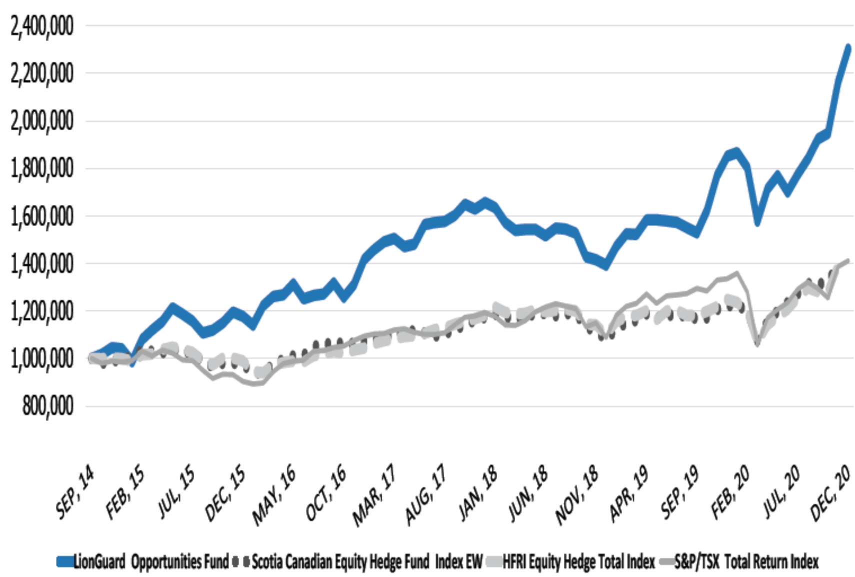
LionGuard Capital Management Inc.
1010 rue Sherbrooke Ouest, Suite 2350
Montréal (Québec) Canada, H3A 2R7
www.lionguardcapital.com

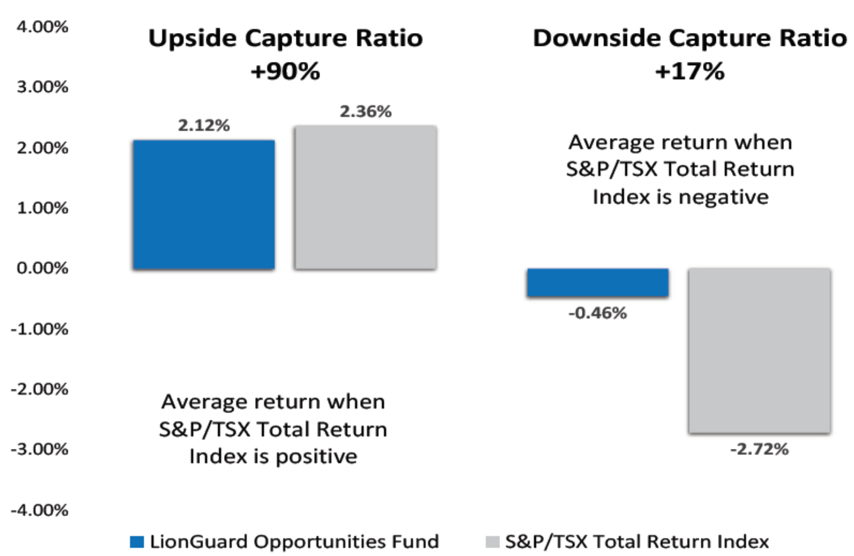
LIONGUARD OPPORTUNITIES FUND
INVESTMENT REPORT – YEAR 2020

Dear Investors,

For the year 2020, LionGuard Opportunities Fund ("Opportunities Fund") had a positive net (after all fees and expenses) return of 24.32%. Since Fund's inception, its annualized net return amounts to 14.27%.



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 90% and downside capture ratio to only 17%.



In addition, since Fund's inception, its annualized net return divided by the largest drawdown since inception amounts to 0.90x. This ratio is frequently used by sophisticated allocators to gauge funds' return profiles relative to the amount of risk they take.

We tend to agree with the underlying rationale behind this metric, which in our opinion is much more telling than the more widely used Sharpe ratio. In addition, we believe it is useful to examine net return / 2nd largest drawdown and net return / 3rd largest drawdown ratios, which for the Opportunities Fund respectively amount to 0.92x and 1.63x.

2020 In Rear View Mirror & Looking Ahead To 2021:

As an incredibly challenging year for so many people ended, we want to take this opportunity to recognize amazing efforts of all those who have kept our healthcare system operating and our economy functioning despite all the risks. We also want to recognize numerous personal and professional tragedies that so many experienced.

When it comes to the overall stock market performance for the year, the disconnect with "Main Street" cannot be more startling. Although Canadian markets have not fared that well, S&P/TSX Total Return Index was still up by 5.6% for the year. In the U.S., the S&P 500 Index was up by 16.3% and by far the best performer, NASDAQ, was up by 43.6%.

The NASDAQ rally was led by the huge stock price appreciation for mega-cap technology companies, which either benefitted from or were largely immune to COVID-related issues. As commented during our quarterly reports throughout the year, lower interest rates and an unprecedented amount of government stimulus played key roles in contributing to stock market performance in 2020.

In conducting our own investment operations, we have taken a highly conservative stance at the onset of the pandemic and until there was sufficient visibility that we are not taking unnecessary risks. Capital preservation has been and remains our primary objective when managing the capital entrusted to us. As a result, Fund's largest drawdown during the worst months for the market (February and March) was a respectable 15.4% (our second largest drawdown since inception).

As outlined in our quarterly reports, despite our conservative stance, we made sure to invest in companies we know very well, and whose operations were not negatively impacted by the pandemic. Rather than re-capping our thought process at the time, please see below the excerpt from our Q1/2020 report:

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 <u>Multiple Scenarios</u>

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 <u>Same Multiple Scenarios</u>

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.

With the record number of new individual investment accounts opened in 1H/2020, there has been an influx of retail investor's capital into the market. The result can be clearly seen in the performance of the companies to which individuals tend to be attracted. In addition to obvious candidates, speculative masses largely embraced the red-hot IPO market.

Numerous low-quality businesses became public in the latter half of the year, yet despite their questionable (in our opinion) business models, they performed extremely well stock price wise. Even the companies for which investment bankers were barely able to raise the capital performed quite well once they started trading. Such a speculative and indiscriminate buying frenzy is bound to end badly for those who do not "get out" in time. When everyone thinks they are geniuses and there is free money to be made, better watch out!

Despite warning signs in select market segments, we do not attempt to make predictions as to the overall market direction. Those who build their investment process around "market calls" rarely do well over time.

Having said that, we are of the view that numerous small- and medium-capitalization companies have just started moving in the direction of their intrinsic values. We are also starting to see a massive increase in M&A activity, which bodes well for many companies we invest in. In our past reports, we wrote extensively on the tremendous amount of dry powder in the hands of private equity and all signs currently point towards them starting to deploy the capital. As prospects for economic reopening increase, so will the competition for target acquisitions from both private equity and strategic buyers.

Currently, we have all reasons to believe that we are entering a major M&A wave across the globe. Most obvious takeout candidates in the Fund include: **Sangoma Technologies (STC), MDF Commerce (MDF), DIRTT Environmental (DRT), Photon Control (PHO), Firan Technology (FTG), American Software (AMSWA), Iteris (ITI), Powerfleet (PWFL), Onespan (OSPN), Donnelley Financial (DFIN)** and others.

Year 2020 Contributors:

For the full year 2020, some of our notable contributors were: **Sangoma Technologies (STC), MDF Commerce (MDF), Issuer Direct (ISDR), DIRTT Environmental Solutions (DRT), Powerfleet (PWFL), Points International (PCOM), Iteris (ITI), Major Drilling (MDI), Canadian Western Bank (CWB), Photon Control (PHO), Strad (SDY), Prontoforms (PFM), Vocera Communications (VCRA), Equitable Group (EQB)** and others. On the opposite side, notable detractors included **Firan Technology (FTG)** and **Sleep Country (ZZZ)**.

Issuer Direct (ISDR) is one of our top contributors for the year. It is not every day that we come across a company that "ticks all the boxes" (*below)*, and as such, we encourage you to review our thorough discussion of the name in our Q3 report as we take this opportunity to highlight that the recent pullback in the stock presents a compelling opportunity to acquire a high quality, high growth compounder at a material discount to intrinsic value with the company trading at a FCF yield of 9.0% on 2020E numbers.

ISDR is a prime example of a rapidly growing compounder. The company *"ticks all the boxes"* and exceeds the criteria that constitute a top bet, underpinned by:

- **Alignment of Interests –** CEO, Brian Balbirnie, owns 16% of the company. In fact, we believe that a substantial portion of Brian's net worth is tied to Issuer Direct. To see such an alignment of interests is rare and should result in proper and disciplined capital allocation.

- **Large Total Addressable Market relative to Size –** ACCESSWIRE's (35% of revenue) market alone is $600M of which ISDR controls 1.0%. Management intends to capture 3%-5% of the market by the end of 2022 as ACCESSWIRE has been growing 20% - 30% Y/Y and will likely sustain growth momentum given investment in digital marketing channels.

- **Recurring revenue (estimated to be 80% of total) with clear visibility for sustained double-digit growth and potentially ~2.0x the business within 2-3 years–** we estimate that almost 80% of revenue is recurring of which we estimate that 60% is likely SW/Cloud-based. We believe the company is well-positioned to achieve double-digit organic growth to be complemented by accretive M&A. In fact, should management achieve the upper end of its newswire market share grab, we believe ACCESSWIRE alone can 1.7x the business within the communicated time frame.

- **Mountain of cash to be deployed accretively, to support ARPU growth –** 27% of ISDR's market cap is in cash. As management has communicated over time, that cash will be deployed in recurring high growth complementary business that could expand the TAM into a multi-billion market while bridging the private to public ARPU gap which is a major positive for ISDR given that private customers account for 52% of all clients.

- **Prime takeout target with 9% FCF yield, double-digit sustained growth –** We view ISDR as a prime takeout target by established strategic players. We believe that as Brian and the ISDR team continue to execute and scale the business, other larger players will begin to see value in acquiring the business. However, cognizant of the market and the potential of ISDR, we clearly favor the route of staying public unless the offer is too good to pass on.

As the company continues to execute on its strategic as well as organic and acquisitive initiatives to build a one-stop communications shop for its customers, ISDR remains one of our top bets and we remain staunch supporters of the company. We view the recent pullback as a great opportunity to buy this high-quality high cash flow business.

PowerFleet (PWFL) is another top contributor for the year. We discovered PowerFleet when it was just I.D. Systems. What presented itself as a nimble, barely profitable company, had the attributes of a powerful dominant telematics and IoT company with significant room for margin expansion and consolidation.

Indeed, months after reading about the company, I.D. Systems decided to merge with Pointer Telocation, creating one of the leading global telematics companies serving ~600,000 units to ensure goods, assets, and equipment are safely guarded, operational, compliant, and up to speed. After thoroughly diving into the proposed transaction and meeting with management at a Boston-based conference in August 2019, we came away with the conclusion that the merger was a win-win for both companies as it had "2+2=5" written all over it. In fact, in what is clearly a competitive market, size, product offering and global reach are of utmost importance as scale tends to bring scale. That is precisely what I.D. Systems brings to Pointer and vice versa as the combined entity provides:

- **A true bumper-to-bumper offering for its clients** – a rare feat in the industry as we believe 4-5 players including PowerFleet have such capability. This puts the company on an advantageous competitive positioning when bidding which is reflected in its product win rate (60%-65%) and the number and size of deals PowerFleet has won and bid on since the acquisition closed late last year. As an example, the company has partnered with one of the leading global forklifts manufacturers, is in the middle of a pilot with one of the top global car rental companies, and is in the process of bidding on a $19M contract with the U.S government.

- **Significant operating leverage** – with the potential EBITDA margin of 25% at scale versus previously expected 15% on day of closing.

- **Shift to recurring revenue from product-rich mix** – with recurring revenue increasing to 55% of total (high visibility subscription revenue) from 37% pre-transaction.

- **Cross selling opportunity** – as IDSY cross sells its products into the Pointer customer base and as Pointer cross sells its products into the U.S Class 1-5 fleet category.

- **Blue chip customer diversification** – with 8,000+ companies including the likes of Avis, Ford, Toyota, Walmart, Danone, UPS, Software, Walgreens, 3M, and Audi.

However, as with most transformative acquisitions, integration always puts a dent on high expectations in the short term. This case was not any different as management had to pull its margin guidance for 2020 concurrent with its Q1 reporting on the back of additional pro-forma platform consolidation investments in H1/20 and investments made to bring Class 1-5 products into the U.S. The company later pulled all financial guidance with the onset of COVID which was the viable thing to do given global uncertainty.

LionGuard Capital Management Inc.
1010 rue Sherbrooke Ouest, Suite 2350
Montréal (Québec) Canada, H3A 2R7
www.lionguardcapital.com

As the share price dropped form $8.00 pre Q1 reporting date to $3.00 at the peak of the pandemic, we capitalized on our research and significantly increased our weight in PowerFleet.

In fact, we built our confidence in the business and its prospects by stress-testing its earnings power under three strict COVID scenarios that called for sizeable organic decline in product revenue (40%+) and a small organic decline in subscription revenue owing to its contractual and recurring nature as we expected minor unit termination and potentially a few weeks/months of discounted prices. Unsurprisingly, even under our worst-case scenario, PowerFleet was a bargain at $3.00. Bolstered by our fundamental research findings and conviction, we took a larger stake in PWFL as it made its way into one of our Top 10 bets.

As the strength of the subscription revenue came to light and as management took effective measures to reduce costs by ~$8.0M/year, PWFL's earnings power more than offset expected top line volatility owing to COVID as it delivered 13% EBITDA margin in Q3/20, taking many by surprise. Concurrent with margin expansion from 4.4% same time last year and positive vaccine news, PWFL's share price appreciated to almost pre-COVID levels and we continue to see significant upside to the story as the company will emerge as a leaner, higher margin entity in a normalized post-COVID world. In fact, PowerFleet has become one of the more compelling reopening "plays" with product revenue likely to see a strong comeback as it recovers from organic product revenue decline this year. Some of the key points that give us comfort in the investment are:

- **Cost savings in 2021/22** – the same investments that derailed near term margin expansion are expected to result in $2M+ in cost savings on top of the $8.0M achieved this year, bringing the proforma company closer to its long-term goal of 25% margin.

- **Operating leverage** – should PWFL achieve its $200M revenue target, examining peers, we believe the company will be well-positioned to see margins expand to 25% over time.

- **Strong pipeline –** as per recent earnings calls, PWFL's pipeline remains robust and its win rate on the product side remains strong. We believe the company is well-positioned to close multiple large deals as we move past COVID including a potential $19M government contract, a potential pilot project with a large car rental company, potential expansion with one of the largest forklift manufacturers, and potential expansion with one of the world's largest online retailers.

- **Takeout target?** – While not a basis for owning the company, we believe that the company is a compelling takeout target and we would not rule out a potential takeout by strategic or private equity investors. We note that private equity firm Abry Partners is a key PWFL investor via its preferred stake which converts into a 19.13% ownership as per the most recent DEF14. We note that two of PWFL Directors are Abry employees.

- **Good execution can bridge the valuation gap from 13x to 16x-17x –** recent telematics precedents indicate a valuation range of 15x-18x for these businesses. We believe that good execution from management with the continued expansion of recurring revenue and profitability will help bridge PWFL's valuation gap vs precedent transactions in the space.

LionGuard Capital Management Inc.
1010 rue Sherbrooke Ouest, Suite 2350
Montréal (Québec) Canada, H3A 2R7
www.lionguardcapital.com

Corporate Updates & Other Funds Performance:

I take this opportunity to highlight the incredible hard work, dedication, and resilience of our employees, all of whom performed exemplarily during 2020. Despite all the challenges, our team has grown by three people during the year. Although new team members have been with us for less than 12 months, everyone is fully up-to-speed and has already become a core part of our team.

We are also very thankful to our clients, many of whom recognized the opportunity presented by the broad-based market sell-off at the beginning of the year and entrusted us to take advantage of market inefficiencies without taking excessive risks by allocating more capital to our funds.

We are pleased with the performance of LionGuard Market Neutral Strategy, which was at +8.26% (net of fees) during the year. It is a "true" market neutral strategy with a target net long exposure of 0%. Note that during the extremely turbulent Q1/2020, this strategy was down by only 0.24%. Since its inception, the Strategy's upside market capture is +14% and downside market capture is -15%. Its annualized net return since inception is equal to 6.64% while its largest drawdown, both based on monthly data, is 2.99% for a ratio of 2.2x.

LionGuard Canadian Small Cap Fund delivered +26.82% gross returns in 2020, which compares very well vis-a-vis its benchmark and industry peers. Fund's value-added over the year amounted to 13.95%.

Yours sincerely,

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