PALISADE CAPITAL

Our Market View in Summary — April 2024

April witnessed the first significant market pullback since last October, in our view not signaling the start of a broader decline but rather a normal correction, consistent with typical yearly market rhythms. Despite this, the month saw notable disparities in sector performance, with early strength in commodities like oil and basic materials due to persistent inflation concerns, though these gains were partially retraced as the month progressed. More notable weakness was seen in the interest rate sensitive sectors like utilities, telecom and real estate as fears that interest rates would remain "higher for longer" set in for investors and drove capital out of those sectors.

Report Summary:

- Early month gains in oil, gas, and basic materials partially driven by ongoing inflation fears
- Interest-sensitive and technology sectors experienced the most significant declines
- U.S. gross domestic product (GDP) growth disappointed, heightening market sensitivity to economic indicators. Slight softening was seen in a handful of economic data points like the Citi Economic Surprise Index, Job Openings and the Services Purchasing Managers Index (PMI)
- Persistent high inflation with slight upticks influenced by specific factors like car insurance
- U.S. rents are expected to decrease, potentially easing inflation in upcoming months

Near-Term Outlook:

- Citi Economic Surprise Index in the U.S. turned negative, suggesting economic data may be underperforming expectations. This doesn't mean that a recession is imminent, just that some recent positive momentum may be slowing
- PMI data has weakened, with the service sector index dipping below 50 for the first time since December 2022
- Economic softening could prompt the US Federal Reserve to consider interest rate cuts. This is what we want to see - interest rate cuts to support the ongoing soft landing that we have been living through for the past two years
- Increased disparity in 2-year government bond yields between Canada and the U.S., reflecting expectations for earlier rate cuts in Canada
- Potential recovery in interest-sensitive sectors like Telecom and Utilities, similar to trends observed last October. "Higher for longer" interest rate fears are fully priced into these stocks at these levels especially if we see the Bank of Canada cut interest rates in the near future

Despite the recent pullback and softening of some economic indicators, in our view the outlook for 2024 remains positive for both Canadian and U.S. stock markets. Supported by strong U.S. economic growth and potential rate cuts, Canadian markets are particularly well-positioned to benefit given their exposure to interest-sensitive stocks. With S&P 500 companies' earnings estimates and profit margins improving, driven by substantial investments in AI and other technologies, the broader market sentiment remains optimistic about overcoming minor economic hurdles and normal market pullbacks like the one we saw in April.

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April 2024

Fellow Palisade Investor,

Please find attached our April 2024 Monthly Update, as well as the Fund Fact Sheets for the Palisade Funds. **This month's client conference call is scheduled for Tuesday, May 14th at 11am MT.** As a reminder, we have switched the format of the calls from Zoom to Microsoft Teams, but the process will be the same if you wish to join the call. You can connect either through your computer or by calling a phone number. The Teams meeting details will be provided the morning of the call. In conjunction with this call, we will be emailing out a presentation that contains data and charts to further detail our thought process and outlook. We look forward to speaking with you then and answering any questions you may have**.**

All Fund performance figures are shown net of fees and expenses and include changes in security values and distributions paid. They do not assume the reinvestment of distributions. The Palisade Vantage Fund currently pays a regular quarterly distribution of $0.11 per unit, or $0.44 per unit per year. The Palisade Select Fund and Palisade Absolute Fund pay irregular annual distributions for years in which taxable net income is positive.

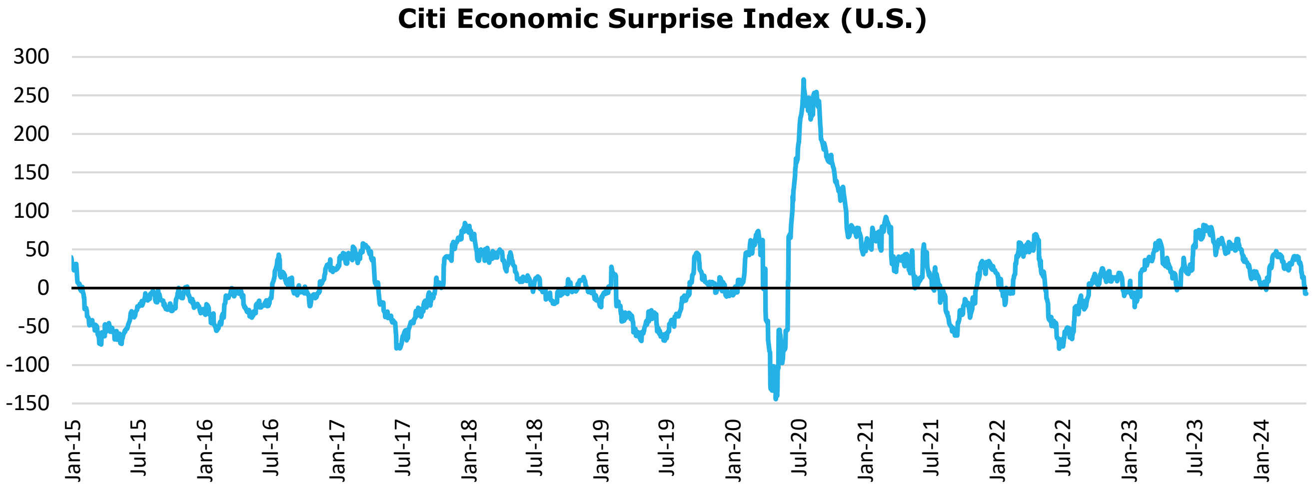
MARKET COMMENTARY

April was the first material pullback in markets that we have seen since October of last year. We don't see the weakness in the month as the start of something bigger or more ominous. Every year in the stock market you will typically see at least a couple of 3%-5% pullbacks. Given that we haven't seen that type of a pullback since October it is reasonable to assess that it was time for a normal breather. With that said, there was quite a wide dispersion in sector returns this month as we saw a strong start to the month in oil, natural gas and basic materials stocks as inflation fears and interest rates continued to stay prominently in the news. These stocks gave back some of their gains in the back half of the month, but overall, they still finished higher on the month while most stocks finished down. Most of the month's weakness was in interest sensitive stocks and technology stocks.

Part of the reason for the weakness this month was persistently higher inflation readings at the same time as gross domestic product (GDP) growth in the US surprised to the downside. It's important to note that this was largely one data point in a generally volatile data set, but given the run that markets had to start the year, we have seen less room for error in the markets as a whole, and also for individual stocks reporting quarterly numbers. There are one-off items that have moved inflation up slightly in recent months (car insurance, for example) but we still expect real-time readings of declining rents in the US to show up in lower inflation readings in the coming months to get the trend back on the downwards track. In the meantime, economic data has been fluctuating a little in the last few weeks, which has contributed to the weakness and volatility that we saw in April.

As the market continues to move up and down based on the short-term expectations for the direction of the US Federal Reserve Funds Rate, we thought it would be appropriate to highlight some areas of the economy where economic data has started to weaken slightly. Does this mean that a recession is near or that the stock market needs to swoon? No, but it will continue to highlight the balance that the US Federal Reserve is trying to find between managing inflation and supporting the economy, when necessary, with lower interest rates.

The chart below shows the Citi Economic Surprise Index in the US. This isn't an indication of the direction of economic data - it shows the degree to which economic data points are surprising to the upside or downside. A reading above zero indicates economic indicators positively surprising in aggregate, and the opposite when the index is below zero. So, the economic data may still be improving overall (as it currently is), but the growth may be coming in a little lower than expected and vice versa when the index is moving higher and above the zero mark.



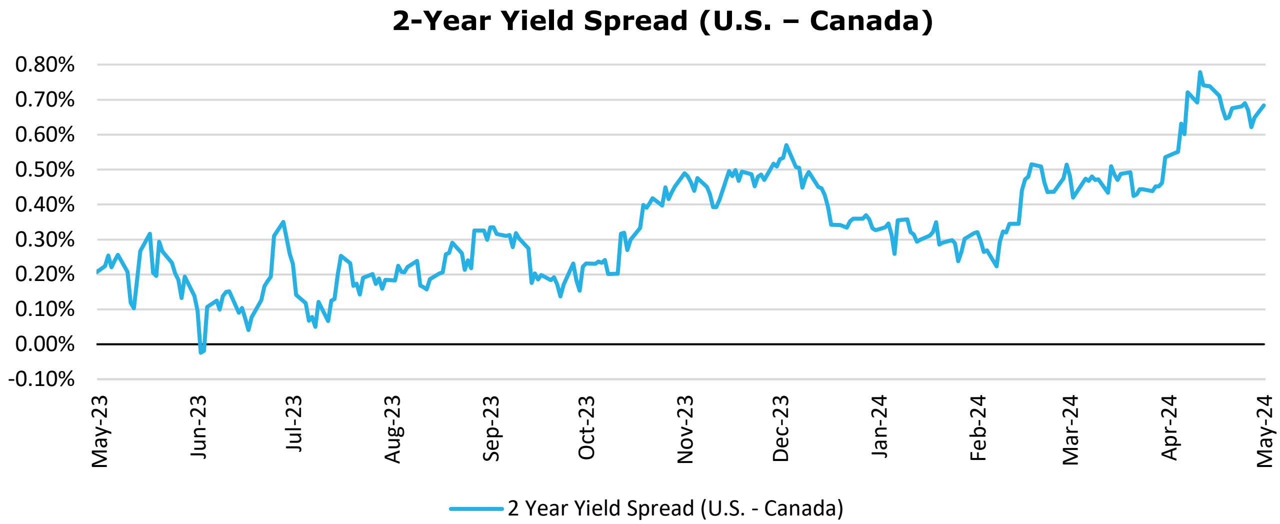
Source: Bloomberg

Citi Surprise Index turning negative. Purchasing Managers Index (PMI) data weakening. Job openings continue to slow.

As you can see, just this month we have started to see more economic data points surprise to the negative after staying consistently positive for the past year. Again, this doesn't mean that a recession is on the horizon, but it shows that the positive momentum in the US economy may be slowing and the impact of higher interest rates may be taking the edge off of growth a little. As these sorts of data points slow it should give the US Federal Reserve room to more actively consider cutting interest rates in the future. We have also seen the monthly Purchasing Managers Index (PMI) for services drop below 50, which hasn't happened since December 2022. At that point the economy was still progressing forward and 2023 turned out to be strong year for economic growth in the US. We expect the same thing to happen this time around.

In Canada, when you combine the soft economic data in the US with our generally moribund economic data, it should lead to the Bank of Canada starting to cut interest rates quite quickly. If our largest economic partner is starting to lose a little economic momentum, we need to be even more aggressive in addressing our interest rate environment because we don't have the luxury of a robust domestic economy to support us. This need for Canada to cut rates more quickly than the US is partially reflected in the spread between 2-year government bond yields between the two countries. In Canada, the current 2-year yield is 4.15% while in the US, the 2-year yield is 4.84%. The spread between these rates has been rising in the last three months, partially reflecting an expectation that interest rates will be lower in Canada.

The chart below shows this spread over the last year and makes it clearer how market expectations have shifted from slightly balanced to an expectation that Canada will need lower rates than the US shortly. Looking at it another way, in the last three months we have seen the yield on US 2-year bonds rise more than their Canadian counterpart because investors fear that the US Federal Reserve will have to keep rates at a higher level. In Canada, the likelihood of rates staying higher for longer is much lower, so the yield on 2-year government bonds has not gone up nearly as much, thus the spread between the bond yields of the two countries has increased to reflect those expectations.



Source: Bloomberg

If we see interest rate cuts in Canada, we should see a bit of a positive reversal and recovery in the interest sensitive stocks. These sectors have been under the most pressure recently and are a core component of the Palisade Vantage Fund. Telecom stocks have revisited their lows of last October and Utilities stocks got close to their October lows in mid-April before bouncing in the last week of the month. Much like in October, we feel there are real opportunities at current prices for some of these stocks. Clearly, market expectations for interest rate cuts in 2024 got ahead of themselves during the first quarter, but those rate cuts are coming (sooner than later in Canada) and the stocks most tied to those rates have largely declined to levels where fear of a "higher for longer" rate outlook is well-discounted, which creates a great long-term buying opportunity for investors.

Broadly speaking, we continue to see upside for Canadian and US stock markets in 2024. We believe that the underlying US economic growth will pull Canada along and eventually lower interest rates will provide additional benefit to the Canadian markets, which have more exposure to interest sensitive stocks. In the US, earnings estimates for the S&P 500 companies continue to go higher along with profit margins, assisted by a massive capital expenditure cycle oriented around artificial intelligence that will boost spending for both industrial and technology-oriented companies. Until there are sightlines to a major crack in those trends, we aren't going to get too worried about a routine market pullback and slight softening in some economic indicators over the past few weeks.

PALISADE FUND COMMENTARY

The **Palisade Select Fund** ("PSF") was up 1.7% in April. The S&P/TSX Capped Energy Index ("Energy Index") was up 3.1%. The WilderHill Clean Energy Index ("ECO") was down 11.9% for the month.

As mentioned earlier, oil and gas got off to a good start in April, but then cooled off in the last half of the month, particularly on the last day of the month. It all comes out in the wash in the long term, but the last day of the month swoon has been very frustrating. In oil and gas, we continue to view the opportunity ahead of us in a sustained light – the Trans Mountain Expansion and LNG Canada will assist with tighter pricing differentials for both oil and gas in the next year and a half; the resiliency and need for traditional energy sources continues to be reaffirmed in the media and improves capital flows to the sector; strong cash flows (particularly in oil-weighted companies) allow for additional dividends and share repurchase programs; and increased global commodity demand maintains a reasonably stable oil pricing environment that allows for some valuation improvement in many of the mid-cap names. This month feels like a time when we need to exhibit some patience, continue to focus on high quality companies and let the investment thesis play out. While large-cap oil stocks aren't as cheap as they were, there still exists notable value in mid-cap producers and energy service stocks.

The PSF is largely fully invested, but we are looking at opportunities to rotate exposure out of some of the more fully valued names into some natural gas and energy service names that haven't participated in the rally to the same degree.

The **Palisade Absolute Fund** ("PAF") was down 2.6% in April. Recent returns have not been what we would want to see for the PAF. As mentioned last month, we have begun making more widespread changes to the screening used for the holdings in the Fund. While we have been including names from these new screens for the last few months, April was the first month when it was fully implemented within the Fund. Unfortunately, we also saw a market pullback that impacted these new holdings, which pulled back the performance of the Fund this month. That said, through the first four trading days of May, the PAF has made back most of those losses. It's a long way to go until the end of the month, but the names in the portfolio are high quality and exhibiting positive fundamental and price momentum. The short book is comprised of stocks with the opposite characteristics. Although no guarantee of future performance, the data for the performance history of the screens going back ten years shows annual returns for the long positions in the mid to high teens in both Canada and the US. When combined with the names coming from the short screen at conservative weights, the back test total portfolio shows a very attractive risk/return profile, including positive returns in 2022 when the market was down dramatically, and only small losses in two of the last ten years.

At the end of the day, the screens act as an efficient high-grading machine that is focused on high quality, well known stocks with consistent track records of execution. Obviously, this isn't the first month that we wanted, but we are confident in the work that has gone into creating the screens and the back tested data and returns. For example, on the long side we are holding companies like Mastercard and S&P Global in the US. In Canada, we own companies like Waste Connections and CGI Group. On the short side a few examples would include Air Canada, Maple Leaf Foods and Canadian Tire. Combined with our broadly positive view on the stock market for the remainder of the year, we expect to see an improved return profile going forward.

The **Palisade Vantage Fund** ("PVF") was down 3.2% in April. As we have been noting in recent commentaries, the appropriate comparison for the PVF is likely to the S&P/TSX Canadian Dividend Aristocrats Index, rather than the broader S&P/TSX Composite Total Return Index. For the month, the S&P/TSX Canadian Dividend Aristocrats Index was down 3.2% while the S&P/TSX Composite Total Return Index was down 1.8%. As mentioned earlier in this commentary, the rate sensitive sectors such as utilities, telecommunications and real estate continued to be under pressure as fears about higher interest rates staying in place for a longer period of time than previously expected continue to hold sway with investors and capital flows. That said, over the course of the month we have seen many stocks get close to the lows that they previously approached in October of last year. These low prices, combined with the fact that we have 15% of the PVF in cash that we can deploy down here makes us excited for the balance of 2024 in these sectors. We will see interest rate cuts from the Bank of Canada shortly, and while the US Federal Reserve is likely on hold for a few months yet, we feel that fear is already priced into these stocks at current levels. We will look to add back some of the telecom holdings that were trimmed in the previous few months, as well as bulking up exposure in names tied to oil and gas royalties and financials that have come under pressure in recent months.

If you have any questions, please feel free to reach out at any time.

All the best,

THE PALISADE CAPITAL MANAGEMENT TEAM

Please note that it is the responsibility of each investor to inform Palisade Capital of any changes to the information provided to us on the most recently completed Know Your Client ("KYC") information form or subscription agreement. Please contact Marni Friesen at (403) 531-2673 or marni@palisade.ca to provide any such updates. If you no longer wish to receive the Monthly Update, please send an email to info@palisade.ca.

All Palisade Fund performance figures are shown net of fees and expenses and include changes in security values and distributions paid. They do not assume the reinvestment of distributions. Income taxes would have reduced returns. The Funds are not guaranteed. Performance of the Funds will fluctuate and past performance may not be repeated. To establish relative performance yardsticks for the Palisade Funds, we provide comparative references to the S&P/TSX Composite Total Return Index ("TSXTR"), the S&P/TSX Capped Energy Index ("Energy Index") and the WilderHill Clean Energy Index ("ECO Index"). Those indices are relevant to our portfolio content however the TSXTR, Energy Index and ECO Index data is provided for general reference purposes and their content should not be construed as directly comparable to the content of the Palisade Funds.