ANTARES INVESTMENT MANAGEMENT

Investing in a Period of Heightened Uncertainty

For many investors, the events of this year are unprecedented. Seasoned investors, on the other hand, will recognize the recent market downturn as part of the normal cycle of investing. After a number of years of rising corporate earnings, the economy has come to an abrupt halt and stock prices have dropped rapidly. Historically speaking, phases of growth and decline have been marked by investors thinking "this will never end". It is typical in the latter stages of either phase for sentiment to be backward-focused and overly optimistic, or pessimistic, as the case may be. As we are witnessing now, cycles come to an end and new ones start.

The past few years have been marked by stock prices that, in many cases, had advanced significantly more than the underlying profits of the companies they represent. This has been accompanied by heavy use of debt by both consumers and corporations, and, in our opinion, an insufficient respect for risk. Some have believed that it is easy to make money in real estate or in the stock market. This view is changing very quickly. We are on record for communicating our concerns about the economic cycle turning down and the risk this could pose to the prices of many equities. In our view, it was only happenstance that the Covid-19 coronavirus got investors rethinking current stock prices. With or without the virus, we believe that markets were setting up for a general decline, sooner or later.

To address the risks, we took several steps well in advance of the current crisis. For example, we have let you know already about our focus on balance sheet strength of each of the businesses in your portfolio. When the economy turns south, "cash is king" while heavy debt limits one's options. In our view, well-financed companies that provide in-demand products and services will get through this downturn just fine. While share prices have declined, we are not concerned about the ability of your companies to weather the storm and emerge in good shape, particularly when compared to their indebted competitors.

More recently, we have made some pro-active changes to the bonds held in your portfolio. This has been done to protect your portfolio from the high levels of debt that many companies are carrying. While we only place money in investment-grade bonds to begin with (as opposed to higher-risk "junk bonds"), we have moved money to higher-grade bonds within that category. These include both high quality corporate bonds and government bonds, which offer added security. In some client portfolios the shift is still in the works. As a side note, junk bonds have declined significantly in the current environment, where investors are once again learning that quality matters.

While we don't want to sensationalize the current situation (we will leave that to the media), it is important that we acknowledge that no one knows how long the current situation will last, nor how deep the impact will be economically. Pundits with strong convictions are guessing and apt to be wrong. Our goal is not to predict the path of the pandemic but to prepare your portfolio for different possible scenarios. This requires thoughtful analysis and a solid framework as bulwarks against *the noise*.

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As a reminder, your portfolio is not invested in "the market". Rather, you hold ownership stakes in a select number of well-financed and profitable companies that offer valuable products or services. While it is true that these companies may experience short-term disruption in their operations due to supply chains and closed locations, we believe their long-term profit generating capabilities are unlikely to be impacted by the downturn. In the meantime, your companies have the wherewithal to work through the current situation and expand their market share. In the future, many may experience higher profits than would have been the case without the downturn. While we wait for the recovery, regular dividends are flowing into your portfolio.

In the coming months, if history is a guide, it is reasonable to anticipate that stock prices continue to be erratic. This is a natural part of the process as the emotions of fear and greed — amplified by Covid-19 — drive short-term price movement. You can expect that we will use these price fluctuations as opportunities to make changes to your portfolio. Some changes may be subtle and others larger: it will depend on the conclusions we draw from our analysis and what the market offers us. Any changes we make will be guided by the twin goals of protecting your portfolio and enhancing its growth opportunities. Please note that cash levels in your portfolio may be occasionally elevated while we are active.

We encourage you to take the long view. Volatile markets can be unpleasant, and the Covid-19 virus is a heavy burden for all of the world to bear. We will get through this and we believe this disruption will set the stage for future growth. Mathematically, larger investment returns are more probable from low price levels.

We wish you and your family strength and courage in these unusual times. We are available over email or the phone if you want to communicate directly with us.

Thank you for your continued trust,

Your Portfolio Management Team

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