Western Investment Club

ANNUAL REPORT

2019 / 2020

May 15th, 2020

www.westerninvestmentclub.ca

Our Mission: To build interest in capital markets among young investors at Western University and teach the fundamentals of investing.

THIS ANNUAL REPORT REPRESENTS A COLLECTIVE EFFORT FROM OUR TEAM TO PROVIDE TRANSPARENCY INTO THE FUND

This annual report is dedicated to all the former members
and alumni of the Western Investment Club.
Without your hard work WIC would not be possible.

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Produced by Maanit Patel & Jack Heinzl

See back for important disclosures

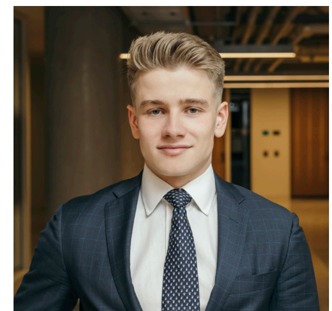
FUND MANAGERS' STATEMENT

Dear fellow members and alumni, as the 2019-2020 academic year wraps up, we are pleased to provide an update on the Club's progress. Since its inception in 1996, the fund has grown more than seven-fold. It has been yet another successful year as WIC continues to grow its influence on the finance community at Western University. We are very proud of what the analyst team has achieved this past year, the performance of the fund, as well as the development of our more than 650 general members.

As of April 30th, 2020, we are managing a fund of $200,000 in assets under management. Since April 30th, 2019, WIC's fund has depreciated 12.0%. Despite a year of ongoing political headwinds, trade tensions, an oil crisis and a global pandemic, the team was able to make 3 new investments and sell 8 previously held positions.

Maanit Patel
Fund Manager

Value investing strategies have continued to struggle through the post-financial crisis bull run and, unfortunately, this trend has not yet broken in the recent downturn. Keeping John Maynard Keynes' famed quote "markets can stay irrational longer than you can stay solvent," in mind, the club elected to dispose our largest positions displaying limited near-term catalysts and significant short-term risk toward the beginning of the academic year. This strategy allowed the club to explore ideas with high levels of conviction and maintain a disciplined approach to capital allocation.


Jack Heinzl
Fund Manager

The turn of the decade was quickly followed by an unprecedented global shutdown due to the COVID-19 pandemic that has affected the lives of billions. As the virus spread around the globe, economies began to shut down and governments enacted shelter-in-place orders, forcing many businesses to change their models overnight. Robert Farrell, one of the great sell-side analysts, once said: "Bear markets have three stages – sharp down, reflexive rebound and a drawn-out fundamental downtrend." In March 2020 the market dropped by roughly 30% due to the pandemic and the Russia-Saudi Arabia oil price war, followed by a quick rebound in April 2020 with the S&P 500 rising 18%. Despite markets in 2020 displaying an uncanny resemblance to Farrell's prognostication, as value investors, we must fight the urge to make predictions surrounding overall market behavior and instead focus on making bets on those investments which we feel carry a significant margin of safety.

Today's market volatility does not reflect any change in our approach to investing; in fact it represents an opportunity for capital deployment. Many investors fear volatility, however disciplined value investors invite volatility as it reveals market irrationality and creates attractive investment opportunities. With approximately a third of its fund held in cash, the club is well positioned to take advantage of market overreactions. Despite a wide array of both investment and speculative opportunities in the market today, the club will maintain a disciplined approach by making investments in businesses we believe have high underlying value.

Aside from the fund itself, our club membership has continued to grow thanks to all of your support. This year, our club reached 650+ dedicated members, making us one of the largest clubs at Western University. We hope the club continues to strive to create a strong community of bright, passionate, and young investors at Western.

Thank you to the analyst team for their hard work, the researchers for their dedication, the alumni for their continued support, and Western's endowment for their generous donation. As Fund Managers, we are very proud of the performance of the fund as well as the growth of our members. We are confident that WIC's future remains bright.

Sincerely,

Maanit Patel & Jack Heinzl

Fund Managers, 2019 / 2020

OUR ORGANIZATION

Our fund was officially created in 1996 with the generous donation of $25,000 from Mr. Cameron S. Marshman, in honour of his wife. Since then, we have managed it with a value investing philosophy. Mr. Marshman's wish was to educate and foster the next generation of investors at Western University by giving them a chance to invest real capital. Today, that donation has grown more than 700%.

FUND STRATEGY

WIC employs a bottom-up fundamental investing approach to every investment. Each idea begins with a screening process to find stocks that are trading below their intrinsic value. Our analysts then conduct an extensive research procedure to understand and evaluate the company. The process can sometimes take months for a single idea. WIC attempts to truly understand a company's valuation as well as the key drivers of its future growth potential before executing a trade. We believe that by conducting an exhaustive research process, we minimize the risk of unforeseen challenges.

For over 40 years, WIC has applied a disciplined approach to portfolio construction. Since all of our investments are high conviction ideas, we do not use beta diversification in our portfolio. However, we try to allocate capital evenly across our groups to find the best ideas within each industry. Lastly, each of our investments maintains a significant margin of safety to provide downside protection.

FIRMS REPRESENTED

SILVERLAKE

ARES

Qatalyst PARTNERS

EVERCORE

CREDIT SUISSE

Morgan Stanley

ALTAS | PARTNERS

Uber

650+

ACTIVE MEMBERS

6

INDUSTRY GROUPS

40+

YEARS OF HISTORY

2019 / 2020 TEAM

EXECUTIVE

Amir Khod
Co-President

Maanit Patel
Fund Manager

Saad Afroz
Co-President

Jack Heinzl
Fund Manager

ALUMNI ADVISORS

Charles Korn
FIG Advisor

Kevin Zhou
NR Advisor

David Zhang
TMT Advisor

Bowen Qian
IND Advisor

Feroz Qayyum
CRG Advisor

Jack Hansen
REHG Advisor

ADVISORY BOARD

Kevin Zhou
Advisor

Matthew Ting
Advisor

Harsh Naik
Advisor

Vinayak Modi
Advisor

Andrew Kim
Advisor

Sam Tammen
Advisor

CONSUMER RETAIL

Teimur Siddiqui
Head Analyst

Ryley Mehta
Head Analyst

Caitlyn Liu
Analyst

Harrion Thomas
Analyst

Sammy Fleisher
Junior Analyst

Peter Matthews
Junior Analyst

INDUSTRIALS

Aaser Sadek
Head Analyst

Aron San
Head Analyst

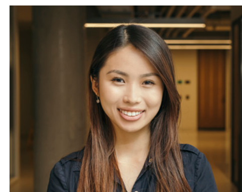
Harsh Shah
Analyst

Nick Tommasini
Analyst

Allen Cheng
Junior Analyst

TECH, MEDIA & TELECOM

Andrew Tan
Head Analyst


Jasmine Yang
Head Analyst

Brad Perez
Analyst

Roy Katznelson
Analyst

Jun Kim
Junior Analyst

Flora Sun
Junior Analyst

FINANCIAL INSTITUTIONS

Emma Juskovic
Head Analyst

Jim Zhou
Head Analyst

Shahryar Safdar
Analyst

Uv Sandhu
Analyst

Aly Dayani
Junior Analyst

NATURAL RESOURCES

Max Lai
Head Analyst

Peter Esposto
Head Analyst

Connor McSweeney
Analyst

Aryan Paliwal
Junior Analyst

Garrick Bracken
Junior Analyst

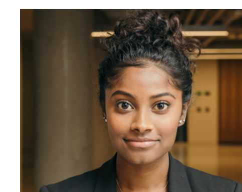
REAL ESTATE, HEALTHCARE & GAMING

Jack Henderson
Head Analyst

Melissa Shang
Head Analyst

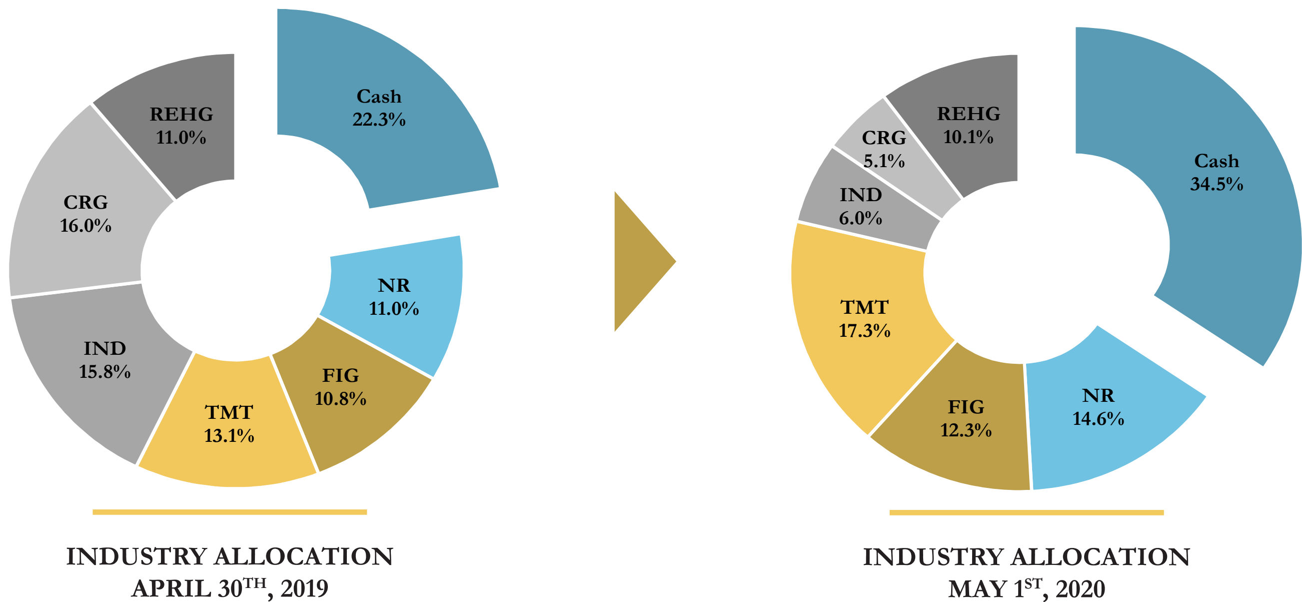
James Silva
Analyst

Liam Niznick
Analyst

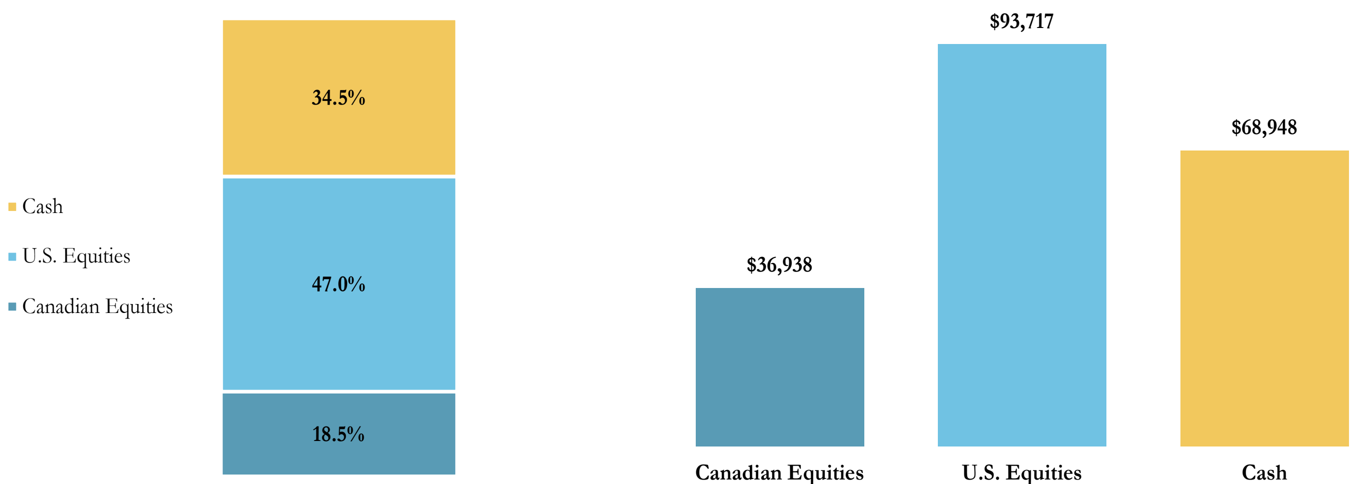

Kate San
Junior Analyst

Anthony Hua
Junior Analyst

PORTFOLIO
AT-A-GLANCE



Given elevated valuations across the board in equities, WIC elected to dispose of 8 holdings and make 3 new investments (2 investments in Natural Resources and 1 investment in Financial Institutions) through the 2019-2020 academic year. These disposals have left WIC significantly overweight in cash which the fund hopes to opportunistically deploy in the coming academic year as we view recent volatility brought on by COVID-19 as an opportunity for value investors.

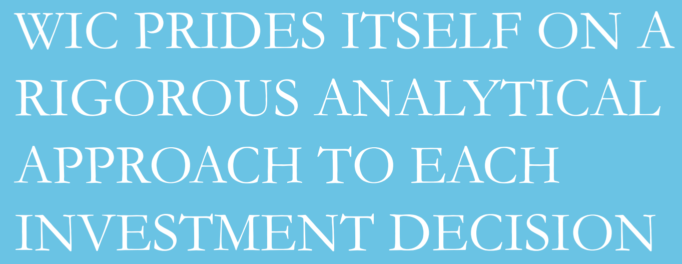


WIC's portfolio is comprised of cash, U.S. equities and Canadian equities. The fund faces foreign exchange risk given significant U.S. equity holdings and does not take action to hedge USD exposure. Cash is held in a Canadian dollar savings account allowing for immediate withdrawals.

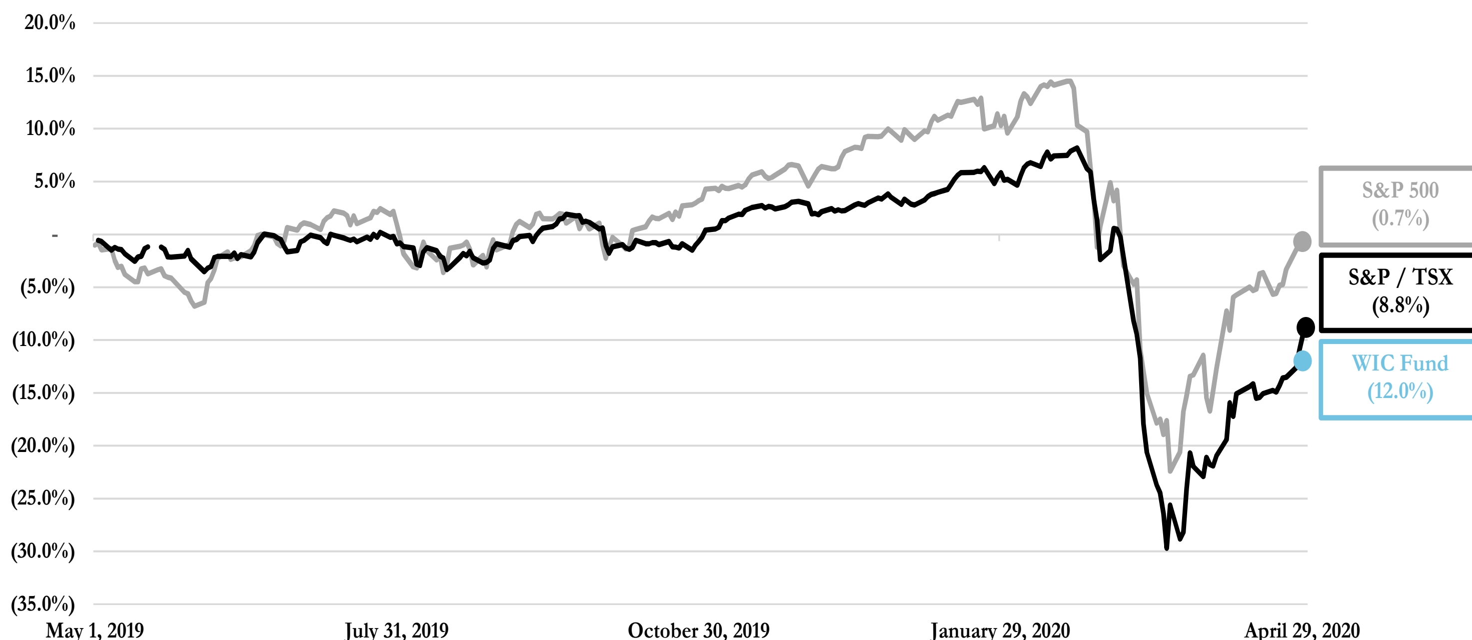
CURRENT HOLDINGS

Canadian Holdings	Symbol	Group	Entry Price
Cenovus Energy	CVE	NR	$13.07
Artemis Gold Inc	ARTG	NR	1.08
Keg Royalties Income Fund	KEG.UN	CRG	10.79
Magellan Aerospace	MAL	IND	18.75
Power Corp of Canada	POW	FIG	34.75
Lundin Gold	LUG	NR	7.75
Suncor Energy	SU	NR	33.13
Transcanada	TRP	NR	43.58
Toronto-Dominion Bank	TD	FIG	55.82
Torc Oil & Gas	TOG	NR	3.40

U.S. Holdings	Symbol	Group	Entry Price
Aercap	AER	FIG	$70.92
American Express	AXP	FIG	109.54
Astronics Class B	ATRO.B	IND	44.54
Berkshire Hathaway	BRK.B	IND	135.23
Covanta	CVA	NR	19.82
Catalent	CTLT	REHG	36.19
EZCorp	EZPW	FIG	6.27
Huntsman Corp	HUN	NR	24.49
Federal Agricultural Mortgage	AGM	FIG	111.18
HCA Healthcare	HCA	REHG	120.88
Iron Mountain	IRM	REHG	56.50
QAD	QAD.A	TMT	27.71
Qualys	QLYS	TMT	48.85
Marathon	MPC	NR	74.18
Premier	PINC	REHG	44.54
Stericycle	SRCL	IND	45.94
Synchrony Financial	SYF	FIG	46.60
Seaworld Entertainment	SEAS	CRG	28.11
Trecora Resources	TREC	NR	16.02
Teradyne	TER	TMT	67.38
Teva Pharmaceuticals	TEVA	REHG	46.41
Thor Industries	THO	CRG	191.68
Unico American	UNAM	FIG	11.98
II-VI	IIVI	TMT	28.92


WIC PRIDES ITSELF ON A RIGOROUS ANALYTICAL APPROACH TO EACH INVESTMENT DECISION

FUND
PERFORMANCE



Commentary

Equity markets saw steady increases until late February of 2020 when COVID-19 pandemic fears reached North American markets following significant declines in Asia. The S&P/TSX has suffered more than the S&P 500 given Canada's higher proportional allocation toward oil and gas and away from technology (which has provided immense support for the S&P 500 throughout 2020). Unprecedented stimulus and flows into large-cap, technology-driven companies (the 5 largest components of the S&P 500, all of which widely regarded as technology companies, now make up over 50% of the index) have left the S&P 500 nearly flat on a 1-year return basis despite massive unemployment and general economic uncertainty in the United States and around the globe.

The WIC fund returned (12.0%) in the same period. Despite this being below both the S&P 500 and the S&P/TSX (WIC's historical benchmarks), we commend the team for their performance. Given WIC's bias toward small/mid-cap U.S. equities, we view the fund's performance as relatively in-line when considering the extreme divergence in performance between mega-cap and small/mid-cap companies seen in recent market activity. As evidence of this, we can look to the Russell 2000 index which tracks the smallest 2,000 components of the Russell 3000 index (which tracks the 3,000 largest publicly-traded stocks in the United States). The Russell 2000 is down over 15% on a 1-year return basis. Operating as a long-only value fund in these times has proven to be challenging and we view an outperformance vs. the benchmark small/mid-cap index in the United States as an overall positive for the fund. This being said, there is always room for improvement in fund results and WIC will look to learn as much as possible from COVID-19's impact on financial markets and use heightened market volatility to deploy capital in high margin of safety investments.

CONSUMER RETAIL GROUP
INDUSTRY REVIEW

Opening Statement

During the final quarter of 2019, many retail businesses expressed the importance of convenience in today's society. Leading retailers successfully added convenience features such as curbside pickup, same day delivery, endless aisles and customized offerings. Many businesses set the stage to add similar features to their offerings as they entered 2020. The ensuing global pandemic has affected many businesses and put a halt to improvement plans. The new objective for many retailers is to survive this global shutdown.

Key Industry Trends

Volatility of Profits

Given increased emphasis on convenience, consumers across the globe have turned to online shopping, leading to e-commerce businesses continuing to outperform traditional brick-and-mortar stores. Many have described this transition to e-commerce as the "Amazon Effect" due to Amazon's role in lifting consumer expectations for convenience . Amazon's dominance has left many e-commerce peers struggling to keep pace at the expense of unsteady profits.

Despite having leading top-line growth figures among all retail segments, e-commerce posted the lowest median EBITDA margins among all segments in 2019. Low EBITDA margins can be largely attributed to lower realized prices and the high cost of competitive logistics. Furthermore, mature businesses are struggling with the transition to e-commerce given limited pricing benefits. These pressures have led to many describing e-commerce as a "winner-take-most" business exhibiting a traditional oligopoly stemming from economies of scale present in all of retail. Traditional retail offers cost benefits stemming from high operating leverage and revenue benefits from product variety, the addition of a digital platform creates a new network effect for larger players and thus further reduces the opportunity for new entrants to become profitable.

To combat the diminishing margins, retailers have been revamping store formats. For example, Canadian retailer Canada Goose has opened new store-fronts as "a journey." The store is an inventory-free retail concept that inspires customers with digital content, interactive product displays and a new cold-room. The goal is to transform customer experience and reduce inventory holding costs in the process.

Impact of COVID-19

First off, we would like to thank all of those on the front lines supporting Canadians with our basic needs for food and medicine. During the last few months, grocery retailers have seen sales skyrocket and stock-outs occur while customers panic-buy in a time of absolute uncertainty. Over the next few months, the consumption mix will primarily consist of home consumption and healthcare products with slight upticks in at-home entertainment and home improvement. On the flip-side, the stay-at-home patterns will have significant economic impacts on travel, entertainment, sports, restaurants and non-essential retail.

The fallout following COVID-19 is largely unpredictable, but many have speculated the collapse of various well-known retailers. Recently we've seen businesses such as J-Crew and Hertz face bankruptcy risk, marking a trend of bankruptcies in the retail space expected to continue in the coming months. This will lead to layoffs and subsequent government intervention may cause a period of unhealthy inflation for certain products and deflation for others. The impact on restaurants is large at scale and has moved up the supply chain to impact their suppliers, potentially altering the cost-structure and business model of the industry for years to come. The aforementioned shift to e-commerce may be accelerated during this time as consumer patterns change. The post-COVID-19 consumer will likely look different from the 2019 consumer but the extent to which things will change remains unknown.

CONSUMER RETAIL GROUP
SELECT INVESTMENTS

XPO Logistics (NYSE:XPO)

XPO Logistics is a global leader in transportation and logistics offering services such as freight brokerage, last mile delivery, order fulfillment and distribution. The company has grown rapidly in the past decade primarily through M&A which has led to management announcing various spinoffs. In late 2019, the stock fell on broader macro concerns and an inaccurate short seller report leading to an attractive entry price for the fund. In early 2020, the company announced that they were exploring opportunities to spin off certain business units. This created short-term value for shareholders but resulted in significant uncertainty regarding the future of the business. Given the company's historical roll-up strategy and management's excellent capital allocation, we felt the spin-off signaled a shift away from XPO's key advantage established through offering a wide variety of complex services. As a result, the fund exited its position after a 10-month holding period for a gain of 42.3%.

Ulta Beauty (NASDAQ:ULTA)

Ulta Beauty was pitched by the CRG team in November 2018 and after reassessing key valuation concerns, the team recommended to monitor the stock for a more attractive entry price. Ulta is the largest beauty retailer in the United States, offering a variety of cosmetic products and salon services. The business currently offers products from over 500 different brands and operates 1,213 retail stores. The team was impressed by the company's financial flexibility due to low debt balances and a leading position in an attractive industry. We felt that the softening of the beauty market was a temporary lull, and that the market would recover with future innovation and unit growth; however, the key concern came from the uncertainty of timing surrounding a recovery. With DTC and e-commerce businesses another consideration when evaluating the company's market position, the team issued a conditional buy at a price of $175 per share. Since the start of the Coronavirus pandemic the stock has settled around $220 following a large sell-off and subsequent appreciation. Given the impact of COVID-19, the future is unclear, and the team will continue to monitor the equity.

Keg Royalties Income Fund (TSE:KEG)

The Keg Royalties Income Fund is a WIC legacy holding that purchased The Keg trademarks and related property from Keg Restaurants Ltd. The Partnership, in turn, granted KRL an exclusive license to use The Keg rights for a term of 99 years. The income fund receives royalties of about 4% of all Keg restaurant revenues. The company has closed all Keg locations for the time being and the fund is down 47% year-to-date. Given the lack of public information on the underlying assets of the restaurants, the true asset value of the fund is difficult to assess. Prior to the pandemic, the fund was up 50% on the position while receiving a steady dividend throughout the investment. The team is hopeful that the business will rebound in 2021 and beyond, and thus had decided maintain its position.

FINANCIAL INSTITUTIONS GROUP
INDUSTRY REVIEW

Opening Statement

The COVID-19 pandemic reaching North America in early 2020 has placed financial institutions under serious pressure with unemployment rising to record levels and many consumers being unable to meet their financial obligations. Governments around the world have deployed extraordinary levels of stimulus to combat forced closures of businesses which has sent the global economic system into disarray. As of the writing of this report, the consequences of our society's steps to combat the virus remains to be seen in full, especially in relation to the financial institutions sector.

Key Industry Trends

Record Low Rate Environment

Prior to COVID-19, banks and insurance companies globally were faced with the lowest global rates in modern economic history. European banks have been especially hard hit by negative rates in many regions as a mismatch between positive-yielding deposits and negative-yielding assets threatens to erode capital. Banks in the United States had experienced a significant rebound from 2009 lows with the S&P 500 Banks Index approaching pre-financial crisis highs in 2019 before being hit hard by the COVID-19 selloff. In September of 2019, overnight borrowing rates between financial institutions in the United States broke through the Federal Reserve's target rate band, spurring an overnight repo operation by the Fed which continued throughout the remainder of 2019 and into 2020. These actions appeared to serve their intended purpose, with the financial sector remaining intact and rates remaining low, supporting a very strong economic environment in the United States. With recent rate cuts bringing overnight rates in the United States to zero (levels not seen since the financial crisis), many have been pondering negative rates in North America, with Tiff Macklem, the newly named Governor of the Bank of Canada, already hinting at negative rates becoming a possibility.

Low rates have also presented an issue for life insurance companies as assets held to satisfy claims yield lower returns. CI First Assets' U.S. & Canada Lifeco Income ETF has shown limited total return over the past decade (compared to broader indices) and has been severely damaged by COVID-19. The longer-term effects of this on pension plans and insurance companies remains to be seen but notable changes can already be observed with pension funds increasingly looking to alternative asset classes such as private equity to generate alpha in their portfolios. As many of these assets become more and more crowded, many have speculated that returns in alternative assets may decline materially. As of now, we have only seen moderate declines in areas such as private equity with the future of the space remaining uncertain and intriguing. Many industry practitioners do not forecast a materially abrupt decline in returns despite many private equity-backed businesses, such as 24 Hour Fitness considering bankruptcy in recent weeks.

Unparalleled global stimulus

Stimulus incited by forced closures of many businesses by governments to combat the spread of COVID-19 has assisted in keeping small businesses from bankruptcy and preserving the ability of households to make utility payments, but the consequences of this level of central bank balance sheet expansion is yet to be seen. With central bank assets reaching record levels as a percentage of global GDP, some have been contemplating potentially significant effects on inflation and currency valuations around the globe. As Milton Friedman famously remarked: "Inflation is always and everywhere a monetary phenomenon in the sense that it is and can be produced only by a more rapid increase in the quantity of money than in output." This quote seems highly relevant in today's environment, with M2 growth reaching levels not seen in decades. As of now, the swift action taken by governments around the world has been able to preserve the financial system and keep delinquencies contained, but what happens next with stimulus, inflation and the spread of COVID-19 remains to be seen.

FINANCIAL INSTITUTIONS GROUP
SELECT INVESTMENTS

Synchrony Financial (NYSE:SYF)

Synchrony Financial is a company focused on providing private label and co-branded credit cards in the United States. The company was spun off from GE Capital in 2014 and has traded in a band between $20 and $40 since the spin off. Given Synchrony's substantial existing receivables portfolio and private label cards being replaced by more versatile co-branded cards over time, Synchrony has looked to other methods to increase revenues including insurance products. Synchrony has been hit hard in the COVID-19 selloff, declining over 50% as the credit quality of borrowers becomes increasingly uncertain. Despite this degradation in credit quality, we view Synchrony as being a relatively safe bet among financial institutions through the cycle. By reaching below where large banks generally would in terms of credit quality, Synchrony is able to generate much higher gross yields from paying consumers than larger institutions. This ability allows Synchrony to absorb significant credit losses even as default rates spike. Given Synchrony's (and competitors') ability to operate through previous cycles while maintaining profitability, we view the business as being a safe investment at present, but will continue to monitor underlying credit quality.

EZCorp (NASDAQ:EZPW)

EZCorp is a recent addition to the portfolio and has withstood the recent market selloff more than most other financial institutions (appreciating 10% from February 2020-May 2020). The company operates pawn shops in North and Latin America and is the second-largest operator in the United States. EZCorp generally benefits in recessionary environments as consumers look for alternative financing options leading to increases in pawn service charges. Our concern surrounding the macroeconomic environment and EZCorp's inexpensive valuation vs. the broader market prior to COVID-19 led us to overweight this position in the Financial Institutions portfolio which has helped insulate the portfolio from the selloff. With EZCorp recently releasing results showing pawn loans (the primary source of income for the company) declining, the initial recession-resistant thesis does not seem to be appearing at present. However, we believe the protracted economic fallout of COVID-19 is when EZCorp will benefit as individuals struggle to source credit from traditional sources.

Banco Santander (BME:SAN)

Banco Santander was a WIC holding initiated in 2014 as the bank was de-risking and diversifying geographically. When reviewing the position in late 2019 we felt that Santander's credit profile was suboptimal despite the bank trading relatively in-line with its peers at 0.85x book value. This valuation did not appear to reflect risks specific to Santander such as outsized exposure to subprime U.S. auto loans and higher-risk geographies in Latin America. We also found that Santander was facing numerous lawsuits surrounding its auto loan business and European mutual fund business, leading us to be skeptical of management's integrity. These findings led us to exit the position in 2019 to free up capital for allocation toward recession-resistant businesses with sounder credit exposures.

INDUSTRIALS
INDUSTRY REVIEW

Opening Statement

The S&P 500 Industrials sector saw sideways price action prior to COVID-19. The strong economic environment in the U.S. and North America in general provided steady demand for industrial companies throughout 2019 and most of early 2020.

Key Industry Trends

Dichotomy emerging between industrial companies

In past downturns the industrial space as a whole has been regarded as cyclical and a space to avoid in periods of recession. However, with supply chains shifting as a result of the increased prevalence of e-commerce certain industrial companies (such as UPS) have not been hit as hard as they have been through previous downturns. On the other hand, passenger airlines have been hit particularly hard by the COVID-19 crisis which has resulted in massive stimulus directed at the sector to combat plummeting load factors. Nobody knows what the post-COVID-19 recovery will look like, but some are anticipating it will affect airlines in an outsized fashion. Following the 9/11 tragedy it took many years for airline traffic to return to pre-9/11 levels and we may see a similar trend post-COVID-19 with many airlines requiring load factors in excess of 80% to maintain profitability.

As for typical large-cap industrial names such as John Deere, Caterpillar, Cummins and the defense basket, the outlook remains uncertain. All of these names have experienced volatile price action in the past 2-3 months but have retained more of their value than one may expect through the selloff (many of the names mentioned above are down 10-20% since late February 2020). As investors struggle to form a view surrounding economic recovery, many have observed that stock prices appear disconnected from the economy. On the other side of this, unprecedented stimulus and the low rate environment globally have been supportive of equity valuations through the pandemic.

WIC has ended the year with industrials underweight versus prior years both as a result of portfolio dispositions throughout the academic year and investments being devalued heavily relative to other holdings in recent months.

INDUSTRIALS
SELECT INVESTMENTS

Stericycle (NASDAQ:SRCL)

The Stericycle position was initiated in late 2018 and revolved around the company being unfairly punished for legal issues despite having a strong foothold in its sectors (medical waste disposal and secure document disposal). The latter segment has been materially affected by COVID-19, and due to the market viewing this segment more favourably than the medical waste disposal segment, Stericycle has sold off through the pandemic. However, due to high switching costs in the medical waste disposal business and Stericycle's dominant market position, we view this aspect of the business as being nearly completely isolated from the pandemic. Additionally, we believe secure document disposal will continue to be a necessary aspect of many occupations moving forward and view current headwinds as inherently short-term. Despite the selloff, the fund is roughly breakeven on its investment and will continue to hold the stock as operational efficiencies continue to improve results in a historically cyclically resilient business.

Berkshire Hathaway (NYSE:BRK.B)

Berkshire has been a long-term WIC holding and has faired somewhat poorly in the recent downturn. Concerns about Berkshire's underlying investment portfolio have placed pressure on the holding company's valuation, however; we are confident in Berkshire's longer-term prospects both in terms of the investment portfolio and insurance businesses. As Warren Buffet recently remarked in his virtual annual meeting, "Never bet against America." We identify with this quote at WIC and view Berkshire Hathaway as providing a diversified exposure to the United States economy while owning a mix of businesses we view as favorable to that of broader-based indices at current valuations. The stock has outperformed the broader WIC Industrials portfolio through the selloff and will continue to be held.

Magellan Aerospace (TSE:MAL)

Magellan has been hit particularly hard in recent times given its exposure to the aerospace industry and commercial airline travel. The initial investment was predicated on certain event-driven theses which have since materialized as well as overall business improvement including both top line growth and margin expansion. We have seen Magellan execute on margin expansion initiatives which we view as strengthening management credibility and have been able to improve the top line in the same period. As a result, WIC has continued to hold the investment as Magellan is a strong company in a space which had been attractive prior to COVID-19. We believe the company is posed to make it through the crisis and recover with the broader aerospace sector as a result of low leverage and ample liquidity. With Boeing announcing a resumption of 737 MAX assembly in the summer of 2020, we are already seeing signs of a recovery at Magellan. As we view the current valuation of the stock as being unfairly depressed, we will continue to monitor the situation for material developments, but we do not believe current market prices reflect an appropriate valuation for the company.

NATURAL RESOURCES
INDUSTRY REVIEW

Opening Statement

The natural resources sector has experienced extreme volatility as of late. We have seen front-month WTI futures prices reaching negative prices for the first time as a result of a sharp decline in demand for commodities around the globe. Depressed commodity prices have led to a decline in the natural resources sector, with gold miners being a notable exception.

Key Industry Trends

Oil collapse and uncertainty

Prior to COVID-19 shutdowns, the United States reached record levels of crude oil production with much of the production coming from the Permian Basin, helping the country return to being a net exporter of crude oil for the first time since the 1940s. A large degree of expansion in upstream North American oil and gas was abruptly brought to a halt as a result of COVID-19. The virus led to us witnessing negative front-month oil prices for the first time in history with May 2020 WTI futures contracts closing at a price of negative $37.63/bbl on April 20th. The S&P 500 Energy Sector has experienced a loss from late February 2020-early May 2020 of around 30%, reflecting the uncertainty surrounding the global outlook for oil prices moving forward. Oil uncertainty was initially brought on by a price war between Saudi Arabia and Russia and we have only recently seen somewhat of a stabilization in crude prices. With a generally depressed environment, we have recently seen notable operators such as Chesapeake Energy disclose they may file for bankruptcy and cease to exist as a going concern. These shakeouts in the oil and gas space may lead to significant changes in the sector as operators look to devise methods for maintaining profitability at lower crude prices.

Flight to safety: gold prices

In sharp contrast to crumbling oil prices is the price of gold which is currently trading at around US$1,700/oz. As investors grow concerned about the macroeconomic environment, the price of gold has been bid up to levels not seen since the financial crisis. This has provided some level of support for the S&P/TSX index as gold majors and juniors continue to push higher. The increase in gold prices is being seen by some as a potentially permanent shift in the space with many forecasting long-term gold prices firmly above US$1,400/oz. If this is the case, we could begin to see more activity in the gold mining space.

Other commodities in limbo

Despite big moves in both crude oil and gold, other commodities such as copper and iron ore have experienced more muted price action through the selloff. Other commodities such as these fell along with the broader market at the outset of the selloff but have since rebounded significantly as a result of demand from China coming back online (as of the writing of this letter, China appears to be largely through the worst of their COVID-19 outbreak). Other commodities such as corn and soybean have also experienced price declines but have outperformed relative to many equities and other commodities (such as oil). Given demand for these commodities is generally linked to activities such as raising poultry and cattle, prices have not been as susceptible to changes in demand stemming from COVID-19.

As the longer-term economic consequences of the world's response to the virus unfold, it will be interesting to observe where broader commodity prices head in the future. Generally, it seems that many commodities have seen significant price declines and may now be set up positively with lower economic activity priced in while also being attractive as a potential hedge for inflation.

NATURAL RESOURCES
SELECT INVESTMENTS

Lundin Gold (TSE:LUG)

Given WIC's outsized exposure to oil and gas in the Natural Resources portfolio following the acquisition of Atlantic Gold, the Natural Resources team identified Lundin Gold as an attractive operator in the gold mining space. The stock has since outperformed the rest of the WIC portfolio and the broader market, returning nearly 25% since we initiated a position in late 2019. The team felt that Lundin Gold's high-quality primary asset (Fruta del Norte) and management track record combined with the market giving the company little credit for significant exploration potential provided an attractive entry point. We also saw gold as a natural market hedge and decided to increase our exposure in the space given concerns regarding the macroeconomic environment in 2019.

With gold prices continuing to climb, Lundin Gold has been one of the best performing stocks in the WIC portfolio as of late. Given that we valued the company using much lower gold prices than we are seeing today, we view the stock positively and will continue to hold our position.

TC Energy (TSE:TRP)

TC Energy was a position initiated in early 2016 (when the company was still called TransCanada Corp.) and has since performed well leading to gains of nearly 50% as of the end of April 2020. At the time of investment, WIC identified TC Energy as displaying significant potential for top line growth which has since come to fruition with TC Energy reporting revenues of over C$13B in 2019, leading to increased profitability through operating leverage. As the company has no direct exposure to oil prices because of its place in the supply chain as an intermediary, the company has not been hit as hard as upstream components of the oil and gas industry throughout COVID-19 (the stock is down ~12% since early March 2020). We believe TC Energy will remain a key component in the North American oil and gas space in the long-term and thus continue to hold the stock.

Suncor Energy (TSE:SU)

Suncor has been a longer-term holding of WIC, with the position being initiated as a result of a favourable view on the company's capital allocation strategy. Since then, certain projects have underperformed (such as Fort Hills) and the company has been damaged by the recent decline in oil prices across the board. We believe that given Suncor's vertically integrated business model the company is in a better position than purely upstream players in withstanding the downturn and will benefit from a normalization of the economic environment post-COVID. Additionally, as certain areas around the globe begin to allow for business reopening, the price of oil seems to have stabilized which will allow for operators in the space to plan for the future with a higher degree of certainty. For these reasons, WIC continues to hold Suncor's equity.

REAL ESTATE, HEALTHCARE, & GAMING
INDUSTRY REVIEW

Opening Statement

COVID-19 has not spared any of the real estate, healthcare or gaming industries with stocks tumbling in each of the three spaces. In the latter half of 2019, changes in regulation in the insurance and broader healthcare industry led to a bull run in the space. The COVID-19 scare has since negatively impacted the stocks of health care facilities (HCA) but positively impacted pharmaceutical businesses (Catalent). The global pandemic has created a lack of visibility into the future of healthcare around the globe.

Key Industry Trends

Changes in Healthcare Reinsurance

Prior to the Affordable Care Act (ACA), the healthcare reinsurance business was a robust model that offered a wide variety of valuable services to clients. This meant high expense loads, but companies in the space were able to maintain profitability. Following the introduction of the ACA, extra demand arrived, leading to new entrants in the healthcare space. However, entrants weren't focused on helping insurers understand their claim, and focused rather on simplifying the interaction, resulting in higher target loss ratios. The ACA also led to insurance carriers turning to the reinsurance market while many high-risk populations were phased out of state-sponsored plans, further driving up the risk on carrier balance sheets and encouraging them to seek support from reinsurers. These changes caused traditional reinsurers to adjust their proposition, becoming accustomed to prompter payment of claims with few questions in the process. Now, however, the newer entrants are being pushed out of the market or becoming more hands-on with their approach due to their inability to generate profits. This has led to the market shifting to land somewhere between two entirely different business models.

Unpredictability in Real Estate

The longest bull market in recent history and strong macroeconomic conditions have allowed the commercial real estate market to flourish. However, the global has caused significant uncertainty, especially with respect to office real estate. With the rise of work-from-home companies such as Zoom Video Communications, many businesses are questioning the need for office real estate. Recently, the CEOs of Morgan Stanley and Goldman Sachs have indicated that working from home could be the new normal for employees going forward. The main question: will these businesses do away with part of their office space after their leases expire? Businesses have been looking to cut costs in office real estate for a few years now including Deloitte in Toronto moving from 300 square feet per employee to 160. These changes may cause sky-high office real estate prices to drop while businesses offering shared space, such as WeWork, will continue to struggle in the aftermath of the pandemic. In contrast to office real estate is commercial real estate. With many retailers expecting to hold higher levels of inventory in warehouses going forward to mitigate future supply chain shocks, commercial real estate could see a boom.

"Value-Trap" in Gaming

Casino operators were some of the first to shut down as a result of COVID-19 in Asia in February, closely followed by operators in the United States. With many industry players having lost about 50% of their value YTD, many have been suggesting casino stocks a potential value investment. It was reported that monthly revenues in March were down 88% year-over-year while many businesses such as Wynn Resorts and Las Vegas Sands have committed to paying employees until the pandemic ends. A key concern with casino operators is the timing of reopening as investors are unaware of how long casino traffic will be reduced. Although some businesses in Macau have begun opening their doors, the demand for services will remain low as tourists continue to fear travelling and public hotspots. While many businesses have looked to shift certain operations to online gaming, market incumbents have created large barriers to entry with sizeable network effects. Furthermore, with all major sports leagues suspended for the time-being, the industry is limited in product offering. Until there is a clear timeline to a vaccine, it is difficult to predict the impact the pandemic will have on casinos.

REAL ESTATE, HEALTHCARE, & GAMING
SELECT INVESTMENTS

Catalent (NYSE:CLT)

WIC initially bought Catalent in February of 2016. The business operates through three main segments: Oral Technologies, Medication Delivery Solutions, and Development & Clinical Services. The business is the largest player in a fragmented industry. The main thesis was predicated around a strong business model and high free-cash-flow generation. Since the initial pitch, the company has consistently generated strong cash-flow and met analyst expectations. The company's diverse footprint of operating facilities and customers has reduced impact from the COVID-19 slowdown. In certain geographies the company has seen an increase in demand due to the pandemic. Recently, Catalent signed an agreement with Johnson & Johnson to be the U.S manufacturing partner for a lead COVID-19 vaccine candidate. Since its initial investment, the fund has returned approximately 101% with the REHG team remaining optimistic about the company's future.

The Stars Group (TSE:TSG)

The Stars Group (TSG) is a Canadian online gaming business most well-known for their online poker arm Pokerstars.net. In recent years the company diversified their operations to include other gaming products such as online slots and a sports book resulting in an equal split among the three segments. The business was well known for their loyalty program and strong player liquidity providing a sticky customer base with high-value customers. Recent diversification and strong network effects has allowed the business to incorporate cross-selling synergies and improve operating margins. In 2019, TSG and Flutter Entertainment entered into an all-stock exchange with TSG shareholders receiving 0.2253 new Flutter shares per 1 TSG share. By assessing the post-merger business and the risk of a deal break, the club decided to sell the stock in November 2019, locking in an annualized return of nearly 15%.

Premier (NASDAQ:PINC)

Premier offers a broad array of services and solutions that help healthcare providers improve operational and financial performance. In 2019, consistent with the poor market environment, the company was facing challenges in their performance services segment due to the significant reduction of the CMS hospital improvement project that the business participated in for the three previous years. Financially, the company delivered 3% year-over-year revenue growth and 4% non-GAAP EBITDA growth, consistent with projections. However, the market sold off the stock as the 2020 presidential election campaign progressed, posing potentially substantial changes to regulation. Amid the COVID-19 pandemic, the business has helped health-care partners manage the unprecedented crisis and has delivered strong financial performance. The online ordering platform and integrated capabilities the business has built throughout recent years are serving them well, but supply chain concerns have resulted in the stock price trading below WIC's entry price. Uncertainty facing the hospital business has led management to outline certain mitigation measures which WIC views as positive for the future of Premier and supportive of a continued holding.

TECHNOLOGY, MEDIA & TELECOM.
INDUSTRY REVIEW

Opening Statement

As the world continues to grapple with COVID-19, many have turned to online solutions to preserve the lifestyle of the past. Shopify is experiencing Black Friday's level of traffic on its platform while Slack and Netflix are seeing unprecedented growth in subscribers. At the same time, many players are rushing to provide contact-tracing tools (such as Apple and Google's API) while others are offering discounts to their products for the duration of the pandemic. While the lockdowns have benefited businesses with exposure to remote working solutions, it has been damaging to many businesses that were already experiencing profitability concerns pre-pandemic. Notably, Airbnb and Uber were forced to announce massive layoffs as the home-sharing platform postponed its IPO process and the ride-hailing app pushed back its profitability goal by several quarters. Until there's more clarity, technology companies will be playing an important role in the pandemic response while utilizing cost-cutting measures and their cash balances to weather incoming fluctuations.

Key Industry Trends

A Reality Check on Unicorns

2019 was expected to demonstrate a strong IPO market as high-profile startups including Uber, Lyft, Pinterest, and WeWork finalized plans to go public. A simple review of these Unicorns reveals they have yet to meet the expectations as returns have lagged the broader market. In a more extreme case, the implosion of WeWork's IPO prospects has become a case study for what not to do as a unicorn looking to IPO. While many highly anticipated IPOs fell short of expectations, a group of less flashy firms stole the show, including Zoom, Crowdstrike, and Datadog. This group of companies had two key things in common: unlike their Unicorn counterparts, these companies primarily operate in core technology seg-ments (software, cybersecurity, etc.) and more importantly, they have demonstrated an ability to turn a profit or report relatively small losses while pursuing growth.

The underperformance of tech IPOs is not particularly surprising. Venture capital portfolios have been stocked with highly valued companies many of which held for longer than ideal timeframes. Inherently, these firms are subject to a deceleration in growth and have had a majority of benefits accrue to early investors, founders, and employees. Public market investors have been left last in a long line of investors looking for value in these companies and are not particularly attracted to premium-priced, cash-burning companies, regardless of private market valuations.

Enterprise Cloud at the Forefront of the Corporate Pandemic Response

In early 2020, enterprise SaaS and cloud solutions felt increased demand as COVID-19 caused many firms and institutions to begin utilizing these firms as an aid in navigating abrupt changes to their workspaces. The pandemic has amplified the industry's spotlight as an influx of enterprise cloud companies, such as Zoom and Slack, completed IPOs in 2019 promoting further dialogue regarding the space. For instance, Zoom experienced an 88% growth in revenues for the 2019 fiscal year before announcing the company had seen its daily meeting participants rise from 10M to over 200M due to its free offerings to several impacted industries.

Cloud's recurring revenue model has proved beneficial for all parties, as the client is able to operationalize IT costs (that otherwise would've been large capi-tal expenditure investments) and the provider has been able to benefit from a more resilient business model due to higher customer lifetime value, constant innovation, and steadier cash flows. This shift is evident as the industry has gone from a ~51% median recurring revenue mix in 2008 to over ~87% today.

Additionally, SaaS businesses have utilized technology to drastically minimize marginal costs and increase scalability. While other online consumer platforms are challenged with several variable costs to provide their service (e.g. Uber paying drivers, Spotify paying artists, StockX paying for authentication, etc.), enterprise SaaS businesses primarily invest in their platform and customer acquisition. While this dynamic provides a more predictable outlook on profitability, it also emphasizes the importance of operating leverage and growth, causing an arms race of SaaS companies to engage in horizontal consoli-dation to offer the best all-in-one platform for their clients. Putting the industry in the midst of today's climate, the distribution model and the actual offerings of the providers will determine the impact of COV-ID-19. While all businesses will have more difficulty onboarding new customers, firms selling high ASP software (which often have longer sales cycle and customer acquisition costs) will be more exposed as businesses will cut or postpone IT budgets. On the other hand, businesses that offer low-impact software, with self-service onboarding and little exposure to SMB (especially within the most-affected industries) are poised to grow faster than before and turn a profit.

TECHNOLOGY, MEDIA & TELECOM.
SELECT INVESTMENTS

Qualys (NASDAQ:QLYS)

Qualys was initially pitched in 2017 as a cloud cybersecurity business expected to benefit from general industry tailwinds. We previously wrote about the company in 2018 and at the time the position had generated 125% in unrealized gains. Today, the position has grown to be the largest in the fund with an unrealized gain of 228%. In recent years, the company has grown rapidly as cloud security consistently beat revenue and earnings for multiple consecutive quarters. In 2019, however, the company showed signs of slow down, missing Q4 2018 earnings by 2% and lowering future expectations. After a disappointing 2019, the stock has performed well through the pandemic, earning 32% YTD. With the shift to work-from-home, many businesses are looking to maintain strong cybersecurity practices and Qualys is well positioned to take advantage of this industry shift. The team is optimistic about the company's future growth prospects and will continue to hold and monitor the investment.

II-VI (NASDAQ:IIVI)

In 2019, one of WIC's largest holdings (Finisar) was sold to II-VI which is a vertically integrated manufacturer of engineered materials and optoelectronic components for applications in industrial, military and semiconductor markets. The acquisition provided shareholders with $15.60 in cash and 0.222 shares of II-VI which traded at $46.88 at the time of announcement. The fund decided to hold a position in the post-acquisition business with the thesis focusing on synergies through the Finisar acquisition and future growth opportunities. The novel coronavirus outbreak has led to many concerns about the business and caused sell-off in the first quarter of 2020. The company has many production facilities in China and other countries that have been hit hard by the virus such as Germany. With ongoing trade tensions between China and the United States, the team will continue to monitor the situation.

Resideo Technologies (NYSE:REZI)

Resideo Technologies is a leading global provider of comfort and security solutions primarily used in residential homes. The company was spun-off from Honeywell in October of 2018. The TMT team decided to pitch the stock at a time when shares were down 65.4% from the date of the spin-off due to earnings misses and other negative short-term events. Despite identifying strong unit economics and industry tailwinds, the team decided to monitor the stock and issued a conditional buy order. The main concern with Resideo was management. With the CFO abruptly leaving the company, the team was uncomfortable with a lack of visibility. A month after the pitch, the CEO also left the business and the stock fell further. Moreover, volatile COGS margins after the spin-off made the team wary and led to significant uncertainty in projected financial performance. Today, with a new management team in place and a share price of $5.27, the TMT group remains interested in the company's future and will reassess a possible investment.

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