



Financial Letter
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Introduction

Hello everyone,

North American stock markets continued climbing in the third quarter of 2020 before pulling back in early September. Since then, the usual leaders—U.S. large-cap tech stocks—regained momentum, reaching for new heights.

The current situation obviously reminds me of my early years in the business, in the late 1990s, when the entire market was soaring, particularly tech firms. Humans are the result of millions of years of evolution and have therefore scarcely changed in two decades. That's why the infamous day traders and other small-time speculators are back with a vengeance, dabbling in stocks on their cell phones. A recent study shows that while retail investors account for only a small portion of market players, their real impact is five times larger since other participants are not as active, which can result in the type of market we're currently experiencing.

Most of us who are longer in the tooth know how this is going to end. But since this particular environment can last for months or even years, it would be clearly unthinkable not to cash in on it.

Since the beginning of the year, all our strategies have added value. The same cannot be said of a number of funds and managers who failed to adjust and are having a tougher year as a result. While not wishing any misfortune on anyone and recognizing that Rivemont will certainly have less spectacular years of its own, I'd like to take this opportunity to thank the many new clients who have joined us in recent months.

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In keeping with the times, you can now follow Martin Lalonde on Twitter at @MartinRivemont. And as always, feel free to visit Rivemont's Facebook page. Lastly, please don't hesitate to contact me at info@rivemont.ca if you'd like to be included in the Crypto and MicroCap Fund newsletter mailing lists.

In this financial letter, I'll give you my take on the past quarter (including the MicroCap Fund) and discuss our pandemic investment decisions. I'll continue by examining the U.S. election and its historic impact on markets. Then, as usual, I'll outline our market outlook and our key positions.

Enjoy!

Third quarter 2020

"Excellent third quarter for the Rivemont MicroCap Fund."

The quarter that just ended saw positive results for all of our strategies and for the broader market, but the Rivemont MicroCap Fund was a particular standout. Here is an excerpt from the Fund's latest newsletter:

Canadian microcaps have fared well in each of the past two quarters. However, we're still far from seeing any kind of major excitement or enthusiasm for the sector. There is still a significant valuation disconnect between large caps and microcaps. Since we continue to find good deals and our microcap valuations are still very reasonable, we feel the fund's portfolio (and the Canadian microcap sector in general) currently boasts a very compelling risk/return profile relative to other asset classes.

Now let's take a look at a few key fund metrics, as at September 30, 2020:

- \$8.43 million in net assets under management.
- 94% invested and 6% in cash.
- 33 portfolio positions, the largest accounting for 10.6% of assets.
- The top five holdings represented 38% of the portfolio.
- Unit value of \$7.58,* for a return of +22.7%** for the quarter.

* Series B units (MAJ724)

** Return net of all costs.

To measure our third-quarter performance, i.e. from July 1 to September 30, 2020, we chose the S&P/TSX Small Cap Index as our benchmark, which reflects the performance of the Canadian small-cap market. To obtain an overview of U.S. market performance, we used the LD Micro Index as our benchmark. During the quarter, the Fund performed as follows against the two benchmarks:

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Q3 2020 Returns	
S&P/TSX Small Cap	6,6%
LD Micro	8,9%
Rivemont MicroCap Fund	22,7%

As you can see, the Rivemont MicroCap Fund had a stellar third quarter relative to its benchmarks. It's hard to attribute this outperformance to any one factor. We simply think it reflects the quality of our security selection, as our target companies have weathered the crisis better than others. The fact that the portfolio is primarily invested in the tech sector has certainly been a major asset amid the pandemic.

To put the entire COVID-19 crisis into context, here are the returns of the same benchmarks for the year to date (YTD), comprising the first nine months of 2020:

2020 YTD Returns	
S&P/TSX Small Cap	-8,6%
LD Micro	2,7%
Rivemont MicroCap Fund	21,8%

Once again, the Fund performed well and demonstrated the resilience of our investment strategy despite extreme market fluctuations during the year.

The number of positions held in the Fund has risen significantly since the beginning of the year, from 25 to 33. There are two reasons for this increase, which we consider to be temporary:

- The sharp stock market declines earlier this year created many bargains and opportunities. At any given time, we track 100 to 150 securities that meet or are likely to meet our investment criteria. These stocks are often still too expensive, and we have to wait for a favourable opportunity to pick them up. This year, the market offered us several opportunities to buy quality companies, and we took them.
- When we sell positions, it can sometimes be hard to find enough market liquidity to dispose of our shares quickly. Accordingly, we have to be patient and wait for the right time, or sell them very gradually so as not to drive down the stock price. We currently hold

"The Rivemont MicroCap Fund maintains a concentrated approach with around 25 stocks."

some positions that individually represent 0.5% – 2% of the portfolio, and we hope to dispose of them in the coming months, as the opportunity arises.

Our objective remains to invest according to a concentrated strategy of about 25 securities, with a high percentage in our top performers. As a result, you can expect that the number of securities in the portfolio will gradually decline and trend down to that level. Ideally, we'd like to hold over 40% of our assets in our top 5 picks, and over 75% in our top 15. At present, we hold 38% and 70%, respectively.

“The remote technology subsector is currently seeing a strong growth.”

The ideas discussed below were also featured in Martin Lalonde's monthly column in Le Droit Affaires, the Ottawa daily's business supplement.

Investing During a Pandemic

Crises like the one we're facing can offer highly lucrative investment opportunities from a sector standpoint. For example, while the energy, finance and real estate sectors are still well below their peaks for the year, the high-tech, healthcare and consumer discretionary sectors are breaking new records every week.

As lockdowns grew more widespread, it became more than likely that the remote technology subsector would enjoy outstanding growth. And Zoom Video Communication is obviously the best example of that. The company has seen its flagship product become indispensable to most organizations in response to the pandemic. Video communications grew exponentially, as did the company's share price, surging from \$70 in February to over \$300 by the end of August.

In the same vein, two other companies have tapped into this extraordinary and unprecedented windfall, reaping enormous profits in the process. Electronic signature expert DocuSign saw its market share skyrocket in spite of fierce competition from established players such as Adobe. Being both user and wallet friendly gave DocuSign the impetus it needed. The stock soared from \$45 last September to over \$200. Remote medical exam leader Teledoc has factored in our special lockdown needs while meeting our understandable medical concerns at this time to continue growing at breakneck speed, with its stock rising fourfold in the past year.

I think it's imperative not to base our investment decisions on sharp market declines or increases in times of uncertainty. Instead, we need to assess the resultant changes in consumer spending habits. There will always be opportunities, but they have to be carefully targeted.

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The U.S. Election

Contrary to what we may intuitively think, in the long run, neither of the two major political parties campaigning south of the border has really had a greater market impact than the other. In fact, good years follow bad, and vice versa, resulting in fairly equal returns (very slightly higher under Democratic administrations).

“The election of one or the other major American party doesn’t have, historically, a great impact on the markets.”

That being said, we have to dig a little deeper to uncover any interesting recurring trends. Historically, the Republican Party has been seen as pro-business and pro-market and ideologically in favour of smaller government. Conversely, Democrats typically pride themselves on protecting workers and advocating greater equality between social classes.

These competing ideologies are captivating to investors, because transitions between Republican and Democratic administrations give rise to statistically interesting anomalies.¹

	Election year	Inaugural year
Transfer of power from Republicans to Democrats	-2.8%	21.8%
Transfer of power from Democrats to Republicans	13.2%	-6.6%

Investors become concerned over Democrats taking power during election years, whereas they get excited about the prospect of a new Republican administration being elected.

What they forget is that no matter the party, politicians are still politicians, who unfortunately have a nasty habit of not living up to their commitments or keeping promises that are too often overblown. When the Democrats come to power, investors ultimately realize it is not the doom and gloom they were dreading, no socialists are clambering at Washington’s doorstep and markets bounce back fairly quickly. On the other hand, when the Republicans take power, we soon realize that they, too, will fail to keep their promises, and market momentum fizzles. Investors have to

¹ Global Financial Data, 1925–2009.

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understand that politicians greatly prefer to focus their energy on getting re-elected than on making ideologically sensitive decisions.

In closing, we must always bear in mind that, when it comes to finance, new legislation is really just an exercise in wealth redistribution. You can take from some of the rich and give to other wealthy people, take from the rich and give to the poor, or take from the poor and give to the rich. And it is up to investors to find attractive opportunities in this environment.

¹ Global Financial Data, 1925–2009.

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Market Prospects

Rivemont Investments			
Subject	Question	Recommendation	Comments
Allocation between equities and fixed income securities	Which are most interesting, stocks or bonds?	Still underweight in bonds.	We recommend adding alternative investments to portfolios.
Distribution between Canadian, U.S. and international securities	Which securities are most interesting: Canadian, U.S. or international?	U.S. equities still lead the pack.	Gold is certainly trending higher.
Distribution between corporate and government bonds	Which are more interesting, corporate or government bonds?	Long-term government bonds have little attraction.	We recommend the most defensive products and cash.
Investments in Canadian dollars or in foreign currency	Do investments in other currencies increase or decrease the total yield?	U.S. assets are still just as essential to our portfolios.	We do not anticipate any abrupt currency movements.



Favorite Securities

You will find below a list of the individual securities with the largest weight in our "growth" portfolio. These stocks were selected based on their respective potential to outperform the stock market. You will find a short description of their activities, the annual dividend, if any, and the total return since their first inclusion in our portfolio.

As of October 26, 2020

1) Symbol: BABA

Name: **Alibaba**

Description: Online retailer.

Dividend Yield: 0.0%

Total Return: 12%

2) Symbol: AMZN

Name: **Amazon**

Description: Online retailer.

Dividend Yield: 0.0%

Total Return: 56%

3) Symbol: DOCU

Name: **DocuSign**

Description: Electronic signature software.

Dividend Yield: 0.0%

Total Return: 293%

4) Symbol: AQN

Name: **Algonquin Power & Utilities**

Description: Renewable energy.

Dividend Yield: 4.0%

Total Return: 2%

5) Symbol: IFC

Name: **Intact Financial**

Description: Casualty insurance.

Dividend Yield: 2.3%

Total Return: 54%

6) Symbol: RY

Name: **Royal Bank**

Description: Financial services.

Dividend Yield: 4.5%

Total Return: 31%

7) Symbol: IBB

Name: **iShares NASDAQ Biotechnology**

Description: Biotechnology companies.

Dividend Yield: 0.2%

Total Return: -3%

8) Symbol: XGD

Name: **iShares S&P/TSX Gold ETF**

Description: Canadian gold producers.

Dividend Yield: 0.2%

Total Return: 57%

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Conclusion

As fall begins and the pandemic seems set to hunker down for the winter along with us, keep in mind that the rapid worldwide stock market recovery we've been witnessing is not a normal occurrence. In our view, we must remain vigilant and not hesitate to increase portfolio cash levels should the need arise. However, it would be irresponsible not to capitalize on the current upturns in tech and healthcare stocks. That's why we believe active management remains the most appropriate response to heightened volatility in the current market.

Sincerely,

Martin Lalonde, MBA, CFA
President

RIVEMONT

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