



Ninepoint International Small Cap Fund

Q2 2022 Commentary

Dear Clients and Colleagues,

We've officially entered a bear market. During the second quarter, The Federal Reserve raised its main interest rate by three-quarters of a percentage point, to a target range of 1.5% to 1.75%, the biggest increase since 1994. The Fed also announced its plan to reduce its balance sheet estimated to be nearly \$9 trillion that it has accrued over the pandemic as early as May, and at a pace considerably faster than had been expected.

The aggressive action led by the Federal Reserve is expected given CPI increased to 8.6% in May and 9.1% for June, the highest since 1981. The S&P 500 reaching lows of \$3,666 mid-June, slightly recovered but dropped 15% overall during Q2. We still see investors concerned regarding the effects of inflation and increased rates.

Oil prices remained flat if you compared the end of Q1 vs the end of Q2, however large fluctuations occurred during the last 3 months reaching as low as \$94.21 mid-April and highs of \$121.51 mid-June. The price decrease was driven by the U.S. announcing another large release of oil from its strategic reserve combined with weaker demands from China.

Consumer sentiment is starting to impact demand for certain products. New home builds are seeing a slowdown despite the shortage of supply while homes on the market are seeing fewer bids. The economy remains at high employment, however some high levered tech names are seeing hiring freeze and layoffs.

The Russian invasion of Ukraine continues to take place and the World Bank forecast that Ukraine's economy will shrink by approximately 45% this year. It's estimated that 50% of their businesses are closed while the Russian GDP is set to contract by 11%. With Ukraine being a top exporter of grain and oilseed, food shortage is becoming a more material risk to many regions.

Continued disruption to gas supplies due to the war in Ukraine saw Germany move to phase two of its emergency energy plan. The next phase would involve rationing gas to industrial users, and potentially to households as well.

Sustained higher inflation is leading to declining consumer confidence in Europe, as the European Central Bank shifts toward raising rates more aggressively to catch up with its American counterpart. The Eurozone's annual inflation rate leapt to 8.1% in May. Top performers in the Eurozone included communication services and energy while real estate and info tech encountered a sharp decline.

The Bank of England increased its official rate by a combined 50 basis points along with two consecutive 25 bps hikes to 1.25%. UK Britain's annual rate of inflation leapt to 9% in April, the highest level in four decades. Britain now has the worst rate of inflation in the G7. The Bank of England expects higher inflation, and in June raised its estimate for the peak CPI from 10% to 11% for October.

For almost two months 25 million Shanghai residents were confined in their homes due to the severe lockdown protocol "zero-COVID policy" set in place by president Xi Jinping. The situation has temporarily eased in some locations but the status can change quickly if new outbreaks take place.

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The Chinese government is signaling that the zero- COVID policy will probably be extended at least into the beginning months of 2023. The zero-COVID policy led to the Shanghai SE Composite Index reaching lows of \$2,886.88 at the end of April with a strong recovery to \$3,409.21 representing an increase of 18% from its lows.

BACK TO NINEPOINT INTERNATIONAL SMALL CAP FUND

During the second quarter, the MSCI EAFE Small Cap Index underperformed the MSCI EAFE Large Cap Index and the MSCI Emerging Markets Index.

In the MSCI EAFE Small Cap Index, Energy, which represents 2.6% of the index, was the strongest performing sector, delivering a negative return of 5.9%. At the opposite end of the spectrum, Materials was the worst performing sector, returning -20.2% for the quarter, with an index weight of 9.4%.

PERFORMANCE HIGHLIGHTS

For the second quarter, our International Small Cap composite delivered a return of -11.1% gross, outperforming the MSCI EAFE Small Cap Index by 3.9% gross.

Our top contributor this last quarter was Biffa (BIFF LN). Biffa is a leading UK waste management company providing collection, recycling, treatment, disposal and energy generation services to businesses and households across the UK. Biffa is fully integrated and concentrates on 60M tons per annum of nonhazardous recyclable and combustible waste produced by households and businesses.

Biffa is the second largest player in the UK market with a leading position in industrial and commercial collection, which are more profitable than municipal contracts. Biffa should benefit from regulatory changes to increase recycling levels and drive stronger end markets for recyclable products. There is a deficit of energy recovery facilities in the UK with more needed in order to maximize the amount of energy generated from residual waste. UK waste collection remains a highly fragmented market, which means a strong acquisition pipeline to complement any organic growth. The valuation for Biffa remains compelling versus peers such as Waste Management in the US and Veolia.

What drove the stock up?

On June 7th, Biffa announced that it had received an indicative proposal from private equity firm Energy Capital Partners (ECP) at a price of 445 pence per Biffa share in cash. The Biffa board said that should the proposal become a firm offer at the same level, it would recommend it to Biffa shareholders and as such granted ECP access to due diligence materials, and ECP has until July 5 to announce a firm intention to make an offer. In the same press release, Biffa states that the business continues to trade well with performance being in line with the board's expectations. The company also announced an enquiry by the HMRC (Her Majesty's Revenue and Customs) on certain aspects of Biffa's landfill tax compliance. The company strongly refutes the HMRC's concerns. No formal claim has been received, and any potential conclusion could take some time which makes it difficult to ascertain the size of any potential liability.

Another highlight this last quarter was Norway Royal Salmon Asa (NRS NO), an independent Norwegian salmon farmer that sells its volume via its own organization. Founded in 1992 on a membership model, it currently operates through 35 fish farming licenses and exports 95% of its sales.

The global market for salmon was estimated at 2.1675 million Kilograms in 2016, with half of it being produced in Norway, and the top 50 producers accounting for 80% of all farmed salmon. With the industry growing roughly 6-8% annually, the salmon market is uniquely positioned to benefit from trends toward healthy diets and food safety. Within that market, Norway Royal Salmon is among the lowest cost producers and one of the most innovative.

So what drove the stock up?

Those that have been following the story will recall that earlier in the year SalMar, a peer of NRS, made a share

and cash offer of NOK 120 per share for NTS, the main shareholder of NRS. This bid pushed the implied value of NRS up and there was the possibility of SalMar fully consolidating NRS in the future. At the end of May, NRS and SalMar announced a plan whereby the two entities will merge, with SalMar as the acquiring company in the merger with the rationale to realize synergies between the companies in the regions where both operate. The value of NOK 265.18 per NRS share gave a small premium over the prior closing price. Operationally, first quarter results were a little disappointing as lower volumes of fish were harvested and price achievement was negatively impacted by the fish suffering from winter wounds.

Our top detractor for the quarter was Aurubis AG (NDA GY). Aurubis is a leading global producer of non-ferrous metals and one of the largest copper recyclers worldwide. Annually, the company produces more than 1 million tons of copper cathodes as well as a number of other metals and additional products such as sulfuric acid.

The company benefits from its exposure to the secular recycling and circular economy model trends. Its multi-metal expertise means the company is well positioned to benefit from increasing volumes and more complex recycling materials. Aurubis started expanding in the US, historically an underdeveloped recycling market, which should further support the company growth over the next few years.

What drove the stock down?

The quarter started well as Aurubis once again increased guidance citing continued high metal prices as the main reason. Aurubis started underperforming in line with the sector as metal prices slid on demand concerns with the Chinese property market being a large contributing factor. Base metals and copper in particular continued to decline towards the end of the quarter due to growing concerns over a global economic slowdown on the back of rapid interest rate hikes across the world and China's struggles with coronavirus.

So why hold? Its main smelting operations are among the most efficient in the world. Even if the price of copper continues to normalize, we could see treatment and recycling charges rise going into 2023. Furthermore, the company's strong balance sheet means the company is among the best positioned for investors who are looking for exposure to materials.

NEW POSITION

During the quarter, we initiated a new position in IPSOS Sa (IPS FR). A leader in market research with a solid brand reputation, IPSOS focuses its expertise exclusively on survey-based research. It is ranked #2 worldwide in this area with a 7% market share. The survey research segment alone accounts for two-thirds of the global market research industry, with the rest consisting mostly of panel studies. It operates 5 segments: marketing, ads, media, opinion/social, and consumer satisfaction.

The company has been able to consistently grow faster than its peers thanks to its geographic mix and capacity to manage its services at a global scale. Indeed, 27% of its business is from emerging countries where competition is more local and demand for advertising research is growing twice as fast as developed markets. IPSOS also benefits from the trend toward surveys being done online. With 60% of its surveys being completed that way and the expectation that it will reach more than 70% in the near future, the company should be able to benefit from a margin standpoint.

OTHER NEW BUYS AND SELLS

Over the quarter, we also initiated positions in Menicon Co and Kurita Water Industries. We will profile these names in future commentaries.

During the quarter we exited Clipper Logistics Plc.

WHAT IS OUR EAR-TO-THE-GROUND APPROACH TELLING US?

Global Alpha is once again travelling to conferences. The equity markets industry consensus coming out of COVID 19 is that live conferences are required by institutional investors. Therefore, we expect a mix of remote

and live conferences to become the norm. We also expect an increasing amount of non-deal road shows by corporations to our offices. We however expect broker analyst live road shows to decline post COVID as banks and brokerage firms concentrate on remote interactions with their analysts. The team is also preparing reverse road shows where plants and corporate head offices become part of a travelling route.

2022 continues to be filled with inflation and supply chain headlines. Many of our companies are affected and we continue to discuss with them the capacity to source material and implement price increases. Many of our companies have pass through contracts with their customers. The majority of our companies have strong balance sheet and are far from having any interest rate concerns.

As a bottom-up fundamental manager, we do not make material sector or country adjustments to the portfolio as a result of these expectations and maintain a diversified list of holding companies with defensible business models and strong balance sheets that are trading at a discount to their intrinsic value. Our portfolio remains well diversified across the many countries, currencies and industries that compose our benchmarks.

The Global Alpha Team

Sub-Advisor to the Ninepoint International Small Cap Fund

¹ All returns and fund details are a) based on Series F units; b) net of fees; c) annualized if period is greater than one year; d) as at June 30, 2022; e) annual returns are from 03/15/2018. The index is 100% MSCI EAFE Small Cap NR USD (CAD) and is computed by Ninepoint Partners LP based on publicly available index information.

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