ANTARES INVESTMENT MANAGEMENT

VALUE PORTFOLIO

The Antares Value Portfolio focuses on companies that, in our analysis, are underpriced in the stock market relative to their underlying worth as businesses. Our strategy aims first to protect investors' capital by not overpaying for a given company - holding fixed income or cash when bargains cannot be found - and second, to grow that capital through share price appreciation as the company's value gets properly recognized within the equity market.

MANAGER COMMENTARY

Our overall goal is to help you achieve your financial objectives.

Despite our defensive stance and currency headwinds, investment results in 2021 have been substantive.

The contrast between the real-world economy and stock markets remains wide.

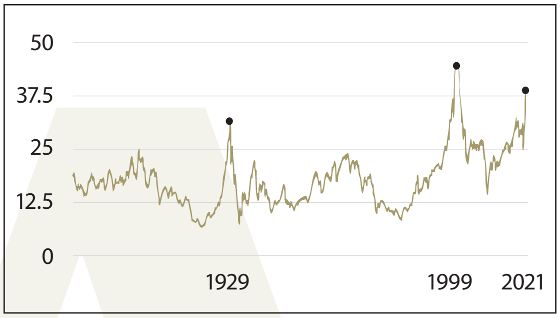
Our overall goal is to help you achieve your financial objectives. We do this primarily by making investing decisions with the aim of protecting the wealth you have already built and continuing to grow your portfolio. At times, it is the protecting that takes precedence, and at other times it is the growth that takes precedence. Oddly, this time-tested approach, made famous by Warren Buffett, is usually at cross currents to the prevailing thinking. When investors are generally pessimistic (cheaper prices) we tend to see opportunity, and when there is general euphoria (high prices) we tend to see risk. Therefore, the performance of your portfolio tends to be very different from the general market and, we believe, most other portfolios. With that said, we are very pleased to see substantive portfolio returns in the middle of a defensive stance, and despite an almost 9% headwind from the depreciating U.S. dollar over the past year.

The contrast between what is happening in the real world (i.e. the economy) and what is happening in the stock market continues to be stark. While Canadian Gross Domestic Product (GDP) is still below the pre-Covid peak, the euphoria around Canadian stock markets appears to be wildly disconnected. Corporate sales and GDP have risen about 1.5% per year over the last decade, and corporate profits have risen about 2.3% over that time. However, for every dollar of profit, investors are now willing to pay 40% more than they were a decade ago. The disconnect between price and profit is the largest it has been since the technology bubble at the turn of the century.[1]

In the U.S., the discrepancy is even greater. GDP is slightly higher than the pre-Covid peak, and GDP, corporate sales, and profits have been growing at a faster rate than in Canada over the last ten years, but investors south of the border (and many Canadian buyers as well) are now willing to pay an astonishing 72% more for each dollar of profit than they were 10 years ago.[1]

The accompanying chart illustrates the continued climb in average prices paid per dollar of profit. Even with the smoothing effects of using the ten-year average profit numbers you can still see the historically high level of the current U.S. market.

Shiller Cyclically Adjusted Price Earnings (CAPE) Ratio - Monthly Data From 1881



July 1, 2021 number: 37.9
All time high: 44 on December 1 , 1999
Source: Robert Shiller

While we believed stock prices were already too high a few years ago, they have continued to get more expensive. As the chart shows, U.S. stock markets are now flirting with levels that have been reached only once before, in the 1999-2000 tech bubble. The aftermath was not a pleasant one. We aim to keep your portfolio from suffering that same fate.

Against that backdrop we continue to try to be rational, looking for opportunities to purchase an ownership stake in a well-run business at a price that makes sense based on the underlying profits and cash flows, not on speculation that someone else might be willing to pay an even higher price.

[1]*Source for data: Bloomberg*

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Stock prices cannot outpace profit growth indefinitely.

We fully exited your investment in Cooper Tire at a nice profit.

We added to your investments in Vistra Energy and Subaru, both of which we view as attractively priced.

It is hard to be rational when others are not in most aspects in life…even more so when investing is concerned. The fear of missing out (known as "FOMO") is simply too great, and many investors succumb to the belief that markets can only go up. Longer term history teaches us that prices cannot outpace profits indefinitely. The longer the disconnect is allowed to continue, the greater the likely fall and the bigger the hit to portfolios.

As you may recall, Goodyear Tire and Rubber made an offer to purchase Cooper Tire, which you had owned, earlier this year. We sold about half of your holding in Cooper Tire shortly after the announcement as the price offered was quite a bit higher than our calculated value of the firm and, in the excitement of the announcement, offers to purchase at even higher prices persisted. We did, however, hang on to half of the ownership stake in case a larger offer was going to come along. Given the superior operating profit margins of Cooper and the fact it had more cash than debt, we felt there was at least a chance of another suitor appearing. There was, as always, a risk that the deal would fall apart at the last minute, but given the parameters of the deal we felt that risk was low. That provided some downside protection while we waited. When it became apparent that no other offers would be forthcoming, we sold the remaining stake. Despite some headwinds from rising rubber prices early in your ownership period and the Covid impact more recently, it has turned out to provide a nice profit overall…just under 20% annualized over the holding period.

This quarter, we have also added to your ownership of Subaru. We still like the company for all the reasons we did before, perhaps even more so now that the price of ownership is reduced. Subaru remains a world leader in terms of profitability; it has the highest average operating margins over the last five years, and in a global industry rife with overly indebted car companies, Subaru's lack of debt stands out. In fact, over 66% of the current stock market price is backed by cash in the bank. If we take away the modest debt, that number is still over 40%. All else being equal, we would rather own a company with low levels of debt and plenty of cash than one that is highly indebted with no cash reserves. There is always uncertainty, and the extra cash buffer provides plenty of safety and flexibility.

We continue to add to the ownership stake in Vistra, the electricity provider with large operations in Texas. We believe the impact of the Texas winter storm will prove to be temporary and the low price will be seen as an historic opportunity to buy shares in this firm. Demand for electricity is likely to continue to increase in the coming years, given population growth and the growing fleet of electrified transport (cars, trucks, and buses). While the storm's impact was substantial and will cost the company a year's worth of profits, it does little more than delay by a year the company's plans to build out its solar and wind generating capacity while decommissioning its coal-fired power plants. Cash flow is substantial, debt is very reasonable, they have the capacity to increase the dividend, and a year from now, the storm issues will likely be forgotten. Temporary hardship and the ensuing price decline can present a golden opportunity for the investor with a long-term focus.

The time for offence and growth will come, but right now we are concerned about generally high prices. We are happy with your current ownership stakes and would also be happy to purchase more when prices are attractive, but we want to do so prudently. After all, it is the downside protection that is paramount, and therefore, more valuable.

Enjoy your summer,

Gerry Bettig, CFA

VALUE PORTFOLIO

The Antares Value Portfolio is available to investors within a Separately Managed Account ("SMA") that holds securities directly, and through the Antares Value Pool ("Pool") which is held in the accounts of multiple investors. Data presented refer to the Pool. SMAs are customized and therefore their holdings and weights may diverge from those within the Pool. Sources for the data include: Bloomberg, NDEX, and Antares calculations. Unless otherwise stated, all data are as at quarter end.

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