JEMEKK LONG/SHORT FUND L.P.

Inception date: July 2004
Q1 2018 Commentary

	Q1 2018	YTD 2018	Since Inception
Jemekk Long/Short Fund	3.34%	3.34%	226.07%
S&P TSX Composite	-4.52%	-4.52%	162.56%
S&P/TSX Small Cap Index	-7.73%	-7.73%	55.10%

* Benchmarks quoted in Total Returns

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As we entered the new year bullishness on equity markets seemed at all highs and 2018 was going to follow the same path as 2017 especially with the tailwind of the tax cuts in the US. Fast forward three months and we find the narrative has changed dramatically as global equity markets struggled with concerns surrounding rising interest rates and trade disruptions. The TSX was not immune to this tough quarter in fact the TSX was the worst performing index out of the G7 nations. In the face of this difficult quarter we are pleased to report the Jemekk Long/Short Fund up was up 3.34% materially outperforming every major index. We will discuss the reasons for the outperformance below.

The TSX had a terrible start to the year. When looking at sectors, Technology was the only positive posting an impressive 10% due predominantly from Shopify while the worst performing sectors were Health Care and Energy continuing its path of underperformance from last year. The TSX Small Cap Index performed worse with all 11 sectors down in the quarter the bulk of which from resource stocks. But we are not throwing in the towel on Canada yet. There are several reasons to be constructive on Canadian equity markets such as the EPS estimates for the TSX have been increasing; stocks in Canada are cheap relative to global peers and discounting too much in our opinion; and the outperformance from the US markets versus Canada is set to narrow. The outlook for oil is polarizing. Compelling arguments can be made by the bulls and bears, and we acknowledge the disconnect from WTI and energy stocks but cannot time when this valuation gap closes. We believe the Bank of Canada will remain accommodative and the Fed continuing its path of interest rate hikes which could hurt the Canadian dollar. The result of a weakening loonie is a positive for many Canadian sectors including energy. We aren't saying we are going all in on energy by any means, but it is one sector which appears left for dead trading at attractive multiples - we are monitoring the energy complex carefully.

In the US, the first quarter began strong continuing where it left off in Q4/17, until volatility reemerged in February. A common theme from our commentaries last year was the surprising amount of complacency and lack of volatility in the markets. This came to an abrupt stop this quarter. The volatility index hovered around 10 throughout 2017 and spiked nearly 4-fold in the first days of February. The selloff in equities was initially driven by fears of potential inflation and rising interest rates but more recently rhetoric around a possible trade war. The market is not favorable to tariffs and threats of trade wars as this brings more regulation which we are beginning to already see - the Trump Administration blocked the Qualcomm/Broadcom merger and talks of breaking up the so called Internet monopolies. Strong global PMI's were one reason to be bullish on equity markets but a risk to the global growth story is the developing trade war between the US and China. This has become front and center and investors are taking note by raising cash and lowering their beta to the market (another headwind for Technology stocks). Volatility is back, and investors need to alter expectations and understand the low vol market is being replaced where a single tweet from Trump, be it related to tariffs, NAFTA, or a personal attack on Jeff Bezos, can set the tone for the trading day.

The Fund entered the quarter 87% net long and exited at 78% as we took note of the risks entering the market and reduced our exposure. As always, we remain nimble and focused on market fundamentals and political friction when assessing our risk appetite. The first quarter of 2018 proved to be difficult and this is reflective in the poor index returns. However, the Fund posted a solid number on a relative basis from a breadth of sectors namely Consumer Non-Cyclical (The Stars Group and Pollard Banknote) and Technology (GrubHub and HubSpot). As for the detractors, the marijuana names took a breather and weakness in the Energy complex.

There was also an M&A transaction that highlights price discovery of a comparable we own. Specifically, we introduced HubSpot to you in Q3/17 as a holding and we remain long but acknowledge the high sales multiple on the stock. However, in March Salesforce.com announced the acquisition of MuleSoft (a comp to HUBS) for 12x 2019e Sales and this bid up the whole SaaS complex outlining the strategic nature of some of these assets. This takeout multiple is 5 turns higher than where HUBS currently trades at.

Following our review of the quarter, we would like to introduce you to a holding we first bought in January last year:

Andrew Peller Ltd (ADW.a) – With a history dating back to 1961, Andrew Peller is Canada's largest publicly traded wine producer and marketer of wines with a 10% share of total consumption. ADW offers a full range of products (wine, cider and whisky) across the spectrum from value to premium brands. The company has demonstrated it can grow organically and inorganically (17 acquisitions since 1995) and M&A continues to be a key focus. The footprint for ADW spans across Canada including wineries in B.C., Ontario and Nova Scotia. With respect to distribution, the company has multiple outlets to sell their brands. You can find Peller owned wines at restaurants, liquor stores and a newly introduced channel, grocery stores, along with any of their 101 corporate owned retail locations under the flagship banner, The Wine Shop.

In September of last year ADW announced the acquisition of three B.C. wineries for $95mm. We like the transaction as the acquired assets are growing faster than the current portfolio (6-7% CAGR vs. 4%) and EBITDA margins are much more attractive resulting in a lift for ADW (33% vs. 13%). Management has stated these wineries are already performing above expectations. In terms of acquisition strategy management believes its early days for the consolidation of the Canadian wine industry and sees a clear multi-year pathway of growth. But even assuming no further M&A the current assets set the stage for future growth and management has clearly demonstrated its experience in driving margins and creating cross platform products (Wayne Gretzky wine and whisky products).

There is a lot to like about the Andrew Peller story. We have confidence management can continue to integrate new assets and further drive unit economics and margins through its premiumization strategy. Early traffic numbers from grocery store sales read positive. We feel the company deserves a scarcity premium due to its competitive advantage from its size and unique positioning in the industry and being a public company. And from a demographic perspective, ADW fits nicely with our theme on tracking how Millennials spend their money. An area where we spend a lot of time.

Overall, we are pleased with the performance of the Fund relative to other major indices. Navigating through the first quarter unscathed was no easy task. Volatility did a 180 as markets swung violently and we stayed on course and remained disciplined. At Jemekk we are constantly asking ourselves are the markets expensive? Said differently, are we being rewarded for the amount of risk we are assuming? As of now, our answer is no. The markets are not expensive. However, nor are they overly cheap. Despite the recent volatility, the global macro backdrop remains positive for stocks. We believe all signs are pointing to a late stage environment, but the cycle is still progressing albeit some inflationary signals are surfacing. We remain constructive on the markets but Q1 has showed us how fragile this market is and the material risks that are beginning to arise. Companies will begin reporting Q1 numbers in the coming weeks and we believe the reporting season will be positive and the market will again shift its attention to fundamentals. This year will be a difficult one for passive investors but shaping up to be an ideal market for those active managers like ourselves.

Thank you for your continued support and we look forward to reporting to you at the end of the second quarter 2018.

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