AlphaDelta Growth of Dividend Income Class
Quarter 2, 2019, Commentary

Hello everyone,

This is the quarterly advisor update of the **AlphaDelta Growth of Dividend Income Class** ("GoDI" or the "Fund") from SciVest Capital Management Inc. (the sub-advisor to the Fund).

This is first *quarterly* advisor update commentary, as we have now switched from a *monthly* commentary schedule. We believe that since the GoDI portfolio changes so slowly through time, and since the growing income strategy is so long-term oriented, a quarterly commentary schedule would represent the better use of everybody's time and resources. Nevertheless, **we will continue to publish and post on our website a *monthly* GoDI Portfolio Disclosure** (http://scivest.com/strategies/manager-commentary).

Attached to this commentary is the GoDI Portfolio Disclosure as of the end of the quarter. The first couple pages of the Portfolio Disclosure show all of the current stock holdings of the Fund, as well as some descriptive, dividend and valuation characteristics for each portfolio holding – plus overall portfolio averages. The third page of the Portfolio Disclosure shows a number of relevant pie charts depicting overall GoDI portfolio exposures and characteristics such as sector, market capitalization, dividend yield and dividend growth "bucket" exposures.

Portfolio Income and Income Growth:

The two primary **objectives of the Fund are to provide its shareholders with: (i) a consistent, and above average, annual distribution yield; and (ii) growth in the absolute level of distributions per share through time (i.e., income growth)**.

We attempt to deliver on these Fund-level objectives by investing in a global portfolio of equities which, on average, pay a higher than average dividend yield and which are growing their dividends per share at a relatively high rate (in the context of their current yield). As shown in the Portfolio Disclosure, **across the Fund's current holdings, the weighted average gross dividend yield is 4.0% per annum** (versus 1.9% for the Russell 1000 Index and 2.5% for the MSCI World Index) **with impressive double-digit trailing 1, 3 and 5-year dividend growth rates of 15.1%, 19.1% and 18.9%, respectively**.

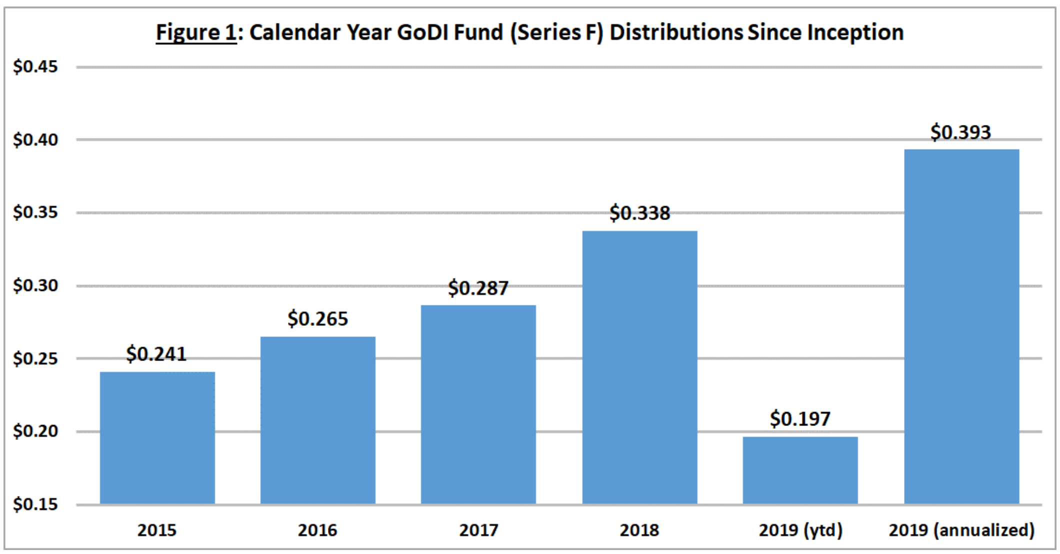
This 4.0% average portfolio dividend yield is extremely well covered by company earnings and cash-flow. Specifically, the 4.0% average dividend yield compares to a portfolio weighted average forward earnings per share yield of 10.4% **(i.e., 260% dividend coverage by earnings)** and forward cashflow yield of 14.3% **(i.e., 356% dividend coverage by cash-flow)**.

The Fund has a unique distribution policy whereby it distributes to its shareholders on a month-end basis *every dollar* (and no more) of dividend income (net of any dividend with-holding taxes) accrued by the Fund during the month. As a result, monthly income varies with the dividend cycle of its holdings, but the distributions perfectly reflect the true dividend income (net of tax) received by the Fund. And, since the distributions are a true reflection of the income received by the Fund, they can be used to judge the true income generation and income growth capability of the Fund.

At the Fund-level, **the trailing 12-month distribution yield of the Fund (Series F shares) as of June 30th is a solid and above average 3.5%**. Note that this distribution yield is also quite tax efficient, as compared to most other income alternatives.

Furthermore, this trailing 12-month 3.5% distribution income yield has been growing through time. Specifically, **the trailing 12-month Fund-level distribution per share has experienced 11.3% growth year-over-year, 7.7% per annum growth over the past three (3) years, and 11.0% per annum growth since the inception date of the Fund** (Series F shares). We consider this **substantial income growth in the context of a relatively high and diversified current income yield of 3.5%**.

To further illustrate this distribution growth effect over time, Figure 1 below shows the total distributions for the Fund (Series F shares) for every calendar year since the inception date of the Fund. Again, note that these distributions per Fund share reflect true underlying income growth resulting from the Fund's portfolio of dividend-paying equities have grown their dividends per share while held by the Fund.



The **current Fund distribution yield of 3.5% also compares very favourably with the June 30th yield of 1.46% on the benchmark 10-year Government of Canada bond**. Even with more than twice the yield of the 10-year bond, **the Fund's income had grown at a rate 11.0% per annum – whereas, of course, a 10-year bond's income does not ever grow**. In addition, the Fund's distributions are far more tax efficient (in taxable accounts) than a bond's income.

Current Portfolio:

The **GoDI portfolio is, as always, very different from global equity benchmarks with a current Active Share of 90.0%** – meaning that 90.0% of weights of our portfolio holdings do not overlap with the MSCI World Index benchmark (alternatively, only 10.0% of the weights of the GoDI portfolio holdings overlap with the MSCI World Index). This means that the GoDI portfolio should provide diversification and differentiation within an otherwise diversified portfolio.

The current GoDI portfolio is itself well diversified across sectors and industry groups with **the largest sector allocation (Financials) currently at 30.8%**. In order of size, we have the following exposures to the Bloomberg defined sectors (plus Real Estate): 30.8% Financials, 10.6% Health Care, 10.4% Consumer Discretionary, 9.0% Energy, 8.7% Technology, 7.8% Real Estate, 7.5% Communications, 2.8% Materials, 2.8% Industrials, 1.1% Consumer Staples, and 0.6% Utilities. In addition, the Fund holds 5.6% in the "Other" sector category, which represents the Fund's investment in the AlphaDelta Canadian Growth of Dividend Income Fund.

On an individual stock holding basis, we currently hold a **diversified portfolio of 70 equity positions** (not including the Fund's holding in the AlphaDelta Canadian Growth of Dividend Fund which itself holds another 35 individual equity holdings). The top 10 individual equity holdings represent 32.4% of the Fund's assets and are in descending order of size: Brookfield Property Partners (BPY.U, 4.2%), CVS Health Corp (CVS, 4.0%), Abbvie Inc (ABBV, 3.7%), Manulife Financial Corp (MFC, 3.5%), Enbridge Inc (ENB, 3.4%), Morgan Stanley (MS, 3.0%), Broadcom Ltd (AVGO, 2.8%), Prudential Financial Inc (PRU, 2.7%), Fiera Capital Corp (FSZ, 2.6%) and Invesco Ltd (IVZ, 2.5%). (See entire GoDI portfolio attached hereto.)

A byproduct of the sub-advisor's growing income investment strategy is that the GoDI portfolio typically has much better (i.e., cheaper) valuations than the overall equity markets. Currently, the portfolio weighted **average 12-month forward price-to-earnings ratio is 11.4x** (versus 17.0x for the Russell 1000 Index and 15.6x for the MSCI World Index) and the **average 12-month forward price-to-cash-flow ratio is 8.3x** (versus 12.0x for the Russell 1000 Index and 10.3x for the MSCI World Index).

Portfolio Changes and Movers:

During the second quarter, we **initiated new positions** in Canadian asset manager Fiera Capital Corp (FSZ), US refiner Marathon Petroleum Corp (MPC), and US healthcare behemoth UnitedHealth Group Inc (UNH). We also **increased (by at least 0.5%) our existing position** in US refiner Valero Energy Corp (VLO).

During the second quarter we **eliminated our positions** in Bunge Ltd (BG), CyrusOne Inc (CONE), Diageo PLC (DEO), J2 Global Inc (JCOM) and Honeywell International Inc (HON). We typically eliminate positions when their forward-looking dividend growth becomes less promising (due to a number of potential reasons) and/or their valuations become excessively high (and thus dividend yields low). We also **decreased (by at least 0.5%) our existing positions** in CVS Health Corp (CVS), Invesco Ltd (IVZ), and Manulife Financial Corp (MFC).

Amongst the quarter-end GoDI portfolio holdings, the five (5) **highest returns during the second quarter** (in descending order) were: Legg Mason Inc (LM, +39.9%), Qualcomm Inc (QCOM, +34.6%), Blackstone Group LP (BX, +28.2%), WPP PLC (WPP, +23.7%), and HeidelbergCement AG (HDELY, +15.6%). Amongst the quarter-end holdings, the five (5) **lowest returns during the second quarter** were: Foot Locker Inc (-30.4%), Steel Dynamics Inc (STLD, -13.7%), Nissan Motor Co Ltd (NSANY, -13.0%), Simon Property Group Inc (SPG, -11.3%), and Intel Corp (INTC, -10.3%).

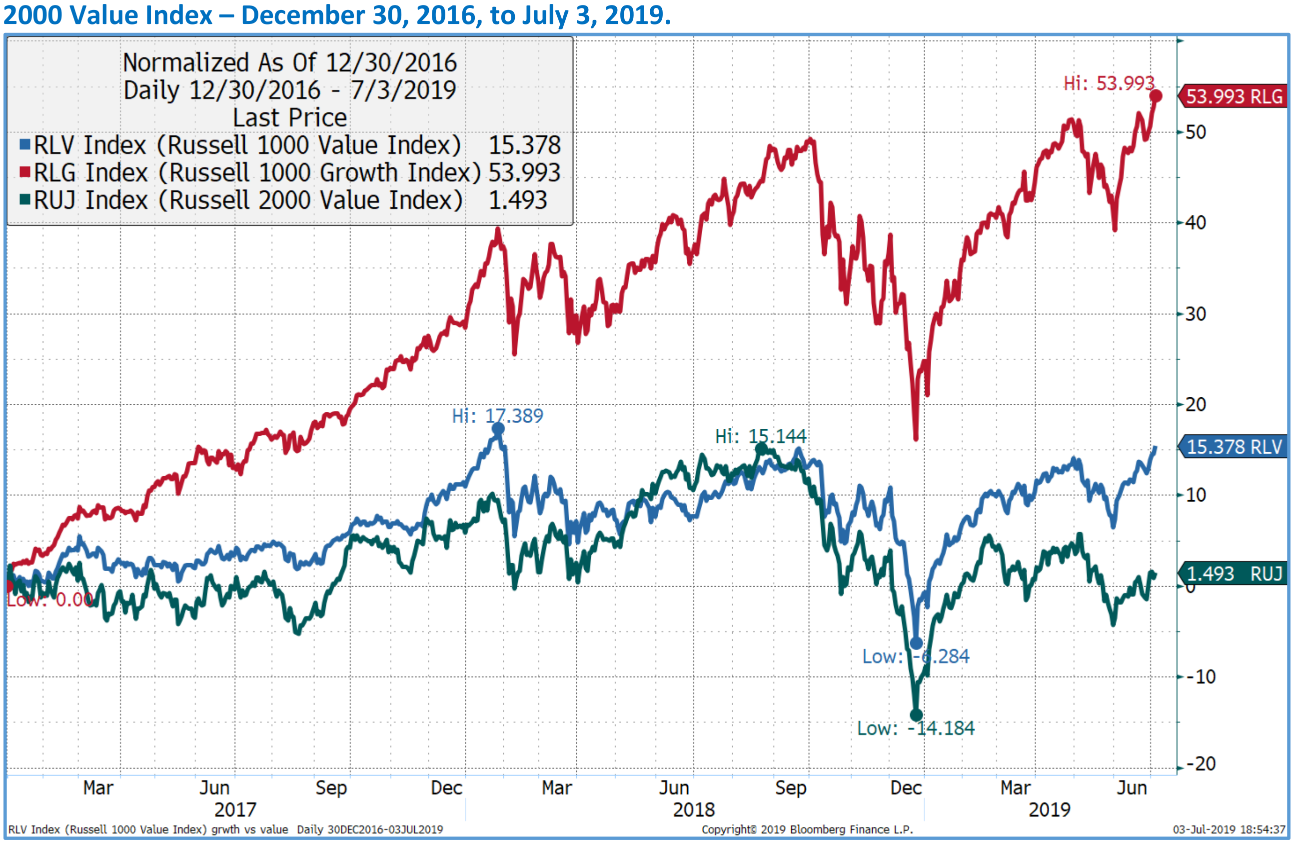
Market Commentary:

During the first half of 2019 the Canadian and US stock markets advanced nicely, rebounding from a sharp correction in late 2018. We believe that part of the reason for this rebound in equity prices is that the interest rate environment changed dramatically early this year from 2018, a year in which we saw multiple short-term interest rate increases from the US Federal Reserve. Many believe that these interest rate increases were the root cause of the 2018 equity market correction.

In early 2019, in the wake of a significant equity market correction, falling long-term bond yields and a continued US-China trade dispute, the US Federal Reserve hinted strongly that they might be willing to start cutting interest rates sometime in the near future if the data warranted such action. This sentiment helped fuel the rebound in equity markets during the first half of 2019. Ultimately this culminated with US and Canadian equity markets reaching all-time highs, and the US Federal Reserve delivering a widely anticipated 0.25% interest rate cut in late July – its first rate cut in eleven years, and the first since the Great Recession.

The markets now expect even more US Federal Reserve short-term interest rate cuts later this year; however, this expectation has led to a recent global collapse in long-term bond yields. This collapse in long-term bond yields has introduced enhanced uncertainty and volatility to almost all markets (bonds, stocks and commodities) in almost all countries. In addition, we face a number of growing global risks in the medium term including a hard October Brexit deadline, an intensifying US-China trade war and a general global slowing of economic growth – as well as a growing global bond market bubble. Nevertheless, we do not currently believe that the pre-conditions for a North American recession exist at the present time, and with both short and long-term interest rates having fallen and continuing to fall all over the world, we believe that Canadian and US equities continue represent reasonable valuation and opportunity in the context of these lower interest rates. In fact, we are surprised that, with the significant fall in all durations of interest rates in almost all countries of the world, that relatively high dividend paying equities with substantial dividend growth have not been well rewarded in comparison to other equities.

Graph 1: Relative Performance of the Russell 1000 Growth Index, Russell 1000 Value Index and Russell 2000 Value Index – December 30, 2016, to July 3, 2019.

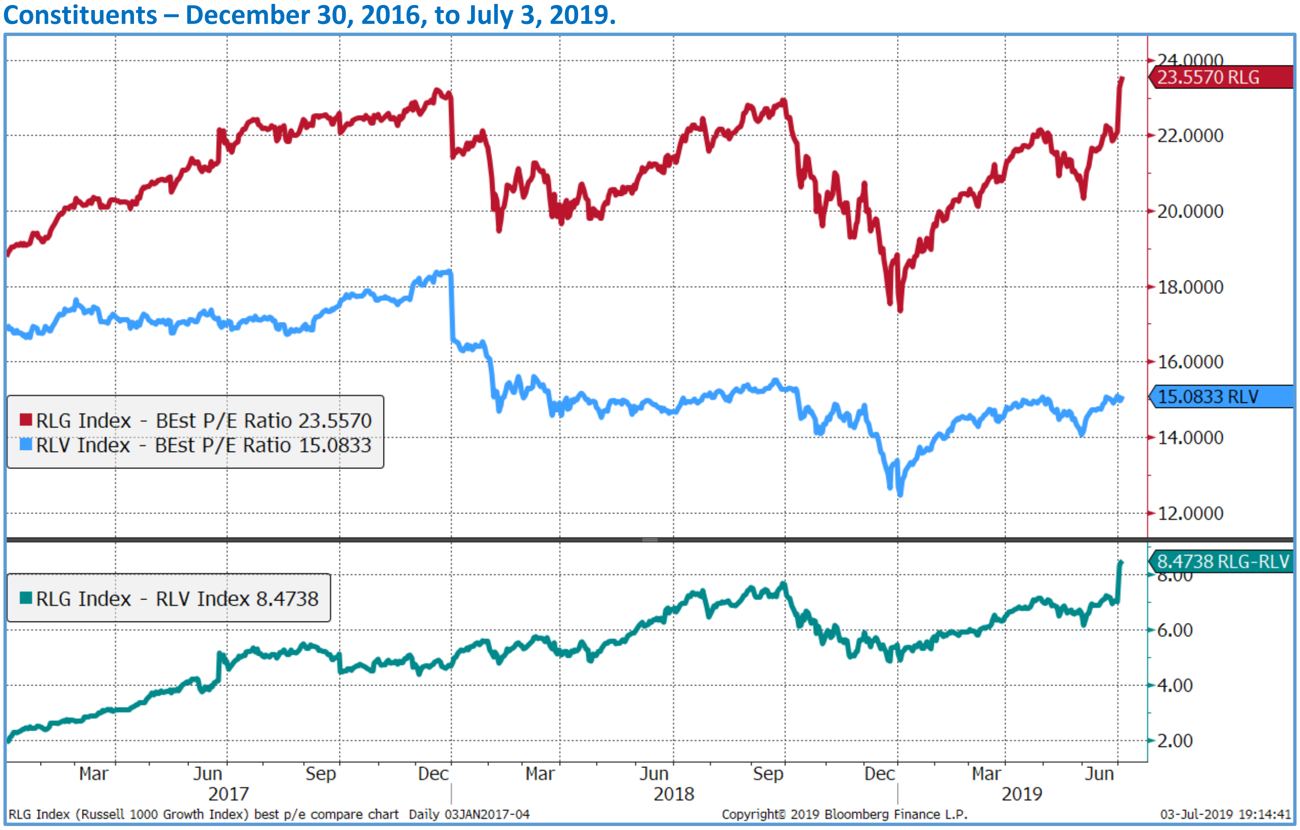


Part of the answer to the lack of outperformance of dividend-growth-at-a-reasonable-price (DGARP) equities is the historic underperformance of US value stocks relative to US growth stocks. Specifically, **as a consequence of our process to simultaneously maximize dividend yield and dividend growth while minimizing price paid, our portfolios generally have a significant value bias. However, as shown in Graph 1 above, US large-cap value stocks have underperformed large-cap growth stocks by almost 40% in the past 2.5 years (as judged by the Russell 1000 Value Index versus the Russell 1000 Growth Index)**. And, US small-cap value stocks have underperformed US large-cap growth stocks by over 50% in the past 2.5 years (as judged by the Russell 2000 Value Index versus the Russell 1000 Growth Index).

These growth-value returns spreads are historically large in nature. In fact, **taking a ratio of the Russell 1000 Growth Index value to the Russell 1000 Value Index value, the current ratio is only exceeded in the past 40 years by the 6 months before and after the peak of the 2000 technology stock bubble**.

Looking at the relative valuation levels of Russell 1000 Value Index constituents versus the Russell 1000 Growth Index constituents, we continue to see a picture whereby it is likely that growth stocks have gone too far relative to value stocks. In particular, Graph 2 below shows the 12-month forward analyst expected EPS relative to current stock prices for the constituents of the Russell 1000 Growth Index relative to the constituents of the Russell 1000 Value Index since December 30, 2016. While growth stocks generally trade at a premium to value stocks (by definition in many cases), Russell 1000 Growth stocks currently trade at 8.5 P/E turns above Russell 1000 Value stocks (i.e., P/E of 23.6x for growth minus 15.1x for value), up from just 2.0 P/E turns just 2.5 years ago. In fact, **over the past 2.5 years, Russell 1000 Growth stocks have increased in valuation from a forward P/E of approximately 19.0x to 23.6x (+24%), while Russell 1000 Value stocks have decreased in valuation from a forward P/E of approximately 17.0x to 15.1x (-11%)**.

Graph 2: Forward P/E Ratio of Russell 1000 Growth Index Constituents and Russell 1000 Value Index Constituents – December 30, 2016, to July 3, 2019.



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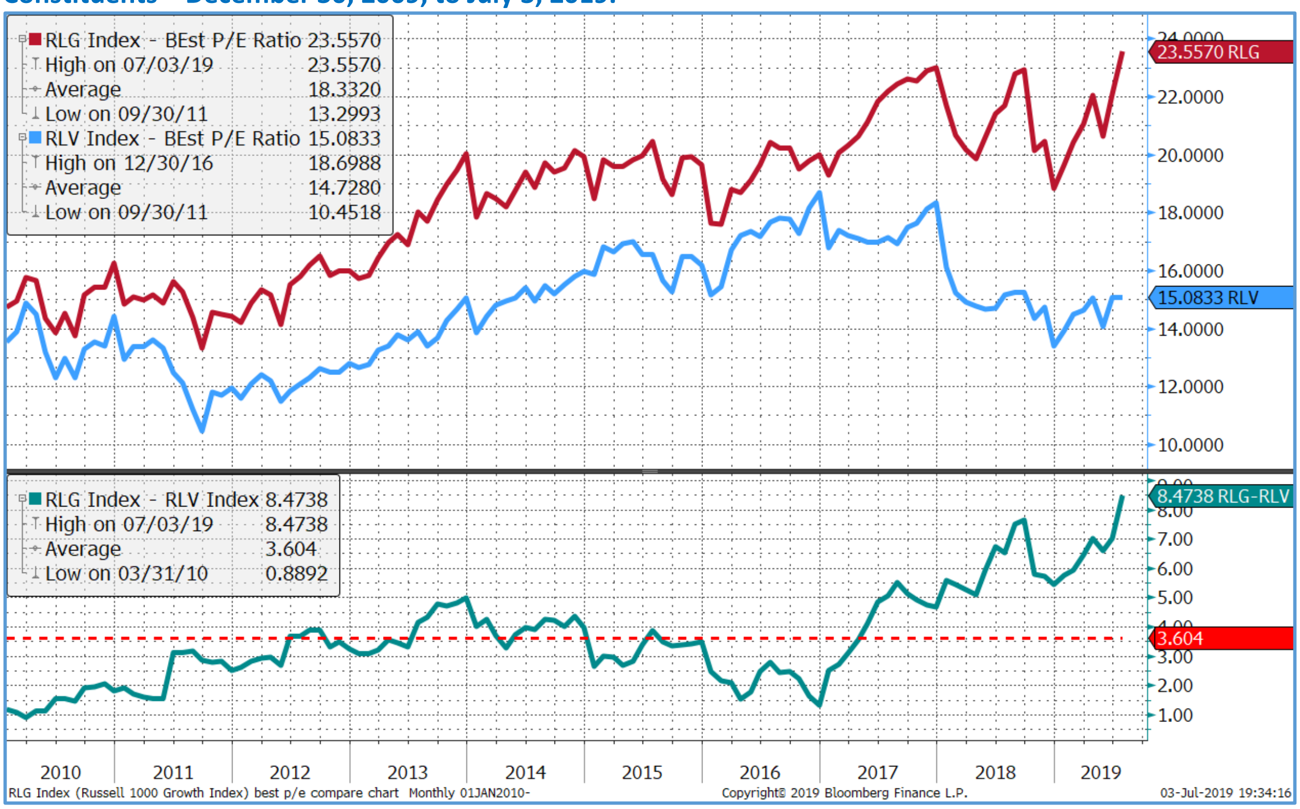
As a result, over the most recent 2.5 year time period where the Russell 1000 Growth Index has a return of +54.0% and the Russell 1000 Value Index has a return of only +15.4%, the vast majority of the return disparity is because the Russell 1000 Growth Index constituents have become much more expressive, while the Russell 1000 Value Index constituents have actually become less expensive. That is, **the Russell 1000 Growth Index's historic outperformance over the past 2.5 years is <u>NOT</u> because the constituent growth stocks have grown earnings and earnings expectations faster than the Russell 1000 Value Index constituents, it is because growth stocks have increased so much in valuation relative to value stocks.**

Graph 3 extends this valuation analysis back to the end of the Great Recession. As noted above, the Russell 1000 Growth Index constituents currently trade at a 23.6x forward earnings multiple while the Russell 1000 Value Index constituents currently trade at a 15.1x forward earnings multiple – in other words, growth trades 8.5 P/E turns higher than value. This 8.5 P/E turn premium of growth versus value compares to average valuation premium of 3.6 P/E turns over this entire cycle (note that this average includes the recent period of excessive valuation spread) – the highest it has been since the Great Recession. Interestingly, **while both growth stocks and values stocks began the current economic cycle each trading close to 15x forward EPS, 8.5 years later value stocks remain at approximately the same valuation level as they began, although growth stocks have become 50% more expensive.** As a result, while some say that "stocks are expensive", we say that only "<u>*some*</u> stocks are expensive" – specifically growth stocks (and low volatility, high earnings quality stocks).

<u>Graph 3:</u> Forward P/E Ratio of Russell 1000 Growth Index Constituents and Russell 1000 Value Index Constituents – December 30, 2009, to July 3, 2019.



While we have a few theories of why these performance and valuation spreads have developed – primarily related to "the machines" and the recent dominance of ETFs over active stock funds – we do believe that these spreads will normalize sometime in the future. Spreads such as these have always unwound in the past, and this time is unlikely to be different. When will this occur? Unfortunately, we have not idea. In the meantime, we take comfort in our portfolio holdings providing an average 4% dividend yield with 19% per annum dividend growth.

Q2-2019 Dividend Announcements:

Since income and income growth are the Fund's primary objectives, each quarter we report those Fund holdings which declared dividend changes during the prior calendar quarter. Recall also that one of our fundamental beliefs is that, if we can select stocks which consistently increase their dividends into the future, then price appreciation must eventually follow – that is, **long-term price appreciation is a *consequence* of consistent earnings and dividend growth**.

Amongst our current 70 GoDI holdings, **during the calendar quarter ending June 30th, 2019, we received 17 declared dividend increases averaging an announced increase of 12.6% quarter-over-quarter** ("QoQ") **and 14.9% year-over-year** ("YoY"), relative to those already known at the end of the prior calendar quarter. There were no dividend decreases during the quarter.

No.	Company Name	Ticker Symbol	Current Ind Div Yld (% per annum)	QoQ Div Increase (%)	YoY Div Increase (%)
1	America Movil	AMX	2.6	11.6	6.3
2	American Tower Corp	AMT	1.8	2.2	19.5
3	Ameriprise Financial Inc	AMP	2.7	7.8	7.8
4	Caterpillar Inc	CAT	3.0	19.8	19.8
5	Celanese Corp	CE	2.3	14.8	14.8
6	CoreSite Realty Corp	COR	4.2	10.9	18.4
7	Extra Space Storage Inc	EXR	3.4	4.7	15.4
8	Grupo Financiero Banorte SAB	GBOOY	5.8	60.7	60.7
9	Invesco Ltd	IVZ	6.1	3.3	3.3
10	Johnson & Johnson	JNJ	2.7	5.6	5.6
11	Lazard Ltd	LAZ	5.5	6.8	6.8
12	Legg Mason Inc	LM	4.2	17.6	17.6
13	Lowe's Cos Inc	LOW	2.2	14.6	14.6
14	LyondellBasell Industries NV	LYB	4.9	5.0	5.0
15	Penske Automotive Group Inc	PAG	3.3	2.6	11.4
16	Unilever PLC	UL	3.1	5.5	6.1
17	UnitedHealth Group Inc	UNH	1.8	20.0	20.0
	Average		**3.5**	**12.6**	**14.9**

Across the 17 dividend increases last quarter, we observe a very strong yield-to-growth combination with an average dividend per share growth rate of 14.9% against an average dividend yield of 3.5% – precisely what the Fund attempts to achieve with its portfolio holdings.

Always remember our primary message: **"Growing income", as opposed to "fixed income", is the only means of maintaining the purchasing power of your (or your client's) income stream over the years and decades to come**.

If you would like more 11information regarding the **AlphaDelta Growth of Dividend Income Class** and its current portfolio (including the up-to-date presentation piece), please feel free to contact me directly or alternatively contact AlphaDelta Management Corp. (www.AlphaDelta.com).

Thank you for your continued interest in the Fund,

John J. Schmitz

John J. Schmitz, Ph.D., CFA