CI Global Equity Alpha Private Pool
First-quarter 2019 Commentary

Market Overview

Following a difficult fourth quarter of 2018, equity markets reversed course sharply in the first quarter of 2019. In U.S.-dollar terms, global stocks (as measured by the MSCI All Country World Index (ACWI)) rose 12.2% over the quarter as investors embraced signs of progress on U.S.-China trade negotiations while central bankers affirmed a continued accommodative stance on monetary policy.

In U.S.-dollar terms, all major global equity markets delivered a positive return. The U.S. market (as measured by the S&P 500 Index) was up 13.6%, outperforming international developed markets (as measured by the MSCI EAFE Index, which was up 10.0%) and developing markets (as measured by the MSCI Emerging Markets Index, which was up 9.9%) in the quarter. On a geographic basis, stocks of companies based in China were the top performers, in aggregate, for the quarter as investors hoped progress would be made on trade talks between China and the U.S. and that China's pledges to further liberalize its domestic stock market to foreign investors would be seen through. High-profile initial public offerings (IPOs) helped increase interest in the tech sector with Lyft, Inc., the ride-hailing competitor to Uber Technologies Inc., coming to market with its IPO in late March.

While equity markets enjoyed a recovery, the global economy continued to show signs of slowing growth. China felt the impact of the trade war with the U.S. with its exports slowing, but trade wars are not fully to blame as exports slowed for Europe and Japan, as well as for the U.S. Many countries/regions have noted a slowing trend in global trade that has pressured growth, including Hong Kong, Japan, South Korea, France and Germany. Uncertainty over Brexit has not helped trade either as companies have delayed, diverted or halted investment within the U.K. and across the European Union. Recent data from the U.S. shows the U.S. economy is experiencing a slowdown as the economic boost from the 2017 tax cuts has faded. Consumer spending, which makes up approximately 70% of U.S. gross domestic product, and factory output have been more muted recently.

The bond market is signalling a slowdown in growth as well. Within the U.S., short-term yields have risen above long-term yields, resulting in an inverted yield curve, which for many investors indicates the risk of a recession is rising. Fixed-income investors pushed the yield on the 10-year U.S. Treasury down to levels not seen since 2017 amidst concerns over global growth.

In Europe, bond yields once again turned negative. For the first time since 2017, the German 10-year government bond yield fell below zero. The total amount of global government debt with a yield below zero has increased to over US$10 trillion, up from a low of US$5.7 trillion in early 2018.

From an earnings perspective, companies are facing a slowdown as a result of moderating global growth and tariff concerns. As growth slows, companies are also finding it harder to pass along the impacts of rising labour, transportation and raw materials costs to customers through price increases. In the U.S., earnings are also being dampened as some of the favourable effects of the 2017 tax cuts roll off. Broadly, corporate America is facing a year-over-year earnings contraction for the first time since 2015. Given the economic slowdown, it may be harder to justify elevated stock valuations as optimism around rising corporate earnings fades. However, offsetting this earnings concern is the continuation of low interest rates.

Stock buybacks have been a major contributor to rising equity markets over the past decade, particularly in the U.S. In 2018, U.S. companies spent a record US$806 billion on stock buybacks, which eclipsed the prior record of US$589 billion set in 2007. Corporate balance sheets have added leverage as the buybacks have been partially financed with low-cost debt. Recently though, buybacks have become politically contentious in the U.S. as politicians from both major parties have pushed the U.S. Securities Exchange Commission to restrict or eliminate them in an effort to encourage companies to invest more in their operations.

Fund Holdings

Holdings of CI Global Equity Alpha Private Pool (the "Fund") during the first quarter of 2019 included Booz Allen Hamilton Inc.; Koninklijke DSM N.V.; Altran Technologies S.A.; HeidelbergCement AG; Schneider Electric SE; Criteo S.A.; Sony Corp.; Covetrus, Inc.; Henry Schein, Inc.; and DS Smith PLC.

Portfolio Activity

During the quarter, DS Smith and Thule Group AB were new purchases, while BTG PLC, Covetrus and Sony, a Japan-based multinational diversified corporation, were outright sales.

DS Smith is a leading provider of recycled corrugated packaging in Europe. The company has a strong track record of acquiring competitors and creating value in this fragmented market. DS

Smith made its first move into the U.S. market in 2017 with the acquisition of Interstate Resources Inc.

Thule Group is a global market leader in a number of product categories, including roof racks, roof boxes and bike racks for the car, camera bags, and multisport and bicycle trailers. The company is also growing rapidly in product categories such as sport bags and suitcases, and jogging strollers.

BTG is U.K.-based global specialist health care company that operates through three business segments: interventional medicine, specialty pharmaceuticals and licensing. BTG was sold from the Fund's portfolio after news that the company agreed to be acquired by Boston Scientific Corp.

Covetrus resulted from the spinoff of Henry Schein's Animal Health business and the subsequent merger with Vets First Choice LLC. Covetrus was sold from the Fund's portfolio when the company's shares were received due to ownership in Henry Schein.

Outlook

There are a multitude of macro-related issues that one could be concerned with currently, and we are cognizant of them as this is the environment in which companies operate. However, our strength lies in our ability to identify profitable companies versus attempting to forecast macroeconomic movements or the magnitude or direction of interest rates or markets. We continue to believe owning a concentrated, high-conviction portfolio of differentiated and sustainable businesses that are acquired at reasonable valuations is the best way we can deliver attractive long-term returns for the Fund. We will look to take advantage of future mispricing, volatility and irrational behaviour given our long-term horizon and expectations of increased volatility.

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