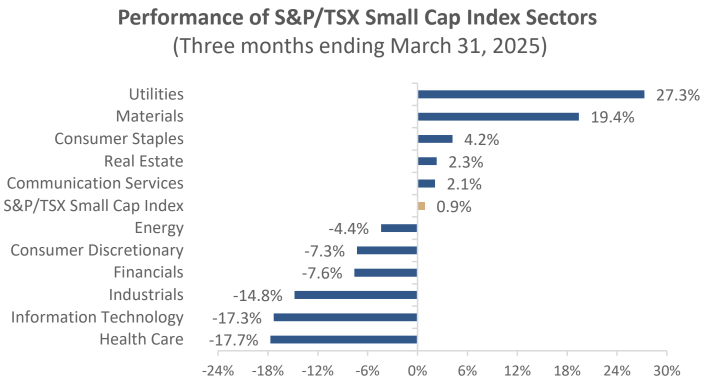
The FGP Small Cap Canadian Equity Fund returned -3.23% in the quarter, compared with the S&P/TSX Small Cap Index return of 0.88%.



Source: Bloomberg

What worked for us?

The leading contributor to relative performance in the quarter was security selection in the Health Care sector, driven by a 15% increase in the shares of Knight Therapeutics Inc., a specialty pharmaceutical company focused on acquiring and in-licensing pharmaceuticals in markets outside the U.S., particularly Canada and Latin America. In March, the company announced the acquisition of Paladin Pharma, an international specialty pharmaceuticals portfolio. The transaction was well received by shareholders given the reasonable price paid, significant synergies potential, and strong strategic fit.

Consumer Staples security selection was the second-largest contributor to relative performance in the quarter, with two investments in the sector performing strongly. Shares of Maple Leaf Foods Inc., a leading producer of fresh pork and poultry, prepared meats, ready-to-cook and ready-to-serve meals, snack kits, and plant-based protein, returned 24%, while shares of juice-maker Lassonde Industries Inc. returned 15%.

Maple Leaf Foods reported robust quarterly results, exceeding analyst estimates, and unveiled even stronger guidance for 2025, including a better-than-expected free cash flow forecast. Management now expects to achieve deleveraging targets earlier than previously planned and disclosed that the company will be able to return additional capital via share repurchases in coming quarters. Driven by stronger-than-expected revenue growth, Lassonde Industries reported quarterly earnings that were well ahead of analyst estimates.

Security selection in the Energy sector also added to relative performance in the quarter, driven primarily by a 19% increase in the shares of contract oil and gas driller Akita Drilling Ltd. The company reported strong quarterly results and a solid 2025 outlook given robust demand for its high-spec rigs, rigs that are purpose-built to efficiently drill deep and complex oil and gas wells. According to our analysis, Akita Drilling remains among the most inexpensively valued holdings in the portfolio, trading at a significant discount to the replacement value of its state-of-the-art drilling fleet.

Elsewhere, relative performance was helped by our portfolio's absence from the Information Technology sector, one of the lowest-returning sectors in the index during the quarter.

What worked against us?

Security selection in the Materials sector was by far the largest detractor from relative performance in the quarter. Our absence from gold and silver producers and explorers accounted for almost all the overall sector underperformance as precious metals equities once again performed strongly as gold prices surged by a remarkable 19% to new record highs.

Investors continued to crowd into gold as a perceived safe-haven store of value amid widespread and growing fears about deteriorating global trade relations, geopolitical risks, U.S. public indebtedness, and the status of the U.S. dollar as the world's reserve currency. According to data published in February by the World Gold Council, over the past 18 months, the estimated total value of gold mined since the beginning of time rose to approximately USD 21.7 trillion, an increase of over USD 9 trillion during this period alone.

As value investors, we continue to struggle with the relatively high valuations of precious metals producers and explorers. Also, despite significantly higher bullion prices, we continue to view near-term risks as elevated for miners because unit operating and capital costs remain well above pre-pandemic levels. At a time when the costs associated with replacing existing gold production are unprecedented, cash margins could quickly decline if demand falters and gold prices revert to the mean.

Among the Materials companies we do own, shares of Winpak Ltd., a manufacturer of flexible and rigid packaging materials and packaging machines, fell 12% amid concerns over the potential imposition of tariffs by the U.S. on imports from Canada. Shares of Richards Packaging Income Fund, a full-service distributor of packaging containers to small and medium-sized consumer products businesses in North America, fell 7% over concerns of potential weakness in customer demand in the event of a recession despite the company's vertically integrated operations and limited Canada-U.S. cross border sales activity. We continue to favour our Winpak and Richards investments given the companies' strong balance sheets and inexpensive valuations.

Aside from Materials, security selection in the Consumer Discretionary sector was the only other notable detractor from a sector perspective in the quarter, led by the decline in shares of two global automotive parts manufacturers: Exco Technologies Ltd., down 21%, and Linamar Corp., down 12%.

Shares of Exco and Linamar declined amid continued significant uncertainty over U.S. trade policy concerning the North American auto industry, specifically the imposition of tariffs on imports from Canada and Mexico, where these companies own significant auto parts manufacturing capacity. While we expect this uncertainty to continue to act as an overhang on Exco and Linamar shares in the near term, we continue to maintain our holdings as both companies remain profitable and are currently trading at severely compressed valuation multiples on a historical basis.

Portfolio Activity

During the quarter, we initiated a position in Mattr Corp., a leading manufacturer of spoolable composite pipes, composite storage tanks, specialty engineered cables, and heat shrink and cold applied tubing solutions. The company's products serve critical infrastructure markets, including energy, water management, electrification, transportation, and communication.

We used to own the company when it was called ShawCor, but exited our investment in 2023 after shares exceeded our fair value target at the time. We added Mattr back to the portfolio primarily on account of the company's attractive valuation, with the current share price less than half its 2023 high. We believe investor expectations for Mattr's growth prospects and profitability in recent years simply ran ahead of fundamentals, leading to the company's valuation multiple to retreat from overvalued levels.

Despite recent weak results, which we view as transitory, as well as tariff concerns, which have acted as an overhang on Mattr's share price, we are relatively bullish on the company's growth prospects. While tariffs represent a potential near-term headwind, recent U.S. acquisitions provide Mattr with a sufficient footprint and flexibility to shift production as needed. Longer-term, tariffs represent a potential opportunity for market share and margin gains. For example, the conventional steel and flexible steel products produced by the company's U.S.-based competitors have until now remained competitively priced, despite being less efficient, as they are manufactured from relatively cheap steel imported into the U.S., as opposed to plastic in the case of Mattr's products.

Meanwhile, the demand outlook for very large fuel and water storage tanks, for which Mattr is an industry-leading producer, remains strong, with the company's order backlog continuing to expand. Very large tank demand is being driven by a combination of replacement demand in the case of aging fuel filling station tanks and from high-growth applications such as data centre water cooling.

During the quarter, we exited our remaining investment in CI Financial Corp. In November, the company agreed to be acquired at a price we determined to be attractive.

Outlook

North American equity markets experienced elevated and persistent bouts of volatility in the first quarter as investors grappled with relentless gyrations in the communication and imposition of tariffs by the U.S. on its global trading partners, including Canada. As we exit the quarter, considerable uncertainty remains concerning the eventual magnitude and implementation of U.S. tariffs, as does the extent of retaliatory measures by those countries whose exports are targeted.

While still early innings, leaders from both the public and private sectors in Canada committed to taking major actions in support of removing longstanding barriers to greater national economic prosperity, such as interprovincial trade restrictions and permitting obstacles, most notably those which have impeded resource development and the construction of new oil and gas pipeline capacity.

Unleashing Canada's inner economic superpower is an exciting proposition, and it would be a lucrative one, likely to draw considerable investment interest like what we have seen in major European markets in recent months. A renewed focus on building Canada could also spur a large repatriation and redeployment of Canadians' vast investment wealth, much of it currently allocated to foreign markets.

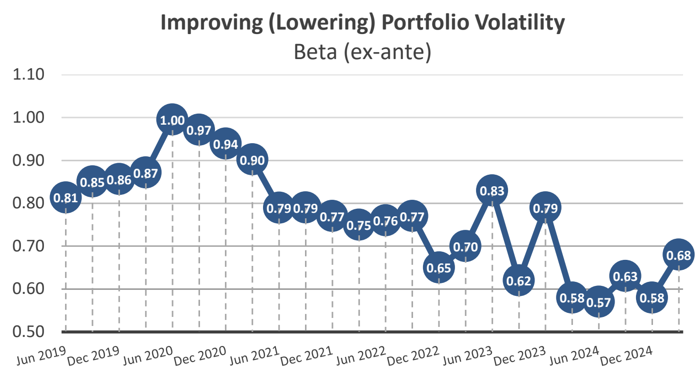
For many years, Canadian equities have suffered from persistent and mostly unwarranted valuation multiple discounts to comparable investments in other markets. The argument for these valuation discounts to narrow or even vanish altogether is increasingly bolstered by emerging catalysts, which we believe are underappreciated amid the ongoing angst.

Among the companies we own and others we follow closely, management teams have directed considerable attention and resources to understanding, preparing for, and mitigating, where possible, the direct and indirect impacts of potential tariffs. We continue to observe a heightened focus on cost structure, a priority which should help these companies quickly adjust if demand falters.

Given the continued uncertainty, new discretionary capital investment is predominantly on hold for the foreseeable future. We expect to see broadening year-over-year declines in investment activity upon completion of current projects and existing programs as 2025 progresses, a situation which will likely help warrant further cuts to interest rates by the Bank of Canada. With many corporations' investment and growth plans now largely frozen, companies are increasingly favouring share repurchases to return capital to shareholders while taking advantage of depressed share valuations.

We continue to find attractive long-term value in the portfolio, which we believe is well positioned for an uncertain future. In addition to compelling valuations, which should offer superior compounding potential and better downside protection in a market selloff, we find that most of our portfolio companies are currently exhibiting some of their best financial health and resiliency in many years as measured by balance sheet strength and liquidity, which helps enable share repurchases. The disparity in valuations between small caps and their comparatively expensive large-cap peers continues to exceed levels that have proven historically unsustainable.

While we seek to add value through our bottom-up analysis and portfolio construction, we are also mindful of striking an appropriate balance between return and risk. Beta is a commonly used measure of volatility. A beta of less than one means the portfolio is expected to be less volatile than its benchmark. At quarter-end, the beta of our portfolio on an ex-ante basis was 0.68, implying the portfolio is 32% less volatile than its benchmark.



Source: Bloomberg

While we continue to maintain portfolio beta below the median level observed over the past five years amid elevated economic uncertainty and market volatility, our risk positioning rose modestly towards the end of the quarter, driven by portfolio decisions. Increasingly, companies with greater cyclicality appear oversold relative to our assessment of the risks, while we find the valuations of a few defensively positioned companies are no longer as compelling following recent gains. Should these relative valuation disparities deepen, we have identified several candidates towards which we would invest additional capital to opportunistically increase the portfolio's risk-adjusted expected return.

DISCLOSURES

The Foyston, Gordon & Payne Inc. (FGP) performance figures and portfolio statistics shown in this report are for the FGP Pooled Funds. Client returns may vary due to cash flow timing and client-specific constraints.

Investment returns and assets under management are expressed in Canadian dollars unless otherwise noted. Investment returns are gross of investment management fees, net of fund expenses for FGP Pooled Funds, and include reinvestment of dividends and income. Returns are time weighted and annualized for periods greater than one year. Values change frequently and past investment performance may not be repeated.

These views are subject to change at any time based upon market or other conditions and are current as of March 31, 2025.

Forecasting represents predictions of market prices and/or volume patterns utilizing varying analytical data. It is not a guarantee of the performance of the stock market, or of any specific investment.

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