

Diversified Core



# When Small Means Big

THE CASE FOR INVESTING IN  
INTERNATIONAL SMALL CAP EQUITIES

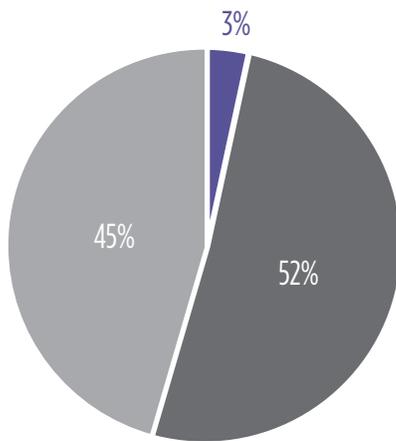


# 1 Address 'Home Bias'

Canada makes up ~3% of the world's investment markets, yet Canadians place 59% of their investments in Canadian securities, and an additional 18% in US securities. Canadian investors face the potential of significant "Home Country Bias" risk and, more broadly, "North American Bias" risk.

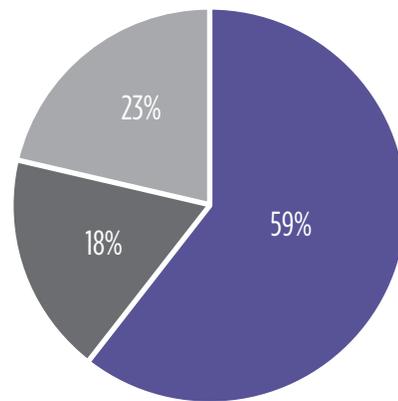
Small-Cap investments that offer exposure entirely outside of North America – for example focused on EAFE markets – may prevent unintended North American concentration, and better diversify a Canadian investment portfolio.

SIZE OF GLOBAL INVESTMENT MARKET



■ Canada ■ USA ■ Rest of World

AVERAGE CANADIAN INVESTOR'S PORTFOLIO



■ Canada ■ USA ■ Rest of World

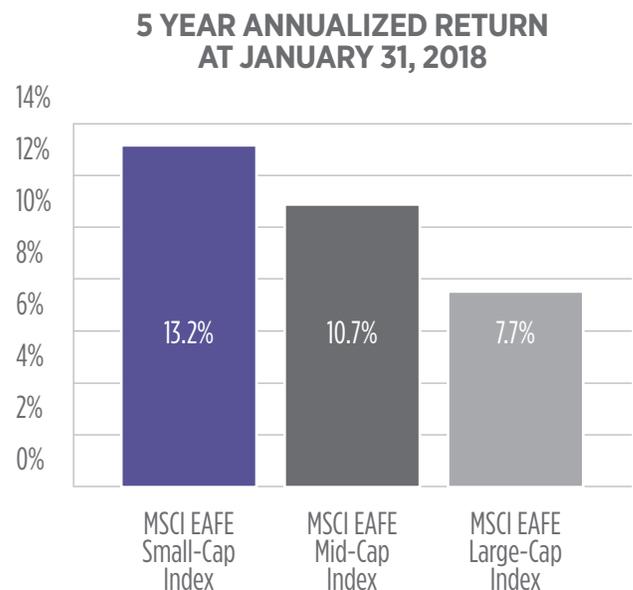
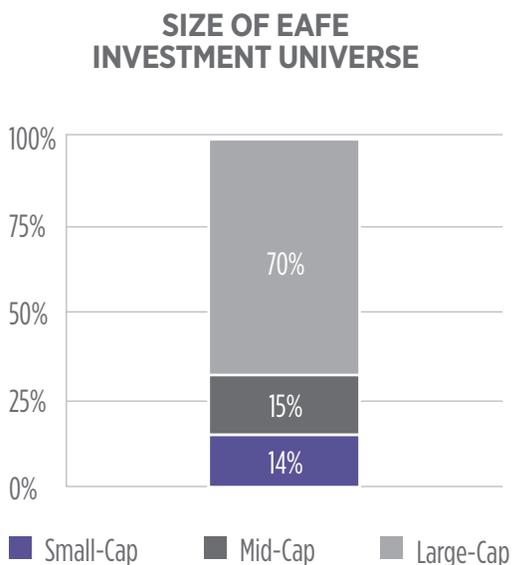
Source: 2016 IMF Coordinated Direct Investment Survey, Russell Global Index, Vanguard..

“ there are 1,167 EAFE small-cap companies with a market capitalization greater than US \$1 billion ”

Source: iShares, MSCI.

## 2 Growth Potential

International small-cap equities are another way to take advantage of the growth potential of small companies. While the international small-cap investment universe only accounts for a small percentage of the international pie (left below), small-cap stocks have provided the biggest opportunity for growth (right below).



Source: Computed by Ninepoint Partners LP based on publicly available index information at January 31, 2018. Small Cap: MSCI EAFE Small Cap Index, Mid Cap: MSCI EAFE Mid Cap Index, Large Cap: MSCI EAFE Large Cap Index.

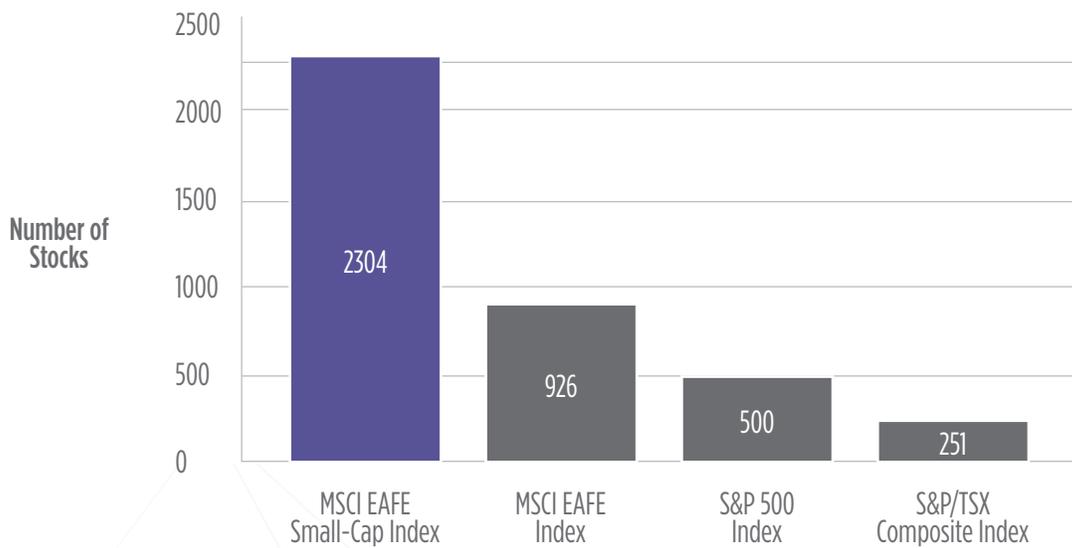
## 3 Not that Small

The average company size in the MSCI EAFE Small-Cap Index is valued at US \$1.2 billion. In fact, there are over 1,100 companies with a market capitalization greater than US \$1 billion. There are only 233 such companies in the S&P/TSX Composite Index, and 49 companies in the S&P/TSX Small-Cap Index.

Many of the stocks in the international small-cap universe are household names in their local market, and some even have global brand recognition.

# 4 An Overlooked Universe of Opportunity

The small-cap investment universe usually offers more choice, and yet tends to get less coverage by investment analysts than larger-cap stocks. This means there is more potential opportunity for active managers to uncover value in stocks that are not on the radar of most investors and analysts.



Source: MSCI, S&P Dow Jones Indices. December 31, 2017.



# 5 Portfolio Diversification

Currently, the major Canadian indices are heavily skewed to the energy, material, and financial sectors, limiting diversification. The international small-cap market provides representation across a broader range of sectors.

# 66%

of the S&P/TSX Composite Index is concentrated in three sectors: energy, financials and materials.

Source: S&P Dow Jones Indices at December 29, 2017.

## SMALL-CAP INDEX COMPOSITION

	MSCI EAFE Small-Cap	S&P/TSX Composite Index
Energy	2.5%	19.7%
Materials	9.5%	11.5%
Industrials	21.4%	9.5%
Consumer Discretionary	16.1%	5.4%
Consumer Staples	7.0%	3.7%
Health Care	6.7%	1.0%
Financials	11.5%	34.6%
Information Technology	11.4%	3.2%
Telecommunication Services	1.4%	4.7%
Utilities	2.0%	3.8%
Real Estate	10.4%	2.9%
<b>TOTAL</b>	<b>100%</b>	<b>100%</b>

Source: MSCI and Thomson Reuters Datastream at December 31, 2017.

“ Canadian indices are heavily skewed to the energy, material, and financial sectors ”

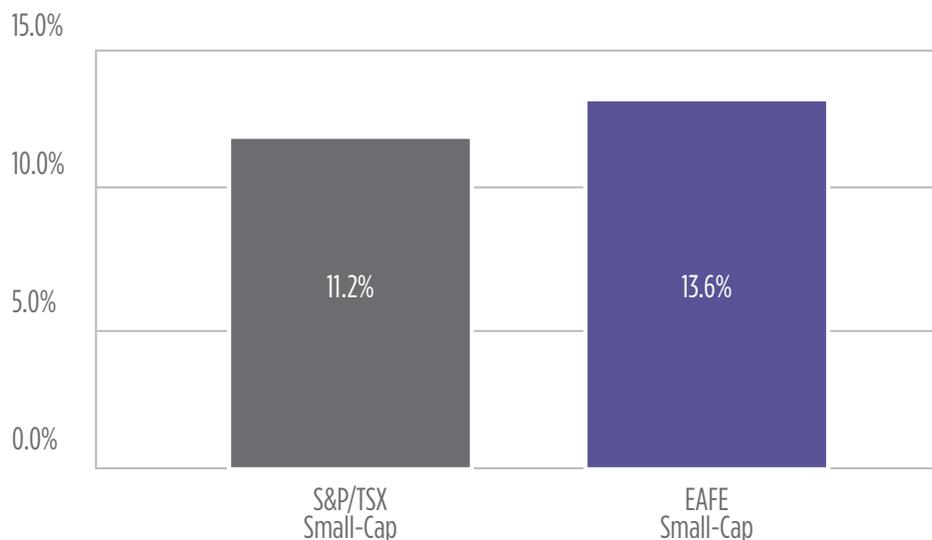
# 6 Active Management Matters

The International small-cap fund category is a category in which active fund managers can pose a strong challenge to ETFs. Fund managers with a higher active share have a greater opportunity to outperform their benchmark by providing diversification across sectors and identifying companies whose share price does not fully reflect their true value or growth prospects.

## WHAT IS ACTIVE SHARE?

Active share measures the percentage of stock holdings in a fund that differ from the benchmark index. Higher active share means a more 'active' fund manager.

### HIGHER GROWTH EXPECTED FROM INTERNATIONAL SMALL-CAP EQUITIES: ESTIMATED 2-5 YEAR EARNINGS-PER-SHARE (EPS) GROWTH



Source: iShares, at January 31, 2018.

## Not Without Risks

Like any investment, international small-cap equities are not without risks. While active managers can mitigate some of these risks through research and careful selection of individual stocks, investors should consider the following:

### LIQUIDITY RISK

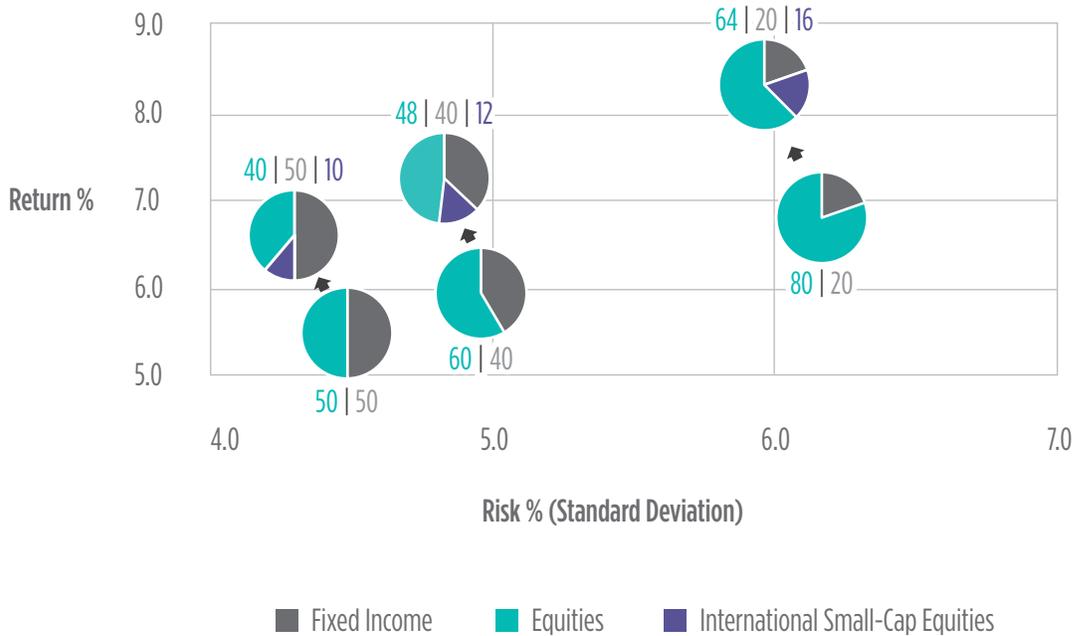
It can take longer to trade a small-cap stock compared to a large-cap stock. Small-cap stocks also tend to be more sensitive to changes in market sentiment such as a change from a bullish to bearish outlook for a particular sector, which can contribute to more volatile performance.

# 7 Long Term Results

Over the long term, a conservative allocation to international small-cap equities in a diversified portfolio has enhanced returns without added risk.

## ILLUSTRATIVE EXAMPLE:

### EFFECT OF ALLOCATING 20% OF A PORTFOLIO'S EQUITY WEIGHTING TO INTERNATIONAL SMALL-CAP EQUITIES<sup>1</sup> (5-YEAR PERIOD)



Source: Data calculated by Ninepoint Partners LP based on available index information at January 31, 2018.

<sup>1</sup>The information provided is for illustrative purposes only and does not represent the performance of any particular investment. It is not possible to invest directly in an index. Fixed income is represented by Canadian bonds (FTSE TMX Canada Universe Index), equities is represented by Canadian equities (S&P/TSX Composite Index), and small-cap (MSCI EAFE Small-Cap Index).

## INFORMATION FLOW

While higher insider ownership aligns with the interests of investors, it can also lead to less transparency and lack of flow-of-information that would be more common with large-cap investments.

## LARGE COMPETITORS

Small companies do not have the same access to credit markets as larger companies because of their size. This can sometimes limit a small company from realizing its potential at the expense of a larger competitor.

# What is 'Market Cap'?

Market capitalization (aka market cap) is the market value of all a company's outstanding shares. It's calculated by taking the market price of a share and multiplying it by the number of shares outstanding. While definitions vary, large-cap firms are generally valued at over \$16 billion and small-cap firms under \$6 billion, leaving mid-cap firms to fall in between.

Market Cap is typically divided into three categories by size:

## LARGE-CAP

Firms that tend to be leaders in their market fall into this category. They are established businesses with the financial resources to weather market downturns, making them less risky investments but may offer less room to grow.

## MID-CAP

As the name implies, a mid-cap stock falls between a large-cap and small-cap stock in size.

## SMALL-CAP

All the largest and most well-known companies started out as small companies in this category. Small-cap companies can range from start-ups, who recently went through their initial public offering (IPO), to companies that are major players in their domestic market.

**To learn more about International Small Cap investing or the Ninepoint International Small Cap Fund please contact your Financial Advisor.**



[www.ninepoint.com](http://www.ninepoint.com)

The Fund is generally exposed to the following risks. See the prospectus of the Fund for a description of these risks: commodity risk; concentration risk; credit risk; currency risk; derivatives risk; exchange traded funds risk; foreign investment risk; inflation risk; interest rate risk; liquidity risk; market risk; regulatory risk; securities lending, repurchase and reverse repurchase transactions risk; series risk; short selling risk; small company risk; tax risk.

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