TSX **DIVS**

SPECIAL COMMENTARY

Evolve Active Canadian Preferred Share Fund

DIVS seeks to provide holders of Units with stable income and long-term capital appreciation by investing primarily in a diversified mix of preferred shares of primarily Canadian issuers, in addition to U.S. and international issuers.

As at March 17, 2020

ETF TICKER: DIVS (Unhedged)
MUTUAL FUND FUNDSERV CODE: EVF100 (Class F); EVF101 (Class A)
SUB-ADVISOR: Foyston, Gordon & Payne, Inc.

FOYSTON, GORDON & PAYNE INC.
INVESTMENT COUNSEL

Active management in Canadian Preferred Shares continue to be an attractive investment opportunity. Foyston, Gordon & Payne Inc. has managed Canadian Preferred Shares since 2012 and the FGP Preferred Share Fund since November 22, 2015.

UPDATE:

In line with most risk assets, preferred shares have had a severe negative reaction to the continued COVID-19 news headlines and the proliferation of panic. Additionally, the rate cut by the Fed and the BoC, which was an effort to calm markets, actually spooked investors and sentiment worsened. Further to that a price war in oil erupted over the weekend and added fuel to the fire that drove equities and prefs down and credit spreads on both corporate bonds and prefs wider.

Pref spreads are now roughly +650 bps which is about 200 bps to 300 bps wider over the last few weeks. From a price level, preferred shares are lower than during the 2008/2009 crisis and lower than 2015/2016 when the global economic landscape reflected a pending prolonged recession.

We have conducted extensive and comprehensive analysis of the companies that we own, and others that are on our watch list of names that we would like to hold at the right price. We view volatile periods like this as opportunities to take advantage of short-term price fluctuations. In that vein, we have been opportunistically investing during this period of volatility.

ECONOMIC UPDATE:

New year optimism faded in February amid the growing impact, both human and economic, of the ongoing coronavirus outbreak. As the outbreak spreads the day-to-day fear and uncertainty will almost certainly impact economic releases in the months to come. Overall growth in China for the first quarter of 2020 will be lower, it is only a question of magnitude. Population lockdowns, business shutdowns, and travel restrictions into the country will all have a dampening impact on GDP growth. The longer all these factors persist the greater the chance that global trade and industrial supply chains are impacted which would further weaken global growth prospects in the short-to-medium term.

MARKET UPDATE:

Commodity prices turned sharply lower at the end of February amid concerns the ongoing coronavirus outbreak will lead to weaker demand for raw materials, fuel and food across the globe. Softer energy markets, slow global growth

and a general flight-to-quality had bond yields heading lower once again. The benchmark U.S. 10-year yield declined by a material 36 basis points in February to end the month at 1.16%. Yields on the comparable Canadian issue also moved lower by a more modest 14 basis points during the month to 1.13%. This decline in yields resulted in positive returns for the overall bond market.

For most of the month global equity markets remained calm and shrugged off the developing risks to global growth. However, this abruptly changed in the final week of February as equity markets globally fell by record levels. The preferred share market continued its recent trend of reflecting negative equity sentiment and fell. Other risk assets responded less drastically than equity markets. Canadian corporate credit spreads for example have yet to see significant widening which, combined with the declining government yields, has translated into positive returns.

PORTFOLIO UPDATE:

The portfolio was stable for most of the month but had a weak finish to February as strong negative sentiment towards risk assets translated into broad selling in the Canadian preferred share market. The portfolio's strategy remains consistent and our outlook for preferred shares continues to be positive, largely driven by the significant yield advantage preferred shares offer relative to other fixed income options available in the market today.

Our portfolio offers an attractive yield of 6.1% providing investors with an additional yield of 370 basis points above the FTSE Canadian Corporate Bond Index. This yield should *increase* slightly over the next two years, *even in the absence of an upward move in key interest rates* as the reference rate remains *modestly* above the average (ultra-low) level seen during the 2015 and 2016 time period.

Furthermore, the primary driver of performance through a cycle for this strategy is security selection, not interest rate anticipation as preferred shares have demonstrated little to no correlation to changes in interest rates over time. Our portfolio is constructed based on thorough credit research and associated valuation methodologies to identify undervalued securities relative to the market. The portfolio's strategy continues to focus on lower risk companies and credit risk-adjusted returns.

Preferred shares continue to trade at historically low levels and offer yields and spreads that are exceptionally wide relative to other income producing assets. These factors should drive outperformance for the asset class going forward. We see meaningful upside in our portfolio over the medium-term and expect this asset class to revert to a more properly priced environment. However, in the short-term, stability in economic data will be challenged as the global economy works through the impact of the coronavirus on GDP growth.