MAXAM CAPITAL MANAGEMENT

Maxam Diversified Strategies Fund – Q1 2019 Commentary

The Maxam Diversified Strategies Fund[1] gained +6.3% in the first quarter of 2019. Since inception the fund has gained +145.3%.

March 31, 2019	5 Years Annualized	Annualized Since Inception	Cumulative Since Inception
Maxam Diversified Strategies Fund	**7.5%**	**9.6%**	**145.3%**
S&P/TSX Total Return Index	5.4%	7.7%	106.4%
S&P/TSX Small Cap Total Return Index	0.2%	6.1%	78.5%
Scotiabank Canadian Hedge Fund Index	3.5%	3.9%	45.3%

Inception date: June 30, 2019

Following a very weak Q4, global equity markets have done an about face and staged a strong rally to start the new calendar year.

So, what's changed?

The reversal in investor sentiment and stock prices has been remarkable. In 2018, fears of rising interest rates, trade wars and slowing economic growth each took a heavy toll on global equity markets – especially in December. Just a few months into 2019 investor sentiment and stocks have rallied sharply higher on expectations that central banks will now remain accommodative, the China/US trade dispute will resolve amicably, and that economic growth will stabilize.

We believe investor sentiment certainly sent the market into oversold territory last December, creating some very attractive opportunities. Today, we are mindful of just how quickly the broad market has bounced back.

Markets tend to cycle from one extreme to the other, in reality the truth is likely somewhere in between. With the benefit of hindsight, we know Q1 was a full *risk-on* environment. Now, only time will tell if the infamous (and not always accurate) Q2 adage of *'Sell in May and Go Away'* will provide another risk-off moment… and fresh opportunities to deploy capital. Whatever transpires, we'll stay true to our core principles and focus on identifying opportunities where we see attractive reward-to-risk characteristics – whether long or short.

Q1 Review.

While the *risk-back-on* attitude of investors in Q1 spurred the majority of equity securities higher, several of our core holdings posted solid gains due to company-specific reasons. We'll highlight a few notable contributors to the fund's positive performance in the first quarter below.

Hamilton Thorne announced strong Q4 and full year 2018 results in February. As a medical equipment and service provider to the Assisted Reproductive Technology sector and developmental biology research market, Hamilton Thorne benefits from several organic growth drivers. Notably, favourable demographic trends such as aspiring parents choosing to start families later in life creates a secular growth market for Hamilton Thorne's products and services. The company also has a healthy acquisition pipeline that we expect management will take advantage of in this very fragmented market.

Maxam Capital Management Ltd.
902 – 510 Burrard Street Vancouver, BC, Canada V6C 3A8 T 604 685 0201 F 604 685 9970

Boyd Group's shares moved higher during the first quarter after they announced strong Q4 results in mid-March and investors observed that their pace of acquisitions was increasing. With two of Boyd's larger competitors – Caliber Collision and Abra Auto Body & Glass – focused on consummating their recently announced merger, we expect Boyd will continue to step-up the pace of its accretive acquisitions. Also not lost on us is this large industry merger transaction itself – highlighting both the benefits of scale and the interest of private equity and pension plan capital in this sector.

HLS Therapeutics also reported Q4 results that were positively received by investors. The solid financial results for this specialty pharmaceutical company were due to an improved product sales mix, lower manufacturing costs on one of their drugs, and lower financing costs from a debt refinancing they completed in Q3 last year. We believe the big needle mover for HLS in the future is their ownership of the Canadian rights to Vascepa – a drug that provides a risk reduction in first and subsequent cardiovascular events. In late March, HLS announced that they received Priority Review Status ("PRS") for Vascepa from Health Canada. PRS is granted "for new treatments that potentially address serious, life-threatening conditions for which no drug is currently marketed in Canada, and for which there is substantial evidence of clinical effectiveness of that new treatment." We're excited about the prospects for HLS addressing this large market in Canada.

Merger arbitrage is a strategy that we like to employ in the fund for its favourable reward-to-risk and market-neutral characteristics. We especially like to hunt for merger arbitrage opportunities in the small-mid cap segment of the market because we find certain transactions can offer the optionality for additional upside.

In early February Crius Energy announced that it was being acquired for $7.57 in cash per share by Vistra Energy. Following that news we initiated a position in Crius that would earn the fund a high single digit IRR through to deal close. Approximately two weeks after the initial transaction announcement, Crius said that they had received a new unsolicited proposal from a third party and that Vistra subsequently agreed to increase their offer from $7.57 to $8.80 per share – a 16% increase to their initial offer. Our fund's projected IRR on the transaction, relative to our initial cost base, increased to over 50%.

Positioning.

We finished the quarter with approximately one-third of the fund in merger arbitrage, shorts and cash equivalents – the balance in long positions.

The fund's long positions are an idiosyncratic mix of businesses; attractively valued companies with catalysts on the horizon, and special situation investments in companies that, on average, tend to be less economically sensitive.

Our short positions today generally share a common theme – namely that we believe the Canadian economy is likely "as good as it gets" for this cycle. Broadly speaking, we believe that a normalization of the credit cycle could hurt Canadian financials – and that an over-indebted and stretched Canadian consumer who is now facing a deteriorating housing market, especially in major cities, could be negative for certain retailers.

While the companies we are short share this common theme, we have chosen each of our shorts for company-specific reasons. Those reasons range from slowing revenue and earnings growth which in turn typically leads to investor disappointment and multiple contraction, to more idiosyncratic issues specific to each business. Our shorts have, on average, been performing well for us despite the strong rally higher for equity markets. We expect that our short exposure will add incremental value as the current market environment evolves.

Our mandate parameters allow us to invest up to 10% of the fund's capital in private companies, however we have historically not allocated greater than approximately 5%. While this allocation is small relative to the overall size of the fund it can be a very good source of alpha.

For private companies we typically target near-term liquidity situations, such as pre-RTO or pre-IPO financings. Over the next couple of months we expect at least three of our private holdings to *go-public* at prices that are materially higher than where we originally purchased them. Stay tuned.

Staying the course.

We continue to focus on investing in companies and situations where we believe we have identified attractive fundamental or hidden value, plus a catalyst or event that will unlock that value. While timing is always uncertain and stock prices are subject to daily shifts in investor sentiment, fundamentals will be rewarded in the long-run – either through share price gains or through corporate transactions.

We believe we have an attractive reward-to-risk balance in the fund today and that we are positioned well to take advantage of opportunities in the current market environment.

Thank you for your investment and your continued trust.

Sincerely,

Travis Dowle, CFA
President & Fund Manager
Maxam Capital Management Ltd.

[1] Returns are for Series A Units and are net of fees and expenses; *Annualized; SI = Since Inception June 30, 2009.
[2] Scotiabank Canadian Hedge Fund Index data as of February 28, 2019. March 31, 2019 data not available at time of publication.