Sionna Canadian Balanced Fund

Fund Commentary

The S&P/TSX Composite Index was down 4.5% this quarter on a total return basis.

While the majority of sectors negatively contributed to the Composite's performance this quarter, energy and financials had the most notable impact.

During the quarter, the Sionna Canadian Balanced Fund underperformed its custom benchmark (45% S&P/TSX Composite Index, 30% FTSE TMX Canada Universe Bond Index and 25% MSCI World Index).

Positive Contributors

The Fund's position in Empire Company Limited (Empire) contributed positively to performance. Management continues to work through the company's operational challenges and is seeing improvements across the business. Sionna believes Empire is taking the right steps to fix its cost structure and the stock remains an attractive investment for the long term.

Sionna's lack of exposure to Enbridge positively contributed to performance this quarter. Enbridge is one of the largest energy infrastructure companies in North America with a prominent footprint in the pipeline business. Pipelines in general were weak this quarter, along with other interest-sensitive sectors as rising rates have become a worry for investors. The company itself has faced some challenges as it determines the appropriate capital structure to fund its large capital expenditure plan, while still growing its dividend. Enbridge has strong assets that have allowed it to generate solid operating cash flow over the long term; however, Sionna believes that there are more attractive opportunities in the energy sector.

CGI Group (CGI) also contributed positively to performance this quarter. CGI is one of the largest IT services companies in the world, providing technology-related consulting and services for large corporations and government agencies. The business is positioned to benefit from the ongoing trend towards digitization, cybersecurity, analytics and modern IT infrastructure. Corporations are increasingly turning to experts like CGI to help save on costs and improve revenues. The CGI management team consists of world-class operators, who are well aligned with shareholders and have a multi-decade track record of creating value.

Performance Detractors

The fund's position in PrairieSky Royalty (PrairieSky) contributed negatively to performance this quarter. PrairieSky is the largest independent owner of freehold land in Canada and earns fees by leasing the rights to produce oil and gas on its lands to energy companies. PrairieSky's land position provides a strong competitive advantage and the royalty business is extremely attractive because the company has none of the capital or operating expenses of a producer. Drilling activity in Western Canada has been weak during the energy downturn; however, the company has been able to prudently grow by adding new land positions and royalty streams, while maintaining a strong financial position.

The fund's position in Imperial Oil Ltd. also contributed negatively to performance this quarter. Oil prices were volatile this quarter, resulting in stock price movements that were not reflective of the underlying value of Imperial Oil's business. Sionna continues to be impressed with the company's financial strength and ability to generate cash flow. As Imperial Oil's expected capital expenditure

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requirements decline over the next few years, Sionna believes that the company will likely return capital to shareholders through increased dividends and share buybacks.

IGM Financial (IGM) negatively contributed to performance this quarter. The company is one of Canada's largest independent mutual fund companies and has a long history of consistent earnings and cash flows. In recent years, management has been focused on improving the performance of its Mackenzie Financial division, which has struggled for some time. IGM continues to maintain a strong financial position and has competitive strengths that support the resiliency of the business.

Select Buy & Sell Activity

During the quarter, Sionna added Royal Bank of Canada (Royal) to the portfolio. Royal is the largest bank in Canada by assets and is the dominant wealth manager in the country. The company operates in a mature oligopoly with high barriers to entry. Royal is the market leader in Canada and benefits from economies of scale. The company has a history of consistently high and above average returns and the management team is mindful of the risks present at this stage in the credit cycle. For the past few years, Sionna has maintained exposure to the Canadian banks primarily through three holdings: Bank of Nova Scotia, Toronto-Dominion Bank and Canadian Western Bank. Sionna has been trimming their position in Canadian Western Bank and switching that capital into Royal Bank, which they believe offers a more attractive risk/reward trade-off at this time. The shares are also trading below Sionna's estimate of its intrinsic value.

Current Positioning

Sionna doesn't know if many consider financial markets to be cool, but apparently they're susceptible to inversion. Such was the case this quarter when investors reacted to positive economic news as if it was bad. In February, the U.S. added jobs at the fastest pace in a year and a half, surpassing forecasts by a wide margin. Wage growth was strong and the unemployment rate remained at 4.1% – a 17-year low. This is all very good news; and the market reacted negatively.

Ironically, the seemingly good economic news caused the market to worry about inflation. The belief was that a tighter job market will increase wages, leading to higher spending by individuals and companies, eventually translating to inflation. An inflation uptick could prompt the Federal Reserve to increase the pace of interest rate hikes. When the Federal Reserve officials met last December, three rate hikes were forecasted for 2018. Given the positive economic data since, there are rumblings that the interest rate may now increase four times this year. Since asset values are theoretically inversely related to interest rates, markets dipped.

However, inflation in Canada has been low and stable in recent years. Inflation only averaged 1.6% last year, compared to 2.1% in the U.S. Canadian investors may also have been concerned about rising trade tensions this quarter. For example, the U.S. proposed to introduce tariffs on steel and aluminum imports (16% of the imported steel in the U.S. comes from Canada). However, Canada was later exempted from these tariffs.

When markets wobble, Sionna sees opportunities. At the beginning of the quarter, the S&P/TSX's price-to-earnings ratio was close to 17 times, a level that was above the historical average. The ratio is now below 15 times and Sionna is starting to see more opportunities emerge as a result.

High and unpredictable inflation would be bad for the market, but losing sleep over it at this point is premature. First, the average inflation in Canada and the U.S. over the past five years were both below the 2% targeted rate. It was not too long ago that the market was worried about

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an era of "stagnation" in which growth, inflation and interest rates would stay permanently low. Second, research by JP Morgan and Scotiabank both concluded that increasing interest rates in a low-rate environment is actually correlated with positive equity markets.

Lastly, maintaining low and stable inflation is a key policy goal for central banks. If the economy overheats, central banks have the latitude to raise rates and keep inflation in check.

The market was quick to flip from worrying about stagnation to worrying about inflation. Seemingly positive economic news was interpreted as negative economic news. This is dizzying, and why Sionna is not convinced that anyone can sustainably predict changes in macroeconomic variables, let alone their implications on stocks. Time and time again, Sionna concludes that the best way to protect and grow capital is to "tune out the noise" and "stick to our knitting." This means conducting bottom-up research and investing in solid companies with good management at a discount to Sionna's estimate of intrinsic value – an all-weather strategy that works. Sionna's consistency and independence can make them look contrarian at times.

About Sionna

Founded in 2002, Sionna is an independent, value investment firm with over 80 years of experience shared among its portfolio managers. Sionna believes that value investing is a craft. It takes discipline and patience and it is the foundation on which Sionna has grown. As an independent firm, Sionna runs its business with clients' best interests in mind and takes a long-term view with focus only on companies that it believes will help compound its clients' capital.

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Contribution Analysis (relative to benchmark)

LAST QUARTER

INDUSTRY

Top 5 Contributors	%	Top 5 Detractors	%
Metals & Mining	0.48	Capital Markets	-0.58
Food & Staples Retailing	0.37	Insurance	-0.33
IT Services	0.23	Paper & Forest Products	-0.25
Banks	0.22	Energy Equipment & Services	-0.24
Equity Real Estate Investment Trusts (REITs)	0.15	Multi-Utilities	-0.14

COMPANY

Top 5 Contributors	%	Top 5 Detractors	%
Empire Co. Ltd. Class A	0.30	PrairieSky Royalty Ltd	-0.58
CGI Group Inc. Class A	0.23	Imperial Oil Limited	-0.52
Royal Bank of Canada	0.17	ShawCor Ltd.	-0.29
Boardwalk REIT	0.12	IGM Financial Inc.	-0.27
Metro Inc.	0.08	CI Financial Corp.	-0.25

LAST 12 MONTHS

INDUSTRY

Top 5 Contributors	%	Top 5 Detractors	%
Oil Gas & Consumable Fuels	1.82	Energy Equipment & Services	-1.38
Food & Staples Retailing	1.67	Media	-1.36
Trading Companies & Distributors	0.89	Software	-0.34
Metals & Mining	0.83	Auto Components	-0.33
Capital Markets	0.59	Multi-Utilities	-0.29

COMPANY

Top 5 Contributors	%	Top 5 Detractors	%
Empire Co. Ltd. Class A	1.38	Aimia Inc.	-1.44
Finning International Inc.	0.94	ShawCor Ltd.	-1.43
Methanex Corporation	0.59	Imperial Oil Limited	-0.52
CGI Group Inc. Class A	0.40	Royal Bank of Canada	-0.39
CI Financial Corp.	0.34	ATCO Ltd. Class I	-0.32

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Quarterly Additions/Deletions

Additions	Deletions
Royal Bank of Canada	Agrium Inc

Sionna Investment Managers® on the BRIDGEHOUSE Independent Platform

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