## PORTFOLIO MANAGER COMMENTARY - JUNE 30, 2020

### Canadian Markets Review

Following a swift market sell-off in March, both North American and European equities enjoyed a sharp rebound during the second quarter. For the six-month period ended June 30, 2020, the MSCI World Index decreased 5.5% led by losses from the Energy sector, which declined 35.2%, while Information Technology was the best performing sector, outperforming the MSCI World Index by 19.6%. In North America, the S&P 500 was down 3.1%, while the S&P/TSX Composite was down 7.5%. Information Technology was the best performing for both indices. In Europe, the STOXX 600 was down 11.7%, led by Spain and the U.K., where the IBEX 35 and the FTSE 100 were down 22.9% and 16.8%, respectively. France's CAC 40 and Italy's FTSE MIB both lost 16.2%, while Germany and Switzerland equities also finished the period in negative territory as the DAX returned -7.1% and the SMI returned -2.3%. During the second quarter, countries around the globe made significant progress in COVID-19 containment. European countries have been able to control the spread of COVID-19 much better than the U.S. As it currently stands, the U.S. remains as the country with most confirmed cases of COVID-19 per million population.

Equity market performance during the first half of 2020 can be dissected into two distinct time frames, namely a period prior to the pandemic and one after the outbreak. Prior to the pandemic, policymakers saw 2020 as likely a year of steady growth with continued strength in the job market. Fed Chair Jerome Powell expressed cautious optimism; this was in stark contrast to 2019 where the Fed cautioned against effects of the U.S.-China trade war on the economy. This optimism drove equity markets to new highs on February 19th, where Information Technology, Utilities and Consumer Discretionary sectors led the market. Following the COVID-19 outbreak, the S&P 500 ended its eleven-year bull run and officially entered into bear market territory in March, but was followed by a swift recovery off its March 23rd trough in the second quarter, marking the fastest market decline in history and the strongest S&P 500 quarterly return since 1998. Unprecedented monetary and fiscal policy support around the globe in combination with re-opening of economics gave investors reasons for optimism during the second quarter. Cyclical sectors including Energy, Materials and Consumer Discretionary led the recovery while defensive sectors including Utilities, Consumer Staples and Communication Services lagged.

Effective policies played an essential role in putting a floor on global equities. In Canada, following three rate cuts in the first quarter, the Bank of Canada (BoC) has kept interest rate unchanged at 0.25% during the second quarter to combat the impact of COVID-19 on the economy. Incoming data confirmed the severe impact of the COVID-19 pandemic, but the impact appears to have peaked. On the fiscal policy side, Canada has increased the amount of direct support to workers through increasing the Canada Emergency Response Benefit and made additional liquidity available to businesses. The BoC expects the global recovery to be protracted and uneven. While the outlook for the second half of 2020 and beyond remains heavily clouded, the Bank expects the economy to resume growth in the third quarter.

According to the latest World Economic Outlook update issued by the International Monetary Fund (IMF) in June 2020, global gross domestic product is projected to contract 4.9% this year. The pandemic has had a more negative impact on the first half of 2020 than previously expected and the pace of recovery will be more gradual. The IMF projected the global growth rate for 2021 to be 5.4%. The path to recovery is predicated upon efficacy of containment efforts, implementation of effective testing, and discovery of a vaccine; layered on top of all these is the restoration of consumer confidence. The intricacy of interactions between multiple factors at play makes forecasting a difficult exercise. However, we do know that the powerful, synchronized, and broad-based fiscal and monetary support demonstrate the willingness of policymakers to take extraordinary steps to alleviate stress in the economy. Equity markets have indeed reacted favourably; the S&P/ TSX Composite is up 17.0% during the quarter. Western Europe and Developed Asia have reopened substantially with minimal effect on virus transmission at national levels. In the United States, the major outbreak in the New York Tri-State Area has been tamped down, resembling the experience of many cities in Western Europe.

Canada has been able to flatten the inflection curve effectively thus far. Looking forward, we expect the current path to recovery to continue. In terms of central bank policy, we expect the Bank of Canada to keep rates steady for the remainder of the year, as the Bank maintains its commitment to continue large-scale asset purchases until the economic recovery is well underway. We anticipate the 2020 U.S. federal election and geopolitical tension between the U.S. and China to be potential sources of volatility heading into the second half of 2020.

**Portfolio Review**

Units (1 Class A share plus 1 Preferred share) of Dividend Growth Split Corp. (the "Fund") was down 11.4% during the first half of 2020. This compares to the S&P/TSX Composite Index, which was down 7.5% over the same period.

The portfolio's underweight positions in Materials and Information Technology detracted from the Fund's gains in the aforementioned sectors. Pandemic induced uncertainties drove major rallies in gold prices as investors sought after safe haven assets. Gold bullion extended the rally off its March low, rising from US$1,577.18/oz at the end of the first quarter to US$1,780.96/oz at the end of June. We have added Gold exposure to the portfolio during the quarter through the purchase of Franco-Nevada. However, we remain cautious on the base metal side as they typically underperform during periods of macro uncertainties. The Information Technology sector was the best performing sector in the S&P/TSX Composite for the six-months ending June 30th. While we have a favorable view on the sector, it is heavily dominated by a limited number of large non-dividend paying players that are not eligible for inclusion in the fund. Shopify alone contributed almost 4 percentage points to the TSX return in the first half of 2020.

The Fund benefitted from being underweight the Energy and Financials sectors. Oil demand deterioration due to COVID-19 led to excess supply in the market and the underperformance of the sector during the period. We favor midstream companies including TC Energy and Enbridge as opposed to oil and gas explorers and refiners, given the highly contracted nature of their pipeline businesses. We are underweight the Financials sector and we hold the large Canadian banks. Banks are currently attractively valued and bank loan losses have been less than expected thus far. We believe banks are much better positioned this time as they are capitalized with strong balance sheets and we don't see a similar solvency crisis this time around like the one we saw in 2008.

We have made several adjustments to the portfolio during the quarter. We have added more exposure to Consumer Staples and trimmed weights from Consumer Discretionary and Real Estate. Many Consumer Staples names were deemed essential during the pandemic, especially large grocery chains including Loblaw, Metro and Sobeys (owned by Empire). Grocers are major beneficiaries of the work-from-home trend; greater grocery demand drove robust same store growth as well as e-commerce traffic during the second quarter. We sold Canadian Tire during the quarter given its weaker e-Commerce presence compared to its peers. Lastly, we decreased the portfolio's office REIT exposure due to the long-term headwind the industry is facing given the adoption of semi-permanent or permanent work-from-home trends across many tenants. We believe lease renewal risk is high for office landlords and the office space may face permanent demand destruction in the medium to long term.

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| Annual Compound Returns[1] | 1-YR | 3-Yr | 5-YR | 10-YR | Since Inception[2] |
|---|---|---|---|---|---|
| Dividend Growth Split Corp. - Class A | (30.9%) | (11.5%) | (1.7%) | 8.3% | 3.4% |
| S&P/TSX Composite Index | (2.2%) | (3.9%) | 4.4% | 6.3% | 4.1% |
| Dividend Growth Split Corp. - Preferred | 5.5% | 5.4% | 5.4% | 5.4% | 5.4% |
| S&P/TSX Preferred Share Index | (7.2%) | (4.0%) | (0.9%) | 0.9% | 1.2% |
| Dividend Growth Split Corp. - Unit | (5.7%) | 0.3% | 3.7% | 7.3% | 4.9% |

*(1) Returns are for the periods ended June 30,, 2020. The table shows the Fund's compound return on a Class A share, Preferred share and unit for each period indicated, compared with the S&P/TSX Composite Index (''Composite Index'') and the S&P/TSX Preferred Share Index ("Preferred Index") (together the "Indices"). The Composite Index tracks the performance of a broad index of large-capitalization issuers listed on the Toronto Stock Exchange ("TSX"). The Preferred Share Index tracks the performance, on a market weight basis, of a broad index of preferred shares trading on the TSX that meet the criteria relating to size, liquidity and issuer rating. The Fund invests in a actively managed portfolio and is rebalanced at least annually. It is therefore not expected that the Fund's performance will mirror that of the Indices, which have a more diversified portfolios. The Indices are calculated without the deduction of management fees, fund expenses and trading commissions, whereas the performance of the Fund's performance is calculated after deducting such fees and expenses. Further, the performance of the Fund's Class A shares is impacted by the leverage provided by the Fund's Preferred shares.*

*(2) Inception Date December 3, 2007.*

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