Market Commentary
Third Quarter 2020

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CI American Value Fund

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Class F returns (in %) as at September 30, 2020	Year-to-date	1 year	3 year	5 year	10 year	Since inception (2000-11-17)
CI American Value Fund	-3.5	2.9	7.9	8.6	12.4	4.3

Source: Epoch Investment Partners, Inc., as at September 30, 2020.

Market Overview

- Stocks had a strong quarter as the economy began to recover from the coronavirus lockdown, with workers trickling back to factories and offices. Global trade also rebounded. Ongoing support from central banks, resilient corporate earnings and optimism on progress toward a COVID-19 vaccine also helped lift equities. In July and August, markets were led by a handful of U.S. mega-cap stocks in the information technology, consumer discretionary and communication services sectors. Stocks cooled off in September as an additional coronavirus relief package in the United States remained bogged down in congressional gridlock. Nevertheless, stocks ended the period with solid gains. Growth indices beat value indexes and large-cap stocks outpaced small caps. The consumer discretionary sector had the best returns. Energy stocks provided the lowest returns by far, falling sharply as demand remained subdued.

- The U.S. dollar weakened against other major currencies after the U.S. Federal Reserve (Fed) announced a new inflation-targeting strategy, where it will tolerate periods of inflation above that target to compensate for spells when it undershoots that target. Many investors interpreted this as a promise to hold rates low indefinitely. Fed officials repeatedly stressed the need for additional fiscal support, highlighting the limits of monetary policy.

- The economy appeared to be reviving from its unprecedented 31.4% rate of decline in the second quarter. Home sales in the United States surged, helped by low mortgage rates. Purchasing Managers' Index data moved from contraction to expansion. Initial jobless claims, however, remained elevated.

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Performance Summary

- Over the third quarter of 2020, the CI American Value Fund Class F (the Fund) returned 4.8%, while its benchmark, the S&P 500 Total Return Index, returned 6.8%.

- Security selection was positive, especially in the health care sector. In addition, a less-than-index weight in energy also made a large contribution.

Contributors to Performance

- In health care, Charles River Laboratories Inc. reported second-quarter revenue and profits that significantly exceeded consensus expectations. The company also raised its forward guidance for full-year 2020 revenue and cash flow generation. In addition, the company also announced the acquisition of Celeron Corp., a provider of cellular products for cell-therapy developers and manufacturers. Cell and gene therapy are the fastest growing areas in biotech, and this helps round out the company's portfolio in this area after purchasing HemaCare Corp. in January. Charles River has a dominant market position in a growing industry being fuelled by biotech innovation. The company should continue to grow at a high single-digit rate, with margin expansion and upside from value added from merger-and-acquisition activity.

- Danaher Corp. also reported second-quarter revenue and earnings that came in well ahead of consensus expectations. They saw a surprise rise in earnings of 35.9% over the previous quarter. Management indicated that orders for Catia and Pall were up 40% to support development and bioprocessing of COVID-19 vaccines and therapeutics. Importantly, Danaher's CEO qualified the COVID-19 opportunity as "large and sustainable." This is clearly a multi-year opportunity. For the quarter, the company generated free cash flow of US$1.3 billion, representing a 40% increase on a year-over-year basis. Danaher is now primarily a healthcare-focused company with exposure to life sciences and diagnostics, biopharmaceutical filtration and dental products. Danaher is a profitable company that generates gross margins of 50% and operating margins in the mid-teens. The company benefits from strong renewal rates and realizes 60% of revenues from recurring sources. Shares in Danaher have been boosted by positive end-market exposure to COVID-19. The company provides equipment and reagents for both diagnostic testing for coronavirus, as well as for bioprocessing to identify COVID-19 therapeutics and vaccines.

- In information technology, Facebook Inc. reported second-quarter results that came in ahead of expectations on both a top-line and bottom-line basis. A key opportunity that is creating shareholder value is the company's e-commerce strategy currently being rolled-out globally helping to monetize the 2.7 billion users that includes Shops (launched in May 2020) on Instagram and Facebook. Facebook

Pay is also being implemented, as well as e-commerce on WhatsApp in developing countries, most notably India. Pay is expanding by allowing users to click through ads enabling users to conduct a transaction. Importantly, the brand advertising boycott has had limited impact on Facebook's operations, contrary to expectations. Gaming could become increasingly valuable to the company as it creates a community—it is a top five vertical for advertising revenue for Facebook today.

Detractors from Performance

- Not owning Amazon.com Inc. and Apple Inc., two large index constituents, detracted from results during the quarter.

Portfolio Activity

- During the quarter, we purchased new companies that fit well with our emphasis on cash generation and optimal capital deployment. For example, in consumer staples, Lamb Weston Holdings Inc. is the world's second-leading producer of branded and private-label frozen potato products, such as french fries, sweet potato fries, tots, diced potatoes, mashed potatoes, hash browns and chips. The company also has a small appetizer business that produces onion rings, mozzarella sticks and cheese curds. While 80% of revenue is U.S.-based, the firm also sells its products in Canada, Japan, China, Korea, Mexico and several other countries. About 86% of the firm's products are distributed into the food-service channel, while the remaining 14% is sold through retail. Lamb Weston became an independent company in 2016 when it was spun off from Conagra Brands Inc. Lamb Weston is a high-quality company that is a leader in a consolidated industry. Management takes a conservative approach to guidance and has a longer-term vision of further consolidating the European market. After several years of attractive volume growth, price increases and expanding margins, Lamb Weston has been temporarily set back due to the pandemic. After a few more quarters of difficult comparisons, the company should realize attractive free cash flow growth. Post the pandemic, Lamb Weston's sales exposure to full-service restaurants could see significant upside as this portion of the business recovers. In the meantime, the company is cutting costs, improving its manufacturing footprint and realizing increased sales in the retail side of the business, as consumer behavior has shifted increasingly towards eat-at-home.

- In communication services, we sold Charter Communications Inc. and purchased T-Mobile US Inc. Charter's stock price had appreciated by over 25% on a year-to-date basis and is now fully valued in our opinion. This is partially based on its traditional cable business, which represents a slower growth opportunity going forward. Meanwhile, T-Mobile has the first and leading nationwide 5G network, covering over 250 million people across 1.3 million square miles, which is bigger than AT&T Inc. and Verizon Communication Inc.’s 5G networks combined. Now, with its supply of ideal mid-band 5G

spectrum (2.5 GHz), T-Mobile is building on that nationwide 5G foundation, increasing capacity and boosting speeds for millions of customers. With the acquisition of Sprint Corp., increased scale has made T-Mobile far more efficient, turning it from a cash burner to substantial cash generator over the past five years, removing questions about its viability. Based on solid execution, today T-Mobile offers a favourable growth story with a lower risk profile relative to many peers at an attractive evaluation.

Outlook

- The macro outlook continues to improve, although the pace of recovery has slowed. Since March we've expected the economic recovery to trace out the Nike swoosh. However, no single letter or shape fully encapsulates the complex recovery taking place. While a few sectors are experiencing a "V" (e.g., housing), the Fed worries that some industries face an "L" (e.g., commercial real estate). Moreover, we believe "K" in many ways has become an apt metaphor for this cycle, with college-educated workers in digital industries thriving, while less-educated workers in some services sectors still struggling.

- Overall, we expect a 90% economy to emerge, with an exceptionally long road back to normal. The COVID-19 recession has hit the service sector particularly hard, and we believe consumers and employees will only gradually return to malls, restaurants, cinemas, offices and airports. This is particularly true for work and other activities where public transit is required. Further, even a month after Labour Day, there remains much debate and uncertainty regarding schools and universities.

- Further, the COVID-19 shock has accelerated several long-standing trends. One is lower-for-even-longer interest rates and a world of yield starvation. The Fed has made it clear that it is "not even thinking about thinking" about hiking rates. The COVID-19 shock has also acted as an accelerant for technology and the digitization/virtualization of the economy. This is being reflected in the shift to working-from-home, EdTech, e-fitness, telehealth, e-commerce, and so on.

- Market volatility typically rises ahead of elections, and the period before this year's U.S. presidential election is proving to be no exception. Moreover, if the election is close, it is possible that the period of elevated uncertainty will last well beyond November 3. During the contested period in 2000, the S&P 500 Index declined by 8% and the 10-year bond yield plummeted by 80 basis points. During periods of rising volatility, high-quality companies with strong earnings visibility and sustainable free cash flow, typically outperform.

- Given this challenging backdrop, the consensus expects S&P 500 Index earnings per share to decline by 20% this year, and then to rise by 28% in 2021 and 15% in 2022. For the MSCI World Index, the consensus expects earnings per share to decline by 19% this year, and then to rise by 30% in 2021 and

16% in 2022. Valuations imbed aggressive earnings growth expectations, and lower-for-longer interest rates, leaving little room for error. This is especially important as we begin the third-quarter earnings season. Last quarter, the vast majority of companies announced above consensus, but most also emphasized the elevated level of uncertainty, a perspective that was reflected in the relative lack of guidance for the remainder of the year and into 2021.

- Looking forward we continue to expect fat and flat returns. That is significant volatility and a relatively wide range across sectors, with overall upside of 6% to 10% over the next 12 months.

- Finally, it is especially crucial in this environment to identify companies that have sustainable cash flows and are focused on maintaining their dividends. Moreover, the yield from equities is likely to be far superior to that attainable in fixed income markets. As a result of the above points, we believe the best-positioned companies are those that have a demonstrated ability to produce sustainable free cash flow and to allocate that cash flow effectively between return of capital options and reinvestment/acquisition opportunities.

Source: Bloomberg Finance L.P., Morningstar Direct and Epoch Investment Partners, Inc.

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