Ninepoint Enhanced Equity Strategy

March 2018 Commentary

Investment Team

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Trump administration officials widely seen as key "adults" in the White House tasked with keeping President Trump's impulsive nature in check continue to leave. March ushered in the departure of both Chief Economic Advisor Gary Cohn and National Security Advisor General H.R. McMaster. Trump appears increasingly inclined to no longer seek any expert advice on a wide range of issues including trade, national security, immigration and the ongoing Russia investigation. The unpredictable and often dangerous nature of his outbursts (usually via Twitter but occasionally also impromptu comments to reporters) has elevated market volatility and appears set to stay that way for a prolonged period.

Much of the equity market focus over the past month has been on Trump's escalating rhetoric regarding trade deficits and his proposed tariffs but the tech sector has also been pressured by rising worries over potential regulation. The S&P 500 (USD) dropped 2.5% last month and finished March down almost 1% for the year. A sharp rally in crude oil (WTI was up 5.7% USD) muted the drop in the Canadian equity market as the TSX dropped just 0.2% last month although it was still down 4.5% year to date as of the end of March.

In the Enhanced funds we used the recent market turmoil to take some profits on our put protection. During late March/early April, when market swings were their most violent, our hedges offset nearly 100% of the downside of equity markets on many large down days with several days actually posting positive returns in for the funds (Chart 1&2). While volatility is higher in 2018 than the record lows seen in 2017, theoretically making hedging more expensive, we are finding that market moves are compensating us for the higher costs allowing us the potential to lock in gains in our hedges, something we haven't experienced often through much of the bull market.

Going forward, we feel incremental news on trade conflicts are likely to be in line with the current negative sentiment and as such will likely be less of a bearish catalyst. We have been more bearish on trade risks for some time but now feel the street has caught up to some of the concerns we've had specifically on Chinese trade. Indeed, as a potential positive catalyst, the final rounds of NAFTA in mid-April may end up highlighting that compromise is possible despite the incessant negative rhetoric out of the Trump administration.

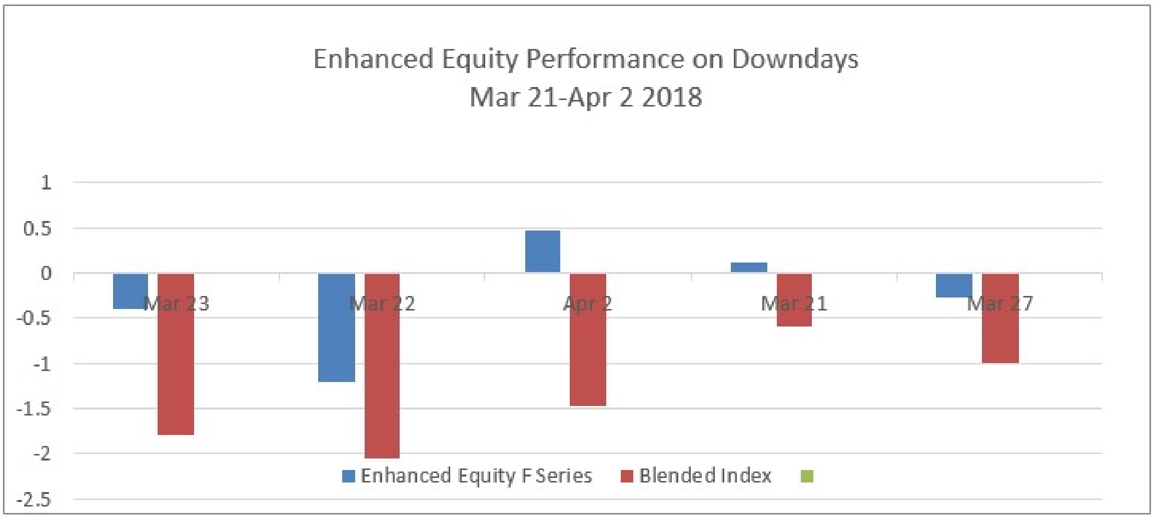
We also continue to see solid Q1 earnings growth for S&P 500 companies as an incremental positive catalyst for equities. Positive catalysts are something we've been lacking subsequent to tax reform passing as markets absorbed higher interest rates, increased trade concerns and a momentum meltdown in large cap technology stocks. At this juncture, we think with these bearish catalysts have been somewhat absorbed (never completely) by markets and the risk reward now skews more positively for equities. As a result, we have reinvested some of the profits from our hedges into purchasing upside call options on the SPY. This shifting of our hedge book allows us to operate with a larger upside capture than would have been case with the initial hedge book while still managing risk to a comfortable level. We have setup our hedges so we can easily adjust how much market exposure we want to take and stand ready to change our more positive positioning if dynamics change.

On the equity front, performance of our individual names was moderately disappointing last month with many of our names reacting to overall downward market pressure without even any underlying exposure to the risk driving the market decline (for example a trade war with China). Financials and Industrials were hit particularly hard last month while energy badly lagged the rise in crude oil prices. That said, we remain very optimistic on our Canadian energy exposure (both producers and service companies) given the very positive price performance of the underlying commodity and our view that oil prices are much more likely to grind higher from here rather than materially lower. Absolute valuations including EV/EBITDA, P/DACF and FCF yield are incredibly attractive now in the energy sector generally and we believe especially on our chosen companies.

As mentioned earlier, we have been actively trading our hedge book to realize some profits, extend expiries and add some upside optionality through calls. The net result is a very attractive upside/downside ratio based on our current portfolio positioning. The current environment remains both volatile and fluid with sharp reversals and large intraday moves. Given the current resident of the Oval Office, we don't expect those trends to break anytime soon.

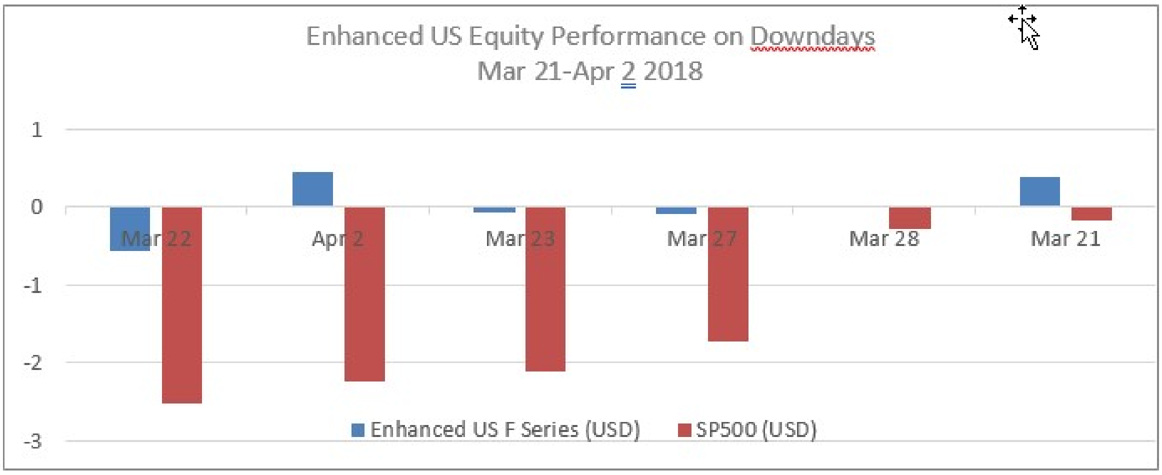
Until next month,
The Enhanced Team

Chart 1



Source: Factset, Ninepoint Partners

Chart 2



Source: Factset, Ninepoint Partners

[1] All returns and fund details are a) based on Class/Series F shares/units; b) net of fees; c) annualized if period is greater than one year; d) as at March 30, 2018; e) inception date for Ninepoint Enhanced Equity Class is 04/16/12. The index for the Ninepoint Enhanced Equity Class; Ninepoint Enhanced Long Short; and Ninepoint Enhanced Long Short RSP is 50% TSX & 50% S&P 500 (CAD) Blended Index and is computed by Ninepoint Partners LP based on publicly available index information. The index for the Ninepoint Enhanced US Equity Class is S&P 500 TR USD and is computed by Ninepoint Partners LP based on publicly available index information.

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