JEMEKK LONG/SHORT FUND L.P.

Inception date: July 2004
Q3 2018 Commentary

	Q3 2018	YTD 2018	Since Inception
Jemekk Long/Short Fund	0.91%	7.23%	238.34%
S&P TSX Composite	-0.57%	1.36%	178.74%
S&P/TSX Small Cap Index	-2.81%	-4.42%	60.67%

* Benchmarks quoted in Total Returns

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Q3 delivered another quarter of positive performance for your Long/Short Fund continuing the trend for the year outperforming its respective benchmarks. Further, the continued outperformance is also in the face of heightened macroeconomic and geopolitical risks. Specifically, the S&P/TSX was down 57 basis points in the quarter and on the year the index is up 1.36%. The TSX Small Cap is faring much worse being down 2.81% in Q3 and 4.42% for the year. Whereas the Long/Short Fund posted a positive print in Q3, up 91 basis points, with a year to date return of 7.23%. We will discuss Fund specifics and our outlook for the balance of the year below.

It was a barbell in terms of performance for the TSX this quarter. On one end, the index had strong gains from the Health Care sector (we remind investors cannabis stocks fall under this sector) +31% and on the other end was Materials dragging down the index by 13%. In terms of individual stock performance for the index - three of the top ten contributors were cannabis related names where Canopy Growth was the top performing stock in the index. This can be attributed to the $5b cash injection from Constellation Brands into Canopy in the quarter which fueled the entire cannabis complex. As for Materials, 8 of the 10 worst performing stocks for the TSX were gold related. As an asset class, gold seems to be left for dead and sentiment remains negative. In the quarter we did have a material M&A announcement in the space - Barrick agreeing to buy Randgold to create the largest gold producer in the world. The management of Barrick are sending a message that they are bullish on the outlook of gold and time will tell if 1 + 1 = 3. The TSX Small Cap was similar in terms of performance with the resource sector being the prime culprit for its underperformance. Namely, the Materials sector dragging down the index by 12%. From this we can see the entire gold complex was being sold rather than investors rotating up or down market.

One material event for Canada was NAFTA, renamed United States-Mexico-Canada Agreement (USMCA), largely renegotiated which removes a key overhang for Canadian markets. Ultimately, the deal going through reads positive however we acknowledge the overall terms for Canada are less beneficial to Canada but the more punitive demands from the US were omitted. Net/net, we look forward to the rhetoric between Canada and the US improving and take solace in knowing Canada escaped a potential major disruption to its economy.

In the US, all three major indices were once again positive for the quarter despite ongoing trade wars between the US and China. In our Q2 letter we highlighted the tit-for-tat gameplay shifting from threat to reality. In September, we saw just that as Trump continued to promote his 'America First' agenda by announcing the third round of Chinese tariffs. The totals for each country's tariffs now stand at US $250b and China $110b. Clearly, the two countries are unable to resolve its trade talks leading to round after round of tariffs. As stated before, we view this as a serious issue and remind our investors no real winners emerge from trade wars. We are keeping a watchful eye on this considering we are fast approaching midterm elections. At the time of writing what's taking center stage is the recent spike in the 10 year treasury yield now back to 2011 levels. From our experience it's not just the magnitude of the rate move but also the speed in which it occurs. The recent move was fairly quick which has led to the more growth oriented stocks to sell off.

Generally, rising long rates put pressure on more highly valued sectors/stocks. We have seen this before, earlier in the year, when in January with the confirmation of rates continuing to rise resulted in the markets falling 12% in a fast, violent manner. So, we wonder, is this event going to lead to another correction only followed by growth stocks being bought again resulting in new highs or is this a real rotation from not only stocks to bonds but also from growth to value? We are monitoring this closely and believe it could be the latter and we have begun to position the Fund accordingly.

The Fund entered Q4 75% net long but will look to increase liquidity by trimming less liquid names and avoiding new stocks that don't fit into our liquidity parameters. We are focused on keeping the Fund nimble and responding to macro events quickly protecting capital for our clients. To date, the Fund has outperformed its benchmarks with significantly less market risk. In the third quarter main contributors to performance came from names such as Hydropothecary and Parkland Fuel while the detractors were The Stars Group and Raging River. In our Q2 letter we mentioned we have been finding new small cap stocks in Canada and have built positions in a handful of names that meet our criteria for compelling ideas. We would like to introduce to you the first installment of 'Small Cap Corner' where we will highlight a new small cap idea and continue to do so in the coming quarters.

Quantum International Income Corp. (QIC) - with a controlling interest in Lucky Bucks, QIC is the owner of the largest coin operated amusement machine (COAM) business in Georgia. So, what are COAMs? These are 'skills based' lottery game terminals usually found in gas stations and convenience stores. QIC owns 60% of Lucky Bucks the primary operating business based in Atlanta, Georgia and the balance is owned by the CEO of Lucky Bucks who remains fully committed to growing the business and holds key relationships down south. We were attracted to QIC after learning of the robust Free Cash Flow being generated by the company. QIC is enjoying strong EBITDA margins north of 40% with minimal levels of capex required. The company is the largest by market share (10% and growing) and the only public company in the space adding a level of sophistication its competitors do not have being primarily mom and pop run stores. One issue we had with the story was the regulatory environment for gaming terminals in Georgia. So, we flew to QIC's office in Atlanta to conduct deeper due diligence on the operations, meet with the CEO of Lucky Bucks, visit game locations, and learn more about the regulatory landscape.

Ultimately, we came back learning there are no plans to disrupt the current regulatory process and in fact QIC is admired by the regulators for being a public company with respect to its financial transparency. We also were impressed by the new warehouse QIC is moving into and the technology being implemented to automate workflow. And most importantly, it was great to meet the CEO of Lucky Bucks who is the key man (which bears risk) and came away knowing he is 100% focused on the business and very much invested (he owns 40% of the operating co.).

We acknowledge there are lot of risks surrounding QIC and the industry in which they are in, but we are looking to the fundamentals (our estimates suggest QIC could double the size of its business financed internally) and the potential to consolidate this very fragmented market (QIC owns 1,800 COAMs and the total addressable market in Georgia is approx. 22,000 and growing). We are mindful QIC is a very small company (sub $100mm market cap) and will manage the position accordingly. We believe QIC is an under the radar company with only one firm to have research coverage. We see this changing in the near term as more people learn about the QIC market opportunity and the impressive EBITDA margin profile.

We continue to be pleased with the performance of Fund given the material macro/political headwinds in the market. We see a favorable set up for Canadian markets in the near term. The NAFTA overhang has lifted, the energy market is showing signs of strength namely a green light for a West Coast LNG facility, the backdrop for gold screens positive and most notably the valuation for Canadian stocks are trading at a material discount to US stocks. These factors could lead to a short term bid to Canadian markets and justifiably so. In the US there are several obstacles in the coming markets that will most likely keep the markets from breaking out - midterm elections in November, another potential rate hike in December, and ongoing trade disputes with China. As mentioned, interest rates are top of mind and being monitored closely.

The market however will shift back to fundamentals in the coming weeks as Q3 reporting begins (S&P 500 expected to post a 19% increase in EPS). We will be listening carefully to management teams provide guidance for Q4 as we see earnings slowing down but remain healthy. However, the market is counting on strong corporate earnings and if this becomes questioned markets will react negatively. Bifurcation continues in the market and one thing hasn't changed, we will err on the side of capital protection.

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

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