PURPOSE SPECIALTY INCOME FUND
Q2 2020 COMMENTARY

Market overview

2020 was never going to be a dull year. As it started, investors were celebrating the signing of the long-awaited US-China trade deal and markets were at record levels. But the US election was everyone's prime suspect to be the event that would control the narrative and direction for the year. Oh, how quickly things changed. While Chinese delegates were in Washington signing the trade deal, the country was already dealing with a disease outbreak that would quickly spiral out of control and destroy many lives around the world.

How quickly everything changed is a great reminder to investors of why they must always be ready to adjust their plans and positioning. As Iron Mike Tyson famously said ahead of a title fight, "everybody has a plan until they get punched in the mouth."

This was supposed to be a year the central banks sat on the sidelines, as they normally do in election years, so as not to seem political. With that backdrop, many expected interest rates to creep higher with global growth. The yield on the US 10-year Treasury was supposed to approach the 2.5% level. No one was expecting that by mid-March rates would be slashed to zero and bonds would rally to record high prices.

The global pandemic seems to have changed our world forever. Simple tasks such as going to a restaurant, watching a sporting event in a crowd or even shaking hands with a stranger seem foreign. We all must adjust to the new normal and be ready to adjust again with the world. 'Buy and forget about it' seems to be one of the casualties of the pandemic. The new normal looks much more volatile.

The VIX index, which looks at implied volatility, is well off the highs of March, but that doesn't mean volatility is gone. There are many ways to measure volatility. One way that seems appropriate is to see how often prices move in dramatic fashion. Morgan Stanley looked at this by tracking three sigma cross-asset moves (a major price move in any asset relative to the previous day's implied three-month volatility) and found that 2020 has already had more of these events than any year since 1998. Things don't look to be calming down anytime soon.

Fears of a second wave of virus cases crept back into the equity market in June and a spike in cases in certain states has caused some of the economic reopening plan to be delayed or rolled back. Until we get a vaccine that is widely available and deployed globally, it appears the new normal will include the virus. Headlines around this will dominate investments and swing prices. But the more complex issue is still to come with the US election.

Regardless of his social beliefs, President Donald Trump has been very positive for the US stock market. Entering the year, betting odds had him easily winning a second term. But as the virus has disrupted many things, it has also affected the election. Debates around how he and his administration handled (or not) the virus have dramatically altered the polls, which now show the Democrats potentially sweeping the election. This event has not been priced into the market and will become the story for the summer.

How a desperate President Trump will respond to worsening polls is becoming the biggest risk to the market. Does he lash out at his opposition even more than before or does he throw money at the problem in the form of tax cuts and stimulus packages? Does he go back to his old favorite plan of engaging in a trade war with China? Any or all of the events will be difficult to predict and model.

The first half of the year is now in the books. After a violent rebound that resulted in the strongest quarterly rally in many decades, predicting the second half of 2020 is very difficult. Safe-haven assets such as gold and large-cap tech stocks have led and appear poised to continue winning.

A rotation towards cyclicals would go a long way to broaden out the rally and place it on stronger footing. For that to occur, global growth needs to reemerge as the story. For signs of this happening, look for a weakening US dollar, a higher 10-year bond yield and a breakout in commodities.

Fund performance and positioning

Fund performance was positive in this environment, with all asset classes contributing positively to the return. Contributions were essentially in line with allocation size. Canadian equities led to the upside due to strong gains in the utilities, financial and real estate sectors. High-yield credit was the next strongest contributor, followed by US equities. The contribution from Canadian preferred shares was disproportionately above its weight. International equity and investment-grade credit were essentially flat.

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We have taken some risk out of the portfolio after tilting into a “risk-on” mode in March, by taking off some equities and allocating back to investment grade bonds. In the long term however, we believe it is likely that strategic asset allocation will shift from fixed income to favour alternative sources of income, such as put writing, or volatility protection, including gold. Fixed income offers modest opportunity foreseeably with central banks taking a dominant role in suppressing rates and buying bonds.

We are taking a cautious stance going into the final half of 2020. We must remember that the stock market is not the economy and the underlying economic fundamentals in North America are weak, despite some degree of recovery. Asset prices remain inflated from central bank interference.

What we do know is that a new normal is taking shape in which consumer behaviour has rapidly changed. When we will return to pre-pandemic levels of activity remains unclear. However, two clear themes have emerged through the market turmoil: the digital revolution for modern society has accelerated and gold has made a return as a classic insurance policy. Recognizing this, future positioning will also adapt. In terms of the larger role of tech in society, we must adjust the traditional approach to pension equity investments which has historically focused on blue-chip dividend stocks. Implementation of such an approach in an income accretive manner is difficult, and is the challenge we are currently tackling to solve for long term investor goals.

In regards to the decline of traditional fixed income, we will look to allocate to alternative sources of income so as not to take excess equity risks. What is clear is that record low yields and extensive bond-buying programs will put a cap of sorts on the income from traditional vehicles.

And lastly, we must not fight the Fed and other central banks. We see little to no value in betting against the market when the buyer of last resort has established an unlimited balance sheet.

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Portfolio statistics

# of Holdings	150
Yield	5.3%
Price-to-Earnings Ratio	13.2
Price-to-Book Ratio	1.9
Price-to-Cash-Flor Ratio	6.5
Average Mkt Cap ($B)	$68.44

Equity country breakdown

United States	33.6%
Canada	29.8%
International Developed	25.7%
International Emerging	10.9%
Total	100.0%

Equity sector breakdown

Financials	15.3%
Health Care	11.0%
Communication Services	9.6%
Consumer Discretionary	9.5%
Consumer Staples	9.7%
Information Technology	8.0%
Industrials	8.5%
Materials	8.2%
Energy	8.2%
Utilities	6.4%
Real Estate	5.5%
Total	100.0%

Asset class breakdown

- North American Equity **28.8%**
- International Equity **16.6%**
- Fixed Income **33.4%**
- Diversifiers **21.6%**
- Cash **-0.4%**

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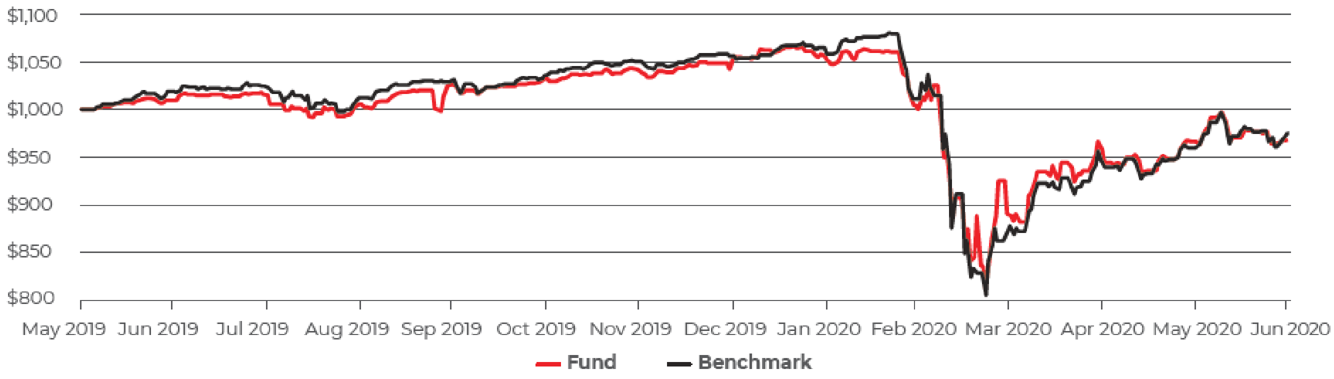
Growth of $1,000



Performance breakdown

Fund Name	1 Month	3 Month	6 Month	1 Year	Since Inception**
Purpose Specialty Income Fund	0.2%	8.9%	-8.3%	-4.2%	-3.3%
Benchmark	1.6%	11.0%	-7.6%	-4.3%	-2.4%
PSIF Model					
Purpose International Dividend Fund	1.4%	6.1%	-10.0%	-4.9%	-3.7%
Purpose Core Dividend Fund	-0.2%	12.0%	-13.4%	-6.7%	-5.2%
Purpose Emerging Markets Dividend Fund	3.5%	9.1%	-7.7%	-4.7%	-3.6%
Purpose Canadian Preferred Share Fund	4.8%	13.6%	-16.7%	-11.8%	-11.0%
Purpose Strategic Yield Fund	3.1%	12.8%	-6.5%	-5.3%	-4.4%
Purpose Premium Yield Fund	0.8%	9.0%	-5.5%	-2.3%	-1.5%
Purpose Global Bond Fund	1.5%	9.7%	-1.4%	0.1%	0.6%
Purpose Money Market Fund	0.1%	0.2%	0.6%	1.7%	1.8%
Bridging Income Fund	0.0%	0.7%	2.7%	7.5%	8.2%
Benchmark Model					
S&P/TSX Dividend Composite Index	1.0%	11.8%	-11.3%	-6.4%	-5.0%
S&P 500 High Dividend Index (USD)	0.6%	14.9%	-27.3%	-22.6%	-19.4%
CBOE S&P 500 PutWrite Index (USD)	1.0%	11.1%	-11.9%	-7.5%	-4.7%
S&P/TSX Preferred Share Index	3.9%	15.0%	-11.2%	-7.2%	-5.6%
FTSE TMX Universe Bond Index	1.7%	5.9%	7.4%	7.7%	8.5%

All data is as at 06/30/2020 and sourced to Bloomberg unless otherwise noted.