LionGuard Capital Management Inc.
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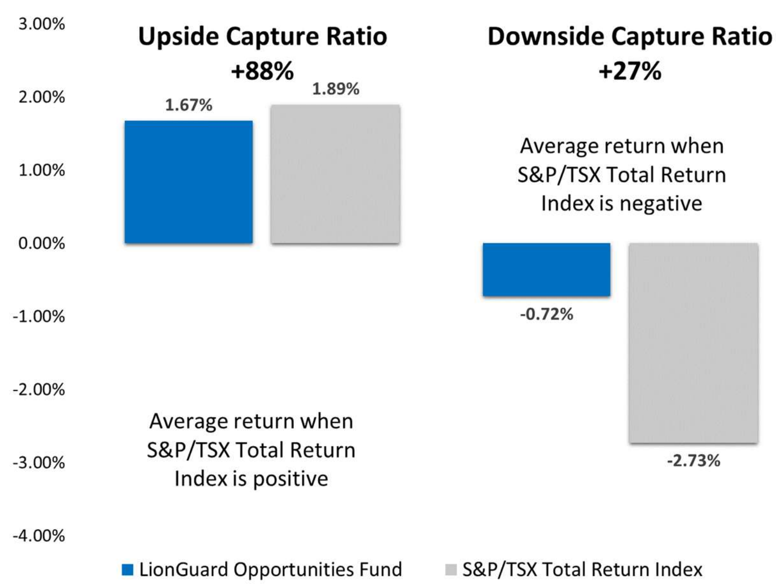
LIONGUARD OPPORTUNITIES FUND
QUARTERLY REPORT – MARCH 2020

Dear everyone,

During the quarter ended March 31, 2020, LionGuard Opportunities Fund ("Opportunities Fund") had a net (after all fees and expenses) return of -14.73%. **Since Opportunities Fund's inception, in October 2014, its annualized net return amounts to 8.66% and cumulative net return to 57.87%.**

Time period	LionGuard Opportunities Fund (net returns)
YTD	-14.73%
1 year	3.74%
3 years (annualized)	1.60%
5 years (annualized)	7.10%
Since Inception (annualized)	**8.66%**
Since Inception (cumulative)	**57.87%**

Since the Opportunities Fund's inception, as compared to the broad market index (S&P/TSX Total Return Index), its upside capture ratio amounted to 88% and downside capture ratio to 27%.



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Triple Crisis – Healthcare, Economic & Energy:

What started as a local virus issue in Wuhan, China, has very quickly evolved into a global pandemic of unprecedented proportions. In the interest of saving millions of people's lives and not overwhelming local healthcare systems, almost all governments elected to shut down their economies by enacting the now-famous "social distancing".

With the unprecedented collapse of the economic activity and little clarity as to the timing of the "shutdown", global stock markets endured some of the fastest and most violent corrections on record. For the quarter, S&P/TSX Composite Index recorded -21.59% and S&P500 Index -20.00%. As expected, smaller capitalization indices were hit hardest with S&P/TSX Small Cap Index at -38.64% and Russell 2000 Index at -30.89%.

Having learned from the still recent financial crisis, central banks and government officials responded by providing extraordinary levels of fiscal and monetary stimulus. Unlike during most recessions, however, this time there is no tangible moral hazard case against bailing out struggling companies and industries.

In addition to Covid-19 healthcare crisis and the economic crisis due to the purposeful shutdown of the economy, stocks were largely impacted by the dispute between Russia and Saudi Arabia on oil production cuts. Big increases in oil production levels at exactly the wrong time, given the global economic slowdown, led to a 66.5% drop in oil prices during Q1-2020 (from $61.06/bbl to $20.48/bbl). With no clear timeline on when the dispute may resolve, and oil stockpiles quickly filling up, numerous equities including those exposed to Western Canadian economy were severely punished.

Some of the typically highly defensive stocks saw their prices fall by more than 40% as their operations were not labeled "essential" during the shutdown period and/or as their business operations were severely impacted one way or another. With the duration of the crisis under question, numerous investors panicked and sold off said quality businesses to record low valuation levels as determined by the multiples on their "normalized" earnings power.

Numerous companies also sold off as investors were "upgrading" their portfolios at any cost by reducing smaller capitalization stocks and buying larger ones. With no marginal buyers stepping in to defend most stocks, we witnessed some of the most volatile daily trading sessions seen over the last 50+ years. This dynamic, as expected, was especially intensified for the smaller capitalization equities, which correct the most during broad-based market selloffs and subsequently (typically) recover the most.

In addition to fundamental investors' worries, market movements were exacerbated by the fact that so many investment decisions these days are made by machines. Also, with record amounts of capital, pre-crisis, flowing to passive investment vehicles, it is no wonder that the disconnect from fundamentals (on an individual securities' basis) during times of market stress is severely elevated.

In conducting our investment operations, I believe we do not deserve much credit in our handling of the crisis in Q1-2020, as it pertains to the Opportunities Fund. This judgment is predicated on the summation of the decisions we made and those we "clearly" should have made given the information on hand at that time. Sometimes, costliest mistakes are the actions one does not take.

ZOOMing In On Fundamentals:

We are of the view that this environment presents great opportunities for long-term investors who have solid fundamental research orientation. Rather than trying to predict the overall market direction (very rarely a good idea) or relying on quantitative decision-making tools (with often unreliable input variables under even more normal market conditions), this is the most obvious time to focus the efforts on fundamental research.

When analyzing businesses in such an uncertain environment, there are three main elements to focus on:

1. **Assessing Balance Sheet Strength**

Balance sheet strength is determined by the Company's level of net debt (or net cash), debt maturities schedule, debt covenants levels, number of banking syndicate members, the strength of banking syndicate members (their capital ratios, their credit rating, whether they are "too big to fail", etc.), location of cash in relation to debt facilities (within the same banking institution or otherwise), etc.

2. **Stress-Testing Free Cash Flow Generation Under Multiple Scenarios**

Given uncertain timing and depth of the crisis, multiple scenarios must be performed (using financial models) to evaluate free cash flow capabilities and their impact on the strength of the company's balance sheet. The only way to do so with a reasonable degree of accuracy is to have an excellent understanding of the company's operations including its ability (and senior management and Board of Director's willingness - which can be assessed based on past behavior, quarterly and annual commentaries, quarterly conference calls transcripts, etc.) to cut costs.

Note: Businesses with flexible cost structures typically fair well under such stress-test analysis, although this can also be quite misleading given government interventions, changing sensitivities at varying levels of the impact, all too common blunders by management teams and others. This analysis also becomes ever more complex for businesses with varying lines of business and operating jurisdictions.

3. **Computing Upside Potential Under Same Multiple Scenarios**

When computing the upside under each scenario, unlike most Wall Street pundits, we shy away from valuing businesses on a famed EV/EBITDA and P/E ratios and instead allocate practically all the weight towards DCF (discounted free cash flow) analysis.

Note: Some of the best managed and strongest companies do not generate positive free cash flow, as their managers choose to invest in growth CAPEX with high rates of return. Assessing management's ability to create shareholder value via growth CAPEX initiatives is one of the key jobs of fundamental research professional. When faced with such cases, we do not shy away from investing in said businesses as they can be some of the best long-term investment opportunities (just think of Amazon). In those *cases, we apply Modified DCF analysis, which segments run-rate cash flow generating ability of the business under Maintenance CAPEX scenario and the expected return from Growth CAPEX initiatives. Of course, different discount rates are applied to each, as may be warranted.*

In our own scenarios, we probability-adjust such diverse cases as a "miracle drug" all the way to a very gradual opening of the economy coupled with a "second wave" of the virus plus the liquidity crisis and "run on the bank". We stay short of social unrest and even more sensational proclamations and it is warranted to point out that our analysis at this time indicates a low probability of this evolving into a financial crisis.

Multiple stress-test scenarios provide us with much-needed comfort to separate temporary mark-to-market fluctuations from cases when a capital position may be permanently impaired. When done properly, this kind of research can lead to materially improved risk-adjusted returns for the Fund as a whole.

In many respects, prudence is still warranted as we have yet to see the full impact of the economic shutdown and because we are quite unlikely to see the same level of economic activity as we did before the crisis in the near-term. It is also unclear whether European and North American economies can successfully "open up" without incurring a new spike in Covid-19 cases. It may not be appropriate to extrapolate from the Chinese experience, as the same levels of monitoring cannot be implemented in economies with stricter individual privacy laws.

At the same time, however, we believe that it makes great sense to acquire on the cheap pieces of businesses with solid balance sheets, which will continue generating positive free cash flow during the "shut-down" (or have a minimal adverse impact on the current balance sheet under severe scenarios) and which will come out stronger than their competitors in the end. Among those securities, we currently come across a healthy number of businesses with large long-term upside potentials under even severe and long-lasting adverse economic conditions.

Q1-2020 Contributors:

During the quarter, one of our notable detractors was **Sangoma Technologies (STC)**. Given unique market conditions in Q1-2020, it is no wonder that most of our positive contributors came from short positions. Two of our notable additions in the quarter included **American Software (AMSWA)** and **Iteris (ITI).**

Sangoma Technologies (STC-TSE) - Please refer to our prior quarterly reports for a detailed discussion of the company. Given the precipitous decline in the company's share price, we believe it is fair for investors to ask for our view on this investment.

In our opinion, recent stock price correction (due partially to the company-specific transitory issues and mostly to the broad-based market sell-off) has nothing to do with the "real" value of the business. As a result, we have been taking advantage of the much lower stock price to become notably larger shareholders of the company.

On the transitory issues front – The management team has communicated openly that growing the recurring revenue stream remains a key priority, and as a result, the company is ready to allocate a greater amount of resources to this segment.

With that understanding in mind, the weaker than expected revenue in Q2-2020 was as expected. At the same time, recurring revenue showed almost a 5% growth quarter over quarter. According to our estimates, the company's service revenue has been growing organically in the mid-teens range for quite some time. Given low UCaaS (united communication as a service) penetration, we believe that this growth rate is sustainable.

We subjected Sangoma to the same stress tests as other companies (refer to the section on "ZOOMing on Fundamentals" for details) and confirmed that we are comfortable with its balance sheet, cash flow generation and the upside potential. Some of the conclusions of that analysis are the following:

- STC does have some debt, however, given its sizeable recurring revenue base and flexible cost structure we do not see this as a concern.

- About 50% of its revenue is recurring and generates a high margin. Services they provide are essential to ensuring the well-functioning of numerous enterprises. In many respects, the benefits of UCaaS are further highlighted by the current "work from home" environment.

- Company's management team has an excellent track record of cutting costs. We, therefore, have full confidence in their ability to do so, if needed, of up-to $8-10M per year.

- We see strong upside potential from these levels (under all scenarios in question) either as a stand-alone entity or as a result of a takeout by private equity or a strategic buyer. In our opinion, Sangoma remains a key takeout target.

American Software (AMSWA-US), a newly introduced supply chain management software company with 56% recurring revenue, is one of our top contributors for the quarter. It is one of our rare finds and exhibits many traits echoing the *"Opportunity is missed by most people because it is dressed in overalls and looks like work"* mentality, as it screens poorly from a growth perspective.

The truth of the matter is, American Software is a misunderstood, hidden gem serving some of the world's largest blue chips (Mondelez, Verizon, Kraft Heinz, Johnson Controls, Starbucks, Canada Goose, Dow, etc). Its Logility offering is consistently ranked as the leader and one of the most visionary products in Gartner's Quadrant for Sales and Operations Planning (S&OP).

At first sight, the company strikes market participants as low single-digit growth, steady business, paying a good dividend in a Supply Chain Management market that is supposedly growing at a ~10% CAGR. In reality, American Software has been undergoing a well-executed upon transformation from a license model to a recurring subscription model, masking the true organic growth potential of the company.

In fact, in a few years, cloud revenue went from non-existent to ~20% of revenue, growing at over 50% consistently, more than offsetting the drop in license revenue and resulting in positive overall organic growth while sustaining healthy profitability margins. We emphasize the importance of the company's profitability and healthy ~3.5% FCF yield despite the ongoing transition, as most companies undergoing such a transformation typically exhibit deteriorating margins and borderline losses in the process.

Management's ability to successfully transform the model while maintaining profitability and healthy cash flow speaks volumes to its acumen and discipline. Through our interaction with management, we believe the company is well-positioned to capitalize on the emerging importance of having valuable supply chain solutions. Specifically, we see management's capital and resource allocation strategy as highly effective to balance growth with profitability as it focuses on three pillars:

1. **Organic Growth & Market Gains:** Hired a seasoned sales executive last year to revamp the sales structure and implement tools to focus on large enterprise deals while better showcasing the company's wide variety of modules, all aimed at expediting market share grab.

2. **Acquisitive Growth with 20% of market cap in net cash:** Opportunity to deploy capital to add complementary technology to its offering while accelerating cloud revenue.

3. **Maintain Dividend Policy:** providing an income stream while they transition into rapid growth. Dividend likely to be maintained given Chairman's >35% voting ownership (All of Class B – 1 vote per share vs Class A at 1/10 vote per share)

In American Software we found a cash-rich company, with solid organic growth potential from cross-selling and new logos, good FCF generation, and the potential for a take-private scenario given the ongoing consolidation in the space and the Chairman's voting shares.

As the shares pulled back due to market uncertainty related to the Covid-19 outbreak, we opportunistically added to our position. While we acknowledge the near-term impact of the virus on pipeline conversion and some of American Software's clients that could result in volatility in the shorter-run, we believe the company will be a net beneficiary over the longer-term as it sheds light on the importance of supply chain solutions.

Iteris (ITI-US) is our Intelligent Transportation and Digital Agriculture business. It operates in two industries undergoing secular growth with a combined Total Addressable Market (TAM) of over $6.0 Bn growing at low to mid-teens CAGR. As we showcase below, we are buying two businesses for less than the price of one. We also provide our summarized view on the impact of Covid-19 outbreak on Iteris' businesses.

Iteris is a misunderstood, well-run operation that screens poorly on a GAAP basis. As the company approaches a major cash flow positive inflection point, it offers significant avenues to unlock value through the potential divestiture of its Agriculture Business and the rapid growth of Smart Mobility, which should result in continued margin expansion. However, few are willing to dig deeper into a small-cap name of such complexity. We encourage our readers to examine this piece as we peel the onion on one of our high conviction names.

Founded in the late 60s, Iteris operates two distinct businesses: Smart Mobility and Digital Agriculture. Smart Mobility is comprised of (a) Roadway Sensors providing traffic visibility, control, analytics, and monitoring for agencies (44% of revenue), and (b) Transportation Systems providing infrastructure consulting services such as planning, design, integration, analytics, etc (50% of revenue). Iteris' Smart Mobility segment has cemented itself as one of the leading players in the industry as it works with over 20 countries, 50 state DOTs, and 1,000s of counties and municipality.

Historically perceived as a boring business with mid-single-digit organic growth, Smart Mobility is a $5.0B market growing at an 11% CAGR. The segment has turned into the company's crown jewel, buoyed by secular trends fuelling growth, including aging physical infrastructure, outdated technology, traffic congestion, urbanization, future of connected vehicles, and the explosion of data analytics. Those dynamics have repositioned the company into investing heavily in that business while aggressively pressing the gas on its SaaS offering, with 25% of consolidated revenue now recurring. This has resulted in a double-digit organic growth business complemented by a sound and disciplined acquisitive strategy aimed at geographic and market expansion given the fragmented nature of the space (*recently acquired company for $11M saw another $2.5M in added revenue within months)*.

You are probably wondering how we have come to label Iteris as a leading player in the space. This stems from two factors (1) Iteris has developed and is managing the design rulebook for the future of intelligent transportation in the U.S (USDOT Connected Vehicle Reference Architecture Design), and (2) on the Roadway Sensor side, Iteris has a touchpoint on over 33% of signalized intersections and continues to capture market share in both Roadway Sensors and Transportation Systems as evidenced by ~mid-teens organic growth (outpacing industry growth). We believe this cash flow generative segment will continue to benefit from (1) higher % of infrastructure budget allocated to technology (from pick and shovel) as seen in yet again a near-record quarter Backlog, (2) increasing proportion of recurring higher-margin software revenue, and (3) a 20% net cash position paving the way for incremental tuck-in M&A every year.

As management continues to execute on its strategy, we would not be surprised to see Smart Mobility taken out by a larger peer down the road, as it provides compelling growth avenues, high market penetration at the government level, and trades at ~7.0x adjusted operating income assuming we attribute no value for the Digital Agriculture business.

Digital Agriculture is Iteris' second operating business funded by Smart Mobility and accounts for ~6.0% of revenue. It is a 100% SaaS offering used by some of the world's largest crop science and farm management information systems companies (i.e Bayer) to support action course for optimal harvesting, farming, watering, spraying, fertilizing, modeling, etc. This segment is in the early stage and had historically been perceived as the company's growth engine before Smart Mobility took over. While we acknowledge the significant long-term potential that comes with Digital Agriculture (growing at over 20%/year), we believe the company is likely to explore strategic alternatives for the business, primarily a sale, as it ramps it up to profitability level.

With Iteris' roots centred around Smart Mobility, we view a potential divestiture as a major positive as (1) it frees up management's time to focus on its core rapidly growing business, (2) it unlocks significant imminent value with some of Digital Agriculture's private peers raising equity at high single-digit to low teens sales multiples, and (3) results in a multiple expansion for the core business as it enhances cash flow

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generation and sheds light on it as a standalone entity. *We believe the cash proceeds from a potential sale can be accretively reinvested into Smart Mobility, creating a larger nationwide transportation specialist.*

Iteris's stock price today is far from reflective of the true intrinsic value of the company as it dropped 50% since the Covid-19 outbreak began despite operating in what is deemed a critical essential industry (infrastructure and transportation), and sitting on a healthy cash balance of 20% of its market capitalization. While we acknowledge the impact of the outbreak on potential delayed backlog conversion in the short-term, we highlight that it is a matter of revenue timing pushback and not cancellation.

Accordingly, the stock price clearly fails to reflect the favorable fundamentals of the business. Under the leadership of CEO Joe Bergera and CFO Douglas Groves, whom we have interacted with on numerous occasions, and the additions of two new directors to the board, including former Raymond James Financial (RJF) Chief Operating Officer Dennis Zank in January 2020, we believe the company is well on track to execute on its strategy of creating shareholder value. We took advantage of the overdone sell-off and continued to build up our position in Iteris.

Corporate Updates:

Despite temporary yet dramatic healthcare and economic challenges, LionGuard remains committed to growing our dedicated team and expanding our operations. To that end, in March 2020, we hired Wei Lin as a Senior Associate, Operations. We welcome Wei to the team and wish him great success at LionGuard.

We take this opportunity to highlight that our other Funds delivered on their mandates in Q1-2020 with LionGuard Conservative Fund ("Conservative Fund") down only 0.24% (net of fees) and LionGuard Canadian Small Cap Equities Fund ("Small Cap Fund") outperforming its benchmark by 7.51% (gross of fees).

May you have any questions, please contact us at any time.

Yours sincerely,

Andrey Omelchak, CFA
President, CEO & Chief Investment Officer
(on behalf of LionGuard Capital team)