

Q3 report

Largely, during the third quarter, equity markets in the U.S. and Canada have moved sideways with the S&P 500 Index finishing the quarter up one percent and the one-year return sitting at 2%.

Beneath these numbers, we saw the market rotate throughout the quarter with momentum and growth industries such as, semi's, home builders, and transports pull back while value names such as Real Estate Investment Trust (REITs) and utilities move up. As a result, more conservatively positioned Pools such as the Barometer Tactical Income and Barometer Tactical Balanced pools, for the most part, were inline with overall markets, whereas, more growth-oriented pools were more closely aligned with growth sectors. As we head into the final quarter of the year, we see a renewed bid under these cyclical sectors – a benefit to our more growth-oriented Pools.

On the macroeconomic front, the Federal Reserve began to cut interest rates this quarter, and while the accommodative monetary policy does abate some

investor fears, generally the effect of this stimulus is not seen in the economic data until about six months from the date of the cut. And as some manufacturing data began to slow, we see a much higher probability of further rate cuts.

Gold continued to rally through July and August before retracing some gains in September, finishing the quarter up 12%. In a world with over \$15trn in debt with negative yields, gold begins to exhibit a relatively positive cost of carry which becomes a more attractive place to park capital. In addition to being considered a safe haven asset that holds its value through an economic downturn. As investors become increasingly concerned with the potential for a recession globally or specifically in the U.S., they have allocated capital to gold.

Oil finished the quarter down roughly eight percent. While it looked like the increased geopolitical risk in Saudi Arabia seen in September might have caused a rally, this did not materialize, and oil finished the quarter below the level it traded at before the attack.

Fixed income markets continued to rally as global investors piled into bonds. Despite a sharp selloff at the beginning of September as yields spiked, investors have demonstrated continued willingness to accept lower yields for the risk profile offered by bonds. Credit conditions remain healthy and spreads are benign.

The U.S. consumer, which represents approximately 70% of the U.S. economy (and 17% of

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the global economy) continue to be strong. This coupled with low delinquencies, growing wages, strong spending on durable goods, improved existing home sales, and historically low employment levels provide underlying strength to the economy despite some slow downs in manufacturing. In our opinion, the market has been discounting this slowdown throughout the quarter.

Portfolio Updates

Barometer Tactical Balanced Pool

Over the course of the third quarter, the Barometer Tactical Balanced Pool benefitted most positively from exposure to the real estate sector. As interest rates continue to trend down, REITs have access to cheaper capital that can be used to finance new projects or to refinance debt at cheaper rates. Exposure to the sector increased from approximately seven to nine percent, as we added Granite REIT (GRT.UN:TSX) which benefits from the higher multiples investors are giving to industrial REITs due to some high profile buyers of large portfolios in the market such as Blackstone Group Inc. (BX:NYSE). RioCan REIT (REI.UN:TSX) was sold out of the portfolio as it began

to underperform its peers. The pool also saw strong performance from the materials sector based on the strength of gold during the quarter. Barrick Gold Corp. (ABX:TSX) and Franco-Nevada Corp. (FNV:TSX) performed well and contributed positively to performance. American Water Works Company Inc. (AWK:NYSE) is a name that continues to work very well in the portfolio, their domestic U.S. focus and stable cash flows are attractive for investors looking for safe places to allocate capital in an environment of increasing uncertainty.

The pool saw some weakness in its exposure to the consumer discretionary sector, specifically in its exposure to Amazon.com Inc. (AMZN:NASDAQ) It was added to the portfolio during the quarter as it began to outperform the broader market on a relative basis but was sold out of the portfolio in August as concerns by investors about the health of the global economy started to impact Amazon's premium multiple.

Barometer Tactical Income Pool

During the third quarter, the Barometer Tactical Income Pool most positively benefitted from

exposure to the consumer staples sector. As a traditionally defensive sector, consumer staples names tend to be insulated from market volatility as they generally have defensible, proven business models with steady fundamentals. Within the sector, the pool owned Procter & Gamble Co. (PG:NYSE), Estée Lauder Companies Inc. (EL:NYSE), Costco Wholesale Corp. (COST:NASDAQ), and Mondelez International Inc. (MDLZ:NASDAQ), and all of these names contributed positively to performance during the quarter. Procter & Gamble Co. and Estée Lauder Companies Inc. especially continue to benefit from a healthy global consumer. The pool's exposure to the real estate sector continues to perform well and contribute positively to performance. During the quarter the pool added Canadian Apartment REIT which still has a high quality portfolio of condos in major Canadian urban centres and has a healthy gap double-digit percentage gap between in-place rents and market rents which indicates that any sort of churn in tenants should have a material benefit to the trust.

Throughout the quarter, the

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pool's performance was impacted negatively by exposure to the industrials sector as some of the names in this sector exhibited some idiosyncratic weakness. Heico Corp. (HEI:NYSE) an aerospace products manufacturer underperformed and was sold out of the portfolio. Barometer has been underweight the health care sector throughout 2019. In the third quarter, the Income pool's only exposure to the sector was in Boston Scientific Corp. (BSX:NYSE) which was sold out of the portfolio after forming a long technical base and breaching to the downside.

Barometer Equity Pool

The Barometer Equity Pool benefitted from exposure to the communication services sector during the quarter. Exposure to the sector was taken from approximately 14% to 8% as profits were taken on Snap Inc. (SNAP:NYSE), New York Times Co. (NYT:NYSE) and Corus Entertainment Inc. (CJR.B:TSX) which were sold out of the portfolio. Industrials sector exposure also contributed positively as Verisk Analytics Inc. (BRSK:NASDAQ) and Air Canada (AC:TSX) remain fundamentally strong and exposed to powerful secular trends. Over the course of the quarter, materials

sector exposure was taken from approximately 11% to 0% as the rally in gold paused in September. Specifically within the materials sector, Agnico Eagle Mines Ltd. (AEM:TSX), and Barrick Gold Corp. (ABX:TSX) performed exceptionally well.

At the beginning of September, many of the pool's names in the information technology sector were negatively impacted by the abrupt reversal in factor performance due to a flight from momentum into value. The pool was stopped out of some names including Lightspeed POS Inc. (LSPD:TSX), the Canadian payment processing company. While Lightspeed contributed negatively to the pool's performance during the quarter, ownership of the security has still added to the pool's performance on a year-to-date basis. This shift also had an outsized impact on some software names like Okta Inc. (OKTA:NASDAQ) and CyberArk Software Ltd. (CYBR:NASDAQ), so these names were sold as well.

Barometer Global Macro Pool

Throughout the course of the third quarter, the Barometer Global Macro Pool benefitted from exposure to the information technology sector, specifically exposure to the semiconductor

industry. As one of the most cyclically sensitive sectors, it outperformed as demand for the most basic building blocks for many powerful themes including cloud computing and 5G bottomed and started to rally. The pool continued to benefit from exposure to solar energy. The pool also held positions in U.S. homebuilders throughout the quarter. As with semiconductors, strong positive performance from the homebuilders is another sign of strength in cyclically sensitive sectors. Solar energy is a theme we continue to favour and one that certainly has runway as the technology improves and investment dollars shift away from traditional energy producers.

Performance during the quarter was negatively impacted by the pool's short positions in bonds. Global investors continued to exhibit an insatiable appetite for bonds, regardless of the yield and the global bond market rally continued through much of the quarter, notably accelerating in August before selling off in September.

The pool had a difficult August. The pool's exposure to the financials

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sector felt the squeeze of lower interest rates. What appears to be a blow-off rally to cap a multi-standard deviation move in the bond market had a negative impact on the pool's fixed income shorts. Exposure to gold contributed positively to performance during the month.

Barometer Long Short Pool

Performance during the third quarter, for the Barometer Long Short Pool was most negatively impacted by exposure to the health care sector. The combination of some targeted positions in the sector like DexCom Inc. (DXCM:NASDAQ), which experienced bouts of insider selling during the quarter, and the remaining cannabis positions such as Acreage Holdings Inc. (ACRG.U:CSE) and MJardin Group Inc. (MJAR:CSE) added to the negative performance. The pool's holdings in the information technology sector, specifically the software names were strongly negatively impacted by the selling of the momentum factor in favour of the growth factor that occurred at the beginning of September. As was seen in the Equity Pool,

Okta Inc. (OKTA:NASDAQ) and CyberArk Software Ltd (CYBR:NASDAQ), sold off as investors moved capital away from securities exhibiting strong momentum characteristics.

The pool's exposure to the materials sector contributed positively to performance as it entered the quarter with an approximately 11% position in gold names, which was sold to zero over the quarter. Exposure to the industrials sector also added to performance with Morneau Shepell Inc. (MSI:TSX), the Canadian Human Resources Services provider which the pool held throughout the quarter, having a positive impact. The pool took a short position in Netflix Inc. (NFLX:NASDAQ) during the quarter which added to performance as investors became concerned about the company's ability to compete with incumbents to the video streaming space like Walt Disney Co. (DIS:NYSE).

Looking Forward

As we enter the fourth quarter, we feel that the market has discounted much of the impact of potential softness in the economy, specifically in the manufacturing

sector which we saw in a pullback in our short-term market breadth models. However, the U.S. consumer remains healthy with generationally low unemployment rates, healthy wage growth, and solid credit profiles. Equity markets have moved around a lot but have not made much headway over the past 18 months. As we look to the final quarter, we look for markets to resolve upwards but remain vigilant of our market breadth models, ready to take a defensive posture should we see prolonged weakness.

The logo for Barometer Capital Management Inc. features the word "barometer" in a lowercase, sans-serif font. A blue checkmark is positioned above the letter 'o'.

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