips, Hager & North Investment Management, Investment Funds Centre, 20th Floor, 200 Burrard Street, Vancouver, B.C., V6C 3N5, or by visiting our website at www.rbcgam.com/reports or SEDAR at www.sedar.com. Security holders may also contact us using one of these methods to request a copy of the Fund's proxy voting policies and procedures, proxy voting disclosure record, or quarterly portfolio disclosure.

Phillips, Hager & North Investment Management is a division within RBC Global Asset Management Inc., the manager of the Fund and an indirect wholly-owned subsidiary of Royal Bank of Canada.

MANAGEMENT DISCUSSION OF FUND PERFORMANCE

Investment Objective and Strategies

The Fund seeks to provide investors with long-term capital growth by investing primarily in shares of large-capitalization, high-quality U.S. companies. To achieve the Fund's investment objective, we invest in quality businesses that have a sustainable competitive advantage, a history of profitability, a solid financial position, opportunities for growth, and a capable management team. We place particular emphasis on a company's long-term return on equity, as this measure is a key indicator of a company's ability to consistently generate profits for shareholders. Additional emphasis is placed on a stock's valuation, given the breadth of the U.S. market.

Risk

There were no significant changes to the investment objective and strategies that affected the Fund's overall level of risk during the reporting period. The risks of investing in the Fund and the suitability of the Fund for particular investors remains as discussed in the Simplified Prospectus.

Results of Operations

The Fund's net asset value decreased to \$899.7 million as of December 31, 2012, from \$958.3 million at the end of 2011. The change reflected \$88.9 million of investment returns, offset by \$147.5 million of net redemptions.

Over the past year, the Fund's Series D units gained 8.9%, which underperformed the benchmark return of 13.1%. The Fund's return is after the deduction of fees and expenses. See the Financial Highlights section for the management expense ratios and the Past Performance section for the returns of other series, which may vary because of differences in management fees and expenses.

During the reporting period, the U.S. equity markets produced a strong 16% return in U.S. dollars, with the majority of the positive performance in the first half of the year. In the later part of the reporting period the market was relatively flat due to concerns over the direction of fiscal cliff negotiations, which were resolved only in part, with further negotiations almost certainly still to come.

Within the market, the leading sectors were Financials, Consumer Discretionary and Health Care, the first two benefiting from an improving economy and housing market, as well as lower unemployment. Health Care rose on improving stock valuations and the election's outcome providing greater certainty over health care policy. The Utilities and Energy sectors lagged. The Utilities sector had been strong but weakened in the fourth quarter due to overvaluation and uncertainty over the taxation of dividends ahead of the fiscal cliff. Energy stocks weakened due to lower prices for crude oil and natural gas.

For the year, the most significant contributors to the Fund's performance were from the Utilities and Industrials sectors. The best absolute returns came from Wells Fargo, Sempra Energy, Gilead Sciences, JPMorgan and Valero Energy. Detractors from Fund performance came from an underweight position and underperformance in the Consumer Discretionary sector, as well as our underperformance in Health Care. The worst absolute returns came from Apache, WellPoint and ScanSource.

Overall, we decreased the number of holdings in the Fund during the year. Our largest positions initiated were Apache, Apple, Oracle, RenaissanceRe and Bank of America. We also added significantly to existing holdings of Aflac and Waters. Our largest eliminations were El Paso, National Oilwell Varco, Intel, Amphenol and Comcast. We also made significant reductions to Gilead Sciences and Sempra Energy on account of valuation.

Recent Developments

We expect the U.S. equity market to face challenges in 2013 as the country addresses the fiscal cliff and the debt ceiling negotiations, in addition to economic weakness in both Europe and China. However, collectively, U.S. companies have strong balance sheets, are experiencing record profitability and are trading at reasonable valuations with the prospect for slow improvement in the U.S. economy.

All outstanding Series B units were redesignated as Series D units effective July 27, 2012. The redesignated units have a lower management fee as compared to the Series B units.

Effective July 27, 2012, Royal Bank of Canada ("Royal Bank") owns 100% of RBC Investor Services Trust (formerly, RBC Dexia Investor Services Trust, referred to throughout as "RBC IS").

Related-Party Transactions

Manager, Portfolio Advisor and Registrar

RBC GAM is an indirect, wholly-owned subsidiary of Royal Bank and is the manager, principal portfolio advisor and registrar of the Fund. RBC GAM is responsible for the Fund's day-to-day operations, provides investment advice and portfolio management services to the Fund and appoints distributors for the Fund. RBC GAM, as registrar, also keeps the records of who owns the units of the Fund. RBC GAM is paid a management fee by the Fund as compensation for its services. The Fund pays a fixed administration fee to RBC GAM, which, in turn, pays certain operating expenses of the Fund.

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

Distributors

RBC GAM, Phillips, Hager & North Investment Funds Ltd., Royal Mutual Funds Inc., RBC Direct Investing Inc. and RBC Dominion Securities Inc. are principal distributors of, or distribute certain series of units of, the Fund. Dealers receive an ongoing commission based on the total value of their clients' Series C, Advisor Series and Series D units.

Brokerage

The Fund has established standard brokerage agreements at market rates with related-party dealers. These related-party commissions were \$2,000 (2011 – \$0), or 0% (2011 – 0%) of the total transaction costs paid for this Fund.

Trustee and Custodian

RBC IS is the trustee and custodian of the Fund. The fees paid to RBC IS are paid by RBC GAM and not the Fund.

RBC IS holds title to the Fund's property on behalf of unitholders and holds the assets of the Fund.

Other Related-Party Transactions

Pursuant to applicable securities legislation, the Fund relied on the standing instructions from the Board of Governors ("BoG") in its capacity as the Independent Review Committee with respect to one or more of the following 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 Fund, (iii) is in compliance with RBC GAM policies and procedures, and (iv) achieves a fair and reasonable result for the Fund. RBC GAM policy requires that an investment decision in respect of Inter-Fund Trading is in the best interests of each Fund.

FINANCIAL HIGHLIGHTS

The following tables show selected key financial information about the Fund and are intended to help you understand the Fund's financial performance for the past five years or for the periods since inception. This information is derived from the Fund's audited annual financial statements. "Net Assets" are calculated in accordance with Canadian generally accepted accounting principles, which are used to prepare the financial statements (see table below). "Net Asset Value" is derived from the valuation method disclosed in the Phillips, Hager & North Funds' Annual Information Form and is used for transactional purposes (see Ratios and Supplemental Data). All other calculations for the purposes of this MRFP are made using Net Asset Value.

Change in Net Assets Per Unit (\$)

For the Year/ Period Ended	Net Assets Beginning of Year/Period	Increase (Decrease) from Operations ¹					Annual Distributions ²					Net Assets End of Year
		Total Revenue (Loss)	Total Expenses	Realized Gains (Losses)	Unrealized Gains (Losses)	Total	From Income (Excluding Dividends)	From Dividends	From Capital Gains	Return of Capital	Total	
Series C												
Dec. 31, 2012	29.40	0.60	(0.62)	0.39	2.07	2.44	–	–	–	–	–	31.76
Dec. 31, 2011	29.22	0.49	(0.56)	(2.33)	2.50	0.10	–	–	–	–	–	29.40
Dec. 31, 2010	27.71	0.51	(0.54)	(1.36)	2.83	1.44	–	–	–	–	–	29.22
Dec. 31, 2009	26.77	0.53	(0.51)	(2.40)	6.32	3.94	(0.12)	–	–	–	(0.12)	27.71
Dec. 31, 2008 ³	24.67 [†]	0.13	(0.07)	(0.31)	1.13	0.88	(0.02)	–	–	–	(0.02)	26.77
Advisor Series												
Dec. 31, 2012	29.40	0.60	(0.62)	0.39	2.07	2.44	–	–	–	–	–	31.76
Dec. 31, 2011	29.22	0.49	(0.56)	(2.33)	2.50	0.10	–	–	–	–	–	29.40
Dec. 31, 2010 ⁴	28.02 [†]	0.09	(0.09)	(0.23)	0.47	0.24	–	–	–	–	–	29.22
Series D⁵												
Dec. 31, 2012	29.20	0.59	(0.37)	0.38	2.05	2.65	–	(0.21)	–	–	(0.21)	31.59
Dec. 31, 2011	28.98	0.49	(0.33)	(2.32)	2.49	0.33	–	(0.21)	–	–	(0.21)	29.20
Dec. 31, 2010	27.44	0.51	(0.32)	(1.35)	2.80	1.64	–	(0.20)	–	–	(0.20)	28.98
Dec. 31, 2009	26.51	0.55	(0.30)	(2.70)	3.39	0.94	(0.32)	–	–	–	(0.32)	27.44
Dec. 31, 2008	33.67	0.70	(0.36)	(2.44)	(5.12)	(7.22)	(0.32)	–	–	–	(0.32)	26.51
Series F												
Dec. 31, 2012	29.32	0.59	(0.29)	0.38	2.06	2.74	–	(0.29)	–	–	(0.29)	31.72
Dec. 31, 2011	29.10	0.49	(0.26)	(2.33)	2.50	0.40	–	(0.29)	–	–	(0.29)	29.32
Dec. 31, 2010	27.56	0.51	(0.25)	(1.36)	2.81	1.71	–	(0.28)	–	–	(0.28)	29.10
Dec. 31, 2009	26.63	0.54	(0.24)	(2.58)	4.87	2.59	(0.39)	–	–	–	(0.39)	27.56
Dec. 31, 2008	33.70	0.74	(0.31)	(3.68)	19.63	16.38	(0.30)	–	–	–	(0.30)	26.63
Series O												
Dec. 31, 2012	29.65	0.60	(0.01)	0.39	2.09	3.07	–	(0.60)	–	–	(0.60)	32.07
Dec. 31, 2011	29.42	0.50	(0.01)	(2.37)	2.54	0.66	–	(0.57)	–	–	(0.57)	29.65
Dec. 31, 2010	27.88	0.52	(0.01)	(1.37)	2.85	1.99	–	(0.57)	–	–	(0.57)	29.42
Dec. 31, 2009	26.93	0.56	(0.01)	(2.76)	3.43	1.22	(0.63)	–	–	–	(0.63)	27.88
Dec. 31, 2008	34.12	0.71	(0.01)	(2.63)	(4.57)	(6.50)	(0.60)	–	–	–	(0.60)	26.93

¹ Net assets and distributions are based on the actual number of units outstanding at the relevant time. The increase/decrease from operations is based on the weighted average number of units outstanding over the financial period. This table is not intended to be a reconciliation of beginning to ending net assets per unit.

² Distributions are reinvested in additional units of the Fund or paid in cash.

³ From November 2008.

⁴ From October 2010.

⁵ Series D was known as Series A prior to November 17, 2008.

[†] Initial offering net asset value per unit.

FINANCIAL HIGHLIGHTS (cont.)

Ratios and Supplemental Data

As at	Net Asset Value Per Unit (\$)	Net Asset Value (\$000s)	Number of Units Outstanding (000s)	Management Expense Ratio (%) ¹	MER Before Absorption (%) ¹	Portfolio Turnover Rate (%) ²	Trading Expense Ratio (%) ³
Series C							
Dec. 31, 2012	31.77	2 915	92	2.02	2.02	34.35	0.08
Dec. 31, 2011	29.42	2 298	78	2.07	2.07	49.36	0.08
Dec. 31, 2010	29.23	947	32	2.01	2.01	40.42	0.12
Dec. 31, 2009	27.72	648	23	1.99 ⁴	2.05	25.55	0.08
Dec. 31, 2008 ⁵	26.79	195	7	1.97	5.48	45.89	0.12
Advisor Series							
Dec. 31, 2012	31.77	1 005	32	2.02	2.02	34.35	0.08
Dec. 31, 2011	29.42	710	24	2.07	2.07	49.36	0.08
Dec. 31, 2010 ⁶	29.23	—	—	2.01	2.01	40.42	0.12
Series D⁷							
Dec. 31, 2012	31.60	162 958	5 157	1.22	1.22	34.35	0.08
Dec. 31, 2011	29.22	186 942	6 398	1.22	1.22	49.36	0.08
Dec. 31, 2010	28.99	190 716	6 579	1.19	1.19	40.42	0.12
Dec. 31, 2009	27.46	203 907	7 426	1.18 ⁴	1.18	25.55	0.08
Dec. 31, 2008	26.53	221 192	8 338	1.18	1.18	45.89	0.12
Series F							
Dec. 31, 2012	31.73	1 412	44	0.95	0.95	34.35	0.08
Dec. 31, 2011	29.33	1 410	48	0.95	0.95	49.36	0.08
Dec. 31, 2010	29.10	1 321	45	0.92	0.92	40.42	0.12
Dec. 31, 2009	27.57	1 234	45	0.95 ⁴	0.95	25.55	0.08
Dec. 31, 2008	26.65	1 103	41	1.17	1.49	45.89	0.12
Series O							
Dec. 31, 2012	32.08	731 423	22 798	0.02	0.02	34.35	0.08
Dec. 31, 2011	29.66	766 923	25 857	0.02	0.02	49.36	0.08
Dec. 31, 2010	29.43	764 872	25 988	0.02	0.02	40.42	0.12
Dec. 31, 2009	27.90	883 436	31 669	0.02 ⁴	0.02	25.55	0.08
Dec. 31, 2008	26.95	965 528	35 825	0.02	0.02	45.89	0.12

¹ The management expense ratio ("MER") is based on expenses for the stated period, excluding commissions and other portfolio transaction costs, and is expressed as an annualized percentage of the daily average net asset value during the period. RBC GAM may, at its discretion and without notice to unitholders, waive or absorb certain operating expenses. MER includes the waiver or absorption by RBC GAM of certain operating expenses, while the MER before absorption shows the MER prior to operating expenses being waived or absorbed by RBC GAM.

² The Fund's portfolio turnover rate gives an indication of the level of activity employed by the portfolio manager. A portfolio turnover rate of 100% is equivalent to the Fund buying and selling all of the securities in its portfolio once in the course of the year. The higher the Fund's portfolio turnover rate in a year, the greater the trading costs payable by the Fund in the year, and the greater the chance of an investor receiving taxable capital gains in the year. There is not necessarily a relationship between high turnover rate and the performance of the Fund. The portfolio turnover rate is not applicable to money market funds.

³ The trading expense ratio represents total commissions and other portfolio transaction costs expressed as a percentage of daily average net asset value during the period. The trading expense ratio is not applicable to fixed-income transactions.

⁴ Effective November 1, 2009, a fixed administration fee was introduced in respect of each series of the Fund. If the fixed administration fee would have been in effect throughout 2009, the adjusted MER for each series of the Fund would be: Series C – 1.93%, Series D – 1.16%, Series F – 0.89%, Series O – 0.02%.

⁵ From November 2008.

⁶ From October 2010.

⁷ Series D was known as Series A prior to November 17, 2008.

FINANCIAL HIGHLIGHTS (cont.)

Management Fees

RBC GAM is the manager, portfolio advisor and registrar of the Fund. Management fees paid by each series of the Fund are calculated at the applicable annual percentages, before GST/HST, of the daily net asset value of each series of the Fund. The breakdown of the services received in consideration of the management fees for each series, as a percentage of the management fees, is as follows:

	Management Fees	Breakdown of Services	
		Distribution	Other*
Series C	1.75%	57%	43%
Advisor Series	1.75%	57%	43%
Series D	1.00%	25%	75%
Series F	0.75%	—	100%

Series O – no management fees are paid by the Fund in respect of Series O units. Series O unitholders pay a negotiated fee directly to RBC GAM for investment-counselling services.

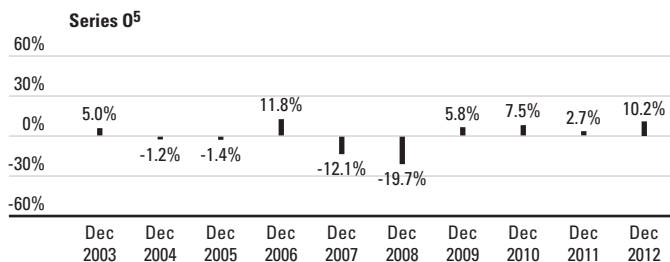
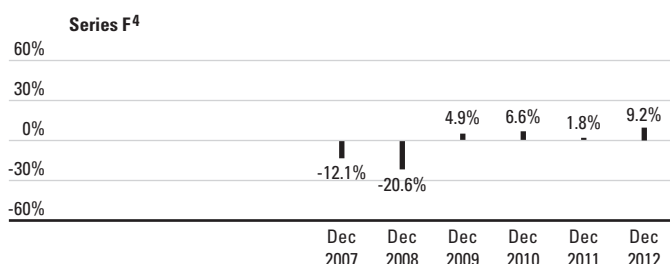
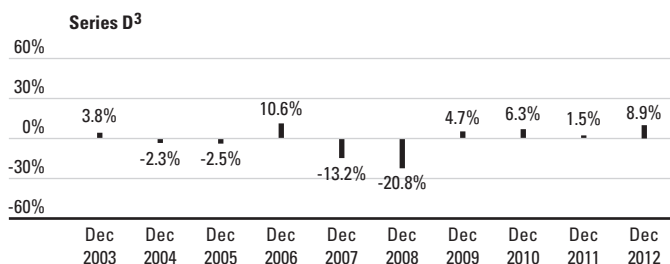
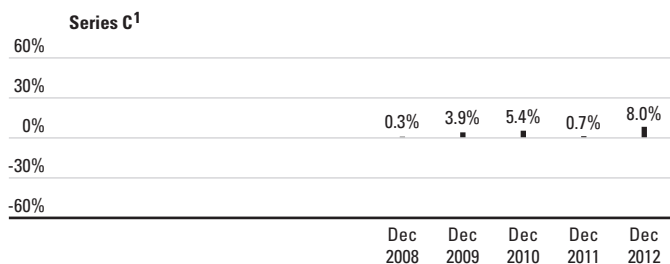
* Includes all costs related to management, investment advisory services, general administration and profit.

PAST PERFORMANCE

The performance information shown assumes that all distributions made by the Fund in the periods shown were reinvested in additional units of the Fund and would be lower if distributions were not reinvested. The performance information does not take into account sales, redemption, distribution, optional charges or income taxes payable that would have reduced returns or performance. Past performance does not necessarily indicate how the Fund may perform in the future. A fund with more than 10 years of performance history is only permitted to disclose the past 10 years.

Year-by-Year Returns (%)

The bar chart indicates the Fund's performance for each of the years shown, and illustrates how the Fund's performance has changed from year to year. The bar chart shows, in percentage terms, how much an investment made on the first day of each financial year would have grown or decreased by the end of the financial year.



PAST PERFORMANCE (cont.)

Annual Compound Returns (%)

The table shows the annual compound returns for each series of the Fund and for each of the periods indicated ended on December 31, 2012, compared with the following benchmark:

S&P 500 Total Return Index (CAD)

	Past Year	Past 3 Years	Past 5 Years	Past 10 Years	Since Inception
Series C ¹	8.0	4.6	—	—	4.4
Benchmark	13.1	8.9	—	—	8.5
Advisor Series ²	8.0	—	—	—	6.0
Benchmark	13.1	—	—	—	10.1
Series D ³	8.9	5.5	-0.5	-0.8	—
Benchmark	13.1	8.9	1.7	2.2	—
Series F ⁴	9.2	5.8	-0.3	—	-2.6
Benchmark	13.1	8.9	1.7	—	—
Series O ⁵	10.2	6.8	0.7	0.4	—
Benchmark	13.1	8.9	1.7	2.2	—

The returns of each series may vary because of differences in management fees and expenses. The Benchmark index returns do not include any costs of investing. See Management Discussion of Fund Performance for a discussion of performance relative to the Benchmark index.

¹ Inception date November 2008.

² Inception date October 2010.

³ Inception date September 1964.

⁴ Inception date June 2007.

⁵ Inception date October 2002.

Series D was known as Series A prior to November 17, 2008.

INDEX DESCRIPTION

S&P 500 Total Return Index (CAD) This index is a capitalization-weighted index measuring the Canadian dollar performance of 500 widely held common stocks representing all major industries in the United States. This index gives investors a broad measure of the overall performance of the U.S. stock market.

SUMMARY OF INVESTMENT PORTFOLIO

(after consideration of derivative products, if any)

As at December 31, 2012

Investment Mix

	% of Net Asset Value
Financials	19.8
Health Care	19.0
Information Technology	16.5
Energy	11.5
Consumer Staples	10.5
Industrials	8.3
Consumer Discretionary	6.5
Materials	2.8
Telecommunication Services	1.6
Utilities	1.3
Cash/Other	2.2

Top 25 Holdings

	% of Net Asset Value
Berkshire Hathaway Inc., Class B	4.0
Exxon Mobil Corp.	3.8
Johnson & Johnson	3.6
Wells Fargo & Company	3.5
Wal-Mart Stores, Inc.	3.4
United Technologies Corp.	3.4
Becton Dickinson & Co.	3.3
PepsiCo Inc.	3.2
Emerson Electric Co.	3.1
JPMorgan Chase & Co.	3.1
Google Inc., Class A	3.0
Aflac Inc.	3.0
Pfizer Inc.	2.9
Johnson Controls Inc.	2.8
Microsoft Corp.	2.8
Waters Corp.	2.7
Archer Daniels Midland Co.	2.4
Cisco Systems Inc.	2.4
Apple Inc.	2.4
Oracle Corporation	2.3
Cash & Cash Equivalents	2.3
WellPoint Inc.	2.2
Noble Corp.	2.2
Apache Corp.	2.1
The Mosaic Co.	2.1
Top 25 Holdings	72.0

The Summary of Investment Portfolio may change due to ongoing portfolio transactions of the Fund. It is updated quarterly and may be obtained by calling our Investment Funds Centre at 1-800-661-6141, by viewing on our website, www.phn.com, or by emailing us at info@phn.com.