FULCRA
ASSET MANAGEMENT INC.

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Fulcra Credit Opportunities Fund

Q2 2017 Commentary

For cycling fans, the Tour de France (the "Tour") in July represents the pinnacle of bike racing for the year. During the 2017 edition, one of the Tour's top stars, Peter Sagan, was ejected from the race, after stage 4, due to his apparent aggressive sprint in the finishing stretch of that stage that led to another Tour star, Mark Cavendish, crashing out of the Tour with a broken shoulder.

AIMIA, the parent company of the loyalty points program Aeroplan, experienced a similar fate when the securities in its capital structure were ejected by investors after Air Canada announced it would not renew Aeroplan as its exclusive loyalty points program after 2020.

While Aeroplan members and Mr. Sagan both collect points for very different purposes, Aeroplan's owner, AIMIA, and Mr. Sagan both experienced rejection for very similar reasons. With AIMIA, its securities, including the bonds, were rejected by investors and sold down aggressively after the Air Canada announcement. Similarly, Mr. Sagan was rejected from this year's Tour, in what appears to be "expert" officials not analyzing evidence thoroughly and letting emotion get the better of them.

Sagan should not have been ejected… We are glad AIMIA bonds were

As cycling fans, we are disappointed by non-participating officials effecting the outcome of this year's Tour. While we can't do anything to benefit from such a "sporting" mistake, as investors, we relish opportunities to take advantage of non-fundamentally wired investors, such as those who owned the bonds of AIMIA.

Due to fears of a credit rating downgrade to non-investment grade and a liquidity crunch from a large redemption mile liability, AIMIA bonds traded down over $20 points in the weeks following the Air Canada announcement. We believe this liability is not fully understood by investors and that AIMIA has multiple levers to manage through this transition. In our opinion, the bonds are very well covered by cash liquidity and strategic investments and accordingly we have made the AIMIA 5.6 percent bonds due May 2019 with a yield to maturity of over 12 percent, at the time of purchase, one of the larger positions' in the Fund. While the fundamental price/ risk relationship of AIMIA's bonds is compelling, so too is its duration.

Interest rate insensitive securities that are priced, almost exclusively on fundamentals, are of the most interest to us … if the price is right!!!

While we had purchased a position in one of the three AIMIA preferreds last year in the low teens, it was our biggest detractor in the 2nd quarter. Nevertheless, we believe these preferreds represent very good value, given that they are a small layer of the capital structure, trade at a substantial discount to its par equivalent and represent a cheaper option than the stock on a turnaround or acquisition (the odds of which we believe have increased).

An All You Can Eat Credit Buffet will Give You an Upset Stomach

Spreads on Investment Grade and High Yield bonds are sitting below historic averages, interest rates are still near generational lows, and the absence of capital markets volatility has conspired to bring almost $900 billion [1] of investment and non-investment grade paper to the US through the first half of the year. At this pace, 2017 will be the biggest year of US corporate debt issuance ever!

We rarely think buying at the time of issuance is smart and the current market, in our opinion, is ripe for serious disappointment in the future. Issuance can be like an all you can eat buffet, initially you feel hungry because the food looks good and the price is right but then you realize they are charging you weekend prices and not weekday prices. However, you are already there so you feel like you should eat but after you eat, you don't feel so great.

Disappointment for some however can mean opportunities for others. As the **mainstream new issue part of the corporate bond and loan market looks expensive** we search for isolated situations like an AIMIA.

A source of opportunities for us has historically been Mergers & Acquisitions, whether a partial (Centric Health) or complete (Tim Horton's) sale of a business. Two positions that currently fit into this category are Rite Aid and Tembec.

In the case of Rite Aid, we have been following the proposed acquisition of the company by Walgreens since it was first announced in October 2015. From the beginning, it seemed that it was going to have

[1] According to SIFMA (Securities Industry and Financial Markets Association), U.S. regional member of the Global Financial Markets Association. www.sifma.org

trouble obtaining approval from the US Federal Trade Commission (FTC). As a result, the companies announced on June 29th a proposal for Walgreens to buy 2,186 of Rite Aid's stores instead of the whole company. This modification was the news we were looking for as we think the probability of a successful transaction is very high and that Rite Aid will aggressively pay down debt once the deal closes. We bought bonds after this modification to the transaction was announced. Our focus is the short-dated bonds that we believe will be called in the first or second quarter of 2018.

In the case of Tembec, an acquisition of the whole company by Rayonier, will improve the credit metrics of the combined entity but a likeminded shareholder (Oaktree Capital) is pushing for a higher take out price. This may have the benefit of extending the transaction and allowing the Fund to clip the 9 percent coupon for a longer period, all while the fundamental operations of the business improves.

While the summer represents an opportunity for many to take some vacation time, it isn't uncommon, in our experience, to find attractive investment opportunities during these "quieter" times. We still plan to get out on our bikes with friends and family; yet, like finding a less travelled road or trail we relish in the opportunity to discover an overlooked investment.

Best regards,

Fulcra Asset Management Inc.

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