Market Commentary
Fourth Quarter 2017

Signature Diversified Yield II Fund

In late 2016, government bond yields and risky asset prices jumped higher after the Donald Trump U.S. election win. In the fourth quarter of 2017, government bond yields again turned higher on the prospects of tax reform. With a sustained global economic expansion, commodities were also stronger, yet modest wage growth kept a lid on inflation. The credit market was largely benign despite many pundits' desire to label the credit markets as "late cycle". The default rate continued to fall in the quarter and corporate credit quality improved, but more by way of earnings growth than debt reduction, a trend we believe continues in 2018. High-yield bond spreads were flat on the quarter. Where sector selection drove 2016 returns as the commodity complex recovered, sector returns were more uniform in 2017 and security selection became more important; a trend we also believe continues in 2018.

Performance for the high-yield bond portion of the fund was slightly hindered over the quarter as strong security selection was offset by the impact of the stronger Canadian dollar. Contributing positively to performance was the fund's positions in financials, technology, and energy. Detractors from relative performance were the retail sector and a few specific bonds subject to idiosyncratic risk. New positions in the fund include longer-maturity Teck Resources bonds. Positions leaving the portfolio included the Pabst Blue Ribbon term loan and bonds of Calpine and Kindred Healthcare.

Performance for the fund's infrastructure holdings were generally positive through the quarter. Transportation infrastructure such as airports, ports and toll roads benefited from the generalized global growth. Volumes in these areas tend to correlate with economic performance and commercial activity. We expect more consolidation in this space following the ongoing acquisition attempt of Spanish toll road operator (and Signature holding) Abertis. We do, however, feel that the expectations – and likely occurrence – of rising global interest rates will restrain the valuation on these types of assets.

Telecommunications infrastructure, including tower, fibre and data centre companies all continued to benefit from higher consumer data consumption and the low interest rate environment during the quarter. In this sector, we remain cautious, however, as potential telecommunication consolidation (reducing the need for growth in tower requirements) could reduce growth expectations in securities with high valuations.

In midstream energy infrastructure, we feel comfortable that growing North American volumes of oil and gas production will continue to support accretive investments and growing cash flows for fund holdings such as Williams Companies, Enbridge and Kinder Morgan. While Canada and the

United States each share the underlying growth, the valuation setup for the U.S. is significantly more favourable due to a weak 2017 performance in the U.S. midstream space (due to money exiting the sector to more growth-oriented industries, and uncertainty around tax reform's impact on the tax-advantaged Master Limited Partnership sector). We believe the value aspects of this sector will show through in 2018 and are comfortable that risks around commodity prices and technological change are generally reflected in valuation levels as we enter 2018.

In aggregate, we believe that infrastructure will continue to benefit from predictable cash flows, irreplaceable assets with monopoly characteristics, and low volatility. Valuations will be key as investors balance strong underlying performance with an expectation of higher cash flow discounting from increased government bond rates.

Our forecast for 2018 sees further spread tightening from both investment-grade and high-yield bonds, supported by synchronized global growth, cautious central banks, and a declining default rate despite pockets of weakness in retail, generic pharmaceuticals, and wireline telecommunications. This spread compression should be sufficient to drive positive returns despite three to four rate hikes expected from the U.S. Federal Reserve in 2018, just like last year. There are wildcards, like Fed policy under the new leadership of Jerome Powell, the future of the European Central Bank's stimulus program, record low volatility across asset classes, groupthink and complacency, and headwinds, principally valuations.

Current spreads (and prices) are on the expensive side of historical averages but not irrational. U.S. tax reform should turn out to be credit positive as lower corporate tax rates boost cash flows. This will be partially offset by increased expenses on the elimination of interest deductibility, but the net effect raises the after-tax cost of debt. Higher after-tax cost of debt should lead to some deleveraging, especially since borrowers' cost of equity has decreased with stocks at or near record highs. Foreign profit repatriation is also a slight credit positive, although there seem to be more beneficiaries in large-cap technology and pharmaceutical investment-grade names than in high yield and proceeds are probably directed to share repurchases and mergers and acquisitions than debt reduction. All told, what companies do with this largesse will determine the trajectory of credit markets in later years.

In our view, 2005 may be the best analogue for 2018. By 2005, the Fed was well along a predictable hiking path, the economic expansion was reaching middle-age, and credit spreads had already come in dramatically. Further, like 2005, we are beginning to see new issuers coming to market with aggressive leverage and looser terms, and we are inclined to believe deregulation at the Securities and Exchange Commission, Fed, and Consumer Financial Protection Bureau likely encourages further credit excesses, but again, in later years. What made 2005 unique however was the surprise downgrade of GM and Ford from investment grade into high yield. In 2018, we think the positive tone persists, but we are watching for the surprises or issues no one is watching. We view higher

idiosyncratic risk, and the requisite importance of security selection as a marginal positive; an indication of market discipline absent when the high-yield bond market was at similar valuation levels in 2013 and 2014. Taken together, a mid-single-digit return driven much more by carry than price appreciation is possible for high-yield bonds in 2018.

Class F Returns (in %) as at December 31, 2017	Year-to-date	1 year	3 year	5 year	10 year	Since inception	Inception date
Signature Diversified Yield II Fund	4.9	4.9	4.2	6.7	N/A	6.9	2/15/2011

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