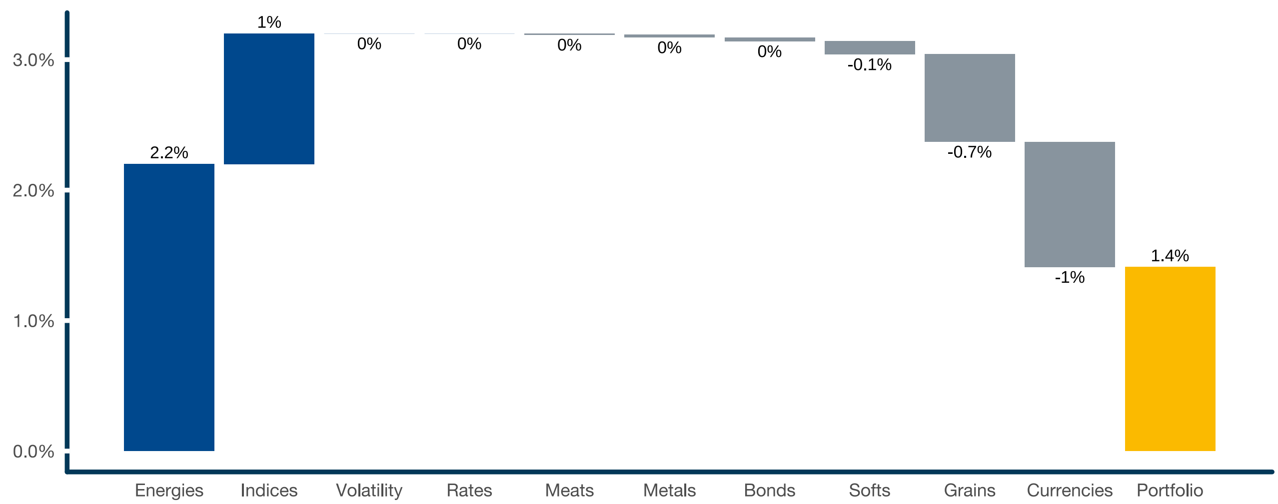
PERFORMANCE REVIEW

The Osprey program experienced yet another positive quarter, rising 1.4 percent and a total year-to-date performance of 9.7 percent.

Figure 1. Q2 Return Attribution



Source: ReSolve Asset Management. Results may differ due to rounding. Performance is expressed in CAD. Strategy attribution is a best efforts approximation, net of all applicable borrowing costs, fees and fund accruals for the period. Indicated returns of one year or more are annualized. Past performance is not indicative of future performance.

The lion's share of gains came from **Energies**, largely from long positions in crude oil (both Brent and WTI), along with gasoil, heating oil and carbon emissions. The large exposure to heating oil earlier in the quarter was reduced and replaced by crude oil, which gained strength in May and June.

Equity Indices were the other major positive contributors, with gains well distributed across multiple markets. Main highlights came from longs in the British FTSE, German DAX and Spanish IBEX, along with the Russell 2000 and S&P500.

Currencies were the main detractors, stemming largely from shorts in the British Pound and Japanese Yen, along with long Euro.

Grains also led to losses, primarily due to short exposures in soymeal and wheat, as well as longs in soybeans.

Profitable longs in German and Japanese sovereign debt were offset by losses in long positions in US 2-year and Aussie 3-year, as well as a short position in Canadian 10-year, leading to an overall flat contribution from **Bonds**.

Similarly, **Metals** offered no meaningful contribution because losses in our long exposure to platinum were countered by gains from long copper and short silver.

RESEARCH HIGHLIGHTS

Our research team made a breakthrough in the integration of feature selection and model specification in a single step. This lays the groundwork for the ultimate objective of running continuous mining on a pipeline of curated features relevant for each market.

The firm also hired two new full-time developers to scale our existing data, feature generation, mining and execution pipelines as we push toward same-day and, eventually, intra-day signal generation and trading.

In addition, our quant team derived a novel optimization procedure, which generates optimal forecasts in the context of all the other assets in the portfolio. Traditionally, predictive models are optimized with unique prediction-based objectives and constraints, and are therefore unaware of how those predictions will ultimately be used in the context of the final portfolio. Our team produced a framework for integrating regression based predictive models in a portfolio optimization setting. Predictive models derived from this method are often quite different from those derived independent of the portfolio decision. Early results look quite encouraging. We invite you to explore a draft of the paper describing this new method here.

More information regarding these projects will be disclosed as they mature.

GENERAL MARKET REVIEW

A wave of positive economic news swept global markets, lifting virtually all boats and renewing risk appetite across the board. Massive fiscal spending and looser restrictions in the wake of declining infections in the US produced 6.4 percent GDP growth, beating expectations. Across the Pacific, China's economy expanded 18.3 percent in the first quarter, its fastest yearly pace on record. Notwithstanding the *base-effect* (easier comparison given the activity plunge during the first three months of 2020), the speed of its recovery has been impressive. Given the sharp rebound in activity, it is not surprising that US corporate earnings season was remarkably strong, beating Wall Street forecasts by the widest margin on record, according to data from Refinitiv[1].

Debate over the expected duration and intensity of inflationary pressures remained a key variable for asset allocation and investment decisions. Recent data offered fuel to both sides of the argument, with *inflationistas* pointing to expectation-beating rises in both CPI (Consumer Price Index) and PCE (Personal Consumption Expenditure), at rates not seen since the early 1990s, coupled with growing evidence of demand outstripping supply across various sectors, causing meaningful shortages and intense competition for raw materials.

The US government's recently released budget proposal, which would see the highest levels of sustained spending since World War II, has also fueled an uptick in growth expectations, leading Treasury Secretary Yellen to admit that "interest rates will have to rise a little bit to make sure our economy doesn't overheat". The deflationist narrative leans on distorted year-over-year comparisons, the potentially transitory nature of current supply-demand imbalances, along with evidence suggesting growth may have peaked early in the Spring. This position is also supported in the intermediate and long-term by global demographic, technology and productivity trends.

Hawkish remarks by senior Fed officials forced chairman Powell to strike a *pacifist* tone, claiming "inflation alone" would not be enough to prompt rate hikes. Notwithstanding the most recent Dot Plot pointing to higher interest rates sooner than previously expected and the first hints at a discussion about tapering the current bond purchase program, market action suggests investors have been positively swayed by the Fed's theatrics, at least momentarily.

After intense pressure in the first quarter of the year, US Treasuries partially recovered some of the lost ground, with the 10 and 30-year bond yields narrowing by 28bps and 30bps, respectively. It is worth noting that the Fed has just crossed the *Treasury Market Rubicon*, surpassing foreigners to become the largest holder of US sovereign debt[2]. Canadian, Japanese and British sovereign bonds were also up, while the French, German and Italian government debt continued to slide, albeit at a slower pace. The US dollar gave back some of the gains accumulated earlier in the year, dropping almost 1 percent as measured by the Dollar index, and considerably more against Emerging Market currencies.

Equity markets steamed ahead, with Canadian, European and US markets leading the way. The double-digit rally in the Nasdaq was bolstered by strong corporate earnings as well as the drop in long-term interest rates, which triggered a resumption of the *growth trade*. Though major Japanese indices were in the red, other Asian markets were mostly up, along with Emerging Markets. But it was the commodity space that once again stole the limelight. Gold and other precious metals suffered intense volatility and a large drop in June but ended the quarter in mid-single digits positive territory, while base metals enjoyed even larger gains. Agricultural markets with large gains in corn, wheat, oils (bean, canola and palm), coffee and sugar. Lumber snapped its meteoric rise with a steep 20 percent decline, though it remained up 30 percent for the year. The energy sector offered the most impressive performance, with natural gas rising between 32 and 89 percent (depending on the contract), while crude and heating oil were up more than 20 percent.

1 https://lipperalpha.refinitiv.com/2021/05/sp-500-21q1-earnings-review-gauging-the-new-earnings-season/
2 https://corporate.nordea.com/article/65844/fx-weekly-a-woke-fed-should-taper-mbs-purchases-asap

Can They Taper Without a Tantrum

The US government pressed ahead with its fiscal agenda. On the domestic front, the White House announced a potential bipartisan deal for an infrastructure spending package, albeit a *slimmed down* version of *just* 1 trillion dollars. While the expectation of a persistent fiscal thrust is one of the main pillars of the inflationary thesis, the rejection of this bill wouldn't necessarily put an end to it. It is worth noting that the recent rise in US Consumer Price Index (CPI) has occurred despite very small rises in Owners' Equivalent Rent (OER, which represents almost a quarter of the entire index) because of a temporary eviction moratorium during the pandemic. Given that home prices have risen sharply across the US over the past year, additional price pressures could be expected once rent rules have normalized. And even though Fed officials admitted they are finally "thinking about thinking about" tapering bond-purchasing programs, their plans to create a digital currency that could be credited directly to every American household, could yet be the most expansionary policy tool ever deployed.

On the international stage, the OECD reached an initial agreement for a global minimum tax of 15 percent that would seek to minimize jurisdictional arbitrage by multinational corporations, though strong opposition is expected both from EU members and the GOP in Congress. At the most recent G7, the US president pressed world leaders to take "concrete steps to counter China's rising influence", along with heavy emphasis on a decarbonization plan. Further antagonism with the Middle Kingdom was spurred by the US Senate's approval of the U.S. Innovation and Competition Act, a 250 billion dollar package aimed at challenging China's technological ambitions. Beijing expressed "strong indignation and resolute opposition" to the bill, suggesting a "paranoid delusion of wanting to be the only winner." A "constructive" tone was celebrated by the US president and his Russian counterpart after a brief summit, though challenges remain over cyberattacks, human rights and Ukraine. While the next moves in this geopolitical 3D chess-game remain uncertain, investors should expect governments to continue increasing their control over most facets of the economy.

Sincerely,

Your ReSolve Team

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