JEMEKK LONG/SHORT FUND L.P.

Inception date: July 2004
Q4 2023 Commentary

	Q4/23	YTD	Since Inception
Jemekk Long/Short Fund	3.89%	-3.25%	195.98%
S&P TSX Composite	8.10%	11.75%	327.93%
S&P/TSX Small Cap Index	5.98%	4.79%	105.64%

** Benchmarks quoted in Total Returns*

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After interest rates rose sharply in Q2 and Q3, the 10-year peaked in Q4 leading to a broad-based rally off the October lows as the Fed narrative, yet again, swung from 'higher for longer' to 'lower rates sooner.' However, this time there was some logic behind the shift, specifically inflation continued to move lower (the 2% target on a six-month annualized core PCE inflation is becoming much more in focus). Performance wise, after an extremely weak start, it was a mirror image from the previous down quarter across the board culminating in a violent rally in Nov/Dec, especially for major US indices. The Dow, Nasdaq, and S&P 500 were up 12.5%, 13.6%, and 11.2% respectively for Q4 (up 13.7%, 43.4%, and 24.3% respectively for 2023 as a whole). The S&P was led by very strong gains from Technology, Communications, and Consumer Discretionary. The only subsectors in the S&P that were down in 2023 were Energy and Utilities. Somewhat similar, yet much more muted results for the TSX where the only down sector in the quarter was Energy, although was still positive for the year. The only down sectors for the TSX for the year were Materials and Communications, both impacted by the rising rates witnessed in 1H 2023. Similar to US indices, Technology was the largest contributor to the TSX for the year. What was noteworthy is almost the entirety of returns for the TSX for 2023 (+11.75%), were in the last two months of the year, as previous to that the Index was negative. For the first time in recent memory smaller companies outperformed their larger counterparts, which we believe is the beginning of a catch-up trade as we expect the valuation gap between the two groups will narrow this year. In other words, we are bullish on mid to small caps and see a fertile hunting ground like we have not seen in several years. A 5% FCF yield is no longer competitive as we are screening companies with 20%-30% FCF yields in the smaller end of the universe.

Clearly the quarter, and all of 2023 was dominated by the "Macro" battle of higher rates to fight inflation. As mentioned above the shift, or pivot, was the overwhelming primary force driving equities in Q4. During the quarter the Bank of Canada had three rate decisions with all three resulting in no change to rates, although the BoC maintains its hawkish stance even in the face of acknowledging a small victory declaring the battle against inflation is being won - but not over yet. Similarly, in the US, the Fed also paused rate hikes in the quarter (the last hike in July) and signaled cuts could be in the offing sometime in 2024. Specifically, the Fed laid out approximately three cuts in 2024, which the market ran with and quickly priced in six. We too see the merit of cuts in 2024, in response to a slowing labor market (ex- Hospitality and Health Care), lower energy prices and a slowing economy. However, it's important to recall their actions will, or at least should be highly data dependent and can change materially (recall coming into 2023 the market was pricing in cuts in June of last year).

To be clear, we are not in the interest rate guessing game, but we do believe the hiking phase has passed and that the war on inflation is largely done. The Fed has two mandates - (1) Maximum Employment (2) Stable Inflation. Currently the US is at full employment and inflation is well on its path to becoming stable as it approaches the Fed's 2% target. In our view, the Fed can achieve a soft landing if they are proactive versus reactive to the above-mentioned employment pressures easing and slower growth. This "goldilocks" scenario is akin to threading a needle, and if possible, is the best-case outcome for equities. However, if history is any guide, we see the employment picture in the US further deteriorating, coupled with a deceleration in economic growth, triggering the rate cuts from the Fed, probably in the second half of 2024. As this is key for a continued rally, following such a strong Q4, we anxiously await further confirmation of the need for easing before embracing the enthusiasm the broader market has taken.

Against the backdrop of this more favorable environment for equities, the Net long exposure for the Fund increased in the quarter from a conservative 63% to 88% as we began to embrace the bullish sentiment arising from interest rates topping out. From a sector perspective there were no material changes other than an increase in Basic Materials, as Gold broke out, and a reduction in our index hedges, primarily accounting for most of the increased exposure. The main contributors of performance for the quarter came from a breadth of sectors such as Basic Materials (Alamos/Kinross), Industrials (Hammond Power and H20 Innovation the latter receiving a takeout offer in the quarter), and Consumer Non-Cyclical (Boyd Group, a long-owned name in the Fund). The primary area of weakness in Q4 was from Energy (Whitecap and Baytex Energy), which surprised us in the quarter as fundamentals improved significantly (SPR inventory beginning to build, OPEC further cuts, and stronger than expected demand). Although we see opportunity in the space, we are hesitant to increase our weighting as the market is clearly signaling a disconnect with our thinking.

On the year, the largest contributors in Q4 were also the same for the year. On the negative side of the ledger, our holding in Aritizia, a retailer, was one of the bigger detractors - a company that enjoyed a COVID bump but was unable to manage operations effectively when growth waned and inventory piled up. On the year as a whole, we are not pleased with reporting a negative number against the indexes, which were strong. Clearly, we were far too cautious and overestimated the fundamental risks such as valuation and an economic slowdown. We were far too slow to embrace the changing Fed narrative, and placed too much emphasis on protection, rather than growth, of capital. Although at times, like the third quarter, we felt justified in our cautious positioning, clearly the powerful rally of Q4 caught us off guard. We also did not foresee Technology, historically a strength for the Fund, to have the year it had, against the backdrop of 500 bps of higher rates. As mentioned above, as we enter the new year, the Fund has increased our net long bias, beginning again to use some leverage, and plans to capitalize on an environment that finally shifts from Macro factors to fundamentals – uncovering many mid to small-cap stocks trading at puzzling valuations.

Following, we would like to highlight a position in the Fund:

MDA (MDA) – Canadian based MDA develops and manufactures space technology primarily for the government. The global space economy is projected to hit US$1.5T by 2040 and MDA is a pure play company to capture this growing market. MDA has three business lines: Satellites (45%); Robotics (29%); and Geointelligence (26%).

The company had a strong year on both the top line and on margin execution. But this was eclipsed by the Telesat contract awarded in August. Specifically, MDA announced a $2.1b contract from Telesat for 198 satellites. This contract in addition to MDA's backlog supports a double-digit revenue CAGR through 2027. Notably, management said they do not expect any additional capex from this contract, which fuels the FCF profile for MDA. We believe this contract lends credibility to MDA and speaks to its renowned technology and execution. The Telesat deal will open the doors to other material contracts, adding to MDA's already healthy backlog.

We view MDA as a catalyst rich story with a growing backlog and strong profit metrics. We believe street estimates are low and the company can beat these numbers, win new contracts (not priced in), and de-lever resulting in multiple expansion as well. It's not often you can get a high growth/high profitability stock without a commanding valuation. MDA trades at 9x EBITDA, several turns lower than its comp group.

In summary for 2023, we over discounted the risks in a year where the Fed took rates to an upper band of 5.5% (from close to zero), there was a regional banking crisis resulting in bank failures down south, the US credit rating was downgraded, a continuation of the Ukraine/Russian war and a new war in the Middle East among other notable events. Despite all this, the S&P 500 was up 24% (although the Financial and Energy heavy Canadian indexes lagged considerably). As we enter 2024, although we have increased our exposures, we remain concerned as many of these risks exist still (absent the risk of higher rates). In addition, the market is at an above average valuation and clearly needs EPS growth to backfill this valuation for a positive year. This is further amplified by the risk of a US recession, that is still on the table, which could cause equities to react swiftly when/if this discussion re-emerges. As such we expect the transition in 2024 to be bumpy, and plan to use nimbleness to capitalize on the expected volatility.

We thank you for your continued support and look forward to communicating with you at the end of Q1. As always, please feel free to reach out to any of us below.

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