HOLDUN

INVESTMENT REPORT

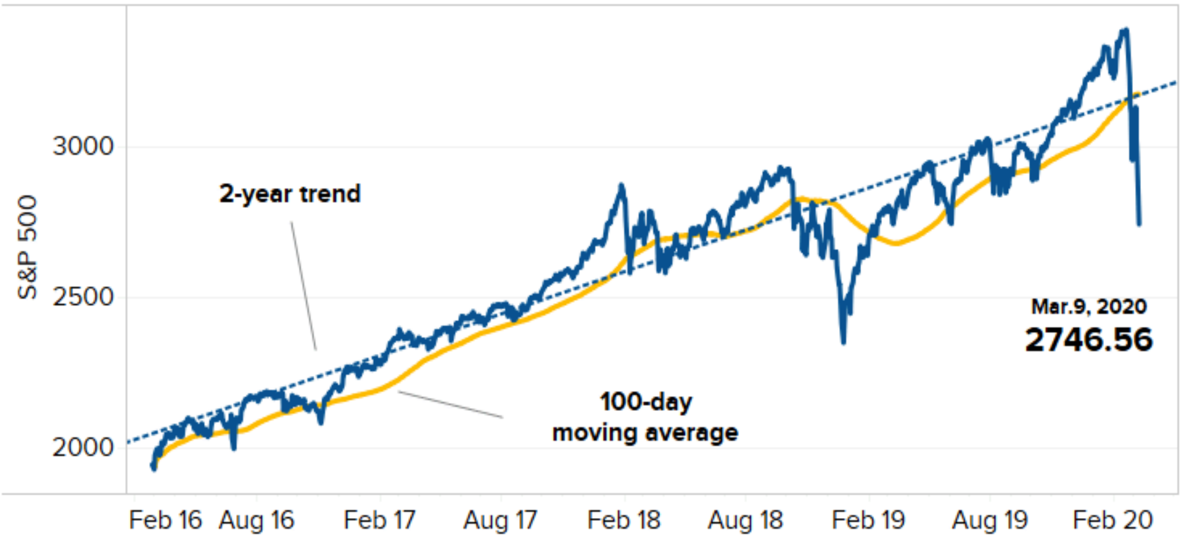
YEAR-TO-DATE AS AT MAY 13, 2020

Photograph by jeshoots.com on Unsplash

Record Highs and Record Lows

The year started as 2019 ended with equity valuations continuing to climb. Buoyed by the easing of trade war tensions between the world's two leading economies, the S&P 500 reached an all-time high in mid-February. However, the celebrations were short-lived. Wall Street's ever-changing level of concern over the coronavirus swung dramatically negative. The spread of the virus beyond China created fresh uncertainty for the global growth outlook and sparked volatility in financial markets. Economies came to a standstill in a bid to contain the virus, and markets tumbled 34% in just 22 days to record the fastest market correction in history.

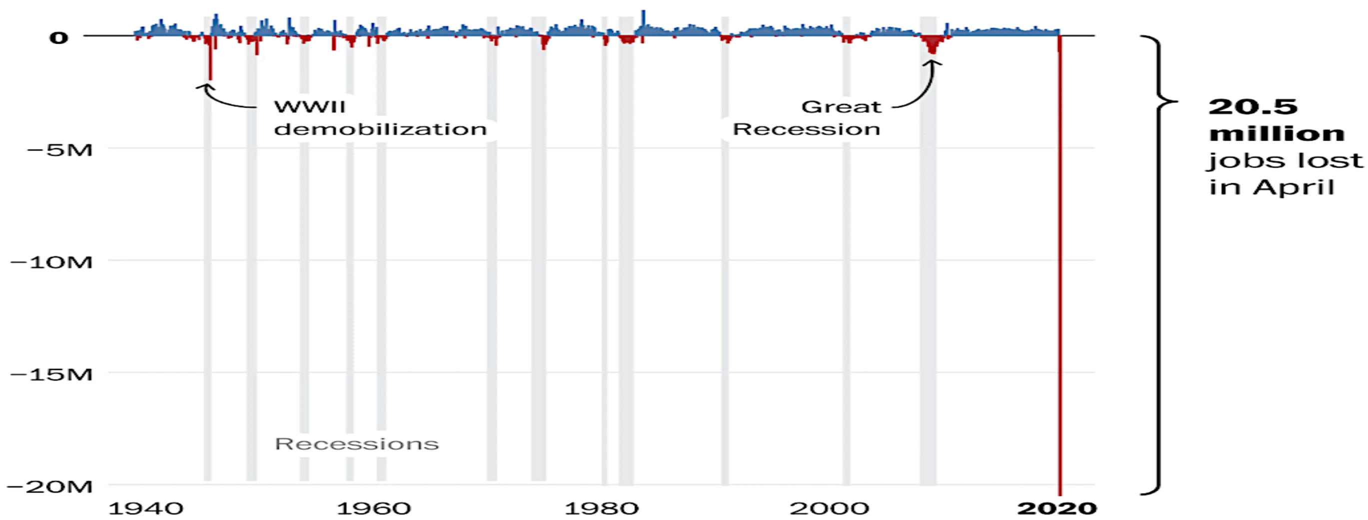
Market Correction



Source: CNBC Markets

Economic data continued to deteriorate as the spread of the virus accelerated around the world. Central to this economic demise was the U.S. unemployment claims figures, which jumped by a staggering 20.5 million in April 2020 alone. To help put this into context, the largest monthly increase in unemployment figures during the Global Financial Crisis was 800,000. The worst month in history prior to this was a loss of 2 million jobs in September 1945 during WWII demobilization.

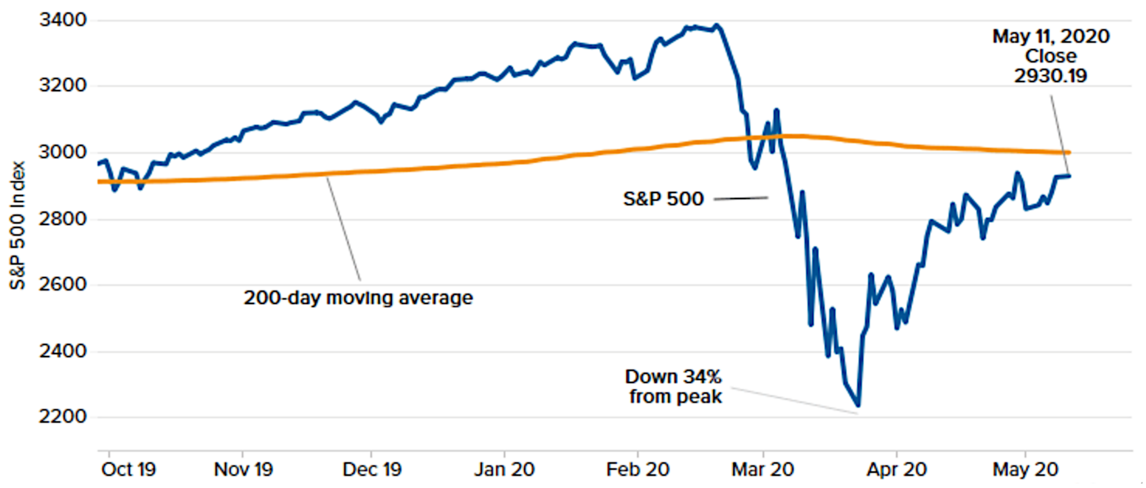
Monthly Job Gains or Losses In The U.S Since 1939



Source: Washington Post

Despite the bleak economic fundamentals, share prices have staged a remarkable recovery. April was the S&P 500's best month since January 1987, albeit after a March rout of about the same magnitude in the opposite direction. Having bottomed at 2,237 on March 23rd, the S&P 500 rallied by 30% by May 8th. Technically, that has put shares back into a bull market, even though they have yet to regain all their pre-pandemic losses.

Coronavirus Comeback



Source: CNBC Markets

But how have markets managed such as startling recovering in the middle of an economic collapse of historic proportions?

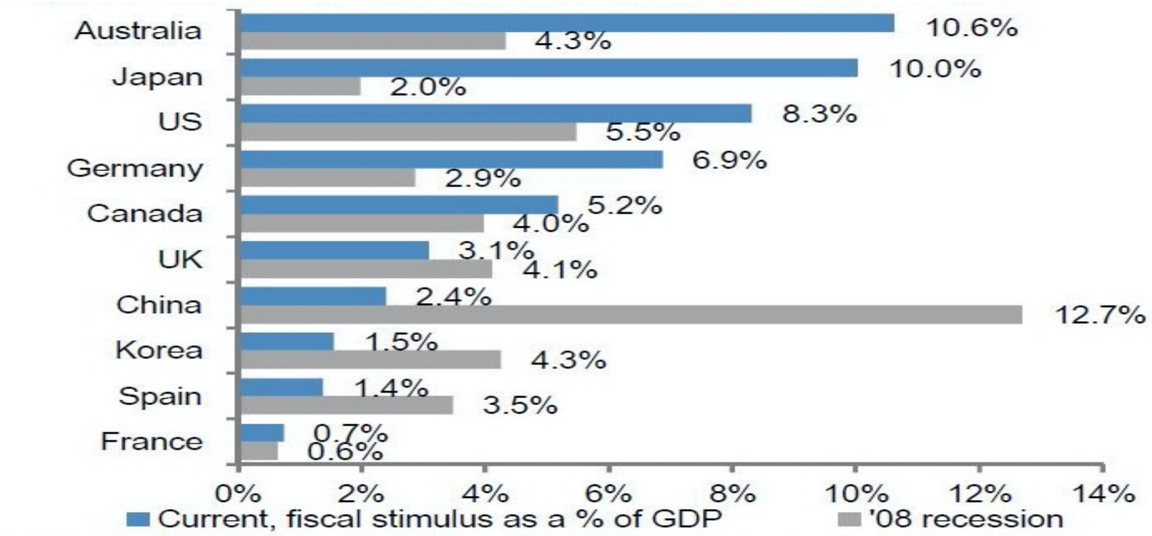
Unprecedented fiscal and monetary support has been at the heart of this market resurgence.

Policymakers around the globe have taken extraordinary steps to support financial markets with more than 50% of the world economy at or near the zero bound for interest rates as Central banks keep rates anchored and continue widespread quantitative easing policies to avoid the dreaded deflationary cycle and ensure market liquidity.

Fiscal stimulus by governments, which looks to soften the economic blow through targeted spending and relief, has far exceeded the Global financial crisis with 8 trillion dollars already dedicated to fighting the pandemic globally.

Fiscal Stimulus, as a % of GDP

CURRENT VS GFC

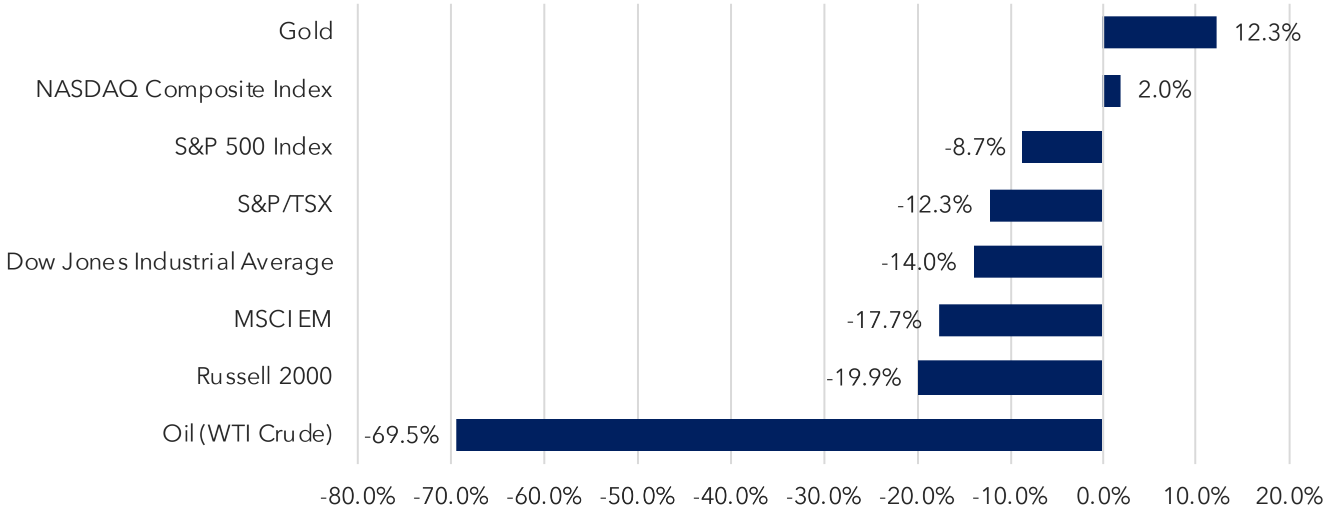


Source: J.P. Morgan Asset Management

Right now, fiscal stimulus is replacing the income that is being lost by people who have lost their jobs, supporting businesses who have lost their consumer base and propping up aggregate demand. This support has, so far, been successful in reducing the severity of the economic disruption as a result of the pandemic and has spurred investor confidence.

A Closer Look

Global Market Performance (YTD to 8th May)



Source: Bloomberg

The S&P 500 has returned -8.7% YTD, recovering strongly following the initial coronavirus induced sell-off. Much of the rebound has been concentrated in the shares of five behemoth stocks. Facebook (+4%), Apple (+7%), Microsoft (+18%), Amazon (+30%) and Google (+5%). This group of companies accounts for approximately 20% of the S&P 500. The healthcare sector has also performed well, down only about 1% Since 1 January. A relatively small 3% exposure to Energy has also ensured that the S&P has not been overly exposed to the major drawdowns witnessed in the Energy Sector this year.

The tech-heavy Nasdaq Index is in positive territory YTD, up 2.0%, highlighting the continued strength of the Tech industry despite the current market uncertainty.

In Commodities, Gold lived up to its safe-haven credentials as a reliable store of value, up nearly 13% YTD, while oil suffered an entirely different faith.

As the global economy came to a virtual standstill, the demand for oil vanished, this, coupled with a poorly timed price war between OPEC and Russia saw oil prices collapse and oil futures run negative for the first time in history as storage capacity issues disrupted the supply/demand function within the oil industry. WTI Crude oil Rallied last week, gaining over 17% but remains down nearly 70% YTD.

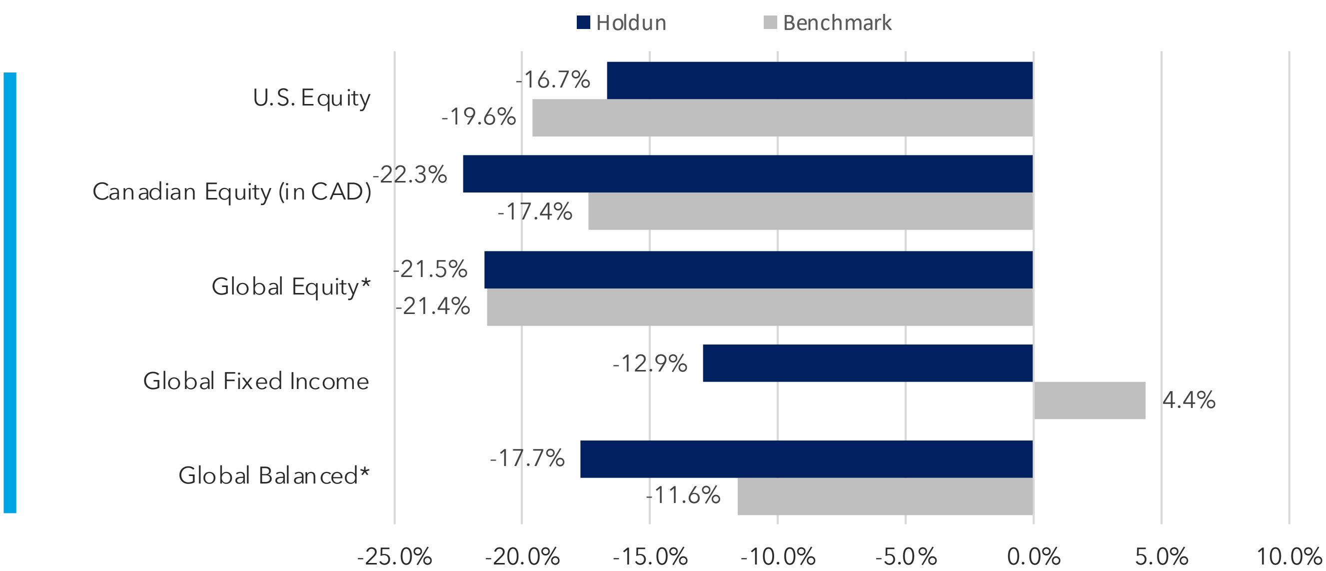
How Did We Fare?

Q1 2020

In the first quarter of 2020, the Holdun Canadian Equity (Model Portfolio) fell -22.3% (in CAD), underperforming the -17.9% reduction in its Canadian benchmark. Over the three-month period, both sector allocation and security selection weighed on performance with our exposure to Energy acting as the primary source of underperformance for the period, detracting by -1.9%. Our lack of exposure to Technology (in Canada) also hurt relative performance.

During the same period, the Holdun U.S. Equity (Model Portfolio) fell 16.7% (in USD), and it outperformed its benchmark the S&P 500 Index, which fell 19.6%. Security selection was the primary driver of relative outperformance with sector allocation, also providing positive relative returns. Our exposure to Consumer Staples was the primary driver of relative outperformance (+1.9%), this was offset somewhat by an overweight position in financials (-1.2%)

Q1 2020 Performance by Strategy - Holdun Vs Benchmark



*Holdun Opportunity Fund (NAV Dec 31,2019)

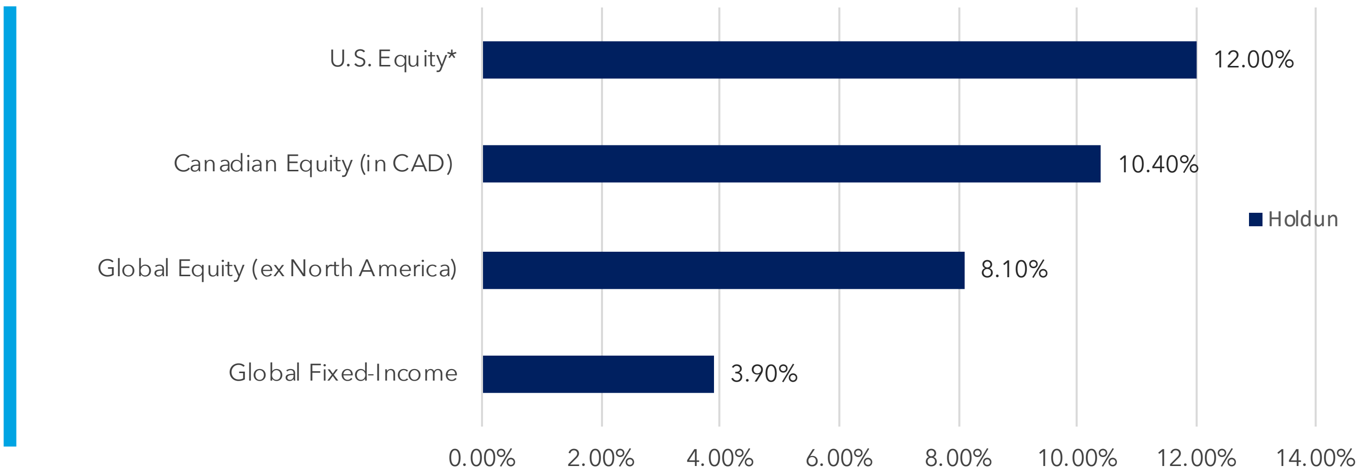
April 2020

In April, all portfolios rebounded strongly.

Both the Canadian Equity and U.S. Equity Fund recorded double-digit returns, clawing back roughly 50% of the losses reported in Q1 with the Canadian Equity fund up 10.4% and the U.S. Equity Fund up 12.0% for the month.

The Global Fixed Income Fund was up 3.9% in April following a poor performance in Q1. We expect this positive trend to remain. The temporary liquidity issues at fault for much of the Q1 underperformance have subsided as buyers now re-enter the secondary market, this increase in demand will help to lift the discounted valuations going forward.

April 2020 Performance by Strategy



**Holdun Opportunity Fund (NAV Dec 31,2019)*

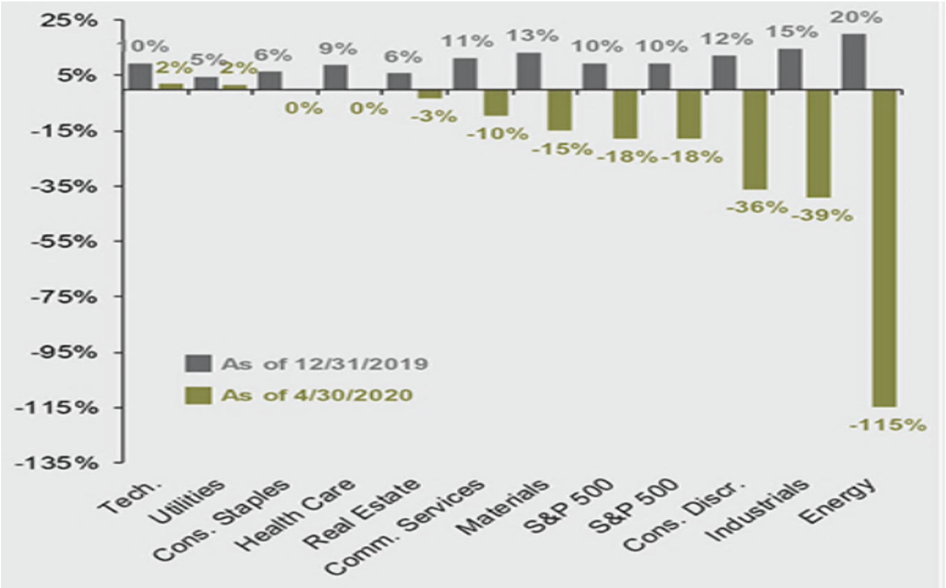
Market Outlook

It is important to remember that the Coronavirus is just the trigger that took the financial market into a period of correction. Record high valuations, anemic earnings figures, and underlying imbalances in financial markets have pointed towards the need for correction long before the coronavirus outbreak. While painful correction is what we require to generate a better and more sustainable outlook, long-term return expectations are improving. However, we are still cautious and expect further challenges over the coming quarters.

So, while the market performance of late would seem to suggest that the most severe economic slump in modern history doesn't matter, that is not the case. Investors are merely focusing on the extensive fiscal and monetary support and its ability to prop up aggregate demand until everything returns to 'normal'. Unfortunately, the success of this narrative is based heavily on the assumption of a shorter virus timeline allowing for a V-shaped recovery. With the economic data continuing to pile up and with the potential for a second wave of the virus still ever-present, a V-shaped recovery is far from certain, and as such, the coast is not yet clear in the short run.

The continuous earnings decline is a testament to this. Analysts' earnings predictions for the S&P 500 in Q2 are now down 28% and negative for all quarters in 2020.

S&P 500 2020 Earnings Growth Estimates



Source: J.P. Morgan Asset Management

At their most basic level, Stock prices are essentially a reflection of a companies' future earnings. The above chart clearly illustrates the deterioration of earnings over the last year, but true to form, the stock market has continued its forward-looking trend and instead focuses on potential earnings growth into 2021 in a bid to justify current valuations. However, the longer these earnings remained suppressed by CoVID-19 uncertainty, the harder it becomes to sustain the most recent rally in the equity market.

What Does All This Mean for Investors

While it is always important to look at the broader economic landscape, it is essential to assess how all these changes will affect specific asset classes and financial instruments in the future.

In the Equity Market, pitfalls still exist, but we have already witnessed the emergence of the 'stay-at-home' winners with technology, communication Services, and Health Care best positioned to take advantage of the current environment.

For fixed-income investors, monetary stimulus has created a challenging landscape, with safe-haven bonds offering interest rates of close to zero, all but eliminating their upside protentional. As the economy moves past the CoVID-19 recession and begins to expand again, these interest rates will remain unattractive over the longer-term.

In High Yield markets, the market volatility of late has caused spreads to widen to their highest point since the Global Financial Crisis. While there may be individual opportunities in this space where careful selection can yield better returns, the potential for widespread defaults amongst high yield bonds is likely in the months ahead, so proceed with caution.

All-in-all, the fundamental changes to the fixed-income asset class as a result of monetary stimulus have continued to drive up bond valuation, effectively deteriorating the future returns previously on offer. The diversification benefits have not gone away, but longer-term investors may want to be underweight fixed-income as the economy re-emerges, opting instead for Alternative Investments such as precious metals, private equity, real estate and venture capital.

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