MARRET INVESTMENT GRADE HEDGED STRATEGIES FUND: Class F, CAD
Commentary for December 2018

MARRET ASSET MANAGEMENT INC.

Fund Stats

Date of Inception	Sept. 30, 2010

PERFORMANCE	As at Dec 31, 2018
Since Inception	4.55%
Month to Date	(0.38%)
Year to Date	(0.30%)
1 Year	(0.30%)
3 Year	4.05%
5 Year	4.08%

Source: Marret Asset Management Inc. December 31, 2018

Market Developments

In many respects, financial market price action in the month was a continuation of November. Global growth momentum, trade tensions and geopolitical uncertainties continued to shake market confidence. Risk assets remained under pressure with seasonal illiquidity and an urgency for risk aversion only adding to the negative sentiment. Major global stock indices declined 3% to 10% over the month.

Investment grade corporate credit spreads widened further in December marking the third consecutive month of this trend. Based on the Bloomberg Barclays Aggregate Corporate Average OAS indices, investment grade corporate credit spreads widened 16, 15, 3 and 1 basis point in the U.S., Canada, Europe and UK markets. The outperformance in Europe and the UK is notable, but these markets underperformed significantly in earlier periods. For the year, credit spreads were 60 and 52 basis points wider in the U.S. and Canada, 66 wider in Europe and 55 higher in the UK. Approximately 70% of the widening in credit spreads across these markets, took place in the final quarter of the year. Investment grade corporate credit spread performance, was vastly inferior to even our worst case scenario (as outlined in our 2018 Outlook), which forecast a 45% probability of a 15 to 25 basis point widening.

Fund returns for the month were -0.38%% versus +1.06% for the FTSE/TMX All Corporate Bond Index. This is a long only Canadian corporate bond index, whereas the Fund invests long/short across U.S. Canadian and European investment grade corporate bonds on an interest rate hedged basis. For the year, Fund returns are -0.29% versus +1.10% for the benchmark.

Market Outlook

In the final quarter of 2018, we expressed great concern about the vulnerability of risk assets and how much tightening was priced into interest rate markets. We warned that stocks and credit were overvalued and that North American Government bond forward markets, were pricing in levels of tightening beyond our view of the terminal rate. Our presentation around this thesis was called “The End is Near”. Given the corrections in markets we have witnessed over the past few months, one might ask the question, “Are we there Yet”. In other words, have risk and rates markets returned to fair value? In our view, further corrective price action in markets is a high probability. This view is based on fundamentals, technicals and market positioning which are summarized below.

Fundamentally, our greatest consideration is always the trajectory of global growth. Global growth peaked in the fourth quarter of 2017 and there are few signs that economic growth is stabilizing. The world’s two largest economies, the U.S. and China, are continuing to slow – China due to trade tensions and the U.S. as Government spending is expected to provide less stimulus. Commodity price weakness is now pressuring business investment spending, and this is taking a toll on growth prospects in emerging markets and countries like Canada and Australia. Europe of course, has a myriad of problems which are creating economic uncertainty such as Brexit, populism and a weak banking system. If you add to this, high Government and corporate debt loads as well as shrinking central bank balance sheets, we find it difficult to project a constructive global economic growth backdrop.

Technically, a significant amount of chart damage has occurred. We are always cautious to jump to technical conclusions when the price action occurs during periods of reduced liquidity such as the last few weeks of December. As a result, we look for consecutive daily closes along with weekly closes below important support levels before we conclude that short, intermediate and long term trend changes have taken place. There is no doubt that the short and intermediate technicals have turned bearish for risk assets and bullish for interest rates. If the S&P 500 spends a full week below 2540-45 area and the ten year U.S. Treasury futures contract, a full week above 120-27, we would suggest that long term reversals have occurred, likely pointing to a recession scenario.

Positioning across risk assets continues to be overweight. This is due to years of low interest rate policy and central bank balance sheet expansion. This has led to considerable growth in some risk asset markets while regulatory policy has reduced the ability for market makers to provide liquidity. We believe this is a very unhealthy combination which can only add to volatility. Additionally, we are concerned that risk has been forced into weak hands making it vulnerable to forced liquidation.

The macro-economic and technical backdrop outlined above is not a positive one for long credit positioning. In short, it depicts weak fundamentals and deteriorating technicals. Our base case for credit spreads, to which we assign a 45% probability is that spreads widen 25-40 basis points. This assumes moderating global economic growth and earnings, alongside of benign central bank monetary policy and a reduction in net new issuance across credit markets. Our best case scenario (10% probability) calls for a 25 basis point tightening in credit spreads. This outcome would need to be based on a correction from end of 2018 oversold levels and the factors that we outline below that would be necessary to extend the economic cycle. Our worst case scenario (45% probability) calls for a 50 to 75 basis point widening in credit spreads on significantly weaker economic growth (but not recession), continued heavy new issuance supply and refunding and little corporate responsiveness to deleveraging.

Given the market outlook expressed above, it is fair to ask, are we too “beared” up about economic growth and risk assets? There is no doubt that the consensus view on risk assets is now to be cautious. We note however, that we were bearish on risk well before the consensus, so it appears the market is just catching up with us. Our views on economic growth and an extension of the current economic cycle would adjust if some of the following changed:

- The policies currently being put in place in China to stimulate domestic demand and encourage infrastructure spending stabilize growth in the 6.0% to 6.5% area.
- There is a comprehensive agreement between the U.S. and China on trade policy.
- The U.S. Federal Reserve limits the fed funds terminal rate to 2.50% to 2.75%, essentially a FED pause.
- Commodity prices stabilize and oil (WTI) trades above $55.

A combination or all of these events in aggregate, would provide a positive impulse to sentiment and global growth. The question then becomes, would it be just short-term or have a lasting impact beyond 2020?

On interest rates, we believe the headwinds which negatively impacted fixed income returns in 2018, are largely behind us. We expect central bank policy to be on hold but look for high volatility in Government bond yields. For the first half of the year, we look for ten year Government bond yields to trade in a range of 2.55% to 3.05% (U.S.), 1.75% to 2.20% (Canada), 1.10% to 1.60% (UK) and 0.10% to 0.50% (Germany).

The two risks to our rather benign outlook on interest rates are:

- Markets inability to absorb increased U.S. Treasury supply due to deficit funding. Interest rates forced higher as the U.S. competes for scare capital.
- Higher growth and inflation in the Eurozone which causes the ECB to tighten monetary policy or fear the ECB is falling behind the curve.

* The strategy aims to generate better risk-adjusted returns over the cycle compared to long only mandates, making the FTSE Canada All Corporate Bond Index a suitable Canadian hedge fund index to compare against. There is no Canadian hedge fund index for a global long and short leveraged fund and most corporate fixed income assets in Canada are managed relative to this index. Provided that the fund's mandate enables flexibility on geographies, strategies, and securities, we selected this index as the most representative amongst those available. The Fund invests in long and short bonds while employing currency hedging and a leverage strategy, whereas the index is a long only corporate bond index.

Performance (%)	Jan-18	Feb-18	Mar-18	Apr-18	May-18	Jun-18	Jul-18	Aug-18	Sep-18	Oct-18	Nov-18	Dec-18
Marret Investment Grade Hedged Strategies Fund	0.80%	-0.40%	-0.47%	0.37%	-0.38%	-0.24%	0.88%	0.27%	0.18%	-0.43%	-0.49%	-38%

IMPORTANT DISCLOSURES

The offering of units of the Fund is made pursuant to its Offering Memorandum only to those investors who meet certain eligibility and minimum purchase requirements. Eligible investors should read the Fund's Offering Memorandum before investing. Investment funds are not guaranteed, their values change frequently, and past performance may not be repeated. Commissions, trailing commissions, management fees and expenses all may be associated with investment funds.

The indicated rates of return are the historical annual compound total returns net of fees (except for figures of one year or less, which are simple total returns) including changes in security value and reinvestment of all distributions and do not take into account sales, redemption, distribution or optional charges or income taxes payable by any securityholder that would have reduced returns.

Series F securities are generally only available to clients who have a fee-based account with their dealer. MAMI does not pay trailing commissions to dealers who sell Class F securities, which means MAMI can charge a lower management fee compared to Class A of the same Fund. A lower management fee may positively impact the performance data shown when compared to Series A.

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The comparison presented is intended to illustrate the Fund's historical performance as compared with the historical performance of the FTSE Canada All Corporate Bond Index. There are various important differences that may exist between the Fund and the stated index that may affect the performance of each. The objectives and strategies of the Fund result in holdings that do not necessarily reflect the constituents of and their weights within the comparable indices. Indices are unmanaged, and their returns do not include any sales charges or fees. It is not possible to invest directly in market indices.

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