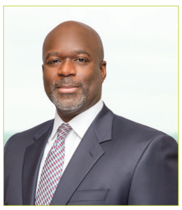
STARLIGHT GLOBAL REAL ESTATE FUND

Real estate equities have room to run



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Key takeaways

- Year-to-date, global real estate has generated a total return of 11.6%[1]
- With a flat multiple, 9.5% EPS growth and a 1.9% dividend yield, U.S. equities appear poised to deliver low double-digit total returns
- The probability of a 25 bps cut have risen to 58.6% in December and 64.0% in January

Macroeconomic Update

Fears of an earnings recession have receded as 2019 S&P 500 earnings estimates are now for 9.5% growth, compared to 23.7% in 2018. Q1 results have impressed and EPS growth is on track to hit 2.9% as companies have outperformed analyst estimates. This exceeds the long-term average of 6% and provides more support for forward P/E multiples of 16.9x vs. the 35-year average of 15.1x. With a flat multiple, 9.5% EPS growth and a 1.9% dividend yield, U.S. equities appear poised to deliver low double-digit total returns from in 2019.

The Federal Reserve Bank appears to have ceased hiking rates just short of what it believes the neutral rate to be. Inflation remains below the 2% target despite strong employment and job growth and the U.S. 10-year bond yield has retraced from a peak of 3.23% in November to the current level of 2.46% (low of 2.37% in March). Currently the odds of a 25 bps increase in the Federal Funds Rate are zero out to January 2020 with the odds of a 25 bps cut rising to 58.6% in December and 64.0% in January[2].

Incredibly, we are still waiting for Brexit as the U.K. parliament cannot agree on the structure of the relationship between the U.K. & Ireland and the EU, post Brexit. Their ineptitude means that the U.K. will have to participate in the EU parliamentary elections on May 23rd, despite their intention to exit the EU. China and the U.S. continue to discuss a new trade deal with the U.S. consistently ratcheting up the pressure on China. China's economy appears to have troughed, given the enormous stimulus enacted since June of 2018. However, a protracted trade war between China and the U.S. would be detrimental to

[1] April 30, 2019. Source: Bloomberg LP. Global real estate represented by FTSE EPRA NAREIT Developed Total Return Index (CAD).
[2] Source: Bloomberg LP.

global and Chinese GDP growth. It remains our belief that China and the U.S. will eventually sign a symbolic deal that avoids further tariffs and paves the way for better relations between the two nations.

Global Purchasing Managers' Indices (PMIs) were stable in April with the Composite at 52.6, flat from March. Services PMI and Manufacturing PMI are both flat at 53.3 and 50.5 respectively. U.S. PMIs rallied with strength in both Manufacturing and Services and across all subsectors, save Inventories. The strong Orders, Prices Paid and Employment readings in both Manufacturing and Services bodes well for continued U.S. economic expansion. China's positive momentum continued with both Manufacturing and Services PMIs up in April. European PMIs were mixed with robust Services PMI growth offsetting weaker Manufacturing PMI. Generally, the strength in European PMIs has been in the periphery countries, while the core nations continue to see PMI weakness. The EU reduced its estimates for GDP growth to 1.2% in 2019, its second downgrade of the year from its original forecast of 1.9%. The outlook for the region likely means the ECB will be on hold indefinitely.

In April, global real estate underperformed global equities and U.S. equities (-1.0%, 3.9% and 4.4% total returns[3], respectively). Despite the underperformance in April, over the long-term global real estate has outperformed global equities and U.S. equities (9%, 8.1% and 8.8% total returns[4], respectively) and this underscores the need for advisors to add a strategic allocation to their clients' portfolios.

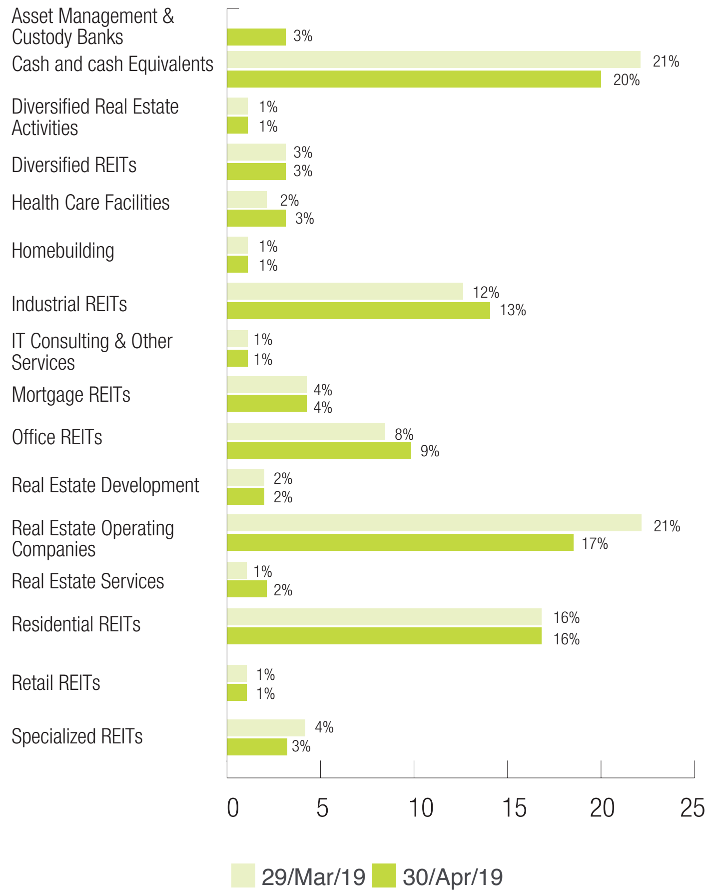
Starlight Global Real Estate Fund Overview

The Fund's geographic and sector allocations are shown (adjacent) here. Assets Under Management (AUM) rose 24% in April. Incremental new capital was largely allocated to our existing U.S. and Canadian positions. In April, we added one new position and no positions were eliminated. The Fund's cash weighting reflects our lag in deploying lumpy capital inflows as the market continued to rise.

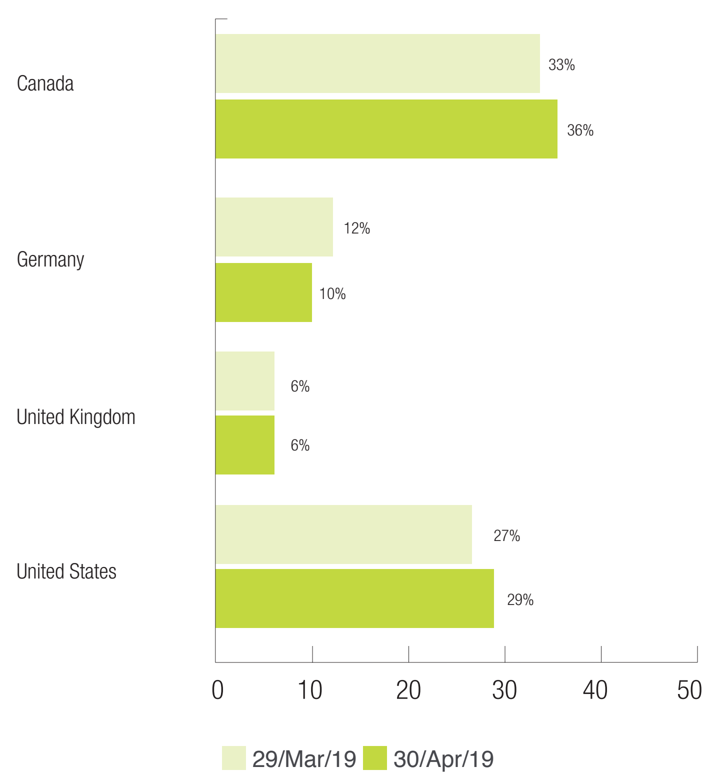
[3] As of April 30, 2019. Source: Bloomberg LP. Global real estate, global equities, and U.S. equities represented by the FTSE EPRA/NAREIT Developed Total Return Index (CAD), MSCI World Index (CAD) and S&P 500 Index (CAD), respectively.

[4] Source: Bloomberg LP from Dec 31, 2002 – April 30, 2019. Global real estate, global equities, and U.S. equities represented by the FTSE EPRA/NAREIT Developed Total Return Index (CAD), MSCI World Index (CAD) and S&P 500 Index (CAD), respectively.

Starlight Global Real Estate Fund – Sector Allocation (%)



Starlight Global Real Estate Fund – Geographic Allocation (%)*



*excludes cash & cash equivalents

Portfolio review

Two of the top contributors to Fund performance in April were Prologis Inc., with a total return of 7.3% and, Americold Realty Trust, with a total return of 5.6%[5].

Prologis Inc. (“Prologis”) is the global leader in logistics real estate with a focus on high-barrier, high-growth markets. As of March 31, 2019, Prologis owned or has investments in, properties and development projects expected to total approximately 772 million square feet in 19 countries. Prologis leases modern distribution facilities to a diverse base of approximately 5,100 customers across two major categories: business-to-business and retail/online fulfillment. Prologis reported Q1/19 results on April 16, 2019, which were ahead of consensus, and the Company also raised its 2019 guidance. Prologis is focused on driving greater rental rate growth and over the last several quarters has been able to exceed its own expectations in terms of both tenant retention and rate growth. We believe management’s increased guidance remains conservative. The U.S. availability rate for Industrial has been declining for 35 quarters and ended Q1/19 at 7.0%, while net absorption (33 million sf) continued to outpace completions (32 million sf). We continue to see upside to Prologis’ share price, despite the strong performance in April, driven by a very favourable supply-demand imbalance for logistics space and a positive macro backdrop.

Americold Realty Trust (“Americold”) is the world’s largest publicly traded REIT focused on the ownership, operation and development of temperature-controlled warehouses. Americold owns and operates 155 temperature-controlled warehouses, with approximately 918.7 million refrigerated cubic feet of storage, in the United States, Australia, New Zealand, Canada, and Argentina. On April 16, Americold announced the acquisition of Cloverleaf Cold Storage for US$1.24 billion, which increases Americold’s U.S. market share to 26.6%. The acquisition solidifies the Americold platform, strengthens the balance sheet, and positions Americold to generate almost 20% FFO growth in 2020/2021[6]. We continue to see upside to Americold’s share price, despite the strong performance in April, driven by a very favourable supply-demand imbalance for temperature-controlled warehouses space, significant near-term growth potential, and a discounted valuation compared to industrial peers.

One of the top detractors from Fund performance in April was Canadian Apartment Properties REIT (“CAPREIT”). CAPREIT is one of Canada’s largest residential landlords, owning interests in over 53,000 residential units, located in and near major urban centres across Canada and the Netherlands. Since CAPREIT’s initial public offering in May 1997, CAPREIT has grown its monthly cash distributions per unit by 93%. We attribute the recent underperformance largely to CAPREIT’s $300 million equity offering which was announced on April 1, 2019 and closed April 23, 2019. The offering was used to fund:

- a $182 million portfolio of 23 Manufactured Housing Communities totaling 3,469 sites across Canada,
- a $155 million portfolio of additional Canadian acquisitions of newly constructed apartment properties that are in the advanced stages of negotiations and diligence (expected to close in Q2 2019),
- and to partially repay the REIT’s acquisition and operating facility, which was used to fund the $66 million acquisition of an unencumbered 1,104 site Manufactured Housing Communities (MHC) portfolio that closed on March 14, 2019.

We view CAPREIT as a core REIT holding, given its long-term track record of steady Net Operating Income (NOI) growth, combined with very strong market fundamentals, sector low leverage, and a relatively low payout ratio. Further we see future upside potential as CAPREIT has recently begun a process to realize development opportunities on over 80 properties, which could add over 10,000 net new apartments suites to the portfolio, principally in Ontario and British Columbia.

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[5] Source: Bloomberg LP.
[6] Source: Bloomberg LP.

Portfolio outlook

The Starlight Global Real Estate Fund now holds 34 positions. We expect to continue deploying capital into these businesses on an opportunistic basis. Longer-term the portfolio should reach a targeted strategic allocation of 30% each to Europe, the U.S. and Canada supplemented by opportunistic investments in Asia and Australia. As Europe works through its legislative calendar, we expect to increase allocations to European real estate firms.

The industrial sector has generated double-digit returns driven by the rise of e-commerce and the need for fulfillment centres, last-mile delivery and logistics facilities. We believe industrial businesses are still compelling on valuation while providing strong dividend growth.

We remain optimistic with respect to the multi-family sector and believe stock selection will be key to generating strong returns. We believe multi-family REITs offer an attractive risk/return profile driven by favourable supply-demand imbalances in many urban cities globally. We look for companies that generate strong cash flow, have a defensive balance sheet and provide exposure to markets with high barriers to entry.

Conversely, we remain cautious on the retail sector as we expect the negative sentiment from e-commerce to continue. Globally, we continue to see retailers reducing their square footage and retail rents declining. Appraisers are reducing retail valuations as the asset class remains out of favour with investors. We believe there continues to be too much supply, and the investment risk remains to the downside.

Overall, we believe the Fund is well positioned to participate in continued up-markets while providing downside protection. We will closely monitor the investment environment and actively manage the Fund's positioning by carefully selecting individual businesses in-line with Starlight Capital's proven investment philosophy.

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