

Round, Round, We Go

October 2019

Trooper's hit from the 1970s could be the theme song for the current political and economic state of affairs. On one side you have the US-China trade war, Trump Impeachment proceedings, BREXIT, a slowing German economy, the Federal election in Canada (honorable mention), low commodity prices, and slowing US industrial activity (see US-China trade war). On the other side, sits the S&P 500 Index at an all-time high, supported by the US consumer which is still in very good shape due to all-time low unemployment and, despite a recent drop (see US-China trade war), robust consumer sentiment.

The US-China trade war is the obvious elephant in the room and with a US election next fall, politics could have a significant influence on the global economy and capital markets. Against this backdrop, with equity indices at all-time highs and interest rates close to all-time lows, we tread cautiously, aware that a resolution of removing this proverbial elephant will trend towards two very different outcomes. An initial positive resolution of tariff removal / trade war truce could restore corporate and consumer confidence and maintain equity market strength with the caveat that interest rates will need to go higher! The opposite would be more tariffs and the continuation of deteriorating economic relations between the 2 largest economies in the world. A period of stagnant or declining economic conditions would likely ensue and with-it, rising risk premiums and lower stock market returns.

Fixed income markets enjoyed strong performance to the end of September in 2019. The US High Yield market¹ (4.4 year duration) is up 11.5 percent, for the first 3 quarters of the year, as credit spreads² narrowed 131 basis points to 402 basis points. This performance was also aided by the 89 basis point drop in the yield of the US 10 year Treasury bond to 1.79 percent through the end of September. In Canada the Investment Grade index³ was up 7.98 percent for the first 3 quarters of the year.

Series F of the Lysander-Fulcra Corporate Securities Fund (the "Fund") returned 0.89 percent after fees in the 3rd quarter and year to date 5.42 percent with an average duration of 1.5 years for the first 9 months of the year. Standard performance of Series F of the Fund, as of September 30, 2019, is 3.4% (1 year) and 5.0% (since inception [December 30, 2016]). Our increasing bias to keep the Fund's bond investments on a short leash (see pie chart) is to minimize potential interest rate volatility and keep dry powder available for mispricing's we suspect could be close at hand. We have conducted due diligence on several new companies through the summer and early fall whose bonds we would be excited to add to the portfolio given the right opportunity.

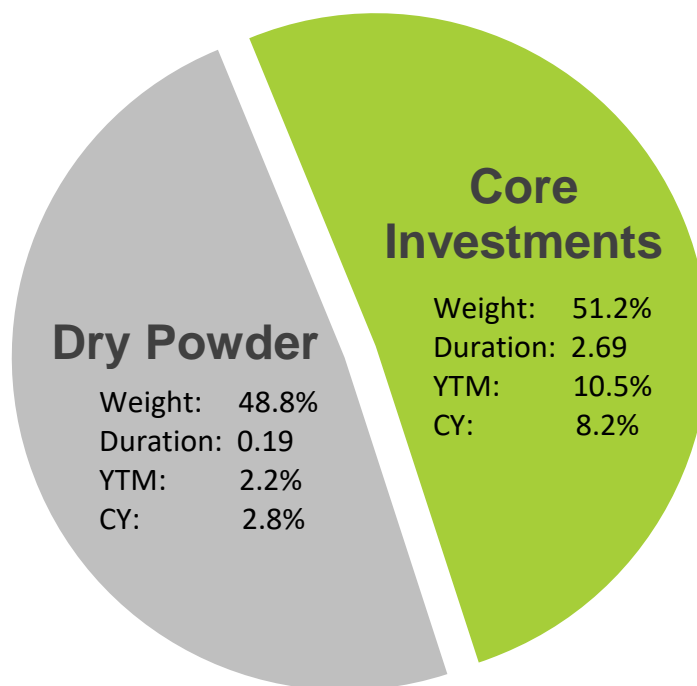
¹ ICE BofAML US High Yield Index

² Option Adjusted Spread

³ Bank of America Merrill Lynch Canada Corporate Index

Combined:

Duration: 1.5
 YTM: 6.7%
 CY: 5.7%



Dry Powder = Cash + Government Bonds + Short term IGs

Core Investments = HY Bonds + Converts + Prefs + Stocks

An integral part of the Fund's absolute return credit mandate is to avoid expensive/costly index mispricing's that can build up due to macro influences, such as a drop-in interest rates. Occasionally, however, these macro forces can create technical pricing discrepancies in the capital structures of companies which Fulcra looks to benefit.

US Bond / Loan mis-pricings

Over the last 5 years, as the global economy has long recovered from the 2008/2009 recession, loose financial standards in loan and bond structures have emerged. Some companies have been able to issue "secured" debt with 1st and 2nd lien's that act more like veils. These loans and bonds either don't possess covenants or have ones that are so weak that they leave the investor with little recourse if cash flow drops. While bonds can be purchased by a diverse set of investors (individual investors, mutual funds, hedge funds, and institutions) loans are primarily owned (over 50 percent) by Collateralized Loan Obligations (CLO's). CLO's are investment vehicles that invest in the loans of non-investment grade corporations. They primarily get their investment capital from institutional investors (i.e. pension funds etc...) and as a result the credit rating agencies are heavily involved in the monitoring of the credit risk of CLO's. Specifically, CLO's will have their overall credit risk measured by what is referred to as the Weighted Average Rating Factor (WARF). If the factor rises in value, it means the overall loan portfolio is getting too risky and the CLO manager will have to sell lower rated loans in the CLO portfolio.



Earlier this year loan prices were hit hard like most risk assets as a result of the broad market sell off in the 4th quarter of 2018. However, a recent drop in loan prices over the last several weeks has been driven by CLO's selling lower rated loans in order to reduce their overall WARF scores. This has resulted in driving the prices of some loans, where an issuer has pari-passu bonds outstanding, to prices where the loan is trading cheaper than its bond counterpart. The Fund currently owns the term loan of PetSmart which is due in March 11, 2022 and trades at a yield of 6.41 percent compared to the pari-passu bond that is due June 1, 2025 and trades at a yield of 5.86 percent.

While this nuanced structural behavior in the loan market is nothing like the vacuum loans traded into in late 2008 and 2009, even a minor adjustment of these institutional rigid structures can create selective investment opportunities for the sensible investor.

This document has been prepared jointly by Lysander Funds Limited ("Lysander") and Fulcra Asset Management Inc. ("Fulcra") and has been prepared solely for information purposes. Information in this document is not intended to constitute legal, tax, securities or investment advice and is made available on an "as is" basis. Lysander and Fulcra do not make any warranties or representations regarding the information herein. Information in this document is subject to change without notice. Lysander and Fulcra do not assume any duty to update any information herein. Certain information in this document has been derived or obtained from sources believed to be trustworthy and/or reliable. Lysander and Fulcra do not assume responsibility for the accuracy, currency, reliability or correctness of any such information. Nothing in this document should be considered a recommendation to buy, sell or short a particular security.

Lysander is the investment fund manager of Lysander-Fulcra Corporate Securities Fund (the "Fund").

Fulcra is the portfolio manager of the Fund.

In this document, "we", "us", and "our" means Fulcra.

Commissions, trailing commissions, management fees and expenses all may be associated with mutual fund investments. Please read the prospectus before investing. Investment funds are not guaranteed, their values change frequently and past performance may not be repeated. The indicated rates of return are the historical annual compounded total returns including changes in unit value and reinvestment of all distributions and does not take into account sales, redemption, distribution or optional charges or income taxes payable by any security holder that would have reduced returns. Historical fund returns provided herein for the Lysander-Fulcra Corporate Securities Fund are based on the net asset value of Series F, which pays a management fee of 0.85%. Different series may have different fees payable which may result in series of the same fund having different rates of returns.

This document may contain forward-looking statements. Statements concerning a Fund's or entity's objectives, goals, strategies, intentions, plans, beliefs, expectations and estimates, and the business, operations, financial performance and condition are forward looking statements. The words "believe", "expect", "anticipate", "estimate", "intend", "aims", "may", "will", "would" and similar expressions and the negative of such expressions are intended to identify forward-looking statements, although not all forward-looking statements contain these identifying words. These forward-looking statements are subject to various risks and uncertainties that could cause actual results to differ materially from current expectations. Readers are cautioned not to place undue reliance on these forward-looking statements. While Lysander and Fulcra consider these risks and uncertainties to be reasonable based on information currently available, they may prove to be incorrect.

Nothing in this presentation should be considered a recommendation to buy, sell or short a particular security. Any specific securities discussed are intended as an illustration of the portfolio manager's security selection process. The Fund may sell these securities at any time, or purchase securities that have previously been sold. The securities or short positions may increase or decrease in value after the date hereof, and the Fund may accordingly gain or lose money on the investment in the securities. The statements by the portfolio manager in their commentaries are intended to illustrate their approach in managing the Fund, and should not be relied upon for any other purpose.



Any unauthorized use or disclosure is prohibited. Nothing herein should in any way be deemed to alter the legal rights and obligations contained in agreements between any ICE Data Services entity ("ICE") and their clients relating to any of the Indices or products or services described herein. The information provided by ICE and contained herein is subject to change without notice and does not constitute any form of representation or undertaking. ICE and its affiliates make no warranties whatsoever either express or implied as to merchantability fitness for a particular purpose or any other matter in connection with the information provided. Without limiting the foregoing ICE and its affiliates makes no representation or warranty that any information provided hereunder are complete or free from errors omissions or defects. All information provided by ICE is owned by or licensed to ICE. ICE retains exclusive ownership of the ICE Indices including the ICE BofAML Indexes and the analytics used to create this analysis ICE may in its absolute discretion and without prior notice revise or terminate the ICE information Indices and analytics at any time. The information in this analysis is for internal use only and redistribution of this information to third parties is expressly prohibited.

Neither the analysis nor the information contained therein constitutes investment advice or an offer or an invitation to make an offer to buy or sell any securities or any options, futures or other derivatives related to such securities. The information and calculations contained in this analysis have been obtained from a variety of sources including those other than ICE and ICE does not guarantee their accuracy. Prior to relying on any ICE information and/or the execution of a security trade based upon such ICE information you are advised to consult with your broker or other financial representative to verify pricing information. There is no assurance that hypothetical results will be equal to actual performance under any market conditions. THE ICE INFORMATION IS PROVIDED TO THE USERS "AS IS." NEITHER ICE NOR ITS AFFILIATES NOR ANY THIRD PARTY DATA PROVIDER WILL BE LIABLE TO ANY USER OR ANYONE ELSE FOR ANY INTERRUPTION INACCURACY ERROR OR OMISSION REGARDLESS OF CAUSE IN THE ICE INFORMATION OR FOR ANY DAMAGES RESULTING THEREFROM. In no event shall ICE or any of its affiliates employees officers directors or agents of any such persons have any liability to any person or entity relating to or arising out of this information analysis or the indices contained herein.