SciVest

April 24, 2008

SciVest Funds Q1 2008 Commentary

Now we are having fun! It has been a long time coming, but *these are our type of markets* and I suspect they will be with us for a good while.

I will discuss this in more detail later, but first a look at our recent performance. Our recent performance, in fact, is starting to reflect this much improved environment for our strategies as can be evidenced by our numbers below.

	1 Month Return	3 Month Return	6 Month Return	12 Month Return	24 Month Return	YTD Mar. 2008	2007
CANADIAN FUNDS							
SciVest Market Neutral Equity Fund - Cl F	**0.3%**	**-1.6%**	**11.3%**	**8.3%**	**15.6%**	**-1.6%**	**9.3%**
SciVest Net Short Equity Fund - Cl F	**0.9%**	**6.0%**	**18.7%**	**6.1%**	**5.0%**	**6.0%**	**-4.9%**
SciVest Commodity Index PLUS Fund - Cl F	**-5.9%**	**6.5%**	**19.0%**	**24.2%**	**17.1%**	**6.5%**	**18.7%**
SciVest Oil Sands Index PLUS Fund - Cl F	**-4.2%**	**-6.1%**	**4.8%**	**12.5%**	**-0.5%**	**-6.1%**	**18.9%**
OFFSHORE FUND							
SciVest Global Net Short Equity Fund - Cl A	**2.0%**	**8.1%**	**19.8%**	**16.0%**	**15.7%**	**8.1%**	**2.6%**
MSCI World Index (TR)	-2.1%	-11.8%	-14.4%	-9.2%	1.5%	-11.8%	5.2%
S&P 500 Index	-0.6%	-9.9%	-13.4%	-6.9%	2.2%	-9.9%	3.5%
S&P/TSX Comp Index	-1.7%	-3.5%	-5.3%	1.4%	10.2%	-3.5%	7.2%
S&P/TSX Energy Index	-0.1%	2.0%	3.2%	9.6%	1.9%	2.0%	7.9%
HFRX Mkt Neutral Eqty Investable Index	2.1%	0.0%	1.0%	-1.4%	7.1%	-0.7%	3.1%
CSFB Mkt Neutral Eqty Investable Index	-1.3%	-2.5%	-3.8%	-3.1%	1.7%	-2.5%	4.8%

The table shows that performance of every fund has been very strong over every medium term period, with the past six month returns in particular standing out. In addition, we have beaten virtually all of our investment benchmarks in every fund over every time period shown.

Since the alpha most of our funds drive off of our flag-ship market neutral fund, the SciVest Market Neutral Equity Fund (the "SMNEF"), it is worth looking at its numbers in more detail. Over the past 6 months, the SMNEF has generated a net after fee return of 11.3% versus -14.4% for the MSCI World Index (that's greater than a +25% spread!) and -13.4% for the S&P 500 (that's also close to a +25% spread). Over the same period, the SMNEF has also trounced the HFRX Market Neutral Equity Investable Index and the CSFB Market Neutral Equity Investable Index which returned 1.0% and -3.8%, respectively. Needless to say, we have been performing very well since the environment turned in our favour this past Fall.

Even over a much longer 24 month time frame, the SMNEF has been generating excellent returns, both on an absolute and on a relative basis. Specifically, the SMNEF has generated a total 24 month period return of 15.6% versus a very anemic 1.5% for the MSCI World Index (a +14.1% spread) and 2.2% for the S&P 500 Index (a +13.4% spread). Similarly, the SMNEF has more than doubled the return of the HFRX Market Neutral Equity Investable Index at 7.1% and crushed the CSFB Market neutral Equity Investable Index at 1.7%.

It appears that three major factors may have turned, or are turning, in favour of our global, systematic, investment strategies: 1) structural; 2) cyclical; and 3) strategic.

First, the structural nature of the quantitative investment management business has turned quickly and dramatically back in our favour. Ironically, a combination of difficult markets for many quantitative managers over the past several years and the massive liquidity-driven sell-off that all purely quantitative investment strategies suffered last August, has driven many firms and funds out of business and has led to huge redemptions and leverage reductions at many of the surviving firms. For example, Goldman Sachs' two large quant funds (Global Alpha Fund and Global Equity Opportunities Fund) alone probably represent approximately $10 billion leaving the quant fund space, which at their 6 to 10 times leverage factor actually represents $60 to $100 billion leaving the quant investment strategy universe. There are several other less high profile collapses at large shops such as AQR Capital Management (managing over $35 billion in Quant strategies, with over $10 billion in hedge funds) where performance problems and redemptions over the past year could add many more $10's of billions of leveraged dollars leaving the quant investment strategy universe. And, then there are the small shops, many of whom just decided to wind-up their funds. In sum, it is reasonable to assume that over the past year several 100's of billions of dollars (on a leveraged basis) have left the quant investment strategy space.

The primary implication of this mass exodus of assets from the quant strategy space is simple – significantly less competition for alpha, which in turn will result in more alpha for all managers that have proven, well-established, alpha generating processes, like SciVest. While not a panacea, less competition will undoubtedly result in higher alpha for the whole quant industry regardless of what I believe is a significantly improved cyclical back-drop for the quant industry.

A more subtle implication of this quick structural shift in the quant space is that managers like SciVest who focus on small and mid capitalization stocks will benefit disproportionally from the quant strategy shake-out. First, in response to the August liquidity crisis many larger quant investment shops have significantly decreased the operating leverage of their funds and most have increased the liquidity of their holdings. The decrease in leverage means even less money invested in the quant space, and the increase in liquidity means that the market capitalizations of their holdings have gone up materially, in many cases totally leaving small capitalization stocks and significantly reducing their holdings of mid capitalization stocks. Second, while smaller in assets under management, many smaller quant investment shops have wound up their quant funds due to the lack of sales prospects in the wake of poor performance. These smaller shops tended to focus more on small and mid capitalization stocks, like SciVest does. The net result of both of these scenarios is far less quant strategy investment in small and mid capitalization stocks than even overall fund losses, redemptions and fund wind-ups would suggest.

Therefore, it is likely that proportionally far more quant strategy money has left the small and mid capitalization segments of the equity market than the large capitalization segment of the market resulting in even less competition for alpha among small and mid capitalization stocks than the large capitalization stocks. This is where SciVest lives – small and mid capitalization stocks, with at least two-thirds of our holdings being less than $2 billion in market capitalization (note, however, that all of our holdings remain highly liquid relative to our small fund size). As a result, SciVest's investment strategies should benefit with disproportionately improved alpha generation from this quick and significant improvement in the structural make-up of the quantitative investment business.

Second, the cyclical nature of quantitative investment strategies (yes, the efficacy of *all* investment strategies are cyclical) has begun turning back in our favour, and we believe that this cyclical turn in quant strategies is just beginning. In particular, our strategies perform the best when: i) stock volatility is higher than average (this creates a consistent stream of opportunities); ii) intra-stock return correlations are low, or put another way many individual stocks are moving in different directions (this creates good return spreads between the "good" stocks on the long side of the portfolio and the "bad" stocks on the short side of the portfolio); and iii) stock selection factors are rational and consistent (this creates the ability to select "good" stocks on the long side of the portfolio that produce higher returns than the "poor" stocks on the short side of the portfolio). If all of these cyclical factors are in place, then SciVest stock selection models should generate very strong returns, or alpha. Unfortunately, for much of 2004 to 2006 not all these cyclical factors were in place, and during some periods, none were in place. On the other hand, all of these cyclical factors were in place during 2001 to 2003 when quant strategies in general, and SciVest in particular, produced very strong performance numbers.

Over the past year, cyclical factor number one has returned in spades. That is, volatility is now back in the equity markets after stock volatility bounced around all-time lows between 2004 and 2006. Most market observers believe that volatility has return to the markets for at least the foreseeable future and we would tend to agree given our very bearish 2 year outlook for the US economy.

Cyclical factor number two has been sparse until the past six to nine months, but appears to have returned strongly since then. That is, individual stock return correlations seem to be much lower now than over the past several years (when all stocks tended to move together) as is evidenced by the large return differences between different segments of equity markets (you can see that in the day-to-day differences in industry returns as well). Will this cyclical factor persist or get stronger? We think the answer to both is yes because of the point in the economic cycle that we appear to be in – that is, entering what we believe to a abnormally long and painful US recession.

Cyclical factor number three has also been very sparse the past four years, but is expected to return in the near future. That is, there have only been periodic short periods of time where identifiable groups of rational stock selection factors have been effective at picking stocks. These waves appear to be getting longer and stronger, as evidenced by the strong consistent performance of "momentum stocks" during the latter third of last year. Morgan Stanley believes that over the next 12 to 18 months the European and US equity markets will once again go through a very long and powerful "valuation phase" whereby stock valuations strongly drive stocks returns (see attached Morgan Stanley research article). Morgan Stanley notes that

valuations as a means of selecting stocks got crushed last year and in general have not been terribly effective for several years. Morgan Stanley also notes valuation spreads (the valuations of cheap stocks versus expensive stocks) is at the highest level in the history that they track. If Morgan Stanley is correct, then the SciVest models will adapt to this new valuation-based market and reap the rewards of these historically wide valuation spreads, and potentially generate significant returns as we did when the models adapted to the momentum-based market in the latter part of last year. In fact, over the past couple of months, the SciVest models in several global markets have lowered their momentum exposures and increase their earnings yield, cash-flow yield and dividend yield exposures – that is, the shift to capture valuation spreads within our portfolios may have already begun.

In sum, low individual stock return correlations, along with high volatility of individual stock returns, creates the opportunity to generate returns that are substantially above average. The catalyst that allows us to capture this opportunity is a strong and consistent stock selection factor regime. Given the nature of SciVest's comprehensive and adaptive models, if such a strong and consistent stock selection factor regime begins again, as Morgan Stanley believes will be the case in the near term, then SciVest will undoubtedly capture this substantial return opportunity (as we did in 2001 to 2003).

Third, we have made significant upgrades in our investment strategies primarily to improve performance and decrease overall volatility risk, and to a lesser degree in response to the quant fund liquidity crisis in August. The most important upgrade that we made to our strategies was going fully global in late 2006. We now trade in the 14 largest developed countries by market size and liquidity. We explicitly and separately model and manage7 global regions within the funds: Canada, US, Australia, Japan, Hong Kong, UK, and Continental Europe (which currently comprises 7 countries). The full Hong Kong model was in fact just introduced to the funds at the beginning of this month. Prior to going global in late 2006, most of the SciVest funds were approximately 80% US and 20% Canadian and, as a result, we relied very heavily on the US models to generate returns. Unfortunately, as discussed above, the extreme competition for alpha among quantitative investors over the past four years (until the shake-out over the past 6 months) was also focused on the US equity markets. Going global allowed us to focus capital on less efficient international markets in an effort to generate higher returns. In fact, I credit our out-sized positive returns the past couple of years relative to other quantitative investment managers largely to this globalization.

In addition, going global significantly increased the diversification and thus lowered the volatility of the funds. For example, while the US represented 80% of the funds several years ago, today it represents only 24%. As a result, the US models and market do not dictate the returns of the fund anywhere to the extend it did several years ago. Furthermore, since our stock selection universe has more than doubled to over 7,000 global stocks, we can now hold far more positions within the funds at lower weights than prior to the globalization – thereby significantly adding to diversification and thus generating lower risk.

As a result, the globalization of the SciVest funds has materially increased return potential *and* materially reduced risk – something that all investors strive for, but rarely achieve.

Overall, therefore, while we are have been having lots of fun lately, I expect we will be having even more fun going forward as structural, cyclical and strategic factors all align in our favour for the first time in fours years.

John J. Schmitz

Commissions, trailing commissions, management fees and expenses all may be associated with pooled fund investments. Please read the offering memorandum before investing. The indicated rates of return are the historical annual total returns including changes in unit value and reinvestment of all distributions and do not take into account sales, redemptions, distributions or optional charges or income taxes payable by any securityholder that would have reduced returns. The rates of return are net of all fees and expenses and are used only to illustrate the effects of the compound growth rate and are not intended to reflect future values of the pooled fund or returns on investment in the pooled fund. Pooled funds are not guaranteed, their values change frequently and past performance may not be repeated.