TETREM
QUARTERLY REVIEW

TAPERED SPREADS, TAPERED VIEW

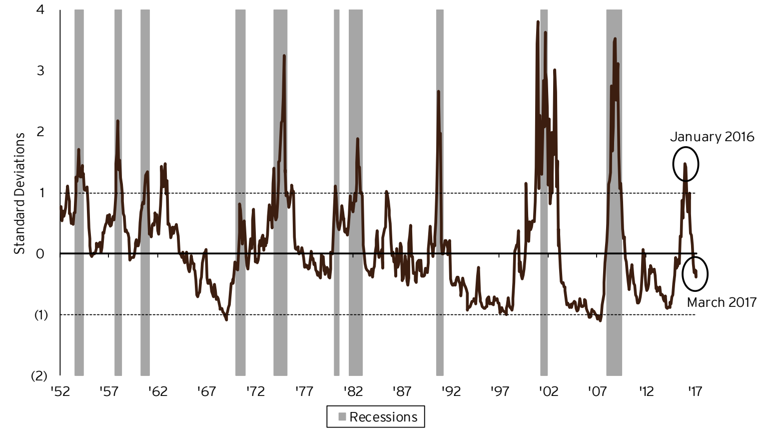
Over the first quarter of 2017 equity markets continued from where they left off in 2016 — firmly in bull market mode. Both the S&P 500 index and the S&P/TSX Composite index rallied to all-time highs during the quarter. From the wake of the Brexit lows in the summer of 2016 these indices surged 19.8% and 16.3%, respectively, to their recent highs. Those invested in equities are enjoying an increase in wealth, albeit with a certain amount of trepidation about how long the good times will last. After all, it is now over eight years since equity markets bottomed during the Great Recession, a long bull market by historical standards. Additionally, against the expectations of many, volatility went into hibernation over the winter. Between October 11th and March 20th, the S&P 500 did not have one day where it closed with a decline of 1% or greater, a record run.

Given this combination of an aging bull market and signs of investor complacency, some market prognosticators are warning of a bear market. However, such a call seems premature. Equity valuations move in reaction to changes in earnings, sentiment and liquidity, and broadly speaking none is flashing yellow yet. During the month of March, the global earnings revision ratio published by BofA Merrill Lynch turned positive for the first time in six years. The last time this indicator was positive, earnings were rebounding from extremely depressed levels coming out of the Great Recession. Future earnings are looking better thanks to improving global growth, something that has not existed since this year's high school graduates were in grade school.

Sentiment is a contrarian indicator, with extreme bullish or bearish readings acting as signals to go in the opposite direction. Recent survey data have moved up commensurate with the equity rally to new highs, indicating caution is warranted. However, there is little to no outright bullishness in the various indicators that we follow. The typical speculative exuberance seen at peaks is absent from the market. If anything, the entire bull run of the last eight years can be characterized as mistrusted and unloved by investors, which provides underlying support from a contrarian perspective.

Liquidity is likely the most challenging factor for the market. Equities have rallied on a rising tide of liquidity fueled by central banks' pushing interest rates down towards zero, and in some cases beyond. Global central banks' balance sheets are continuing to expand. However, it is now quite clear that the US Federal Reserve is in a tightening cycle. While short-term rates that remain below 1% can hardly be viewed as restrictive, the trend is higher. Capital markets have thus far taken rising rates as a positive signal that global growth is accelerating. For the time being, improving growth is trumping higher rates.

Figure 1 US Valuation Spreads



Source: Empirical Research Partners. As of March 31, 2017.

While we maintain the perspective that equities will continue to benefit from a rising tide, we are making active adjustments to the portfolios that we manage. We are concerned that value is getting harder to find within Canadian and US equity markets. Just over a year ago, commensurate with the decline in oil prices, we pointed to wide valuation spreads between the cheapest and most expensive quintiles of the US equity market (Figure 1). Thanks to strong equity markets and the rally in value stocks, this dispersion is now mostly gone. There are still plenty of cheap stocks in the market, however many of them are in secularly challenged areas where we have little to no interest. As value investors we are not afraid to buy into out-of-favour areas of the market; in fact that is where we have typically found our best investment opportunities. However, we are wary of areas that face secular challenges. A key tenet of our investment philosophy is to take advantage of investment controversies, but only if we see the controversy as temporary, while avoiding those that are secular in nature.

A good example is the Retail sector, where it is hard to argue the issues are temporary. Department stores face an existential threat from changing consumer habits and the onslaught of online retailing. Brands are now going direct-to-consumer via online sales while Amazon continues to attack high margin retailers, capturing market share in the process. Meanwhile there is simply too much retail square footage in North America. This is not to say that "bricks and mortar" retailing is going the way of the dodo bird, far from it. The negative sentiment has given us the opportunity to build out positions in Aritzia and Dollar General, two retailers with strong growth prospects. Niche retailers with a value proposition that resonates with the consumer will thrive, but legacy retailers will continue to be challenged for years. The next recession, whenever it comes, will be particularly cleansing for the industry.

(Continued on page 4)

MARKET OVERVIEW

- The S&P/TSX Composite returned 2.4% in the first quarter. Gains were broad based, with nine of eleven sectors in positive territory.
- The heavily weighted Financials and Materials sectors contributed the most to the market's advance. The Canadian Banks reported strong quarterly results while the Gold sub-sector rebounded from the prior quarter's selloff.
- Energy was a notable laggard, giving back some of its gains from 2016 as oil prices declined 6% during the quarter.

S&P/TSX SECTOR PERFORMANCE

Sector	Quarterly Total Return (%)
Utilities	7.3
Consumer Discretionary	7.0
Information Technology	7.0
Materials	6.1
Industrials	5.3
Telecommunication Service	5.0
Real Estate	4.7
Financials	3.5
Consumer Staples	2.6
S&P TSX	2.4
Energy	-5.5
Health Care	-10.1

TETREM'S TOP TEN CANADIAN POSITIONS

Security	Weight (%)
Royal Bank Of Canada	8.8
Bank Of Nova Scotia	6.7
Toronto-Dominion Bank	5.8
CCL Industries Inc	5.1
Cash	4.9
Suncor Energy Inc	4.2
Canadian National Railway Co	4.1
Manulife Financial Corp	3.8
Keyera Corp	3.6
Canadian Natural Resources	3.4
	50.3

NOTEWORTHY PORTFOLIO CHANGES

▲ MacDonald Dettwiler	▼ Shaw Communications Inc
▲ Winpak Ltd	▼ Canadian Imperial Bank
▲ Aritzia Inc	▼ Detour Gold Corp

TETREM'S QUARTERLY RESULTS

- Tetrem's Canadian Equity Portfolio advanced 2.0% during the quarter, trailing the benchmark by 42 basis points.
- Stock selection within Consumer Staples and Industrials contributed positively to performance.
- Positioning within Energy and Information Technology detracted from relative results.
- Notable positive contributors: Premium Brands Holdings, Uni-Select, CCL Industries.
- Notable detractors: Tourmaline Oil, Vermilion Energy, Mullen Group.

MANAGER COMMENTARY

The portfolio's higher quality companies were among the quarter's standouts. Royal Bank of Canada, the largest holding, was the biggest contributor to Q1 performance. The bank continues to generate steady growth across its business lines all the while expanding its capital buffer to protect against a potential downturn. In February, Royal announced a 5% dividend increase, exceeding consensus expectations and sending a strong signal about the board's confidence in the bank's outlook.

Merger and acquisition activity within Canada's oil patch is having a positive impact on the portfolio. Canadian Natural Resources (CNRL) shares rallied when the producer announced a $12.5 billion acquisition of oil sands assets, leveraging its operational excellence and financial strength to gain market share. Prior to the announcement, CNRL had raised its dividend by 10% and management indicated they could drive down their oil sands operating costs to sub-$20 per barrel, a level that will further enhance its competitive position. Our view remains that the market will continue to reward strong cash flow generating companies which can remain profitable at low energy prices.

We initiated a position in MacDonald Dettwiler & Associates (MDA), a global leader in satellite technology, after it announced its intention to merge with DigitalGlobe Inc, the leader in high-resolution earth imagery. MDA has an attractive combination of favourable long-term fundamentals and an inexpensive valuation. Prior to our purchase the company's shares underperformed, in large part due to a downturn in satellite sales that we believe is transitory. In our view, the market is overlooking a number of positives. One is the rise of Ultra-High-Definition video, which requires substantially higher data transmission capacity than prior technologies and should drive future satellite demand. Another is MDA's opportunity to grow its share of business from NASA and the US military, where it is currently under-represented. We believe that earnings and valuation will expand once the merger is consummated and investors see evidence of improvement.

In February, the TSX reached an all-time high. With valuations expanding, we've taken advantage of strength in the market to opportunistically exit or trim some of the portfolio's holdings. We exited four positions and initiated in two, which further consolidates the portfolio into higher conviction investments. As a result, the portfolio's cash balance is a bit higher than normal and we are ready to deploy the cash into several stocks at specific price levels.

Daniel A. Bubis, CFA *President & Chief Investment Officer*

TETREM'S CANADIAN EQUITY PORTFOLIOS - HISTORICAL PERFORMANCE (% return denominated in CDN$ - see performance disclosures at end of page 4)

		Annualized Returns to March 31, 2017										
	Q1 2017	1 year	3 year	5 year	10 year	15 year	Since Inception	2012	2013	2014	2015	2016
TETREM CANADIAN EQUITY COMPOSITE												
Gross of Fees	2.0	19.7	4.3	8.7	4.7	8.4	9.9	8.8	25.7	5.7	-8.8	20.6
Net of Fees	1.8	18.9	3.6	8.0	4.0	7.7	9.2	8.1	24.9	5.0	-9.4	19.8
S&P / TSX Total Return Index	2.4	18.6	5.8	7.8	4.7	7.4	7.3	7.2	13.0	10.6	-8.3	21.1
TETREM CANADIAN EQUITY DIVIDEND COMPOSITE												
Gross of Fees	3.6	14.1	5.1	-	-	-	10.2	-	23.4	4.8	-5.5	16.1
Net of Fees	3.4	13.3	4.4	-	-	-	9.4	-	22.6	4.2	-6.1	15.4
S&P / TSX Total Return Index	2.4	18.6	5.8	-	-	-	8.9	-	13.0	10.6	-8.3	21.1

MARKET OVERVIEW

- The S&P 500 reached an all-time high during the quarter, returning 6.1%, its fourth consecutive quarterly increase.
- Information Technology was the top performing sector, ending the quarter up 12.6% due in large part to Apple's 24% advance.
- The Energy sector lagged amidst renewed concerns of oversupply. WTI oil dipped below the psychologically-important $50/barrel level, though it closed the quarter at $50.60.

TETREM'S QUARTERLY RESULTS

- Tetrem's US Equity Portfolio gained 2.7% during the quarter, lagging the S&P 500 by 333 basis points.
- Stock selection within Energy, Materials and Real Estate contributed positively to relative performance.
- Portfolio results were negatively impacted by investments within Information Technology and Industrials.
- Notable positive contributors: Goodyear Tire & Rubber, Dow Chemical, Corning.
- Notable negative contributors: Schlumberger, Qualcomm, United Parcel Services.

S&P 500 SECTOR PERFORMANCE

Sector	Quarterly Total Return (%)
Information Technology	12.6
Consumer Discretionary	8.4
Health Care	8.4
Utilities	6.4
Consumer Staples	6.4
S&P 500	6.1
Materials	5.9
Industrials	4.6
Real Estate	3.5
Financials	2.5
Telecommunication Services	-4.0
Energy	-6.7

TETREM'S TOP TEN US POSITIONS

Security	Weight (%)
Cash	6.7
Alphabet Inc	5.2
Microsoft Corporation	4.8
EOG Resources Inc	4.2
Schlumberger Ltd	3.9
Johnson & Johnson	3.8
Wells Fargo & Company	3.8
Dow Chemical	3.7
Citigroup Inc	3.7
Union Pacific Corp	3.4
	43.4

NOTEWORTHY PORTFOLIO CHANGES

▲ General Electric Co	▼ Corning Inc
▲ Dollar General Corp	▼ Spectra Energy Corp
▲ Citigroup Inc	▼ Macy's Inc

MANAGER COMMENTARY

The quarter began with optimism that the Trump Administration would implement positive changes for the economy. Optimism soon turned to doubt as the inability to pass healthcare reform provided a timely reminder that policy implementation is often difficult. After reaching an all-time high on March 1st, the market staged a pullback that was short-lived, and with good reason. The US economy remains on strong footing with economic indicators pointing to an improving fundamental backdrop. Consensus S&P 500 estimates show year-over-year earnings growth accelerating to 6.9% in the first quarter of 2017, up from 3.9% in the fourth quarter of 2016.

The portfolio's positioning within the Information Technology sector (i.e. not owning Apple) detracted from results during the quarter, but there were several positives. Portfolio holding Corning Inc. reached our price target and we sold the position. We first purchased the shares in 2013 when they traded below book value, a level we viewed as unsustainably low. In late 2015 we identified an incremental mean reversion opportunity in their display glass business and we purchased additional shares. The opportunity played out as expected and, with the valuation having expanded by over 40% since we initiated the position, we locked in profits.

Alphabet Inc., formerly known as Google, reported its 28th straight quarter of near 20% revenue growth. It is astonishing that a company of this high calibre trades at only a small premium to the broader market. When adjusting for the $88 billion in net cash on the balance sheet, Alphabet's valuation is even more compelling. Looking forward, the company has several avenues for growth. YouTube's share of video advertising spend remains small relative to traditional TV and is likely to expand. Investments in Artificial Intelligence have the potential to generate a plethora of unique and innovative products and solutions. Profit margins continue to improve as cost cutting initiatives take effect, and we see opportunities for more of the same.

During the quarter, we initiated a position in Dollar General (DG), a discount retailer focused on selling products found in your typical grocery store. DG has developed a niche store expansion strategy that avoids big-box competitors like Wal-Mart by targeting towns with fewer than 20,000 residents. The stock has come under pressure lately – hence our interest – as same store sales have lagged historical trends and analyst expectations. Our analysis suggests the weakness is being driven by transitory factors, specifically food deflation and financial pressure on its core customer whose annual income is sub-$40,000. We expect both headwinds to abate in the second half of 2017, leading to a higher multiple on the currently depressed shares.

Ben Ellis, CFA *Portfolio Manager*

TETREM'S US EQUITY PORTFOLIOS - HISTORICAL PERFORMANCE (% return denominated in US$ - see performance disclosures at end of page 4)

		Annualized Returns to March 31, 2017										
	Q1 2017	1 year	3 year	5 year	10 year	15 year	Since Inception	2012	2013	2014	2015	2016
TETREM US EQUITY COMPOSITE												
Gross of Fees	2.7	17.8	6.0	10.7	6.5	8.4	10.2	10.3	37.9	9.9	-3.9	13.3
Net of Fees	2.6	17.1	5.3	10.0	5.8	7.7	9.5	9.6	37.0	9.2	-4.6	12.6
S&P 500 Total Return Index	6.1	17.2	10.4	13.3	7.5	7.1	7.9	16.0	32.4	13.7	1.4	12.0
TETREM US EQUITY DIVIDEND COMPOSITE												
Gross of Fees	3.4	16.1	10.5	-	-	-	15.4	-	34.3	14.8	0.1	16.7
Net of Fees	3.2	15.4	9.8	-	-	-	14.6	-	33.4	14.1	-0.6	16.0
S&P 500 Total Return Index	6.1	17.2	10.4	-	-	-	14.9	-	32.4	13.7	1.4	12.0

(continued from page 1)

Our worst nightmare is a company that faces secular challenges and has an over-leveraged balance sheet. Perhaps the business survives, but we have seen the act play out too many times with the same denouement: equity holders are wiped out as debt holders take over and accelerate the restructuring process. The point here is not to pick on retail; it just happens to be a good example of an industry that faces multiple challenges that stack the odds against investors. Cheap valuations are a siren song to the ears of a value investor, but we are resisting the temptation to deploy capital into the many value traps that litter the market.

The cornerstone of Tetrem's investment process is our VMER framework, the lens we use to analyze and monitor companies. VMER is simply an acronym for value, mean reversion, economic moat and risk. Our best investments have historically come from opportunities where both value and mean reversion scores are high. Economic moats and conservative risk indicators provide ballast to the investment decision process in the form of capital preservation and reduced volatility. Value manager nirvana occurs when we identify investment opportunities where all four characteristics are strong. Every so often the market provides a target-rich environment of value stocks. Most often this happens during an economic recession when seemingly no one wants to own stocks, valuations are crushed, and the forces of economic mean reversion are on the cusp of improving. This can be seen in Figure 1 where the shaded areas indicate economic downturns, periods that have always provided multiple "fat pitches", particularly for value investors. Today is not one of those periods. Eight years into an economic expansion, valuations, while not excessive, are not cheap either. Therefore, within our VMER framework we are increasing the emphasis on economic moat, and reducing the constraints of valuation by letting winners run. Our focus is on companies that generate persistently strong cash flows, and where management has a record of returning cash to shareholders in the form of dividends and stock buybacks.

Ultimately we are investing in companies that exhibit a combination of solid financial strength and reasonable valuation characteristics. As a result our portfolios hold fewer stocks, are more concentrated in high conviction positions, and cash balances have edged higher. If market volatility increases and better value emerges, we will not hesitate to deploy cash in an opportunistic manner. Notwithstanding the strong equity returns of the past year, we continue to believe we are in a low return environment, which thereby limits the potential drag from cash if equities continue to move to new highs. It is worth noting that we have been managing portfolios with very low cash balances for the past few years. We are not believers in having cash to "time the market"; it is a bit of a fool's game where it is hard to dissect luck from skill. However, when quality value is harder to come by, it is nice to have dry powder available for new potential targets as they emerge. It's a conservative approach, one that we think makes a lot of sense in a market where value opportunities are comparatively rare.

Daniel A. Bubis, CFA *President & Chief Investment Officer*

ABOUT TETREM

Tetrem Capital Management offers money management services to institutional and private clients. Our investment portfolios are focused on Canadian and US equities, rooted in our long-standing contrarian value style and tailored to the specific needs of our clients.

Investing is our profession and we are committed to doing it well. Our experienced team's primary focus is seeking out and investing in undervalued companies. For each of our investment portfolios, we employ fundamental and quantitative analysis in our rigorous stock selection process, with a focus on preserving and growing our clients' assets.

For more information about Tetrem Capital Management please visit our website, www.tetrem.com, or call and ask to speak with us about our investment services.

204.975.2865 or toll free 1.866.975.2865

Performance Disclosure

Tetrem Capital Management Ltd., an independent investment management firm, claims compliance with the Global Investment Performance Standards (GIPS®). To receive a complete list of composite descriptions please contact us at the above phone number.

To receive a presentation that adheres to the GIPS standards, please contact us at the above phone number or see the "performance" section of our website at www.tetrem.com.

Composite Descriptions:

Tetrem Canadian Equity Composite
Contains fully discretionary Canadian equity accounts following a value investment strategy. Inception date: January 1, 1997.

Tetrem US Equity Composite
Contains fully discretionary US equity accounts following a value investment strategy. Inception date: January 1, 1997.

Tetrem Canadian Equity Dividend Composite
Contains fully discretionary Canadian equity accounts following a value investment strategy with stocks that pay a dividend or are expected to pay a dividend. Inception date is November 30, 2012.

Tetrem US Equity Dividend Composite
Contains fully discretionary US equity accounts following a value investment strategy with stocks that pay a dividend or are expected to pay a dividend. Inception date is November 30, 2012.

Returns represent past performance. Returns stated within this newsletter are gross of fees unless otherwise indicated. Past performance does not guarantee future results. Different types of investments involve varying degrees of risk.

The S&P/TSX Composite Total Return Index comprises approximately 71% of the market capitalization for Canadian-based, Toronto Stock Exchange listed companies and provides broad economic sector coverage of the Canadian markets.

The S&P 500 Total Return Index consists of 500 stocks chosen for market size, liquidity, and industry group representation.

Tetrem's mandates are available to institutional investors such as pension plans, group retirement plans and foundations and certain individual investors who meet specified investment criteria. Performance of the mandates is not guaranteed, the values change frequently and past performance may not be repeated.

The content of this newsletter is intended for information purposes only and does not constitute an offer to buy or sell products or services of Tetrem nor is it intended and/or financial advice on any subject matter or specific security mentioned. Any commentaries, reports or other content are provided for your information only.