

Phillips, Hager & North U.S. Special Equity Fund

Annual Report 1992

The PH&N U.S. Special Equity Fund commenced operation on October 13, 1992.

Results to December 31, 1992 were encouraging as the Fund rose from its initial price of \$10.00 Cdn. Per share to \$11.88 Cdn per share on December 31, 1992. This represents a gain of 18.8% to investors in the Fund over a 2 ½ month period. A strong U.S. dollar during the period accounted for 2.5% of the gain. After a 2 cent dividend, the Fund ended the year at \$11.86 Cdn per share.

Results in U.S. dollars and Canadian dollars relative to relevant market indexes are as follows:

INITIAL "QUARTER" OCTOBER 13 – DECEMBER 31, 1992

PERFORMANCE COMPARISONS *

	RETURN
US Special Equity Fund \$CDN	18.80%
US Special Equity Fund \$US	16.30%
S&P 500 \$CDN	9.80%
S&P 500 \$US	7.309%
S&P MidCap \$CDN	15.70%
S&P MidCap \$US	13.20%
Russell 2000 \$CDN	19.30%
Russell 2000 \$U.S.	16.80%
Wilshire 5000 \$CDN	11.50%
Wilshire 5000 \$U.S.	9.30%
NASDAQ \$CDN	20.30%
NASDAQ \$U.S.	17.70%

* includes income in all cases.

FUND VALUATION

DESCRIPTION	MARKET VALUE	% TOTAL MARKET
American Pac Corp	59,568.75	0.43
Andros Inc.	35,264.70	0.25
Applied Materials	42,889.50	0.31
BIC Corp. Common	46,225.35	0.33
Blockbuster Entertainment Corp.	381,240.00	2.73
BMC West Corp.	11,754.90	0.08
Carnival Cruise Lines, Inc. A	882,316.44	6.32
Charming Shoppes Inc.	299,432.25	2.15
Clayton Homes Inc.	663,496.59	4.76
CML Group Inc.	696,398.40	4.99
Conner Peripherals	26,369.10	0.19
Cooper Tire & Rubber	349,978.32	2.51
Diceon Electronics	63,540.00	0.46
Digital Equipment Corp.	128,668.50	0.92
DSG International	263,691.00	1.89
EKCO Group Inc.	12,549.15	0.09
Federal Ntl. Mtge. Association	1,019,102.18	7.30
Fisher-Price Inc.	15,964.43	0.11
Franklin Resources Inc.	44,478.00	0.32
Fruit of the Loom Inc. Cl. A.	655,002.09	4.69
Healthcare Compare	381,240.00	2.73
Health Trust Inc.	1,187,086.05	8.51
Intel Corp. Common	1,260,379.44	9.03
Intl. Dairy Queen	127,080.00	0.91
Jones Apparel Group Inc.	557,166.38	3.99
Kellwood Co.	34,311.60	0.25
Magma Copper Co. Cl. B.	333,140.22	2.39
Masco Inds. Inc.	311,282.46	2.23
Merrill Lynch & Co.	733,442.22	5.26
Phillips Van Huesen	36,853.20	0.26
Read-Rite Corp.	325,642.50	2.33
Seitel Inc.	31,452.30	0.23
Service Merchandise	184,266.00	1.32
Shoneys Inc.	29,546.10	0.21
Singer Co.	18,029.48	0.13
Tandy Corp.	616,242.69	4.42
Torchmark Corporation	631,571.72	4.53
Tyco Laboratories Inc.	210,317.40	1.51
Unifi Inc.	438,426.00	3.14
Unum Corporation	437,790.60	3.14
Verifone Inc.	12,866.85	0.09
Vishay Intertechnology	<u>335,601.61</u>	<u>2.55</u>
Total Value of Portfolio	\$13,951,664.47	100.00
Total Cash & Dividends Receivable	<u>96,381.91</u>	
Total Net Assets	\$14,048,046.38	

NET ASSET VALUE PER UNIT DEC 31/92 \$11.86 (EX-DIVIDEND)

Since this is the first report of the PH&N U.S. Special Equity Fund, the following summary of the Fund's objectives and investment philosophy is presented.

Investment Philosophy

The Fund is designed for knowledgeable investors who desire an aggressive approach to investment management, with the goal of superior investment results through capital appreciation.

The Fund will focus on well managed, high potential stocks, regardless of their market capitalization.

As a group, less mature small and medium sized companies provide more dynamic growth opportunities than the more mature segment of the market. For this reason, small and medium sized companies will be an area of concentration for the Fund.

These companies may have reduced marketability from time to time. For this reason, holdings of individual companies will be matched to their apparent liquidity and will tend to be kept relatively small.

Growth potential is not limited to smaller companies. Some very large companies operate in dynamic areas of the economy and on occasion outperform their smaller competitors through market dominance. The Fund will try to capitalize on these opportunities by assuming large positions in such companies. This concentration may also increase the Fund's short term volatility.

Selection of reasonably priced stocks with exceptional growth prospects, whether small or large cap, will be the key of the Fund's success. An internal guideline directs that 70% of the companies in the portfolio of the U.S. Special Equity Fund will differ from those held by the Phillips, Hager & North U.S. Equity fund. This portion of the Fund will always include a significant number of small and medium cap stocks.

Economic and Market Outlook

In short, the economic outlook is good. After a mild recession in 1990, the U.S. economy has staged the slowest recovery of the post war period. This has resulted in the lowest inflation rate in decades and correspondingly low interest rates. Low interest rates stimulate business. The fact that the recovery is progressing at a slow rate will likely mean that interest rates will be slow to rise which should, in turn, result in a sustained period of economic growth ahead.

For a number of years, a great deal of cost cutting and restructuring has taken place as management concentrated on being cost competitive. The prevailing mood of business remains sober. When one considers that economic downturns normally occur in reaction to unsustainable boom conditions, the lack of excesses in the current environment gives further reason to believe that the economy is on a firm footing.

The slow economic growth in the U.S. has just recently taken the Real Gross Domestic Product into new high ground. This makes the U.S. one of the strongest economies in the world. On the other hand, the economies of Germany and Japan are still experiencing a slowing in their rate of economic growth. Worldwide pressure is building for governments to stimulate growth and foster job creation as opposed to limiting inflation. Recent interest rate cuts in Germany and Japan tend to confirm this view. At a later date, renewed world economic growth should reinforce the expansion in the U.S.

The U.S. equity markets rose very modestly last year. This was because of the slow earnings recovery of U.S. business in general. Cyclical and basic industries had particularly poor results. The performance of individual companies was quite different with some managing very strong earnings growth. The market focused on these companies, making good stock selection very rewarding.

The current year is beginning with P/E ratios of about 16 time earnings based on 1993 estimates of earnings for the Standard and Poor's Index. As a general rule, when inflation is low, interest rates are low and stocks tend to have a higher price in relation to earnings than when the reverse is true. Today's economy looks much like that of the 1960's when inflation was low and economic growth moderate and steady. During that period, price earnings ratios averaged about 1.7 times.

The stage is set for accelerated economic growth and a more normal rate of earnings growth. Well managed companies will continue to show superior growth in this environment. It is likely that cyclical and basic industry groups will start to show better results this year.

All this suggests that the U.S. equity market will rise in 1993 fuelled by earnings growth. While the underlying economic climate will be stronger than in 1992 and overall earnings gains easier, there will continue to be large variations in earnings results among individual companies. Stock selection will remain of paramount importance to achieving superior investment results.

Yours truly,

A handwritten signature in cursive script that reads "Rudy North". The signature is written in black ink and is positioned to the left of the typed name.

Rudy E. North