DESAUTELS CAPITAL MANAGEMENT

2020

2020 COVID-19 SPECIAL REPORT

Global Equity Fund

2020 COVID-19 SPECIAL REPORT

Darius Kuddo, *Incoming Global Equity Strategist*
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GLOBAL EQUITY FUND
A WORLD IN TURMOIL

Dear Investors,

We came into the new year thinking our main concern would be the outstanding US-China trade war, but were then met with the threat of a real war following the death of Qasem Soleimani in Iran and resulting tensions. But with the onset of COVID-19, those events now feel insignificant and in the distant past. COVID-19 has infected hundreds of thousands of people, sent stock indices into bear markets, and threatens to plunge economies worldwide into recession. YTD as of March 13th, the Global Equity Fund has returned -22.3% vs. -16.1% for our benchmark. Up until midway through this crisis, we had been outperforming our benchmark on both an absolute and risk-adjusted basis, as many of our bottom-up investment theses were playing out as expected. With current volatility, our performance against our benchmark changes everyday.

HOW DID WE GET HERE?

Earlier this year, we were fairly bullish on equity markets, although we were aware of certain risks. We were looking for stocks with good upside potential, but that would also be resilient in case of a recession. We were not, however, ready for a black swan crisis in the form of a global pandemic that would derail all of our expectations for the year. On the last day of 2019, the World Health Organization (WHO) had received notice from Chinese authorities of a cluster of pneumonia cases with unknown cause. Two weeks later, the WHO reported the first case of the virus, yet to be named COVID-19, outside of China. While China had begun to lock down parts of the country, and airports around the world began screening incoming passengers, stock markets were ignoring all of these warning signs and hitting all-time highs almost every day. Even after Apple announced on February 17th that they expected not to meet revenue guidance for its first quarter, markets kept pushing higher as they had been over their nearly 11-year-long bull market. The tipping point came a week later as market participants began to realize that there were major risks of a supply shock impacting world economies as a result of China's extremely rigid quarantines across the country that severely restricted factory workers and their ability to continue producing parts for supply chains that relied on them. Following this supply shock to the economy, what then became more apparent was that COVID-19 would also lead to a demand shock as countries around the world began to lock themselves down in order to try to contain the spread of the virus.

What then came as another surprise was Saudi Arabia's unexpected decision to increase oil production coupled with the decision to undercut market prices by $6-8 per barrel as a result of a breakdown in OPEC negotiations with Russia for coordinated cuts in oil production in response to falling oil demand worldwide, all of which ultimately caused stock markets to plunge and trip circuit breakers along the way. Many North American energy producers are at risk of bankruptcy now that oil prices are below their breakeven prices. These companies are at least partially hedged in the short term, but prolonged low oil prices could spell disaster. Canadian producers generally have stronger balance sheets and are more likely to be bailed out by the government, but they are still at risk.

The fact that there are both supply and demand shocks leads to arguably justified panic selling in the markets as there is potential for real economic impact. The Fed has been quite active, now cutting rates to zero and pledging trillions of dollars in capital injections to limit the economic fallout as a result of COVID-19. What has been worrying is that the market has reacted to these emergency measures quite negatively, calling into question their ability to keep the US out of a recession.

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A WORLD IN TURMOIL

The US federal government's reaction to this crisis has also been worrying given the slow speed and apparent unwillingness to confront the true reality of this virus' implications, although President Trump's declaration of a national emergency and partnership with the private sector on March 13th rallied markets quite a bit. What is unclear is how this crisis will continue to unfold over the coming months.

WHERE COULD THIS GO?

This crisis marks the first time in modern history that the world has had to confront a pandemic of this magnitude with a real effect on the economy on a global scale. There is a lot we do not know, especially how this virus is going to progress and when the market will hit its bottom.

Many experts have publicly stated in the last few days that the virus has not reached its peak in terms of infections. We have seen what COVID-19 can do to countries, especially to Italy, which has seen country-wide lockdowns, and France, which has closed restaurants, cafés, and cinemas until further notice. There is evidence that most Western countries are following the same path in terms of infection rates, which could mean that the US and Canada could mirror hard-hit countries like Italy if more is not done in order to contain the spread of the virus. Healthcare systems may be at imminent risk of becoming overloaded with patients who need more advanced care if the pace of the virus does not slow.

What has been good news is that China has been able to curb their increase in infections as a result of the measures they implemented early-on in the crisis, leading many factories and stores to reopen. While this is positive, the results may not be transferrable elsewhere given China's stronger control over its people compared to Western countries.

There are certainly some catalysts that could help turn around this crisis. Perhaps quite obvious, some sort of vaccine or other treatment for COVID-19 would help limit its spread and treat patients faster. This being said, if there are rapid advances made in this space, it is unclear how fast they would be able to produce and distribute such a treatment in order to make a tangible difference given the current rate of infections. Even with evidence of an effective treatment that could rally markets in the short term, a recession could still be imminent and would likely cause markets to continue to sell off.

Many have pointed out how spring/summer weather typically kills off many related viruses as they degrade with heat. Given that countries like Singapore and Australia who have rather warm weather this time of year have also been severely affected by this virus, it is possible that COVID-19 is different from related viruses and will continue to spread rapidly even with a change in weather.

What is becoming more evident and agreed upon by more and more market participants is that a recession will occur as a result of this crisis. There is a big credit crunch happening right now. Corporate spreads are currently at 12-year highs and companies are drawing on their credit lines in order to find liquidity amid poor sales. Firms are significantly cutting back on activity in capital markets and are otherwise finding it more difficult to find financing. Despite rate cuts, there seems to be little evidence of positive impacts on business spending. With majority of Americans living paycheck to paycheck, a small reduction in wages as a result of the COVID-19 crisis could trigger defaults and lead to huge impacts on the financial sector and the economy.

It is difficult to forecast exactly how this crisis will pan out. The WHO and World Bank have estimated that the

GLOBAL EQUITY FUND
A WORLD IN TURMOIL

cost of a severe global pandemic could reach as high as 4.8% of global GDP, representing over $3 trillion. Various theories exist to predict the length of a recession, but none are statistically significant. The last recession was sparked primarily by a global financial crisis. This time, we face a possible liquidity crisis as well as both supply and demand shocks. This would also mark the first time we enter a recession with rates close to or at zero. Getting out of such a recession may prove to be quite difficult given limited Fed ammunition and falling confidence in them to protect the economy. Calling a market bottom is of course a difficult, if not impossible, task. Perhaps a statement, and investment action by a well-known investor, like Warren Buffet, that points to improving fundamentals in the economy could potentially cause a turnaround in the future, just as Jamie Dimon had done at the tail end of the last crisis.

IMPACT ON OUR PORTFOLIO

At the beginning of the year, we were bullish on Energy and Financials. These sectors were hammered over the past two weeks and explain in large part our YTD underperformance. Industrials and materials were also hit hard as they are inherently cyclical, but we were partially hedged with large exposure to gold producers. Compared with our positioning six months ago, we have lowered our downside both at the fund level and at the individual holding level, given that many of our recent investment theses were centered around resiliency in a recession scenario. Looking forward, the general theme will be to build a portfolio that can weather this crisis and a recession. In times of crises and broad market selloffs, there are also investment opportunities for astute investors. Some stocks are oversold, while others are still too expensive. Differentiating between the two requires a lot of careful and rigorous analysis. It's not an easy task, but it's the task that's ahead of us, and a task we look forward to it.

DCM NOTE

The past few weeks have marked the first time that Desautels Capital Management has experienced a market downturn comparable to past recessions. It is a scary time, but also a one-in-a-lifetime learning opportunity. There is a lot of uncertainty we face, not only in the markets, but also in our personal lives.

Many of you have likely started working at home as a result of COVID-19. For us, McGill has shut down its campus and classes for at least the next two weeks. We don't know what classes, exams, and assignments may look like going forward. Despite this, we will power forward and continue to work with the best we have and resume pitches over videoconference. As J.K. Rowling once said, "we are only as strong as we are united, as weak as we are divided." As a society, we have endured a lot in the past and always been able to recover. All of us will have our own struggles and hurdles, but I am confident we will come together and return to life as normal, no matter how long it takes or what we will face along the way. As investors, we deeply appreciate your support of the program and we thank you for the incredible learning opportunities we have been blessed to receive.

Yours truly,

Darius Kuddo, *Global Equity Strategist*

PERFORMANCE SUMMARY
GLOBAL EQUITY FUND

Global Equity Fund Returns

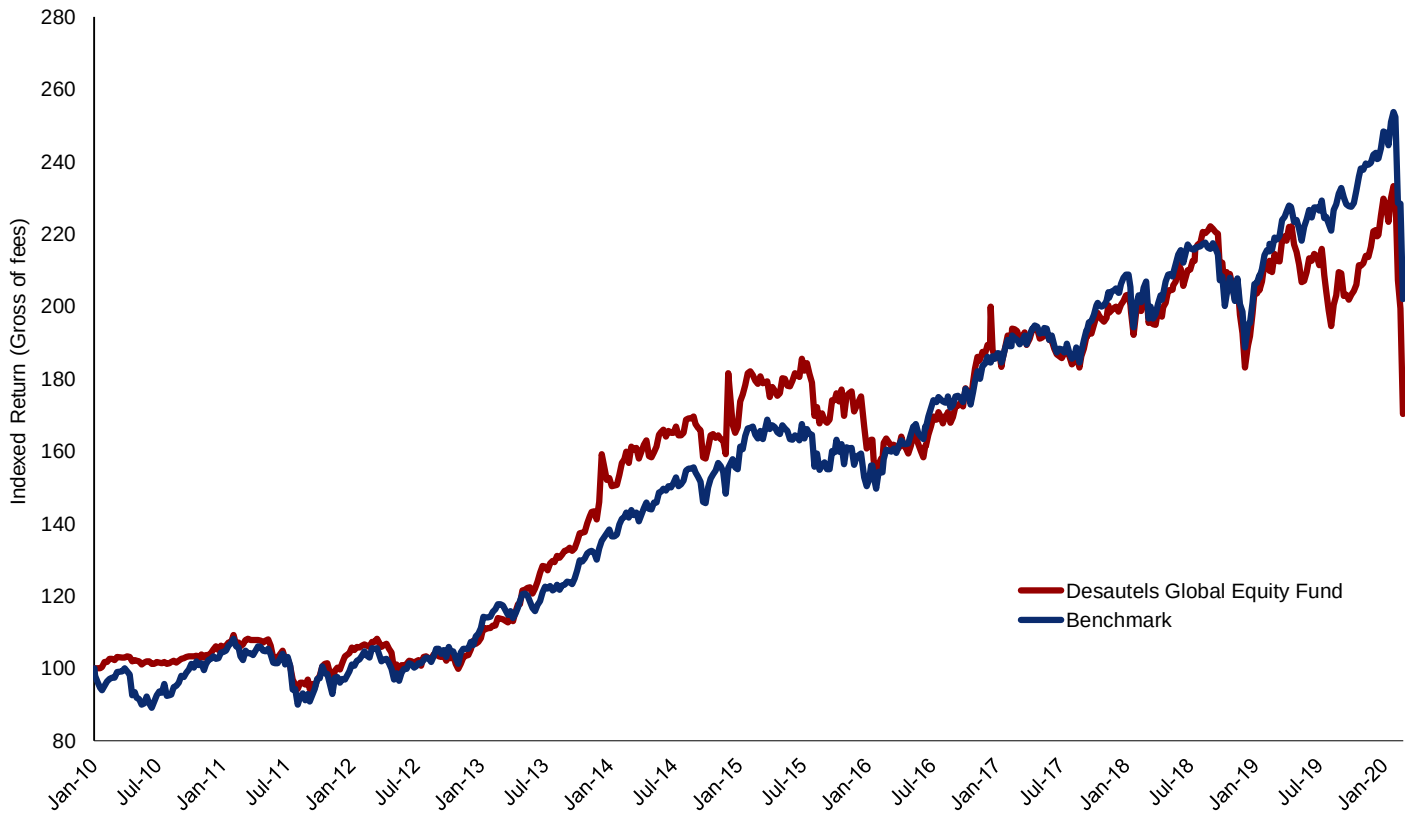
Performance Metrics Since Inception	Equity Fund	Benchmark
Annualized Return	5.5%	7.3%
Annualized Std Dev	13.4%	11.7%
Annualized Sharpe Ratio	0.24	0.43
Beta	0.88	
Annualized Gross Alpha	(1.2%)	

Performance metrics are calculated gross of fees.

Equity Performance Metrics 2020	Equity Fund	Benchmark
Return	(22.3%)	(16.1%)
Annualized Standard Deviation	44.4%	41.7%
Sharpe Ratio	(0.71)	(0.63)
Beta	1.05	
Alpha	(5.4%)	

Performance metrics are calculated gross of fees.

Global Equity Fund Since Inception



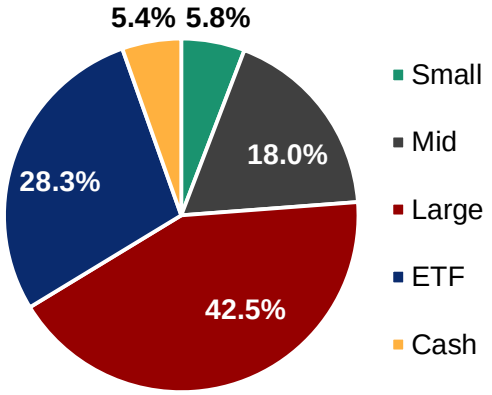
**Note: Performance is calculated gross of fees. Benchmark is a blended 60% S&P TSX, and 40% S&P 500 (measured in CAD). From inception until February 28, 2013, benchmark was the MSCI World Index. Inception date was January 20, 2010.*

PERFORMANCE SUMMARY
GLOBAL EQUITY FUND

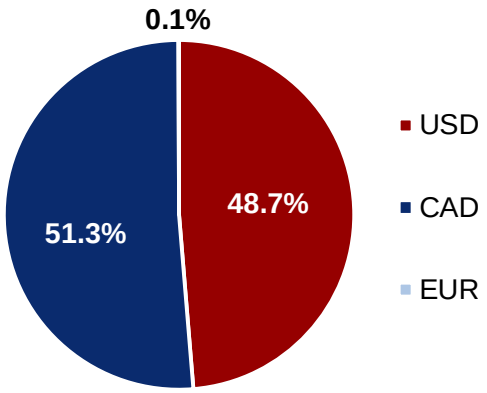
Global Equity Fund Current Sector Allocation

Sector	Global Equity Fund	Benchmark	(+/-)
Communication Services	6.1%	7.6%	(1.5%)
Real Estate	6.1%	3.5%	2.6%
Energy	8.4%	11.0%	(2.6%)
Consumer Discretionary	7.4%	6.3%	1.1%
Information Technology	16.0%	13.5%	2.5%
Healthcare	8.5%	6.3%	2.2%
Financials	21.6%	24.3%	(2.7%)
Industrials	5.0%	10.3%	(5.3%)
Consumer Staples	4.2%	5.3%	(1.1%)
Materials	8.3%	7.5%	0.8%
Utilities	3.3%	4.5%	(1.2%)
CAD	2.1%	0.0%	2.1%
USD	3.2%	0.0%	3.2%
EUR	0.1%	0.0%	0.1%
Total	**100.0%**	**100.0%**	**0.0%**

Global Equity Fund Current Size Exposure



Global Equity Fund Current Currency Exposure



PERFORMANCE SUMMARY
GLOBAL EQUITY FUND

Global Equity Fund Current Holdings

Security Name	Sector	Currency	Units	Local Cost	Price	CAD Value	Weight
ISHARES US FINANCIALS ETF	Financials	USD	875	$142.98	$108.89	$131,980	5.4%
BANK OF MONTREAL	Financials	CAD	1,550	$100.56	$70.56	$109,368	4.5%
ADOBE INC.	Information Technology	USD	230	$254.40	$335.50	$106,889	4.4%
LOBLAW COMPANIES LIMITED	Consumer Staples	CAD	1,580	$56.50	$66.49	$105,054	4.3%
BANK OF AMERICA CORP	Financials	USD	2,920	$15.01	$24.16	$97,722	4.0%
FACEBOOK	Communication Services	USD	400	$192.64	$170.28	$94,349	3.9%
ISHARES EXPANDED TECH-SOFTWA	Information Technology	CAD	310	$235.65	$210.68	$90,469	3.7%
SIMON PROPERTY GROUP INC	Real Estate	CAD	720	$139.44	$89.77	$89,532	3.7%
NORNICKEL	Materials	CAD	2,500	$23.42	$25.34	$87,766	3.6%
ISHARES S&P GLOBAL CONSUMER	Consumer Discretionary	USD	3,000	$38.72	$29.18	$87,540	3.6%
EAST WEST BANCORP INC	Financials	USD	1,975	$46.85	$31.96	$87,435	3.6%
ARITZIA INC SUBORDINATED VOTING	Consumer Discretionary	CAD	5,300	$14.92	$16.29	$86,337	3.5%
TRANSDIGM	Industrials	CAD	150	$549.09	$414.72	$86,171	3.5%
ISHARES S&P/TSX CAPPED UTILITIES	Utilities	CAD	3,400	$30.21	$24.35	$82,790	3.4%
BLACKBERRY LIMITED COMMON	Information Technology	USD	12,500	$8.11	$6.02	$75,250	3.1%
ISHARES S&P/TSX CAPPED MATERIALS INDEX ETF	Materials	CAD	6,400	$13.43	$10.58	$67,712	2.8%
ISHARES NASDAQ 100 INDEX ETF	Information Technology	USD	1,050	$64.79	$62.94	$66,087	2.7%
SVB FINANCIAL GROUP	Financials	USD	300	$231.37	$156.67	$65,106	2.7%
PROSUS	Information Technology	USD	3,850	$14.79	$11.98	$63,890	2.6%
MGM GROWTH PROPERTIES	Real Estate	CAD	1,950	$30.08	$23.21	$62,693	2.6%
SAREPTA	Healthcare	USD	450	$132.43	$99.83	$62,228	2.6%
SUNCOR	Energy	CAD	2,750	$45.21	$22.45	$61,738	2.5%
ISHARES GLOBAL HEALTHCARE (CAD)	Healthcare	CAD	1,250	$49.86	$47.86	$59,825	2.5%
BMO GLOBAL COMMUNICATIONS INDEX ETF	Communication Services	USD	2,700	$23.63	$21.37	$57,699	2.4%
SUMMIT MATERIALS, INC	Materials	CAD	2,550	$26.86	$14.73	$52,030	2.1%
CI FIRST ASSET US & CANADA LIFECO	Financials	USD	7,000	$11.21	$7.35	$51,450	2.1%
PEMBINA PIPELINE CORP	Energy	CAD	1,750	$37.85	$28.71	$50,243	2.1%
ORCHARD THERAPEUTICS PLC	Healthcare	CAD	4,600	$11.97	$7.40	$47,152	1.9%
SAVARIA	Healthcare	USD	4,350	$14.29	$10.00	$43,500	1.8%
MARATHON PETROLEUM CORP	Energy	USD	1,200	$44.14	$24.92	$41,423	1.7%
ISHARES S&P GLOBAL INDUSTRIALS	Industrials	CAD	1,500	$34.04	$25.73	$38,595	1.6%
PAREX RESOURCES	Energy	CAD	2,500	$20.21	$14.14	$35,350	1.5%
SEVEN GENERATIONS	Energy	CAD	10,700	$8.08	$2.08	$22,256	0.9%
PERFORMANCE SPORTS GROUP LTD	Consumer Discretionary	USD	10,985	$7.16	$1.00	$10,985	0.5%
EURO	EUR	EUR	899			$1,380	0.1%
U.S. DOLLAR	USD	USD	57,137			$79,147	3.2%
CANADIAN DOLLAR	CAD	CAD	51,819			$51,819	2.1%
				Net Asset Value		**$2,436,786**	

Economics

2020 COVID-19 SPECIAL REPORT

Andrew Guerrand
Seth Obadia

ECONOMICS
PANDEMIC + OIL SHOCK

OIL TENSIONS

To understand the current oil price war, it is important to look at the backstory. Over the past couple of years, low oil prices have caused severe problems for Saudi Arabia, including the need to borrow to finance its budget, derailing economic plans, such as high-tech cities, and reducing the size of Saudi Aramco's IPO. Amid these unfavorable circumstances, Saudi Arabia experienced a reprieve in 2017, when it collaborated with Russia to limit supply and increase prices. Recently, Russia wanted to boost production in order to boost its economy and thus stepped up demands on Saudia Arabia, specifically for them to invest more in Russia and back Kremlin's Turkey efforts, the latter of which Saudi Arabia would not agree to because it viewed that as likely to draw the ire of the US. Consequently, Russia rejected a Saudi plan to cut crude output (1.5 million bbl/d) amid falling oil demand in China. The 1.5 million cut would have been allocated as follows: OPEC's 13 member nations to cut 1 million bbl/d to year-end while the remaining 500,000 bbl/d would be cut amongst 10 Russia-led oil-producing allies.

Since that deal fell through, on March 7th, the Saudis announced a plan to boost production, driving down the price of oil. On March 9th, oil prices decreased by a third, the most significant decline since the 1991 Gulf War. Then on March 10th, Saudi Aramco announced plans to boost production by 1 million bbl/d, which would cost a reported $30 billion. Regarding the decision, a senior Saudi official remarked, "It was the Saudi declaration of war against Putin." Following the decision, Aramco's shares fell 18%, while Russia responded that it would boost production by 500k bbl/d. OPEC's other members are pressuring both sides to reach an agreement.

Algeria, Iraq, and the United Arab Emirates are likely to be hit the hardest. In order to balance their respective state budgets, oil prices need to remain above $92, $59, and $68 a barrel, respectively. Non-OPEC members Kazakhstan and Ecuador are considering emergency measures to fill their budget gaps.

According to the WSJ, both parties believe it can withstand a prolonged price war. However, Saudi Arabia is more exposed as its federal funding depends heavily on oil revenue, but perhaps less than fellow OPEC members since it can process oil at very low costs. It is estimated that Saudi Arabia requires oil prices above $60 a barrel to balance its budget. In contrast, Russia relies less on oil — less than ⅓ of its budget derives from oil revenue — and since the country accumulated massive reserves, the Russian finance ministry could withstand ten years of prices at $25 to $30 a barrel. Also, Moscow's oil sales have not suffered as much as other producers, as China has continued to buy for storage.

Russia and Saudi Arabia are both being pressured by OPEC members to reconcile. Russia has more leverage than Saudi Arabia, but all countries lose when oil prices are this low, which makes it likely to be a short-term issue. An OPEC delegate said, "We are expecting a last-minute agreement, but one that would entail heavy lifting from Saudi Arabia and a minor, if any, cut from the Russians."

These issues, coupled with lower demand, are creating a unique situation in the oil industry. In fact, according to the IEA, the 2020 base case global oil demand forecast was reduced by 1.1mm b/d, and demand is expected to fall year-on-year by 90k b/d, which is the first time since 2009. More pessimistically, Goldman Sachs estimated that COVID-19 would reduce global crude demand

Source: WSJ, RBC Economics, Bloomberg, Capital IQ

ECONOMICS
PANDEMIC + OIL SHOCK

by ~2.1mm b/d in 2020, while the H1 IHS Markit and Standard Chartered estimated a reduction of ~2mm b/d from the year earlier.

Measuring the impact of oil prices on the US stock market can be tricky. The average correlation between oil prices and US equities is not far from 0. Why? Because oil prices can be affected by both demand shocks and by supply shocks. For example, if there is a positive demand shock for oil because of an improving macro landscape, we would expect a positive correlation. On the other hand, if there is a positive supply shock, due to increased production, we would expect a negative correlation as lower oil prices would generally help the overall economy, at least those parts of the economy not linked to the oil sector. Clearly the market did not react positively to the recent sharp drop in oil prices, but it remains to be seen if low oil prices will help limit the length and severity of a US recession.

Regardless of the reason, an abrupt oil price selloff is always a negative for the energy sector. Morgan Stanley reduced US GDP growth by 0.15% to 0.35% in Q1 2020 as oil and gas extraction and refining represents 1.7% of the US economy. The energy sector will likely see bankruptcies, job losses, loan defaults, and reductions in capex. The amount of debt borne by energy companies is unprecedented. Energy companies have ~$88 billion in bonds due this year, with expected defaults surpassing 2016 levels. Also, the amount of oil and gas debt trading at distressed levels increased by 14% to $81.5 billion from $71 billion. This amount of outstanding debt and the potential for default is certainly cause for concern for the ~1.5 million individuals employed in the energy sector spread across 945,000 downstream jobs, 471,000 upstream/oil field services jobs, and 69,000 midstream jobs.

COVID-19

The overall economic impact of COVID-19 is hard to assess. UNCTAD warns of a $1 trillion cost to the world economy, with global growth under 2% versus 2.9% in 2019. Consequently, it is estimated that global average policy rates will drop to nearly 1.50% by the end of 2020, versus about 1.80% previously. Of note, some projections point to China's GDP being reduced to below 5% in 2020 versus 6.1% in 2019. This represents their slowest pace since 1990, but it is projected to recover to 6.4% in 2021. China's all-industry PMI collapsed 24.4-points, while the rest of the world PMI fell by ~ two points.

Of particular concern is the rise of corporate debt, which could send many companies in default. In 2019, outstanding debt held by non-finance corporations reached a record of $13.5 trillion, with a substantial portion coming from riskier bonds. Research suggests that approximately one-sixth of US companies will not have the cash flow to cover interest payments. In 2019, the IMF warned a crisis half as severe as the 2008 recession could put 40% of corporate debt at risk. Consequently, closely monitoring corporate debt, especially high risk, will be paramount.

In response to the decline in economic activity, central banks are lowering rates and governments are implementing policies to reduce the shock. For instance, the US fed implemented a $1.5 trillion intervention in short-term funding markets via three $500 billion repo offerings, which will expand the Fed's portfolio by over 35%. In addition, as expected, Fed lowered the benchmark to 1.00%-1.25%, which should not be understood as an easing of the burden on businesses, but rather a realignment with other central banks ahead of international coordination shortly.

Source: WSJ, RBC Economics, Bloomberg, Capital IQ

ECONOMICS

PANDEMIC + OIL SHOCK

Indeed, earlier this evening, the Fed cut interest rates to 0%. While the goal is to supply liquidity to the banks, it does not solve consumer spending, such as flight cancellations and empty restaurants. Despite the Fed stimulus announcement at 5pm, S&P 500 futures were trading limit down 5% just 15 minutes after opening at 6pm. We expect a lot more central bank stimulus in the coming weeks and months. While we do believe central bank stimulus is appropriate, it remains to be seen if it can turn things around, or just limit the damage.

Source: WSJ, RBC Economics, Bloomberg, Capital IQ

Consumers

2020 COVID-19 SPECIAL REPORT

Kanishk Shah
Alexandra Tremblay
Selena Zhu

CONSUMERS
A WILD RIDE

STAPLES AS SAFE HAVENS?

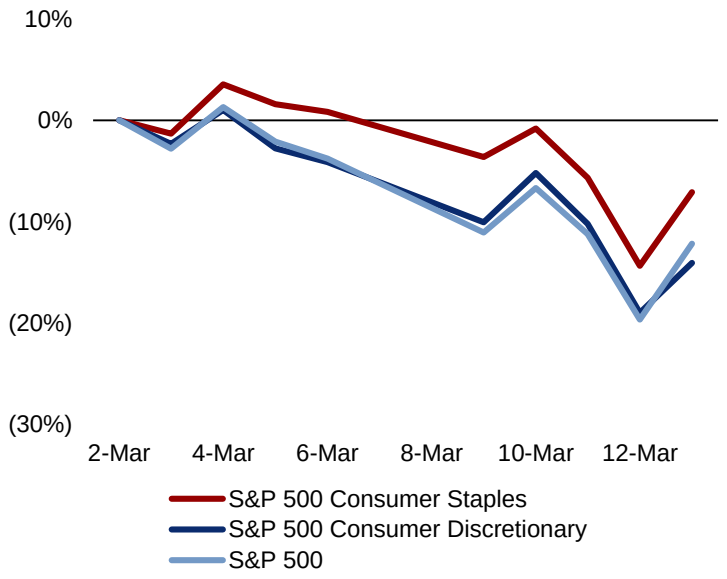
Since the COVID-19 outbreak, Consumer Staples has outperformed the overall market, returning (7.1%) during the first half of March compared to a broader market return of (12.2%) over the same period (Figure 1). As the COVID-19 pandemic triggers fears of coronavirus outbreaks in major cities around the world, Staples' outperformance is predominantly attributable to the wave of panic buying across supermarkets as consumers prepare for prolonged quarantine periods, prompting many to stockpile household necessities such as toilet paper, disinfecting wipes, and groceries, particularly non-perishable food with long shelve lives. Given the sharp increase in demand for Staples products evident from reports of empty supermarket shelves, the Consumer Staples subsector has become increasingly representative of a defensive investment opportunity, one characterized by steady revenue streams and relative stability amidst a period of extreme market volatility and uncertainty. Thus, we believe that the recent outperformance of the Staples subsector over the broader market is primarily reflective of a surge in investor demand for defensive equities as investors sought to seek shelter from the storm. Going forward, if the COVID-19 pandemic continues to worsen, we predict that Staples will be in a stronger position to weather the impact of COVID-19 than the broader market, capitalizing on heightened consumer demand for necessities such as household products and groceries.

DISCRETIONARY

On the other hand, Consumer Discretionary has underperformed the overall market, returning (14.1%) during the first half of March (Figure 1).

Cruise line stocks, such as Carnival, Royal Caribbean Cruises, and Norwegian Cruise Line, in addition to other travel-related stocks have been hit hard. Casino/resort stocks like MGM and Wynn went down by almost 50%. Going forward, discretionary stocks will most likely suffer from demand concerns if COVID-19 continues to worsen as consumers limit discretionary and unnecessary product purchases. The overall consumer sentiment on discretionary spending has gone down. Fast-food restaurants that offer premium products are a good indication of overall consumer sentiment because a large proportion of them currently cater to two themes that have been overwhelming within the consumers sector: premiumization of products and a change in tastes and preferences towards healthier alternatives. On average, companies within this sub-sector that have outperformed peers have been hit hard. Companies such as Chipotle have declined by ~30% over the past month. These stocks are sensitive to announcements regarding the COVID-19 outbreak, along with the broader market index.

Figure 1: Subsector and Benchmark Returns



Source: Bloomberg

CONSUMERS
A WILD RIDE

AIRLINES - A LEADING INDICATOR

Travel has been a concerning factor for a large number of businesses, as well as individuals because it is where people are the most vulnerable to contracting the virus. From a recent call with a large North American airline, we have been told that demand for flights had not been seriously impacted by the virus until the recent announcement of the pandemic. Airlines are currently unsure about future levels of demand because ticket sales have been further sensitized to news releases. The recent announcement in particular generated a spike in cancellations.

As we expected, discretionary travel has been the first to take a hit. Both individuals and families have started to cancel their trips. We expect businesses to follow, cancelling work-related travel plans.

Given the massive hit that airlines have taken over the past month, we believe that reactions in their stock price represent a leading indicator for overall investor sentiment with respect to consumer discretionary spending. Moving forward, we will be monitoring demand for ticket sales which will drive airline stock prices and make investment decisions based on commentary provided related to ticket sales.

In terms of our holdings, the consumers sector currently holds Aritzia, a Canadian-based clothing retailer, and Loblaws, a Canadian-based grocery chain that has exposure to pharmaceuticals. Aritzia is currently down ~36% over the past month because it has been affected by the broader factors which impacted the discretionary sub-sector. On the other hand, Loblaws has maintained most of its value, declining only ~6% over the past month because increased demand that grocery stores have recently faced. The increase in demand is a direct consequence of the decline in spending on restaurants and overall discretionary spending.

The emphasis that consumers have been placing on isolation has created an increased demand for household supplies, which has driven topline growth for Loblaws. We believe their positive performance will continue as the volatility within the market remains; however, their ability to maintain topline growth at current levels may be impacted as fears around the virus start to fade. The partial decline in the stock price can be attributed to the decline in demand for the higher-value discretionary products that they offer, as well as the overall decline in the market.

Source: Bloomberg

Energy

2020 COVID-19 SPECIAL REPORT

Zhao Kang Chen
Alessio Marcogliese
Duncan McHattie
Riley Wolever

ENERGY
UPSTREAM PRODUCERS

Holdings: Seven Generations Energy, Suncor, Parex Resources

CAN US & CANADIAN PRODUCERS SURVIVE ON $30 OIL?

Each basin in North America requires oil prices to be significantly above the current market price in order to be profitable, except for a handful of wells. Specifically, the Permian basin requires $46-50 WTI to breakeven, the Eagle Ford requires around $48, and the Canadian Oil Sands requires around $40 WTI. This figure for the oil sands is misleading, however, as the spread between WTI & WCS varies over time. Long-term futures prices range between $33.6 for June 2020 and $46.38 for December 2023, suggesting the market expects low prices for a many years.

There are large concerns in the market surrounding the ability of oil & gas companies to meet debt payments when prices are this depressed. Of the $936 billion in oil & gas bonds in the US, 12% were distressed, where yields were above 10%, on March 9th. Fortunately, Parex & Seven Generations, representing our upstream exposure, are both responsibly levered. We are currently analyzing the likely scenarios for default rates, which will be dependent primarily on the length of this oil price war. North American upstream companies cannot survive $30 WTI if it remains at this level for a long time, considering their breakeven prices. However, this is improbable since Russia & Saudi Arabia also lose out when oil is this low, so this conflict is likely a remain a short-term issue. Therefore, how North American upstreams fair will depend on the length of the depression in prices, and how American & Canada's governments react and if they offer any stimulus. We believe that E&P's with strong balance sheets will be able to weather the storm. However, many E&P's, especially in the US, do not have strong balance sheets, and we therefore foresee a high number of bankruptcies, similar to the market. An estimated $27 billion in oil & gas bonds come due this year, and decreased investor sentiment has depleted companies' abilities to refinance their debt. Much of their survival in this environment is company-dependent. For example, a company like Whitecap has hedged 50% of their production, as is industry standard. We believe that Canadian firms, given their strong balance sheets, and going off of the market correction in 2014, can outlast low prices for a year.

Furthermore, Premier Kenney in Alberta has also hinted at providing a lifeline for the sector, such as temporary liquidity if the depression of oil prices persists. We will be watching carefully the political response at federal and provincial levels.

WHAT DO NAV MODELS LOOK LIKE WITH $30 OIL?

A company such as Suncor is a going concern given that they are hedged by their downstream operations, with both their fuel retailing and refinery operations benefitting from lower oil prices.

Seven Generations has been the holding that has struggled the most. Assuming that prices remain this low for the remainder of their 2P reserves, our model claims that the company should trade around $3.28. The company is currently trading at $2.08 and we believe that the market may be overly pessimistic in assuming bankruptcies in this space.

Our updated analysis for Parex, another of our holdings, shows a new target price of $14.28, slightly higher than the current trading price of $14.14.

Source: Bloomberg, CME, CBC

ENERGY
UPSTREAM PRODUCERS

WHAT DOES OIL IMPLIED VOLATILITY LOOK LIKE?

Market prices have stayed at around $31 for WTI and $35.44 for Brent since the initial crash at the market open on March 9th. Implied volatility, which can be considered a measure of downside risk, hit 100% on March 9th and on March 12th, a level not seen since December 2007. Implied volatility fell modestly to 94% on March 13th. For options going month by month to March 2021, it falls by roughly even increments to 41%.

COULD RUSSIA AND SAUDI ARABIA AGREE TO A CUT AND SEND OIL PRICES BACK UP?

China consumes about 14 million barrels per day, equivalent to the combined needs of France, Germany, Italy, Spain, the UK, Japan and South Korea. Since the beginning of the virus, Chinese oil demand has decreased by 20%. OPEC still sees a rise in global crude oil demand for 2020 despite the spread of COVID-19, but now expects an increase of just 60,000 barrels per day. This constitutes 920,000 barrels per day less than initially projected. As a means to counter this radical change, OPEC initially agreed to slash production to artificially prop up the price of oil, but Russia was uncooperative. As a means to push back, Saudi Arabia and the UAE planned to retaliate by ramping up their crude oil production. As of now, the crude oil futures market is over flooded. Saudi Arabia has a significantly lower break-even oil price than Russia.

With Russia attempting to undercut Saudi Arabia, we believe that the Saudis will outlast the Russians, forcing them to eventually settle given their break-even price advantage. Russia is also facing some severe economic and government problems as natural resources make up around 60% of their GDP. Additionally, the Ruble has also depreciated by 11% against the American dollar in the past two days. This sustained pressure on the Russian economy as well as the ruble will force Putin's government to eventually settle with the Saudis. Therefore, we believe that the Russians, despite being hard-headed, can strike a deal in the next couple of months given the clear break-even advantage that the Saudis benefit from. Our proprietary view is that a deal will be struck by the end of April.

WHAT'S GOING ON WITH NATURAL GAS?

Henry Hub futures, the American natural gas benchmark, has seen a modest price drop to less than $2/mmbtu for 1-6 month deliveries. AECO data is difficult to find in the short term, and we are continuing to form an opinion on the effect of this price war on Canadian natural gas producers.

Investor sentiment is not as bearish on natural gas as it is on oil. Part of the reason for this is that natural gas is much more of a local commodity and the companies producing it are largely less reliant on Chinese demand, which is where crude producers have seen the biggest hit. Lower crude oil prices are expected to lead to a slowdown in US shale drilling, which would reduce the amount of associated gas produced. This might then lead to a decrease in overall natural gas supply, leading to a boost for natural gas focused producers. Natural gas inventory figures will be published on March 19th which may move markets as well in conjunction with any news this coming week.

Source: Bloomberg, CME, FT

ENERGY
OTHER VERTICALS

MIDSTREAM

Holdings: Pembina Pipelines

Valuations in the midstream sector have also been hit, with our midstream index down 60% since December 31st, 2019, and down 47% since the beginning of March. Midstream companies, without secured capacity, may have issues as E&P companies cut production going forward. Pembina lost almost 20% of their stock value on March 9th the general rout. Further analysis is needed on their contracts to determine their exposure to various Canadian producers, who will themselves be differentially impacted by lower oil prices.

The effect of such a compression in oil prices on a midstream company such as Pembina is dependent upon the nature of the contracts associated with their assets, and the counterparties associated with said contracts. A certain portion of Pembina's transportation contracts for their pipelines do not include take or pay commitments, which means they are exposed to decreases in volume due to unprofitable crude prices for upstream producers. Also, Pembina is exposed to market spot prices at which they sell petroleum products, as well as Liquid Natural Gas price spreads for processing plants, but most of these operations are hedged.

The largest risk for Pembina is counterparty risk, which is the risk of upstream companies being unable to honor contracts. Pembina's two largest counterparties, accounting for the biggest percentage of their contracts, are Suncor & Canadian Natural Resources. Suncor is rated A- and CNRL BBB+ by S&P, which are of the upper echelon of upstream producers. Unfortunately, Pembina releases limited information on their counterparties. This being said, the drop in oil prices is certainly a headwind for Pembina, but given their responsible leverage, they have the ability to weather the storm. We believe that Pembina's earnings will return to pre-crisis levels at some point in the near future, probably in the second half of 2020. We therefore retain the opinion that the stock is undervalued, as it has fallen over 40% recently, which we see as unjustified.

DOWNSTREAM

Holdings: Marathon Petroleum Corporation

Marathon opened on March 9th down nearly 25% over the weekend, amid a broader loss for the downstream/refining sector of 35%. Compared to other verticals, the downstream sector is doing well as input costs have decreased through the lower oil prices. On the other hand, a global economic slowdown will decrease demand for refined products, squeezing margins. This has led it to fall less than other verticals.

UTILITIES

Holdings: None

In the long run, an economic slowdown will be a source of concern for regulated and unregulated utilities stocks as demand decreases, but we believe that much of the decrease seen so far has been as a result of forced selling, and that there are opportunities that we should look out for in this space.

RENEWABLES

Holdings: None

Some commentators seem to think that over the last decade, renewables investment has become decoupled from the price of oil. Although the collapse of oil prices following the great recession of 2008 did lead to a decline in renewables investment, this was not true after the second crash in 2016.

Source: Bloomberg, CME

ENERGY

OIL PRICES – A CLOSER LOOK

We decided to examine the effect of the change in oil prices on change in price of our holdings. We used the historical LTM prices of WTI and Suncor to perform a regression analysis on their daily deviation from their average prices (Figure 1). Interestingly, this regression has generated an output with a fairly high correlation of 0.688, based on 250 observations, equal to the number of overlapping trading days.

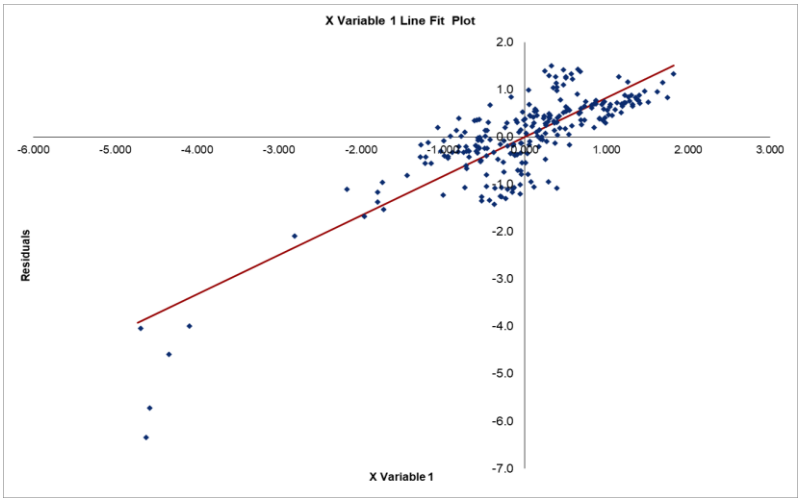
FIGURE 1 – 1 YEAR REGRESSION

Regression Statistics	
Multiple R	0.829551766
R Square	0.688156132
Adjusted R Square	0.686893606
Standard Error	0.560686115
Observations	249

ANOVA

	df	*SS*	*MS*	*F*	*Significance F*
Regression	1	171.3508768	171.3508768	545.063033	1.93538E-64
Residual	247	77.64912316	0.31436892		
Total	248	249			

	Coefficients	*Standard Error*	*t Stat*	*P-value*	*Lower 95%*	*Upper 95%*	*Lower 95.0%*	*Upper 95.0%*
Intercept	1.63287E-14	0.035532039	4.59549E-13	1	-0.069984428	0.069984428	-0.069984428	0.069984428
X Variable 1	0.829551766	0.035532039	23.34658504	1.93538E-64	0.759567338	0.899536194	0.759567338	0.899536194



We have then conducted the same analysis on data YTD (Figure 2) to examine whether the COVID-19 outbreak has caused a change in the impact on prices. Based on this model, we obtain an even higher correlation of 0.916. This is not surprising. When oil becomes more volatile, its impact on stock price becomes much more dominant, compared to company specific factors like operational efficiency. As long as oil prices remain volatile, we expect a continued high correlation.

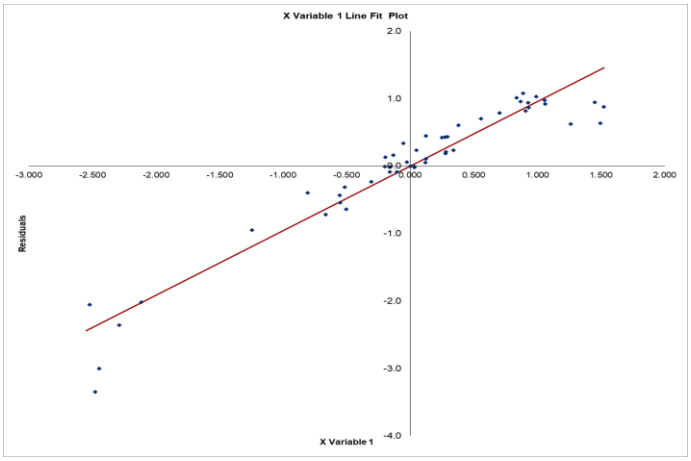
FIGURE 2 – YTD REGRESSION

Regression Statistics	
Multiple R	0.956829663
R Square	0.915523003
Adjusted R Square	0.913763066
Standard Error	0.296642667
Observations	50

ANOVA

	df	*SS*	*MS*	*F*	*Significance F*
Regression	1	45.77615015	45.77615015	520.2020165	2.0852E-27
Residual	48	4.223849846	0.087996872		
Total	49	50			

	Coefficients	*Standard Error*	*t Stat*	*P-value*	*Lower 95%*	*Upper 95%*	*Lower 95.0%*	*Upper 95.0%*
Intercept	1.61053E-15	0.041951608	3.83902E-14	1	-0.084349362	0.084349362	-0.084349362	0.084349362
X Variable 1	0.956829663	0.041951608	22.80793758	2.0852E-27	0.872480301	1.041179024	0.872480301	1.041179024



Financials

2020 COVID-19 SPECIAL REPORT

Miller Cressman
Jared Gaffe
Frédéric Lam
Marc Latif
Shelly Qian

FINANCIAL INSTITUTIONS
INVESTORS ON THEIR GUARD

PERFORMANCE THIS YEAR

The Financials Institutions sector is one of the sectors that has been hit the hardest by the recent market slump. As of March 13th, the S&P 500 Financials Index is down 35% YTD. After an improvement in the macroeconomic environment sent the sector soaring at the end of 2019, the climate quickly deteriorated, leading to the sharp decline. Banks have been hit the hardest as investors are pricing in several rates cuts, slower loan growth, as well as a slowdown in capital markets activity. We believe that the market may be overshooting, and our grey sky valuation of Bank of America, which incorporates some of these headwinds, suggests that such a decline may not be warranted. On the other hand, we believe that REITs were trading at a very high P/FFO and that a certain correction may be justified, leading to a fairer valuation now. Diversified financial companies, such as Visa and American Express, have seen a more modest decline in price, in line with the broader S&P 500.

BANKING INDUSTRY UPDATE

Interest income

Net interest income projections should be lowered given the rate cuts. This decrease in net interest income is driven by the fact that the rates that banks receive on their loans falls more quickly than the rate that they pay for deposits. At the beginning of March, the Fed cut the rates by 50 bps to 1.25% to give a boost to economic activity amidst an unexpected acceleration of the spread of COVID-19. Following this, the market is already pricing in 3 more rate cuts for their next meeting. Similarly, the Bank of Canada cut rates twice in March, from 1.75% to 0.75%, to counteract both the impact of COVID-19 on business activity, as well as tanking oil prices that will particularly hurt the country given its large exposure to energy.

Interest income may be adversely impacted by the lower loan growth given the general slowdown of the economy. In terms of commercial loans, banks with high exposure to the energy, retail and industrials sector are expected to be hit the hardest. Given the fact that BMO has the highest exposure to the energy sector out of all big Canadian banks, as well as some exposure to U.S. industrials, we will monitor loans performance more closely in the next few months. Both the U.S. and Canadian government have proposed stimulus packages, which could support loan growth. In the U.S., the House of Representatives passed legislation to provide sick pay leave. In Canada, Finance Minister Bill Morneau announced a $10 billion injection into credit for small and medium sized Canadian businesses hit by COVID-19, while Superintendant of Financial Institutions Jeremy Rudin plans to lower the domestic stability buffer requirement to one percent, which should result in more than $300-billion in additional lending capacity for major banks. These packages should help alleviate the impact of the slowdown in the economy on net interest income in the short term.

Although it is unclear how much loans performance will deteriorate in the coming months, banks' fundamentals are stronger than they were during the last recession, suggested by charge-off ratios across all big U.S. banks at around 0.58% for 2019, compared to 1.24% for 2007.

Fee income

We expect fee income to be negatively impacted as well in the short term, as the slowdown in economic activity is expected to reduce capital markets, advisory and underwriting activity. Not only is the high volatility in equity markets making businesses more weary to engage in M&A activity, but a defensive approach may be favoured over growth, as businesses brace for a

Source: Bloomberg, Financial Post, L.A. Times.

FINANCIAL INSTITUTIONS
INVESTORS ON THEIR GUARD

slowdown in economic activity. The extent to which interest income and fee income will be affected by recent changes in the environment is still unclear, and we will continue to monitor the situation and seek out opportunities in the banking industry.

IMPACT OF RECENT DEVELOPMENTS IN THE ENERGY SECTOR

On March 9th, Saudi Arabia and Russia abandoned their joint supply curbs with OPEC and threatened to increase production despite an already depressed demand resulting from the effects of COVID-19. The subsequent collapse in oil prices sparked fear within the banking sector as investors anticipate bankruptcies among North American energy companies.

American upstream energy companies are highly leveraged and have $86 billion of debt coming due between now and 2024. These companies are particularly vulnerable in the midst of the oil price war as cost of production in America is far greater than Saudi Arabia and Russia. Therefore, as oil prices drop and credit markets tighten, these companies will face difficulties repaying or refinancing their loans.

Canadian producers are relatively better positioned. In 2014, as US producers levered up with higher-yield debt to focus on growth, Canadian producers de-levered and compressed their operating costs by 30% on average. Canada's big six banks have also learned their lesson from 2014 and have been gradually reducing their exposure to the energy sector. Currently loans to energy companies account for around 2% of total loans held by Canadian banks, down from an average of 5%-10% prior to the 2014 oil crash. Moreover, on March 11th, Alberta's premier Jason Kenney urged Ottawa to provide relief to Canada's energy industry and reiterated his demand for the release of $2.4 billion from a fiscal stabilization fund for provinces impacted by plunging revenues.

Default rates within the energy sector are largely dependent on the length of the oil price war. Currently, about a third of US upstream energy companies require a WTI price of $55/barrel to breakeven while Canadian oil sands have a breakeven price of around $40/barrel. With WTI prices currently at about $30/barrel, North American upstream companies will not survive if these prices persist in the long term, resulting in increasing provisions for credit losses among banks. However, the oil war will likely be short lived as Russia and Saudi Arabia are also under pressure. Despite the fact that Aramco has over 50 years of reserves and a cost per barrel below $9, the IMF estimates that the kingdom's budget requires an oil price of over $80.

Nevertheless, default risk within the DCM Financials portfolio remains low as only 1.4% of BAC's loans are directly exposed to the energy sector. While BMO has the largest exposure among Canadian banks, the figure still remains low at 2.8%.

Source: Bloomberg, Rystad Energy, Financial Times, The Globe and Mail

REAL ESTATE
BIG LOSSES "ON THE HOUSE"

REAL ESTATE PERFORMANCE

The current market environment will be a challenge for real estate investment trusts. Traditionally, as interest rates decrease with business cycles, REITs attract investors since they are able to take on cheap debt to grow their operations. However, the rate cuts in the current crisis in which we find ourselves are indicative of a recession similar to that of 2008, and thus the poor economic outlook we anticipate has been the main driver for the losses sustained by real estate stocks. In addition, COVID-19 will affect the likelihood of tenants to generate strong income and being able to pay their leases to the REITs. We have thus seen real estate stocks tank in comparison to the general equity market. Furthermore, at the end of last decade, we had seen REIT stocks trading at multiples of 30x P/FFO, which we deemed to be non-sustainable and could explain, in addition to the decreases in interest rates, the significant drops in prices that some REIT stocks have faced recently. The gaming/gambling REIT sector, in which we hold MGM Growth Properties, has seen declines ranging between 33% and 42%, with MGP seeing a less severe decrease to its stock price of 32.1% since February 21st. In comparison, competitors such as Gaming and Leisure Properties Inc (GLPI) and Caesars Entertainment Corporation (CZR) have seen returns of (34%) and (41.5%) within the same time period.

Following the losses generated recently, MGP saw its P/FFO valuation drop from 22.28x at the end of 2019 to a more reasonable 16.25x. However, as MGP's business model involves it purchasing the assets from MGM Resorts and leasing it back to them, we believe it is the latter that will see more severe decreases in its performance and MGP can still drive value through its ownership of unique assets on the Las Vegas Strip. Our second real estate stock is Simon Property Group (SPG), the biggest mall operator in the US. One of the main reasons behind our investment in SPG was its modest valuation of 12x P/FFO earlier in 2020. As the market leader in its sub-sector, in addition to the cheap price tag, SPG was seen as a solid defensive stock. Our outlook for the acquisition of smaller competitors like Taubman Centers was deemed positive as we believe it was a great opportunity for SPG to increase its ownership of Class A malls in the US. However, with the expected reduction in consumer spending in the foreseeable future coupled with the avoidance of large gatherings of people in one place, like the malls owned by SPG, we expect stores within those malls to close down to cut costs, which will see SPG's performance tumble. However, we believe the market has incorporated these factors, as the stock is down by over 36% since the beginning of the sell-off in February, which has led to SPG currently trading at a very modest 8.43x P/FFO multiple. While we keep on monitoring the company's fundamental performance within the near future, we believe closing our position in MGP and doubling down on SPG could be an opportune investment, especially when taking into account SPG's cheap price vis-a-vis other market dominant REITs and their strong distribution yield.

Finally, we believe it is important to keep monitoring other sub-sectors of real estate that have performed fairly well such as self-storage REITS. For instance, Public Storage (PSA) and Extra Space Storage (EXR), the two biggest self-storage REITs by market cap, have seen returns of (6.4%) and (11.6%). With demand for storage remaining fairly constant and households emptying grocery stores due to panic buying recently, they are seeking additional storage space to keep their newly purchased items in and we expect self-storage REITs to keep doing fairly well within the near future.

Source: Bloomberg, Yahoo Finance, WSJ.

Healthcare

2020 COVID-19 SPECIAL REPORT

Jesse Li
Sean McNally
Arasan Thangavelu

HEALTHCARE
MAJOR DISRUPTION IN THE INDUSTRY

In recent weeks, the major headlines in the healthcare industry have been surrounding the COVID-19 virus outbreak. Almost all sectors in healthcare have been substantially impacted both directly and indirectly by the outbreak. Although research companies are responding rapidly by funding programs to find a treatment for the disease, other implications have permeated in the industry, particularly the disruption of healthcare supply chains and company employee-work policies.

INCREASED GLOBAL EFFORT FROM BIG PHARMA AND BIOTECH

Several large drug manufacturers as well as biotech companies have begun work on the development of an effective treatment for COVID-19. On March 5th, the U.S. Senate approved $8.3bn in funding to help combat the virus, including research and development efforts. However, guidance from biopharma companies suggests that a viable cure, if any, is months or even years away. Currently, treatment mostly consists of supportive care. Here is a list of the top running candidates in the process:

• **Takeda** (NYSE: TAK), Japan's largest pharmaceutical company, is developing a plasma-derived therapy to mitigate and potentially prevent the COVID-19 illness by taking antibodies from recovering patients and transferring them to infected people to trigger a more effective immune response.

• **Gilead** (NASDAQ: GILD) is undergoing clinical trial to test a new experimental drug stemming from the company's previous therapies for Ebola. Gilead expects human data result to be available by April with up to 400 patients in the study.

• **Sanofi** (NASDAQ: SNY) and **Regeneron** (NASDAQ: REGN) have partnered in a research trial to see whether drugs used to treat rheumatoid arthritis could help ease the damage, but not cure, the lung and respiratory damage caused by the virus

• **GlaxoSmithKline** (NYSE: GSK) partnered with China-based based biotech Clover Biopharmaceuticals to design a vaccine to strengthen the induced immune response to COVID-19. The process still remains in pre-clinical stage.

• French drug-maker **Sanofi** is partnering with the U.S. government to work on an antibody-based treatment. The company expects to have a research candidate ready for in vitro testing within six months and a clinic study ready within a year and a half.

• **Johnson and Johnson** (NYSE: JNJ) is looking to develop a new vaccine. The U.S. government has agreed to fund development through Phase 1 testing.

The upshot: some companies like Gilead are looking to treat the underlying disease, while other companies like Sanofi are working on vaccines to prevent the disease. Until several months from now, it remains unclear which of the two will have greater effectiveness.

IMPACT ON HEALTHCARE WORKERS

Many healthcare organizations, both public and private, are imposing strict regulations by ordering employees to work from home. The FDA announced that it will be postponing inspections of overseas manufacturing plants, giving exception to only those deemed 'mission critical'. They also stated the

Source: Bloomberg, Biopharma Dive, Fierce Pharma, CNN, WSJ, Financial Times

HEALTHCARE
IMPACT ON BROADER ECONOMY

recent epidemic may also affect review of other novel drug approval processes through April.

Large drug-makers, like Eli Lilly, Biogen and Takeda are asking employees to stay at home if they can. Biogen has already confirmed outbreak of virus amongst nearly two dozen employees who attended a conference last month. Senior executives at biopharma companies are also limiting their travel.

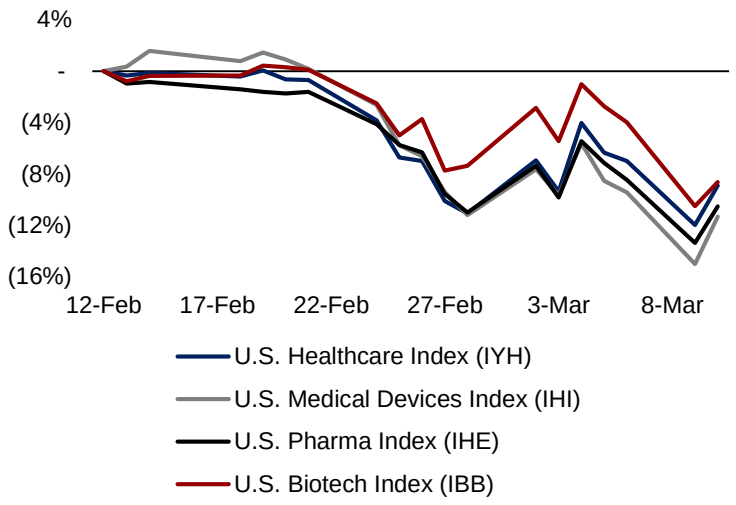
SUPPLY CHAIN DISRUPTION

Biopharma companies are keeping a close eye on supply chains as COVID-19 has halted production and exports in several plants globally. Companies are seeing delays in shipment of manufactured drugs and officials are becoming increasingly worried about drug supply originating from China, which produces 90% of the ingredients that go into drug manufacturing. India, which supplies 40% of the US' generic drugs, also restricted exports of a range of pharmaceutical products including common antibiotics and acetaminophen (the active ingredient in Tylenol) to protect its own domestic supply. As Charley Grant of the WSJ says, "the good news is that large global pharmaceutical makers tend to hold substantial inventory. So if disruptions in China ease over the next two months, serious shortages may well be averted… until the second or third quarter." In addition, overall shortage of medical devices is leaving hospitals and healthcare workers dangerously low on supplies.

DCM OUTLOOK

Although the market has been heavily focused on the negative impacts of the coronavirus outbreak, we don't believe it is completely unjustified. Given export restrictions and heavy reliance on China for many healthcare companies' manufacturing supply, we believe there will be short-term earnings impacts.

Figure 1: One Month Performance of Subsectors



Healthcare subsectors in pharma and medical devices have been hit the hardest, mainly due to supply chain shocks. Medical devices have traditionally been safe plays in downturns, but multiples in this sector were significantly elevated in the last 5 years, potentially at overvalued levels. As a result, we do not believe this sector is an attractive bet. For example, Medtronic is down 23% since early February 12th, demonstrating our conviction to stay away from medical devices for the moment.

We foresee China eventually lifting bans in the near future as they show signs of recovery while countries such as in India and Italy will continue to persist with restrictions. We will monitor the potential spread of the virus in China as people slowly return back to work. Interestingly, major drug companies who are developing potential treatments for the virus have also seen their share value decline to similar levels. This signals to us that the market believes an effective treatment for the virus is still bleak in the near-term, which we believe is fair given the limited clinical data so far.

Source: Bloomberg, Biopharma Dive, Fierce Pharma, CNN, WSJ, Financial Times

HEALTHCARE
A BUMPY RIDE AHEAD

We foresee generics in pharmaceuticals to be the hardest hit in the industry from supply chain disruptions. The world's largest generic companies Mylan (NASDAQ: MYL) and Teva (TLV: TEVA) have seen their shares slide by more than 30% each in the last month. We view this as a potential attractive investment opportunity given the large discount but will choose to wait until mid-year to reevaluate. We believe these two leaders in generics have strong potential to recover once the dust settles, though a longer-term investment horizon will be required.

Meanwhile, biotech shares also slid in line with the overall healthcare index. We believe this is an overreaction by the market that's caused by association with overall negative sentiment in stock market and healthcare industry. Biotech valuations are mainly driven by future revenues generated by approval of novel drugs. Moreover, many new therapies have specialized manufacturing operations in North America and Europe rather than China. Though we admit the FDA may be more focused on approving COVID-19 treatments, we believe this is simply a delay in the approval process and does not provide justification for a large drop in intrinsic valuation. Therefore, we do not recommend any sell-offs of our current holdings of Sarepta Therapeutics or Orchard Therapeutics despite the recent drop in share price.

SUMMARY

COVID-19 has led to several negative implications in the healthcare industry, but have also presented sub-sectors which trade at a significant discount due to the overall market sell-off. We will continue to monitor the drug development process for an effective cure as well as the supply chain business of the pharmaceutical companies. All our holdings have suffered from the recent sell-off, ranging from our medical devices exposure in Savaria, to our biotechnology/gene therapy exposure in Sarepta and Orchard Therapeutics. The latter companies have not offered updates on the impact of COVID-19 on their operations, which means clinical trial readouts are likely still in progress. Of course, many healthcare companies have since shifted their focus to aiding in the containment of the virus, which may lead to bottlenecks in approvals and readouts at the FDA. This delay will affect Sarepta and Orchard's pipeline in terms of timing, not probability, and we therefore feel confident in holding these businesses.

Our companies are well capitalized and can sustain until late 2021 given current cash burn rates which means they will only need to tap capital markets until this time where we except conditions to improve.

Our thoughts are with those affected and wish to thank the many who have dedicated their lives to responding to this pandemic.

Source: Bloomberg

Materials & Industrials

2020 COVID-19 SPECIAL REPORT

Maxime Barbeau-Di Meo
Serge Krikorian
Hashaam Nadeem

MATERIALS & INDUSTRIALS
CYCLICAL IMPACTS OF COVID-19

SUMMIT MATERIALS

Summit Materials operates in the construction materials sub-sector within the US. Our initial theses involved the fact that they were well positioned to benefit from industry tailwinds and significant greenfield opportunities, as well as because they were trading at a significant EV/EBITDA discount relative to their larger peers. It has taken a big hit recently, down 40% YTD with a beta of 2.04, compared to its two major competitors Vulcan Materials, (18%) with a beta of 0.95, and Marietta Materials, (25%) with a beta of 1.01. Although COVID-19 doesn't directly impact construction, it has led to greater fear of slowdown among consumers, potentially reducing their willingness to invest in new housing, leading to less construction activity and consequently affecting Summit's business. Furthermore, it is possible that the cost of building materials could rise if production from overseas slows down, both negatively affecting the construction sector and Summit. Concerning our outlook, we remain hopeful on Summit Materials because of their strong balance sheet, and our belief that their exposure to the US government infrastructure FAST ACT spending will help them survive this difficult period for residential and non-residential construction. Going forward, we believe borrowing rates will remain low, therefore customers will have a greater incentive to purchase their own homes, a trend which we believe Summit can benefit from post-crisis.

NORNICKEL

Nornickel, a Russian industrial conglomerate operating mines and smelters, is our holding in the metals and mining sub-sector. Our initial theses revolved around Nornickel's ideal position to capture growth in Hybrid and Electric Vehicles given its product mix and that Nornickel's focus on ESG will create long-term value.

Given that China reflects around 50% of global nickel and copper demand along with 29% of palladium consumption, the COVID-19 outbreak poses great downside risk in the Metals sector. Nickel and Copper manufacturers, including Nornickel, have experienced a dip in sales following a complete shutdown of the economy and a reduction in Chinese demand for industrial used copper and nickel used in stainless steel production. In the last three months, Nornickel has seen a drop of 20% in its stock price compared to its peers Vale and BHP which are down 21% and 37.5%, respectively.

Given the recent positive reports regarding the economic recovery from the outbreak in China, we believe copper demand will recover due to continued infrastructure investments. The long-term driver of nickel batteries for electric vehicles, combined with the Indonesian ban on nickel exports which has impacted supply, makes us remain hopeful for an increase in nickel demand.

For Palladium, another metal in Nornickel's portfolio that composes 33% of revenue, stricter vehicle emissions standards around the world are supporting demand for Palladium in more advanced automobile catalytic converters.

Given the strong fundamentals of Copper, Nickel and Palladium coupled with Nornickel's positioning as the largest producer of Palladium and Nickel in the world, we remain confident in the stock going forward.

Source: Bloomberg

MATERIALS & INDUSTRIALS
CYCLICAL IMPACTS OF COVID-19

TRANSDIGM GROUP

Regarding our only industrial sector exposure with Transdigm, we decided to look at how COVID-19 and a potential recession would affect the commercial aerospace market, which forms the majority of TDG's revenue. TDG develops, distributes and manufactures commercial and military components for aircraft. A slowdown in this market and the halt of many flights has pushed TDG's stock price down 23.75% in the past month, compared to its closest peer Heico who is down 22.50%. The best way to analyze air traffic impact by COVID-19 would be to look at China, which has started to contain the pandemic. In a rather interesting BRP report regarding air traffic in China, airport capacity in the country was down 48% the week ending March 6th, compared to a decrease of 70% at the peak of the virus. To add to that, production of Airbus planes resumed in Tianjin, China, showing positives signs for aircraft production. Overall, it seems like air traffic is slowly picking back up, at least in China, as containment reduces the impact of the virus. That said, as the virus is becoming more and more international, it will be interesting to see how air traffic in countries like Italy will react when latest air traffic data becomes available. Also, with the US announcing a 30-day travel ban coming from Europe, we can expect airport capacity dropping even faster than what we saw in China. This is not necessarily bad news as a successful containment of the virus would be more beneficial for aircraft manufacturers in the medium-to-long run. Regarding TDG specifically, airlines are expected to use the COVID-19 as an opportunity to catch up on deferred maintenance, meaning that Q1 aftermarket revenues will remain strong. That said, we obviously expect a very big slowdown in revenue in the near future with the market slowly picking back up as panic in the public hopefully dissipates and air traffic picks back up similar to what we are seeing in China.

Finally, we also note that a liquidity crisis could prove quite important for the industry if a recession hits. Potential M&A opportunities may emerge in the market as liquidity pressures affect smaller aerospace suppliers.

Source: Bloomberg

TMT

2020 COVID-19 SPECIAL REPORT

Miller Cressman
Jared Gaffe
Frédéric Lam
Marc Latif
Shelly Qian

TMT
IT HOLDINGS PROVE RESILIENT

SECTOR OVERVIEW AND UPDATE

As of March 13th, in Information Technology, our fund returned 3.4% YTD while the benchmark returned (3.5%). Communication Services returned (10.4%) while the benchmark returned (8.1%). Adobe has returned 8.5% YTD, Facebook returned (11.5%), BlackBerry returned (27.9%), Prosus returned (14.2%), and Teladoc returned 49.5% YTD before we sold it on March 2nd.

The Technology sector can be broken down into hardware and software. Hardware companies have been impacted the most recently due to issues stemming from both the supply and demand shocks. Manufacturing is impacted because of factories being shut down in China, causing a complete slowdown in products getting to end consumers. The over-dependence on China was fully apparent in the past weeks. Most companies do not have alternative means of production and will be seeing shortages of their products. On the demand side, a large portion of these companies depend on China for their growth as they have been the largest growing market for many technology companies. Some of the companies that were impacted the most were Apple and Microsoft, which both saw share price depreciation of over 18%. The market has recently become somewhat optimistic on the supply side as signs seem to show levels of COVID-19 subsiding in China, and factories beginning to re-open. The drops in share price seem to represent the drop in business that will be seen due to China. If the virus continues to worsen, the problem will worsen significantly. Seeing that factories have begun to open is important for hardware companies as they were nearing close to no inventory. If the virus worsens, they will see a significant effect from product shortages which will significantly impact the sector.

For software companies, seeing that the supply is not dependent on China, the effect on the share price has been based on demand. Software companies have been impacted more substantially than hardware as they are more dependent on disposable income and cash burn. IBM is down 24% and Oracle is currently down 20%. If COVID-19 were to continue to spread, it would put more pressure on technology companies as many of their expenses are sunk and they depend on extensive amounts of sales to make up for the high costs of production. The software companies that are most at risk are those that do depend on disposable income. Certain ones like video game producers will see a large decrease in sales in a worsened environment. Certain companies that make products for businesses will see less of an impact, like video security or communication services companies, as businesses are dependent on them and not willing to give them up.

For media, the major outstanding risk is decreased advertising spend from companies feeling economic pressure and current market volatility. Media companies have a majority of their revenue stemming from advertisements, and as the economic environment worsens, the first expense to be cut is usually marketing. The companies most at risk are those that do not generate high return per advertising dollar for their customers, as these are the first ones that will be dropped. Certain media companies could benefit from this crisis, particularly those that generate high return per dollar of advertising which might increase their market share in this environment. If COVID-19 were to continue, it would cause continued pressure on many different sectors, further putting pressure on their advertisement spending. This in effect will put even more pressure on the media companies.

Source: Bloomberg, Capital IQ, Company Filings

TMT
IT HOLDINGS PROVE RESILIENT

For Telecommunications, returns have been much more stable in comparison to technology and media, as usual. Looking at the IYZ US Telecommunications ETF, it is currently trading at $26.49, down 14% from its high of $30.79. This industry is much more stable and recession-proof than the other two sectors, as most of its revenue is not cyclical and does well in recession cases. If COVID-19 were to continue, there would be similar impacts felt again, but less significant compared to the other sectors.

HOLDINGS REVIEW

Adobe is a software company that focuses on Digital Media and Marketing, and is known for products such as Photoshop and Acrobat. We initiated a position in Adobe due to its entry into Martech as an industry leader via its acquisitions of Marketo and Magento, due to its quasi-monopolies in certain segments that would make it resilient in a recession, and due to certain cross-selling opportunities. During this difficult period, the second thesis has really begun to materialize. Adobe has been quite resilient since the outbreak of COVID-19. In terms of YTD returns, Adobe has returned 8.5%, compared to (3.5%) for our Information Technology benchmark. In Adobe's Q1 2020 earnings call on March 12, the company reported record revenues, and beat analysts' estimates for both revenue and EPS. This is in part due to the fact that Adobe's revenue is relatively predictable due to its subscription-based business model. The company has seen little impact so far in terms of demand, but acknowledges that some enterprises will delay bookings, postpone services, and reduce marketing expenses, and provided Q2 guidance that accounted for this. Overall, we believe that Adobe's quasi-monopolies and its defensive abilities in downturns may prove to be valuable as this bear market and crisis endure, and will continue to hold the position.

Teladoc Health Inc. is a telehealth company that provides telephone and videoconferencing technology to provide on-demand remote medical care via mobile devices, the internet, video and phone. It is currently the largest telehealth company in the world with operations in 120 countries and 22 million registered clients. We initiated our position in Teladoc due to our bullish views on the telehealth industry, the company's position as a market leader, and a potential misunderstanding of the regulatory environment on utilization rates. We recently sold our position in Teladoc, capitalizing on a 92% return on the stock since initiating our position. Overall, the company has returned 49.5% YTD and was the fund's best performer in 2020 before we exited our position. Since this exit, the company's returns have been relatively stagnant, and we believe that we sold it at a time when retail investors had driven the price too far up following positive Q4 2019 earnings results on February 26th. The company's stock price rose almost 16% on the day following earnings, and we felt as though our thesis about the market's understanding of the potential TAM of telehealth had finally materialized, and the COVID-19 crisis had demonstrated the importance and potential of telehealth services going forward.

Source: Bloomberg, Capital IQ, Company Filings

FIXED INCOME

2020 COVID-19 SPECIAL REPORT

Stanislav Timoshenko
Benjamin Caron
Lauren Kirigin
Ekaterina Semenova
Sisi Wang

Performance Summary
Fixed Income Fund

2020 YTD in Review

Dear Investors,

The Fixed Income Fund has been in the process of reallocating capital to match the fund's duration with that of the benchmark. This was done by focusing on fundamental analysis and single corporate security selection. The strategy resulted in favourable returns YTD, despite the recent volatility and general uncertainty surrounding global performance of both equity and bond markets. The fund returned 4.0% YTD compared to 4.3% return of our benchmark. These results are a combination of multiple factors that impact our performance: duration, credit selection, currency exposure, sector exposure, and performance of specific corporate bonds. Relevant information regarding the fund positioning can be found below. The Fixed Income Fund's performance was positively impacted by the long duration of the portfolio as well as the defensive nature of our corporate holdings.

Fixed Income analysts focused on maintaining a defensive position for the year as the team witnessed an increasingly worrisome global situation; a 25bps rate cut was anticipated to be seen in 2020. Nevertheless, the situation has significantly worsened as the number of individuals infected with COVID-19 has spiked worldwide. Following this development, the WHO has labeled the spread of the disease a pandemic and urged individuals to self-isolate. As professionals started to question future economic growth, the Fed responded with a 50 bps rate cut, surprising many on the downside. Following this decision, in addition to Trump's announcement to restrict travel with the EU, and WTI's 39% price crash, bond markets saw an alarming spread expansion. Option-adjusted spreads reached the level of yields seen in 2016. For instance, S&P Canada IG Corporate Bond Index expanded 59bps m/m while the HY Bond Index expanded 127bps m/m. S&P US IG Corporate Bond Index expanded 84bps and the US HY Bond Index expanded 199bps. The Fixed Income Fund believes this reaction is justified due to the fact that both oil price, COVID-19, and travel uncertainty has a potential to have a real economic impact on many layers of the globally integrated US and Canadian economies. The fund was able to generate positive returns due to the fact that the corporate holdings' spreads expanded by a lesser amount relative to corporate debt securities contained in the fund's benchmark. More information regarding the holdings is to follow.

FIXED INCOME METRICS SINCE INCEPTION	Fixed Income Fund	Benchmark
Annualized Return	4.6%	3.1%
Annualized Std Dev	4.8%	5.5%
Annualized Sharpe Ratio	0.46	0.14
Beta	0.54	
Annualized Alpha	1.8%	
Tracking Error	0.6%	

Performance metrics are calculated gross of fees.

FIXED INCOME PERFORMANCE METRICS 2020	Fixed Income Fund	Benchmark
Return	4.0%	4.3%
Standard Deviation	7.3%	9.9%
Sharpe Ratio	0.22	0.20
Beta	0.66	
Alpha	0.9%	
Tracking Error	0.6%	

Performance metrics are calculated gross of fees.

FIXED INCOME FUND RETURNS			As of Mar 14, 2020
Time Period	Gross Return	Net Return	Benchmark
YTD Return	4.0%	3.9%	4.3%
Mar-20	(0.4%)	(0.4%)	(0.4%)
Feb-20	1.5%	1.5%	2.4%
Jan-20	2.9%	2.9%	2.3%
Since Inception*	4.6%	4.0%	3.1%

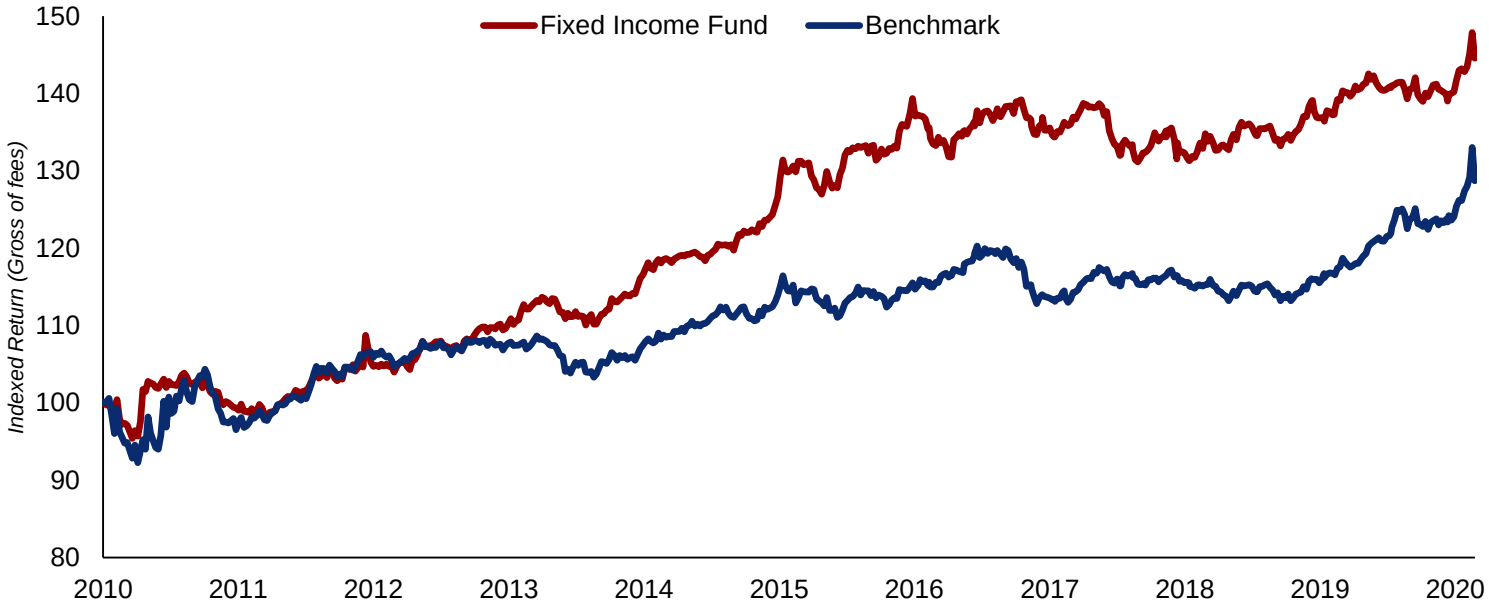
**Returns are annualized.*

Source: Bloomberg

Performance Summary

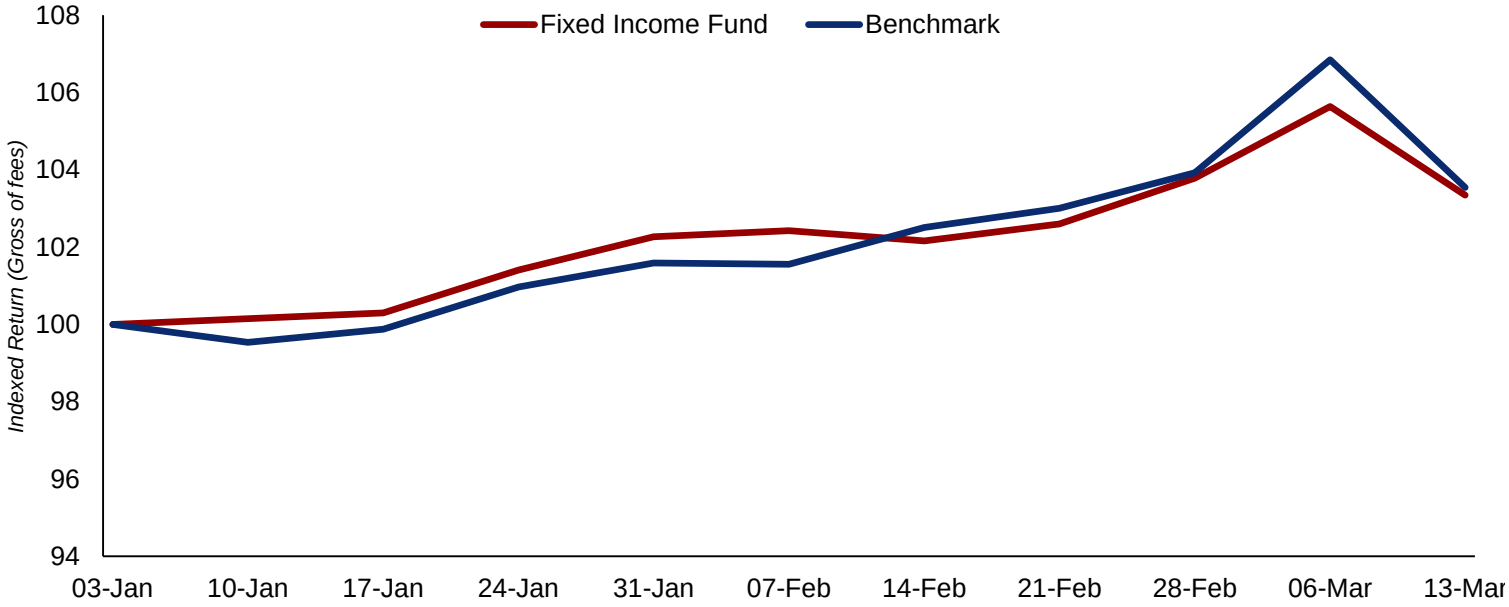
Fixed Income Fund

Figure 1: Fixed Income Fund Performance Since Inception



Note: Performance is calculated gross of fees. Benchmark is a blended 45% DEX Universe Bond Index, 45% Barclays Aggregate Index, 10% Citi/S&P

Figure 2: Fixed Income Fund Performance YTD



Note: Performance is calculated gross of fees. Benchmark is a blended 45% DEX Universe Bond Index, 45% Barclays Aggregate Index, 10% Citi/S&P

Source: Bloomberg

Performance Summary

Fixed Income Fund

Figure 3: Fixed Income Fund Credit Rating Exposure

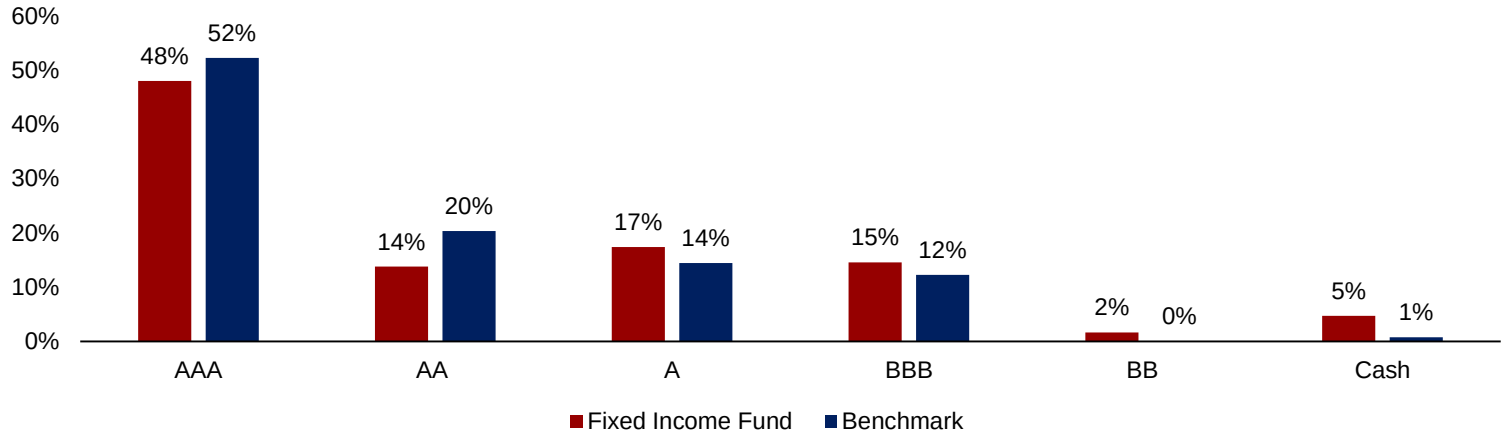
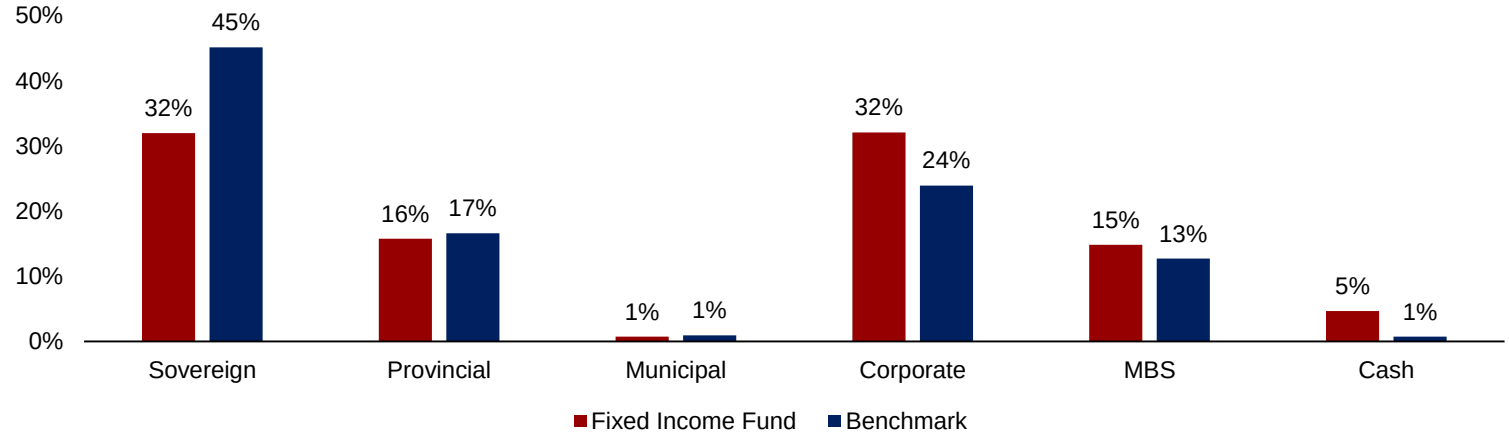
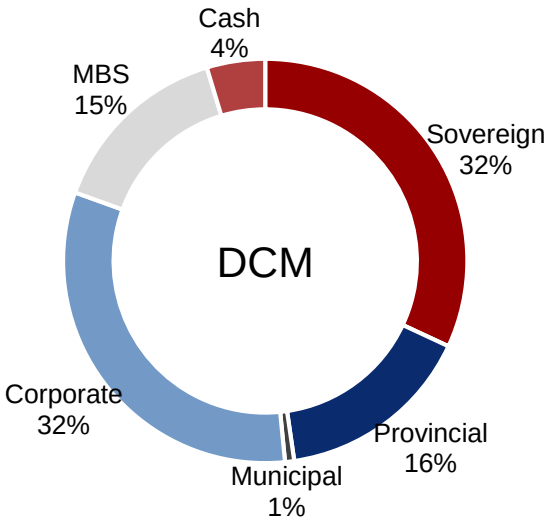
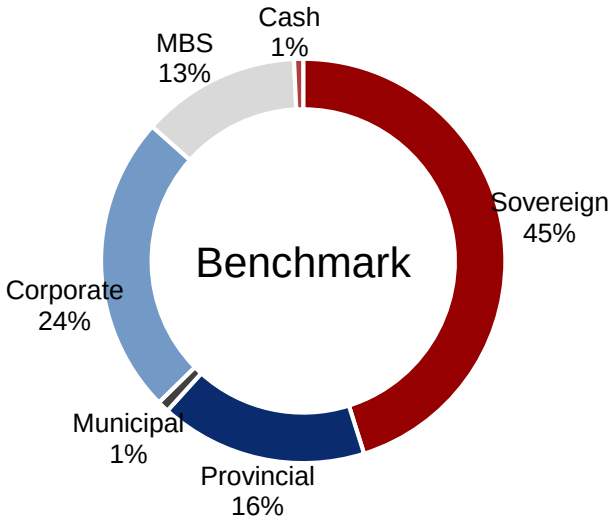


Figure 4: Fixed Income Fund Sector Exposure







Source: Bloomberg

Performance Summary

Fixed Income Fund

Figure 5: Fund Duration Positioning

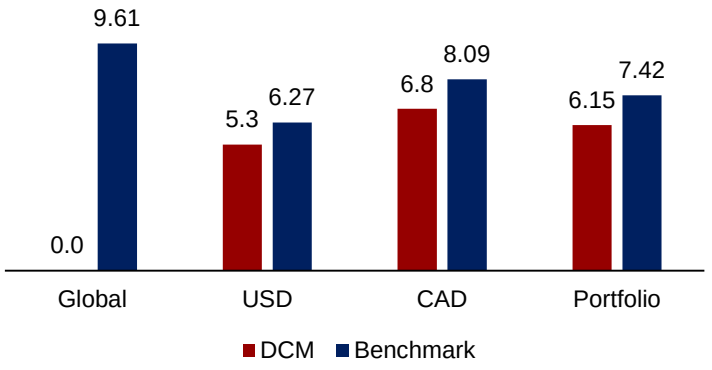


Figure 6: Fund Currency Allocation

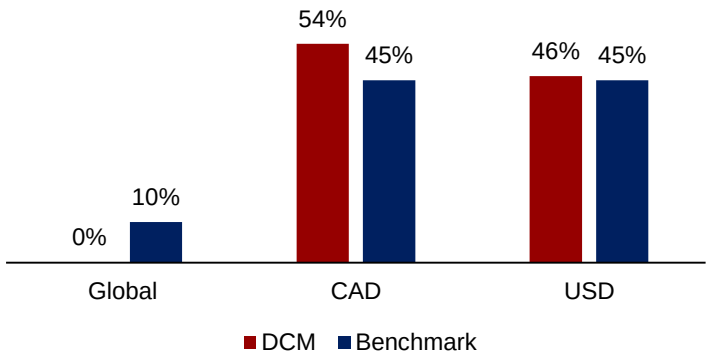


Figure 7: Fixed Income Fund Holdings

Fixed Income Fund Holdings (as at March 12, 2020)												
#	Security Name			Currency	Duration	Rating	Units	Local Price	Local Value	Base Value	%
Bonds & ETFs											
1	Province of Alberta Canada	2.550%	2022	CAD	2.64	A+	40,000	104.59	41,834	41,834	3%
2	Cogeco Communications Inc	4.925%	2022	CAD	1.83	BBB-	22,000	106.58	23,448	23,448	2%
3	Dollarama Inc	2.337%	2021	CAD	1.32	BBB	23,000	100.92	23,211	23,211	2%
4	407 International Inc	2.470%	2022	CAD	2.40	BBB	20,000	102.11	20,421	20,421	1%
5	Greater Toronto Airports Authority	7.050%	2030	CAD	7.76	A+	60,000	145.54	87,322	87,322	6%
6	Russel Metals Inc	6.000%	2022	CAD	1.89	BB-	25,000	100.50	25,125	25,125	2%
7	SmartCentres Real Estate Investment Trust	3.834%	2027	CAD	6.70	BBB+	20,000	107.20	21,441	21,441	1%
8	iShares Core Canadian Long Term Bond Index ETF			CAD	15.78		750	27.20	20,400	20,400	1%
9	iShares Core CanadianUniverse Bond Index ETF			CAD	8.30		15,300	32.99	504,747	504,747	33%
10	iShares Core U.S. Aggregate Bond ETF			USD	6.11		3,520	114.72	403,814	555,184	37%
11	iShares MBS ETF			USD	3.66		470	108.72	51,098	70,253	5%
12	iShares Short Treasury Bond ETF			USD	0.38		200	110.90	22,180	30,494	2%
13	Schwab Short-Term U.S. Treasury ETF			USD	1.88		510	51.38	26,204	36,026	2%
Cash											
14	USD			USD					5,307	7,297	0%
15	CAD			CAD					52,034	52,034	3%
							Total			1,519,238	100%

Source: Bloomberg

FIXED INCOME
A ROLLER COASTER RIDE

ENDLESS AND UNPREDICTABLE

A significant concern for the fund is the overall level of corporate debt in the US. The level of non-financial corporate liabilities is quoted by FRED to be at its highest level at 10.1 trillion USD; 83% higher than in 2000 implying a 17.6% increase y/y. Average Net Debt to EBITDA is at 4.3x, a level comparable to pre-2008/9 crisis. Average interest coverage ratio of 3.2x appears to be less concerning due to the fact that rates have been at their historical low. Hence, all interest coverage ratios seem better than in pre-2009. Nevertheless, this level still appears to be problematic given that average IOR for the period from 1970 to 2017 is equal to 3.7x. As a result, if the situation with COVID-19 worsens and we witness border closure between the US and Canada, it would be reasonable to expect deterioration in the credit metrics, possible default of highly levered companies and further spread expansion of corporate debt securities. To prevent this situation, strict measures need to be put in place by the American and Canadian governments and central banks.

Figure 1: S&P Canada Corporate - OAS

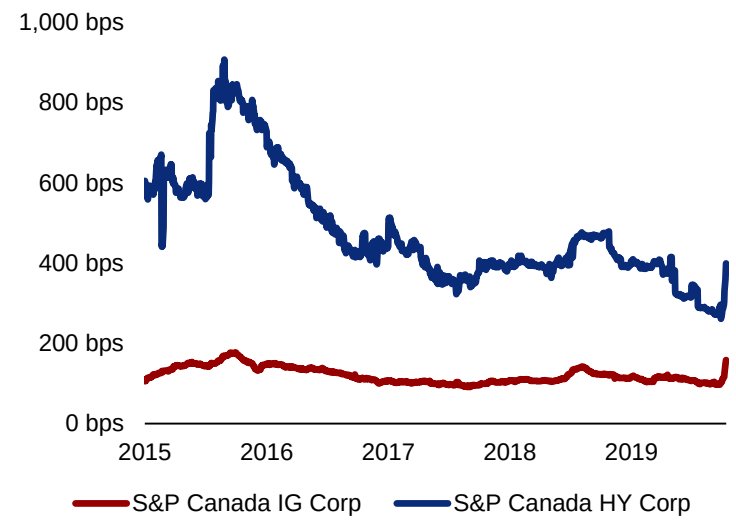


Figure 2: S&P US Corporate - OAS

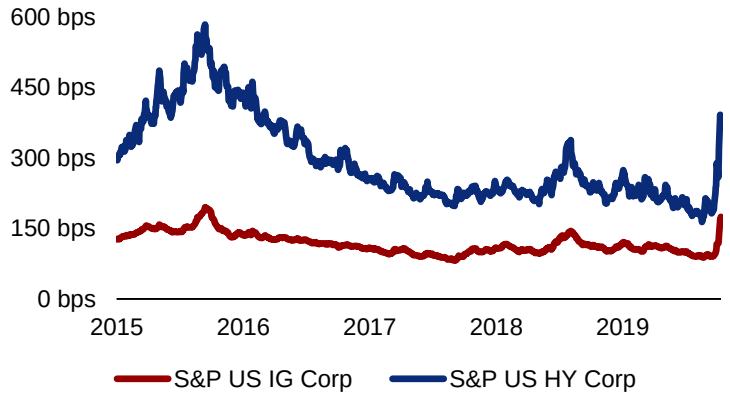


Figure 3: Average Debt Metrics

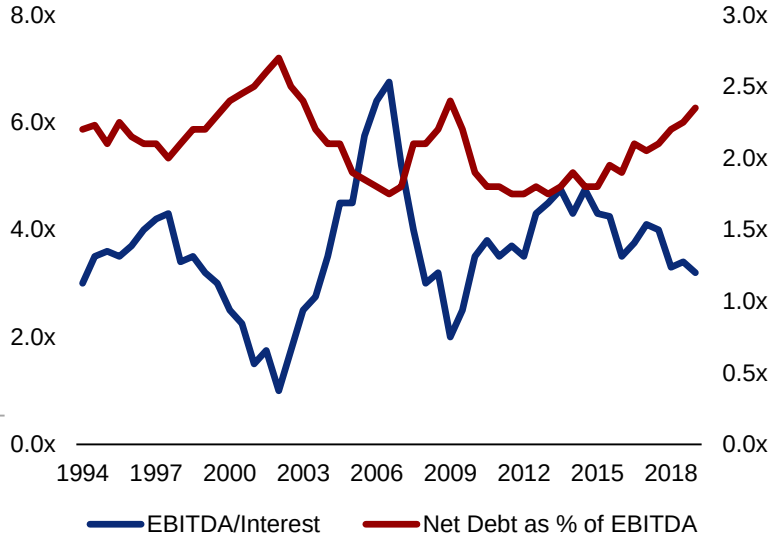
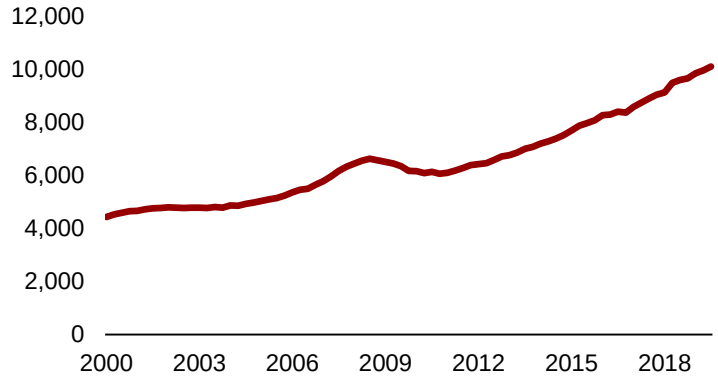


Figure 4: Average Corporate Debt (in USD bn)

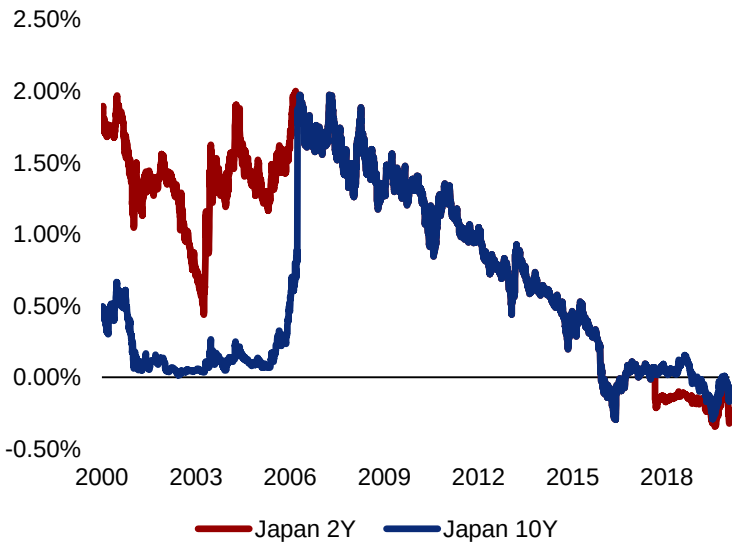


Source: Bloomberg

FIXED INCOME
A ROLLER COASTER RIDE

As of March 13, 2020, the market was pricing in a 68% probability of rates reaching 0-25bps level at the next Fed meeting on March 18th. As we saw earlier this evening, the Fed didn't wait, and lowered rates to 0%. Given the 39% drop in WTI and an increasing number of infected in the US, this outcome is not surprising. Any disruption to the flow of goods and interaction of individuals across the borders can be a catalyst to a recession. In such scenario, it would be expected to see central banks' attempt to manage inflation by lowering rates even further or engaging in quantitative easing. Of course, we have seen rates go negative in many parts of the world, and that is certainly a possibility in the YS as well.

Figure 5: Japanese Historical Yields

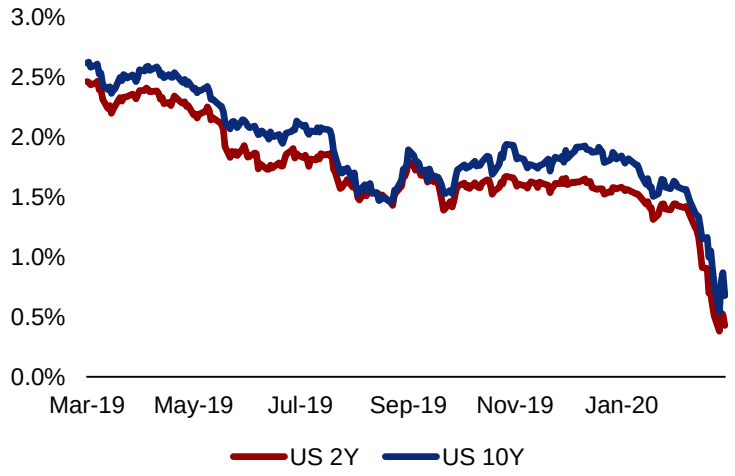


With US long-term yields at record lows, fixed income investors, including ourselves, are wondering if they should reduce exposure to these expensive bonds. But lowering duration may not be the right strategy. As we've seen in Japan, for example, yields can get even lower (Figure 5).

Instead of investing in a 10-year US bonds, one could invest in 1-year bonds, and rollover the position for 10 years. In this case, one would have to compare the 10-year yield to the average expected 1-year yield over the next 10 years. Based on the economic outlook ahead, it looks like policy rates will likely stay quite low for long, and we would not be surprised if short-term yields turned negative. Thus, overall we are not planning to deviate significantly from our benchmark duration.

One important risk factor to consider, however, is the risk of changing long-term inflation expectations, which could quickly push long-term yields back up. This can happen, if, for example, the market believes that the Fed will have to print enormous amounts of money to stimulate the economy out of this crisis/recession. Note, however, that the last time the Fed printed ~$3tr to fight the 2008 crisis, inflation remained, somewhat surprisingly, rather subdued over the next 10 years. Whether the same would happen this time around is an important question that we are currently analyzing.

Figure 6: US Historical Yields

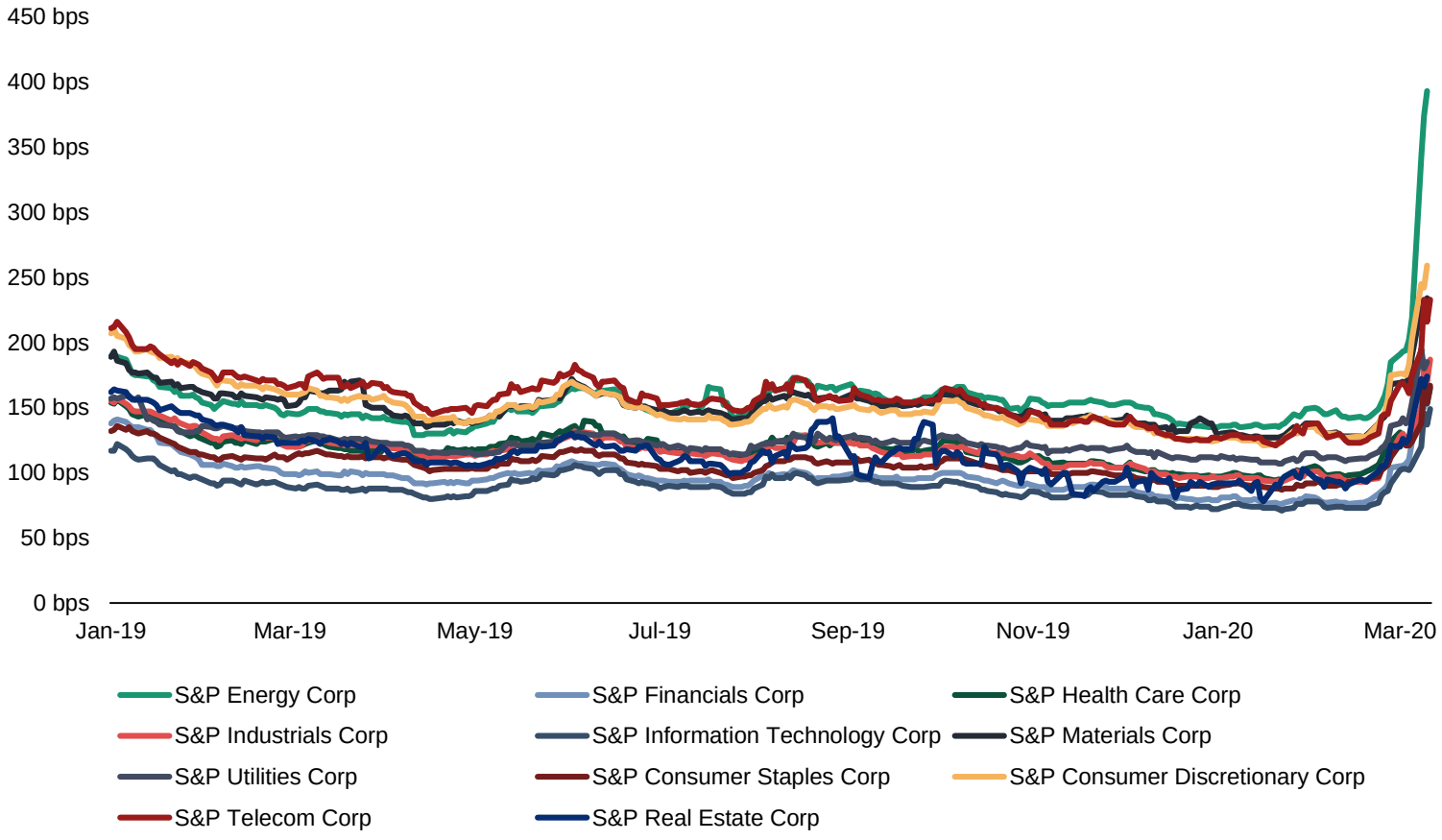


Source: Bloomberg

FIXED INCOME
A ROLLER COASTER RIDE

Given the crash in oil prices, it is not surprising that the Energy sector saw the highest spread expansion (+248bps) across all sectors (Figure 8). Although spreads have expanded across the board, we would not be surprised to see even further expansion given the severity of the current crisis and the risks to a serious and long recession. Going forward, we will continued with a very conservative approach, which has served us well this past year.

Figure 8: US Industry Sectors - Corporate Bond OAS



Source: Bloomberg

Fixed Income Fund

HOLDINGS PERFORMANCE AND OUTLOOK

COVID-19 in Review

The fund was able to generate positive returns YTD given that selected corporate holdings' spreads expanded by a lesser amount relative to corporate debt securities contained in the fund's benchmark. However, we realize the importance in evaluating the impact of COVID-19 and current macroeconomic conditions on the fund's holdings.

As a reminder, GTAA operates Toronto Lester B. Pearson international Airport via a 60-year ground lease from Her Majesty the Queen. The rationale behind this investment was to capitalize on favourable industry trends, namely local population growth and a rise in international middle class, as well as the strong economic moat formed by multiple geographic exposure and route demand elasticity. Recently, the evolving impact of COVID-19 has forced airlines to respond to changing circumstances. GTAAIR 7.05% 2030 has seen a 50bps spread expansion to 146bps since the virus has gained international recognition. Air Canada has temporarily suspended flights to Beijing and Shanghai until April 30 and those to Hong Kong until May 30. Non-stop Toronto-Seoul flights are suspended until May 31 and flights to Italy have ceased until May 1. China and Italy are among the 1st quartile of destinations per flight route frequency from Toronto Pearson. While other routes are still operating normally, lower passenger volume, caused by reduction of non-essential travel, is to impact commercial revenues. Revenue is expected to be adjusted downward given the federal government's recent recommendation to avoid all non-essential international travel. Although significant in impact, no default is expected given the leniency of associated covenants requiring revenues to be 1.25x annual debt service payments.

Next, 407 International Inc. is responsible for operating, maintaining, expanding and managing Highway 407 under a concession agreement scheduled to expire in 2098. Investment in this fixed income security was driven by high predictability of cash flows given trip length, quality and toll rates as well as a strong economic moat from continued ability to finance route expansion projects with operating cash flows. In the current climate, ETRHWY 2.47% 2022 has seen a 26bp spread expansion. This is largely attributable to the perceived decrease in volume on the toll route. Dependent on commuter traffic of the Greater Toronto Area, the CDC's recommendations to avoid large crowds and substitute in-person meetings for video conferencing when at all possible has reduced individual travel to and from the workplace. If COVID-19 advances to the stage that all movement of individuals is halted through self-quarantine, generated revenues are expected to be starkly reduced. In the event of a potential default, the government of Canada has a strong incentive to support the project's recovery due to its nature and investors as the Grantor may cure the Concessionaire Default per the indenture. As such, the risk associated to changing economic activity is priced in by investors.

Additionally, SmartCentres Real Estate Investment Trust is a Canadian real estate provider that manages approximately $9.5 billion of investment properties spanning across 34.1 million square feet. The Trust had seen spread compression of 47.47bp since DCM's position was initiated as of 4Q2019. However, recently OAS has demonstrated a spread expansion of 50bp. Amid heightening COVID-19 fears, retail volume is reducing in stores as inventories are quickly

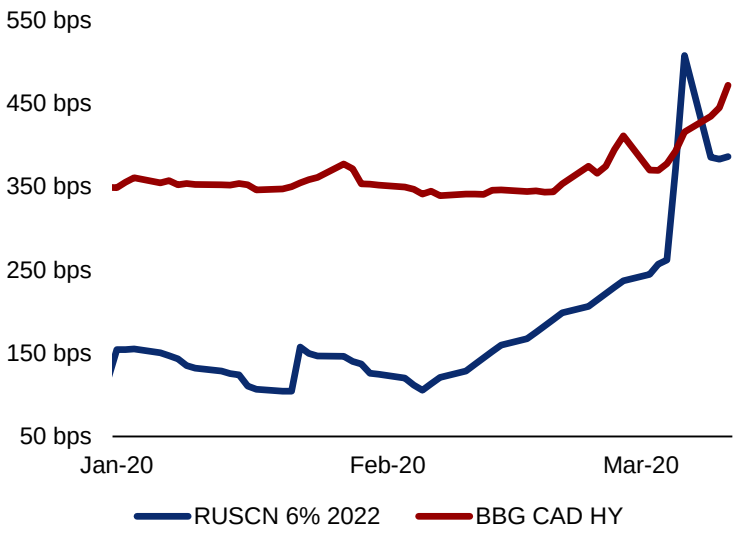
Fixed Income Fund

HOLDINGS PERFORMANCE AND OUTLOOK

purchased in single, large hauls for stockpiling shopping patterns and associated panic purchasing. If public fear remains present, we do expect future store traffic to drop for the time being. However, given the contract nature with lessees, paired with a diversified portfolio into retirement centers and individual developments, revenues are not expected to take a significant hit if recovery is expected during 3Q 2020.

Finally, Russel Metals is a metal distribution and processing company located in Mississauga, ON. It is one of the largest distributors of metals in North America. It carries three distinct segments: metals service centers, energy products and steel distributors. Their customers are mainly from manufacturing, oil and gas, and construction industries. Although initial investment was driven by favourable industry trends, flexibility provided through low operating leverage and the nature of international trade partners, depressed oil prices will represent a major headwind for Russel. Declining count of active rigs and stalled rig exploration will undeniably reduce demand for products in their energy segment that represents roughly 42% of their EBIT mix, 7% more than in 2008 due to few acquisitions in that segment. Management has reiterated their capability in adjusting their business mix, and is inclined to put more efforts in their metal service centers in attempt to mitigate this risk factor. Steel prices have stabilized at around $580/ton. Nevertheless, we expect downward pressures on steel prices due to disruption in global demand and supply chains arising from the coronavirus outbreak, alongside lower Chinese steel prices.

Having two distinct business units, one in the U.S. and one in Canada, the company profited from higher steel



prices set by the market during the Trade War because of the tariffs. This catalyst has played out really well during the past year as the company reported quarterly results exceeding those of the pre-recessionary environment of 2008.

At this point, we would expect the company to call this specific tranche of debt next month, on April 13th, in order to refinance it. Although, it is hard to believe that such offering will sell smoothly in the market based on the state of the global economy with the overhang of the coronavirus outbreak.

On a positive note, Russel is still expected to profit from ongoing construction projects in Canada and the U.S. in the near future, providing stable cash flows through their metal service centers. We will continue to monitor closely our position in Russel and for the time being are confident in our decision to hold our position.

Although exposed to COVID-19 and travel, risk is controlled via the nature of our 407 ETRHWY, GTAAIR, SmartCentres and Russel Metals holdings.

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