Qube Quarterly

2015: Q3

Who Doesn't Love a Good Scandal?

There are Lessons Here to Be Learned.

Qube Investment Management Inc.

Free of influence from bank, brokerage, and securities dealers, Qube is one of the few truly independent investment management firms in Western Canada.

Our only agenda is to take care of you while managing and expanding your wealth.

We believe that when clients place their trust in portfolio managers, they deserve, in return, transparency. By publishing this quarterly activity report and engaging in personalized account reviews, we want to give you insight into how we think about investing and what we are doing with your investments.

Proper stewardship of your investments also means managing portfolio risk by incorporating responsible investing principles into all aspects of our work. Therefore, we continue to act on your behalf to demand the best from management in the companies you own.

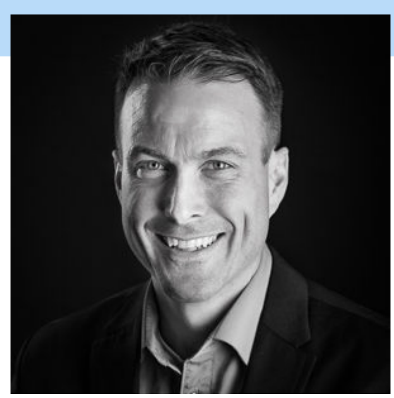
Much can be gained from tax and retirement modeling. We remain ready to assist all clients with planning services to ensure you minimize taxes and maximize your after-tax returns.

You work hard for your money – so we will, too.

Ian Quigley, MBA

Qube Investment Management Inc. is a registered portfolio management firm in the provinces of Alberta and British Columbia.

We are proud to serve you from our offices headquartered in Edmonton!



Greetings from the Editor

Contributing Writers:

Ian Quigley, MBA

Patrick Choi, B.Com

Quarter 3: 2015

Our low oil environment persists. While this has taken the wind out of the Canadian economy, it should (eventually) assist in stimulating a sluggish international region. China's slowdown has proven a larger challenge than first anticipated, while Europe continues to disappoint with poor economic results. In the meantime, Canada dropped interest rates, while US stocks continue to post positive earnings thanks to a strong US economy. 2015 continues to be the rerun story of a global economy flying on a US engine. I continue to wait for good economic news outside of the USA.

This summer at Qube we said goodbye to Arden Tse while welcoming a number of new faces to our team. I look forward to sharing comments from Christopher Pu, who joined us this month on a part-time research basis. Chris has a Master of Science in Biochemistry & Molecular Biology from UBC, is a Level 3 candidate in the CFA program and a part-time student in the University of Alberta's MBA program. Also joining our research team part-time is German Martinez (GeGe). GeGe brings a Master of Arts degree in Economics from the Philippines and is currently a full-time student in the U of A MBA program and a Level 2 candidate in the CFA program.

Anya Tonkonogy has officially changed her role with Qube, joining Qube Investment Management Inc. in a full-time client relations and business development position. We are very excited to have her helping our investment clients in the year ahead!

This quarter's theme is "Lessons Learned," with our lead article talking about the VW debacle and the importance of governance research in the investment decision process. We hope it's informative for you, and as always, we invite your comments and questions!

Ian Quigley, MBA

Kaleo: to call, summon, or invite...
Our invitation to you, to invest with us

At September 30, 2015

	YTD	2014	2013	2012	Since Inception (Jan 2011)
KALEO A	**3.0%**	**20.7%**	**33.7%**	**12.2%**	**14.3%**
KALEO B	**4.6%**	**17.9%**	**33.4%**	**9.3%**	**13.5%**
KALEO FULL	**3.5%**	**22.0%**	**35.0%**	**12.6%**	**14.5%**
S&P 500 (US Benchmark)	8.9%	24.0%	41.5%	13.5%	18.6%
S&P TSX (Canadian Benchmark)	-7.1%	10.9%	12.7%	7.2%	2.7%
50% TSX / 50% S&P 500 (KALEO BENCHMARK)	0.9%	17.5%	27.1%	10.3%	10.7%

Kaleo is Qube's stock model, which is offered as follows:

Kaleo Full – currently a 43 stock + 2 index ETF model offered to clients with $1M+ positions

For clients with positions between $250,000 to $1M, we offer two subsets of the Kaleo Full model:

Kaleo A – currently a 24 stock + 2 index ETF model

Kaleo B – currently a 24 stock + 2 index ETF model

Our model portfolios were launched in January of 2011. They continue to report a lower risk metric (beta) and generate a superior return when compared to our performance benchmark of 50% of the TSX (CAN) & 50% of the S&P 500 (US) indexes.

We currently aim to hold a stock for 3-5 years in our Kaleo models. This means we have an average portfolio turnover of 25%. In other words, a quarter of our positions change each year on average. One goal with Kaleo is to generate income through dividends. An investor entering Kaleo at inception would have a dividend yield today of over 3.5%. Many of the companies in our portfolio increase their dividends each year, so an investor can therefore grow his or her dividend over time. An investor entering Kaleo today would see a starting dividend yield of about 2.0%.

In the management of our Kaleo model, we use both company specific / fundamental analysis and macroeconomics to determine our positions (what to buy/sell).

Our research universe refreshes each year and we currently track between 150 and 200 companies. To learn more about our investment philosophy, please see our investing brochure at www.qubeconsulting.ca.

Also, please read our disclaimers on the back page of this newsletter.

Kaleo at a Glance

Patrick Choi
Ian Quigley, MBA

The VW Scandal: Lessons to Be Learned.

Ian Quigley, MBA

Stalin wanted it first, but failed, largely because of the language barrier. Hitler tried in 1934 and was successful. Designed by Ferdinand Porsche, Germany got its car for the masses, the VW Beetle. Russia got the Lada (and nobody cares who designed it).

The Porsche clan has maintained a long integrated history with VW, with Ferdinand's son-in-law Anton Piëch managing the original VW plant in 1941. Anton's son, Ferdinand Piëch, was the chairman of VW from 1993 until his resignation in 2015. Despite being a public company, investors were never fully informed about why he resigned. Rumors centered on trouble between him and the CEO at the time. To some, Piëch was a saint and the savior of VW from prior financial hardships. To others, he was simply the highest paid, most entitled auto executive in Europe.

To the Porsche family, VW has always been their own. In their eyes, it did not belong to the people of Germany, who privatized the company in the 1960s, or to the pension funds who invested in it, or to the general public who bought its shares on the German stock exchange. VW's legacy is the Porsche legacy. Since privatization, they patiently and stealthily accumulated additional shares. Then in 2008, with the help of the Qatar Sovereign Wealth Fund and some complicated and sneaky legal maneuvers, they took the controlling interest.

Outside of the Porsche clan, Qatar, German institutional investors and the State of Saxony (in Germany), less than 10% of the company is available for outside investors.

Today VW is a $45 Billion dollar company with over $200 Billion in annual revenue, and is the second-largest automaker in the world next to Toyota. This has been a problem for the Porsche family. If they could simply increase an already small market share in the USA, they could then claim first place and become the largest automaker in the world. Global domination: for the Porsche family, a righteous destiny.

Scandal 2015

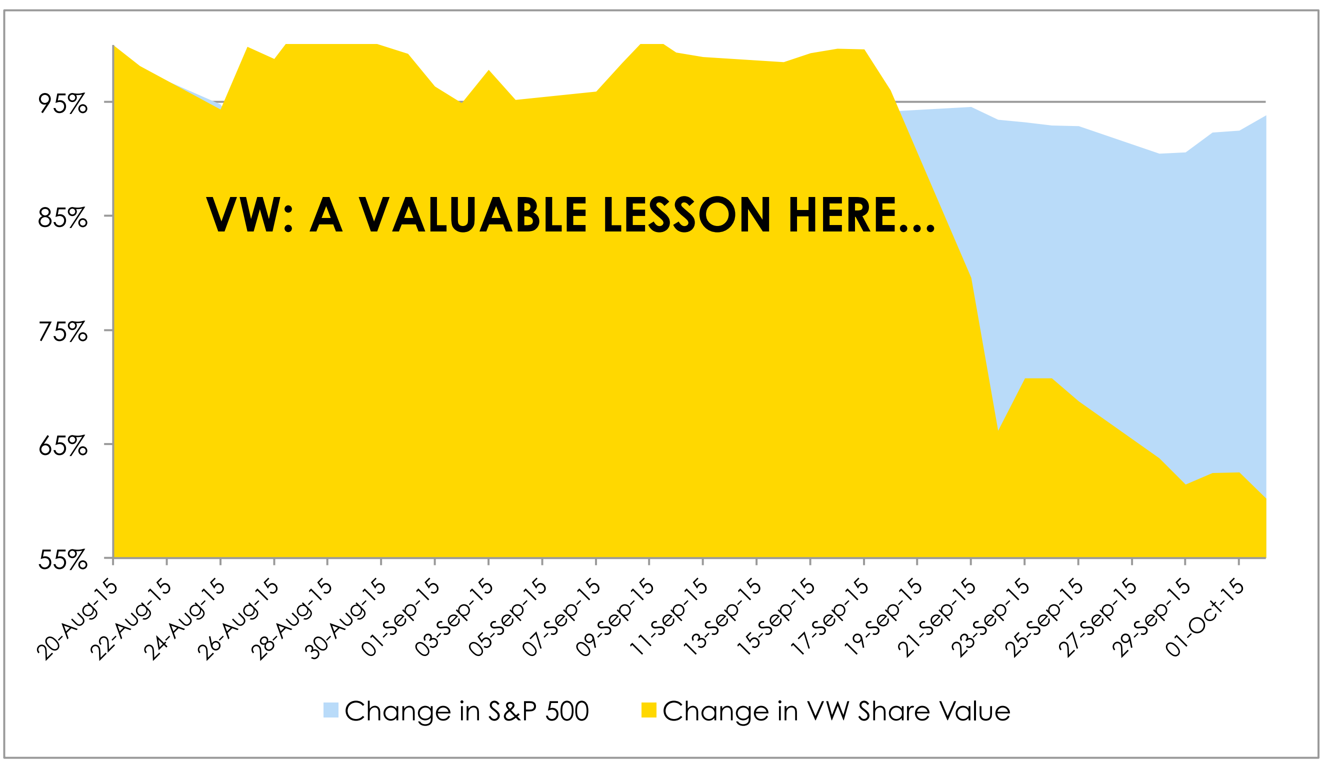
A previous VW scandal in 2008 included secret brothels, bracers and bribes, and as juicy as that sounds, the 2015 scandal is even better. VW employees created secret software that ran on millions of its diesel-engine cars that would change the emissions profile while American regulators were busy measuring them. Under normal operating conditions, the cars are actually mini-environmental disasters, emitting up to 40 times the NO_x limits measured by regulators. American emission standards are

higher than in Europe (largely to offset the higher population of pickup trucks), making it difficult for even the best of diesel makers (Honda and Mazda).

Who would believe such an allegation, made on September 18th from America's Environmental Protection Agency (EPA), that VW's onboard software would monitor and switch on special NO_x-controlling software only when the regulators were driving? The EPA was confident enough to immediately order a recall on 500,000 cars and subsequently, on Sept 22nd, VW admitted over 11,000,000 cars were using the regulator-tricking software.

Almost overnight, the company's shares collapsed by a third (see chart), losing nearly $15,000,000,000 of value to its shareholders (that's 15 billion). On the basis of 482,000 cars sold and a maximum fine of $37,500 per vehicle under the Clean Air Act, the Department of Justice could fine VW $18 billion, which is unlikely based on other similar cases. On top of this, VW faces billions in fines elsewhere and other financial penalties related to civil lawsuits. Add in VW's ruined reputation, which, according to Kevin Plank (CEO of Under Armour), is gained in drops but lost in buckets. Reputational damage will take years to rebuild.

Yes, the big boss Martin Winterkorn has resigned, a traditional solution to a systemic problem. A systemic issue, because it would take many, many people inside VW to enact a tactic like this. Sadly, the problem here runs deeper, down to the owners who elect the board of directors that monitor, govern and prevent "management-gone-wild" scenarios. One can argue that the buck stops with ownership; owners direct how they want the corporation to be run.



The good news is that few investors actually own VW. There are less than 9% of VW shares on the open market and Qube does not have a position in VW in any of its models. The bad news is that companies like VW are far too common. VW is controlled today by what many consider its founding family (the Porshce / Piëch dynasty). This family has been ranked the 8th wealthiest in the world, and are not motivated by the same things that we are. They are not interested in benign middle class dreams like maximization of shareholder value. They will aim for global domination and have no qualms about risking our shared value in their quest.

Governance is the Engine

Governance at VW has checks and balances uncommon to American companies. For example, German law requires an 80% vote for all major decisions and operates under a special system of co-determination (worker rights). This is why, in 2008, a scandal broke. The *Guardian* newspaper broke the story on sleazy activities of VW involving bribes, free Viagra and sex workers. CEO Ferdinand Piëch was unresponsive to external investors, uncommunicative about product development and strategy and unapologetic when examined in court about methods used to recover ailing employee relations.

Piëch (grandson of Porsche's founder) was the second largest shareholder in Porsche, and also sat on the boards of **both** companies while at the helm of VW. In theory, these companies were competing for market share. Instead, analysts found billion dollar emergency loans between the companies during tight times. How would you feel if the company you invested in was making risky billion dollar loans to a competitor without your consent?

Businessweek has called the rule under Piëch a "virtual autocracy." In 2002, he reached mandatory CEO retirement at the age of 65, but remained as Chairman and retained his "dictatorial power." In 2012, Piëch appointed his spouse (a former kindergarten teacher) to the board - a board appointment not designed to protect shareholder value, but to strengthen and demonstrate family control.

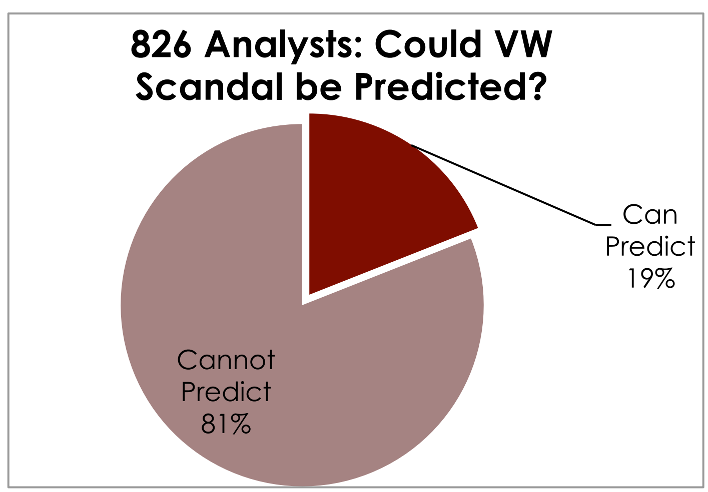
Is There a Lesson Here?

A survey of CFA Institute *Financial NewsBrief* members asked if the share decline at VW could have been anticipated through analysis of the company's governance and internal controls. The answer: 81% of 826 respondents said no.

Why? The majority of analysts ascertain that decisions are based on public information. As VW used deception, the scandal was therefore not something that could be predicted.

Qube Passionately Disagrees

Governance failures at VW have been within the public domain for years, including a major expose in 2009 revealed in articles from the *Financial Times*. While spotting the exact manifestation is impossible, considering the risk in human capital management is entirely possible. The VW history of ignoring outside views and disregarding classic external controls, while affording the temptation for boundless self-



gratification was toxic and present for all to see.

If you invest in VW, you are not investing in a global blue-chip automaker; you are investing in the Porsche/Piëch family, Porsche/Piëche ambitions and Porsche/Piëche values. You cannot rely on spreadsheets, mathematics and classic business analysis, but must consider the unrestrained and unaccountable human capital leading the organization. Qube has always shied away from such situations, but sadly admit a negative screen on shares, unduly influenced by founding families, would be too restrictive on any investment model.

According to research by the consulting firm McKinsey & Co., family-controlled firms made up 19% of the Fortune Global 500 in 2014. They define family firms as companies whose founding families have the biggest stake, at least 18%, plus the power to appoint the chief executive. By 2025 McKinsey forecasts there will be more than 15,000 companies worldwide, with at least $1 billion in annual revenues, of which 37% will be emerging-market family firms.

Approximately 85% of $1 Billion-plus businesses in South-East Asia are family-run, along with around 75% in Latin America, 67% in India and almost 65% in the Middle East.

While shy of such firms, Qube has taken positions over time in Nike, Loblaw, IGM Financial, Nordstrom, Microsoft, Talisman and Yahoo, all considered to be subject to founder influences. These investment positions required extra attention to ensure the cost/benefits of the founder influence were understood and included in the decision.

What Lessons Are Learned?

Governance research is not a waste of time and effort. VW shares have plunged by a third in value from this scandal, an event that demonstrates a misguided corporate culture where deception of a regulator was institutionalized throughout the entire company. We can reduce this type of risk by continuing to include governance in our investment decisions. At Qube, Brenda Wilber and Stacey Quigley perform regular analysis on each company in our portfolio, calculating an associated ESG (Environmental, Social and Governance) Score which impact our interest in holding the shares.

Further, Qube has participated in four United Nations PRI (Principles of Responsible Investment) engagement committees: Steering Committee, Director Nomination, Responsible Fracking and Labour Standards in the Supply Chain. By collaborating with other portfolio managers, we have promoted higher levels of corporate responsibility that will benefit all investors.

Finally, Qube plans to be active again in 2016 with submissions of proposals to the boards of companies we have positions in during the season of annual shareholder meetings. Our focus, as in 2013/14, is on governance.

We continue to believe that it is our duty to promote better governance, and in fact an important risk management technique to avoid holding investments where scandals can wipe away massive share values overnight.

Qube plans to register shareholder proposals for the upcoming AGM season on the topics of Board Refreshment, Standards of Director Independence and Auditor Rotation.

While we paused this work in 2014, in 2013 we were the third most active investor for such proposals In North America.

A Canadian Pension Crisis?
For some…

Ian Quigley, MBA

Introduction

2008 brought one of the sharpest declines in stock market values ever seen in the 200-year history of North American equity markets. This particular downturn also spurred a new round of analysis on the adequacy of the Canadian retirement system, addressing a growing concern that what we are dealing with is a "Pension Crisis". In 2014, over 60% of Canadians surveyed reported retirement income stress as a top financial concern. The average Canadian retirement age crept up from age 61 in 1997 to age 63 in 2013, and anxiety could also be driving recent rounds of government program cutbacks, implying challenges at the core of our retirement system. The age of eligibility of the Old Age Security/Guaranteed Income Supplement (OAS/GIS) will increase form age 65 to 67 (between 2023 and 2029), and the Canada Pension Plan will soon make an early retirement less palatable. Compounding such issues are Canada's aging population of baby boomers: those over the age of 65 will increase from 15% to 23% by 2035. For those worried about a retirement system under stress, this evidence appears to indicate a challenging future ahead.

Not everyone sees this stress, however; not all Canadians are worried about our retirement system. Numerous studies and papers have been published that inform us that the system is okay, and not in crisis. These investigations propose that over 80% of Canadian households are well prepared for retirement, and that we have a 'perception gap', not a 'funding gap' to deal with. We have misunderstood relevant elements prior to retirement, while overestimating our consumption needs during retirement; perhaps we are more adaptive than accounted for.

Experts drive policy, and policy impacts the taxpayer. If policy makers decide there is a crisis, much can change in the years to come. When it comes to our retirement system, the experts are divided, and the dialogue on both sides is impassioned

Are Canadians Saving Enough?

This is a critical question: if there is a pension crisis coming, Canada will have increasing proportions of senior citizens struggling with poverty (and straining the social fabric of society). If there is a pension crisis coming even though we live in one of the safest and wealthiest countries in the world, it potentially becomes a place that cannot secure food, shelter and clothing for its aging citizens.

This is also a question that is difficult to answer, as it encompasses complex assumptions about increased life expectancy, future investment returns, salary growth, future expenditures and taxes. Nonetheless, numerous working groups, actuarial studies and task forces have looked at this issue since 2008.

Interprovincial Working Group in Retirement Income Adequacy (2009)

Each jurisdiction in Canada (provincial/territorial) is responsible for its own pension and retirement income policy and there were a number of task forces commissioned prior to 2008. However, the 2009 Federal-Provincial-Territorial Ministers of Finance Steering Committee was the most comprehensive seen in many years, and was led by Jack Mintz, a professor and public policy expert.

> *While 80% of Canadians are well prepared for retirement, 20% are not; this demographic is specific to non-unionized, moderate to middle income workers. The number of these people unprepared to retire is expected to grossly increase in coming years.*

According to Mintz's 2009 study (remembering that the data set is complicated), he found that Canadians are saving less today than they did 25 years ago. More complexity was added when Canadian housing markets appreciated rapidly in recent decades and Canadians became more comfortable with stock market investing. Retirement models tend to ignore mortgage payments in the savings rate and do not contemplate the capital gains realized from investment portfolios. Today, homes have become a larger store of wealth than they were 25 years ago, and far more Canadians hold stock portfolios than ever before.

Mintz's work proposed a pension crisis within a specific subset of Canadians. Both lower and upper income Canadians were found to be in good shape; it was the modest income earners and middle class who were found to have challenges. Within this group, it was only those who do not have defined benefit pension plans offered by their employer, who were at greatest risk, and this is a growing group of workers that represent one-fifth of all Canadians.

Organization of Economic Co-Operation and Development (OECD)

According to a 2013 OECD study, Canadian seniors over age 65 are able to generate, on average, 93.3% of the average income of the general population, using the average taxable income in 2013 of $31,690/annum. Further, the poverty rate of seniors in Canada (2010) was recorded at 7.2% while the poverty rate of the general population was 11.9%. These are good statistics, and they rank Canada in the top half of the G20, but the percentages have slipped since last measured by the OECD in 2007. At that time, the poverty rate amongst seniors was at 5.0%. This slide has pushed Canada from 5th to 11th place in the G20 in three short years, and occurred even after the dramatic improvements seen since 1970, when nearly 30% of seniors in Canada had income below Statistic Canada's after-tax low-income cut-off. One cannot help but worry about the reversal in trend.

Statistics Canada: Recent Analytical Papers

Statistics Canada devotes time to track the welfare of Canadians in retirement with regularly published papers on the subject. A significant paper published in 2008 by Sebastian LaRochelle-Cote determined that Canadians were doing fine in retirement, and that much of the negative data published on slipping replacement ratios (the ratio of retirement to pre-retirement income) was potentially misplaced. For example, slipping ratios could be related to increasing ownership of real estate (not factored into the equation), or the impact of double income households and their ability to retire on much less than peak pre-retirement income. However, the study also identified a large number of Canadians who were found to have inadequate savings. Consistent with the Mintz findings, these people could be identified based on moderate or middle-income levels and their access to an RPP (Registered Pension Plan) offered by an employer.

In an expanded 2010 study, LaRochelle-Cote reaffirmed the work from 2008, including slippage in the middle/moderate income demographic. The researchers found that 20% of this demographic were unable to achieve better than 60% replacement ratio at retirement, a troubling statistic that would likely cause standard of living reductions. Outside of this middle income demographic, the finances of Canadian retirees were found to be healthy.

In 2012, the same authors at Statistics Canada re-did the study to include real estate as a financial asset available for the generation of retirement income. This study was able to reaffirm earlier findings that retired Canadians are generally in good shape; however, it did conclude with a caution about baby-boomers. Younger baby-boomers have yet to retire and might exhibit different savings and investing habits than their predecessors; therefore, historical trends may not be as stable as many would hope.

K.D. Moore, from the C.D. Howe Institute, also used a simulation tool developed by Statistics Canada in 2012, to determine how many households fail to keep a similar standard of living in retirement. This study affirmed the other modern reports, stating that today, 17% of Canadian households fail to meet basic retirement transitions. Extending from the present, this study then projected the transition problem, increasing to as high as 44% of the moderate/middle income population in the coming decades.

The Australian Solution

According to an article in the *Canadian Tax Journal* in 2009, when employees are automatically enrolled in a retirement plan, but given the choice to opt out, participation rates are much higher than when the employee must choose to participate, sometimes jumping from 49% to 86% (Horner 2009). Research suggests that auto-enrollment could be more effective than employer contribution matching – a surprising finding, to say the least.

Australia underwent a pension reform in 1992 that many in Canada today wish to adopt, including the Fraser Institute. Australia installed a mandatory "RRSP-like" program, where enrollment is required and employer contributions mandatory. Employers must contribute a minimum of 9% of an employee's gross earnings up to a maximum threshold (rising to 12% by 2019-20). Contributions are placed into an individual account that is privately managed by the employee; they are restricted to conservative asset allocations and investment strategies. There is also flexibility to withdraw funds from the accounts prior to retirement for medical emergencies or financial hardship, and any balance in the accounts can be transferred to a dependent tax-free at death. Investment income is taxable, but withdrawals are tax-free after age 60. This approach is expected to hit replacement ratios of 90% for middle-income wage earners by age 67.

In the United Kingdom, the Turner Commission looked at various approaches to expand retirement savings and recommended automatic enrollment (also with the choice to opt out). They found 74% support for this option, where the default participation rate contributes 4% from employees pay (when they earn middle-income wages), and is matched with 3% of pay from the employer. This has yet to become legislated, but is expected.

The Ontario Solution (ORPP)

In August of 2015, the Premier of Ontario announced details on the pending design and implementation of a new Ontario Retirement Pension Plan (ORPP), with a projected start date of January 2017. This is a major development in the Canadian retirement system, as the ORPP will not be optional but mandatory for some employers. Those who do not offer a workplace pension or retirement plan meeting minimum quality standards will be required to enroll in the ORPP. Enrollment and contribution levels will be phased in, reaching 1.9% for each employer and employee by 2021. It appears that employees will be able to submit paperwork to exit such a program, but automatic enrollment remains a key feature in the plan design. If implemented in 2017, it is very likely that other provinces will consider following Ontario's lead with similar programs.

Qube's Solution: Call Us!

The tools have been created, and the facilities exist: we need to ensure employees make regular use of them. If you are a client, or a prospective group savings client, we would like to share our ideas on how to break employee apathy and change the inertia. This includes a mix of employee education and one-on-one engagement that motivate and work towards a future where retirement crisis is reduced, at least on your shop floor.

TRADES UNDER REVIEW
Buy

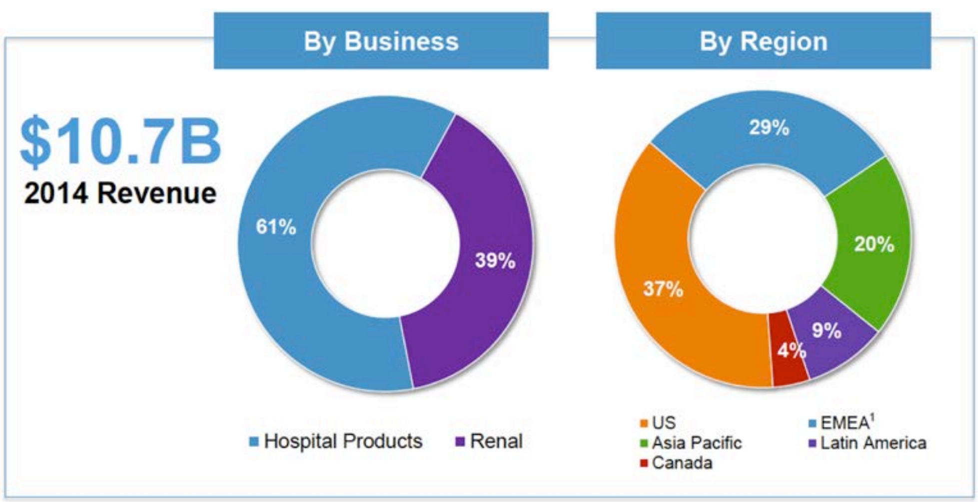
Focused Growth

Patrick Choi

On July 1, 2015, Baxter International (a company held in both Kaleo A & Kaleo Full) successfully spun off their bio-pharmaceuticals business into a company named Baxalta, which we now also hold in our Kaleo A & Kaleo Full model. Due to the spinoff, shareholders received half the original value in the new Baxter shares and the other half in Baxalta shares. In the coming weeks, we will be looking at increasing our holdings of Baxter & Baxalta into full positions in our Kaleo A & Kaleo Full model.

BAXTER:

Following the separation, Baxter will have a broad global footprint built around fluid systems, renal therapies, parenteral nutrition, inhalation anesthetics and bio-surgery products. The focus will be on developing new and healthier solutions in hospitals, in-center, and home based therapies. Of particular note is that Baxter continues to retain a 19.5% ownership stake in Baxalta, which is currently worth approximately $4.2B.



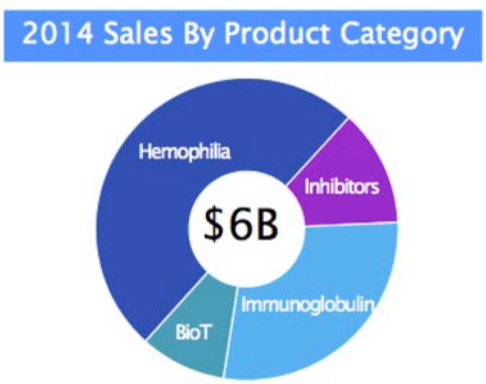
We are planning to pursue a full position in Baxter due to the following reasons:

1) Baxter has strong brand recognition with more than 70% of sales in market-leading positions. This will be important when Baxter markets new products, captures future growth through the rise in funding for medical care in emerging markets and also through the aging population of more developed economies.

2) Much of the underperformance for the core Baxter portfolio had to do with management. With factors such as the spinoff of Baxalta, the focus on margin improvements, a new CEO in 2016, and greater outside pressure from activist Dan Loeb, we believe Baxter can achieve financial performance that is at least similar to peers like Becton Dickinson. If financial performance can be improved in the next few years, then our calculated P/E multiple of 21.3 looks to be cheap when compared to better run peers like Medtronic at 31 P/E and Becton Dickinson at 32 P/E.

BAXALTA:

Following the spinoff, Baxalta will become a leading provider of therapeutic treatments focused on rare conditions, chronic diseases or limited treatment options. Their focus is on transformational, targeted therapies for patients with limited treatment options. Currently, their products are based around bleeding disorders (hematology) and immunology, but is expanding to meet unmet medical needs in niche areas of oncology (cancer), as well as technology platforms such as gene therapy (using genes to treat or prevent disease e.g. inserting a gene into a patient's cells instead of using drugs or surgery).



We believe there are 2 ways to win in a full position investment of Baxalta:

1) Baxalta seems to be undervalued on a P/E basis when compared to other large cap, biopharmaceutical companies like Biogen, Amgen and Celgene. If Baxalta continues to show organic growth as per our analysis, then we believe the share price should increase to reflect both margin expansion (to be more inline with peers), and revenue/earnings growth.
2) There has recently been an explosion in M&A activity surrounding pharmaceutical, medical and biotech industries. Companies like Teva, Allergan, and Valeant have become common Wall Street headlines, announcing one acquisition after another. We believe Baxalta to be one of the prime targets for these acquisitions, as evidenced by Shire's offer to buy Baxalta for an equivalent price of $45.23, which was (and still is) a substantial premium to its current price. While this particular deal seems to have fallen off the table, it serves to highlight the undervaluation of Baxalta, and the potential for similar M&A deals in the future.

TRADES UNDER REVIEW

Sell

Trading Up for Growth

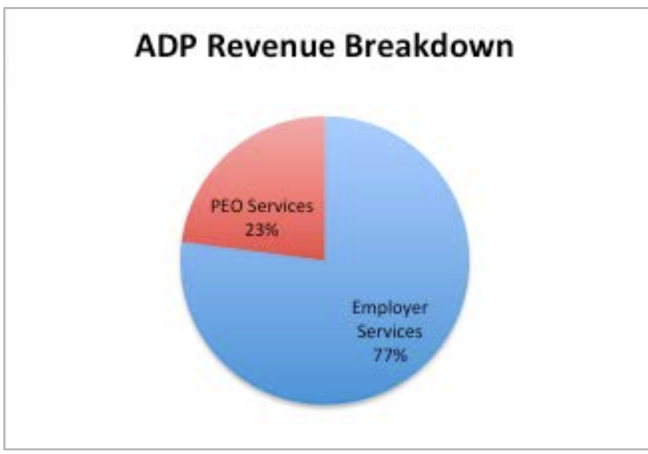
Patrick Choi

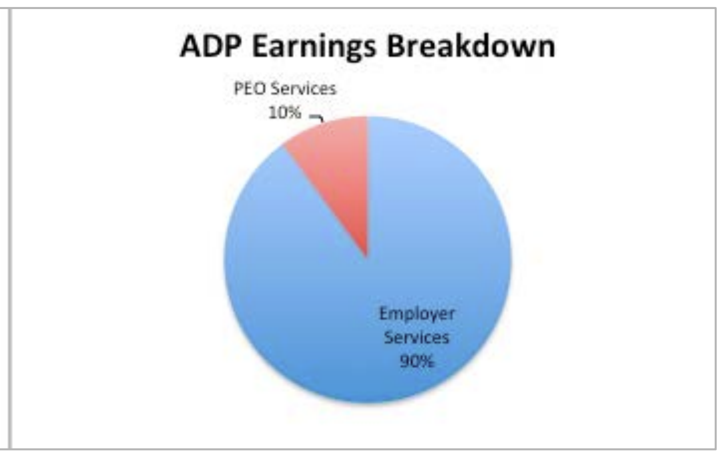
ADP is an American business that focuses on Human Capital Management (HCM), which includes recruitment, talent management, payroll and retirement services. Their business is split into 2 parts: Employer Services (HR management tools, including payroll) and Professional Employer Organization Services (HR management and benefits administration). ADP was founded in 1949, has over 60,000 employees and annual revenue of over $10B.

By far, ADP's revenues and earnings are concentrated in Employer Services, where their solutions are being sold in more than 100 countries. The most material is in the US, Canada and Europe, with the primary components being payroll and time and attendance management.

Due to ADP's brand, global presence and comprehensive offerings, ADP has a very large client base of 630,000, with a historical retention rate of approximately 12 years on their Employer Services segment.

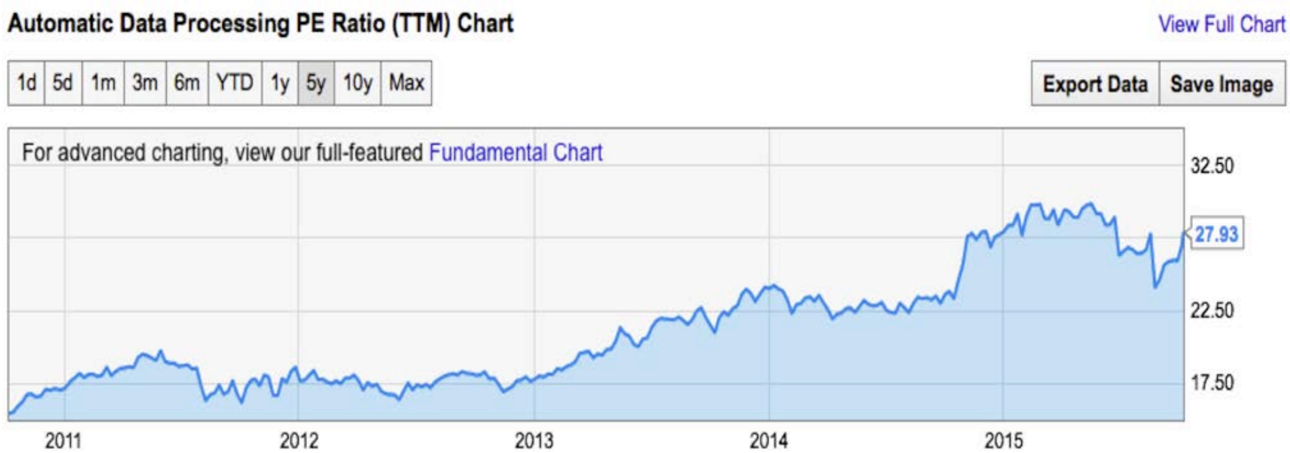
Why Sell ADP?





Despite the many great aspects of ADP as an investment, we feel there are three particular risks, which, when taken together, outweigh the positives at this time.

1) **Valuations.** ADP is no longer low-priced. From our quantitative analysis, we believe ADP is only fairly valued. On a P/E basis, ADP is near its 5-year top (as with most stocks) and is trading at a P/E of 28, which is now far above the market of 17.



2) **Leverage.** ADP has always been a highly leveraged business due to the consistency of their business model. Recently, ADP has expanded their leverage (Assets/Equity) from approximately five in 2012 to seven in 2015. On August 28, 2015, ADP announced plans to initiate a $2B debt offering with most of the proceeds used to buyback stock. Keeping everything else constant, this would increase ADP's leverage to about 12. Putting it another way, $30B of ADP's assets will be funded by debt, with $3B of equity left over. If something "bad" were to happen to ADP, shareholders of a $40B company would be fighting over the $3B left after debts are paid. In other words, we feel that the use of leverage has become excessive.

McDonald's Announces It's Answer to $15 an Hour Minimum Wage
Self-Service kiosks–

3) **Competition.** Due to the emergence of the "cloud", ADP is currently facing competition from both smaller and more established rivals. Cloud technology has enabled companies to compete against the entrenched ADP by eroding the efficiencies and synergies gained from ADP's focused operations. In the Human Capital Management space, ADP's competitors now include Ceridian, Oracle, Microsoft, Salesforce, Workday, Paycom, Paylocity, among others. In addition to the squeeze from competitors, there may also be a long-term risk at the top due to automation. We are already seeing this trend in the low-end jobs segment, with cashiers at grocery stores and fast food workers. It is possible that the unique automation once offered by ADP could be "insourced," eliminating the company from the value chain, similar to what has happened with tax filing. Fewer individuals today use an accountant to file personal taxes than ever before. Could this happen to ADP as well?

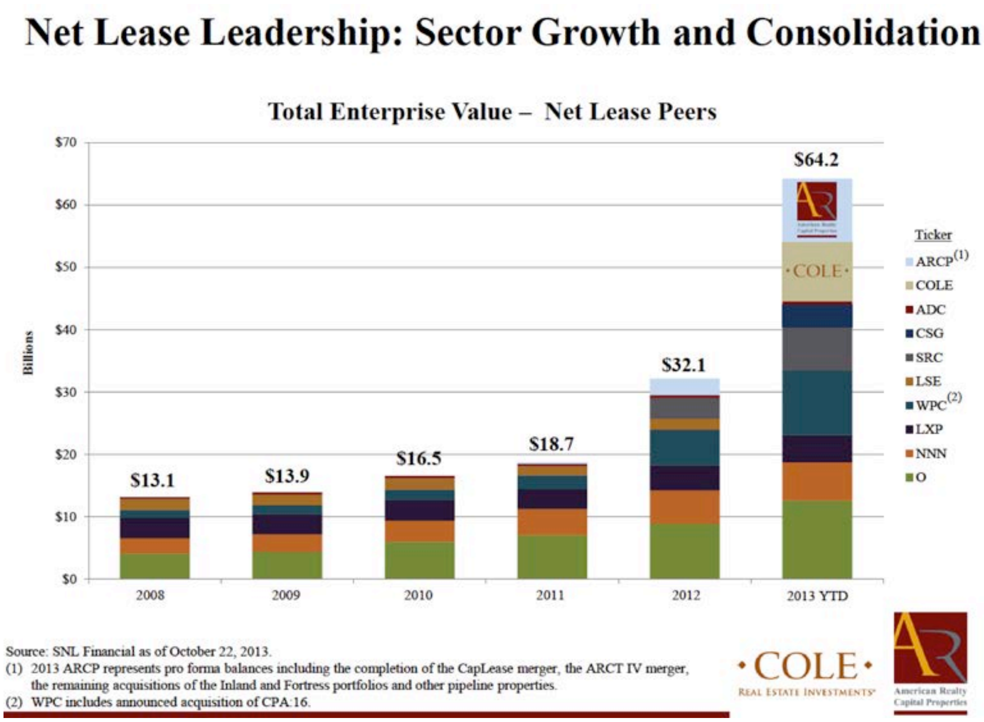
TRADES UNDER REVIEW

BUY

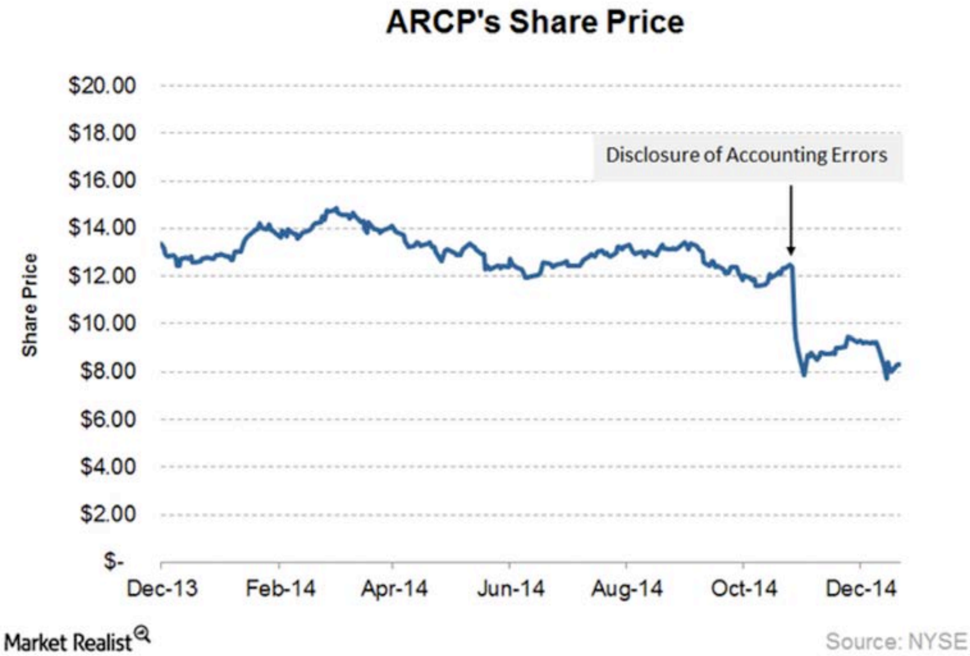
Trading Up for Growth

Patrick Choi

Value investing requires digging, the excavating of numerous situations in an attempt to uncover potential investment opportunities. VEREIT is an excellent example of a find. VEREIT is a Real Estate Investment Trust, trading on the New York Stock Exchange, that has a market capitalization of $7.5B while offering a 6.7% dividend yield. Why? Prior to July 28th, VEREIT was known as American Realty Capital Properties (ARCP). At its height, at was a $22B enterprise-valued REIT that made up approximately 1/3 of the net lease market and was headed by Nicholas Schorsch, one of the most influential real estate personalities in America.



This all changed in late October 2014, when the company disclosed it had overstated "Adjusted Funds From Operations (AFFO)", which effectively wiped out 1/5 of ARCP's share price. Since then, VEREIT (ARCP) has languished in this post scandal trading range of about $8/share.



Why VEREIT?

Our thesis on VEREIT is based on valuations. Being a real estate company, valuations should be more concrete than on other types of companies. The assets held are tangible. They are made of brick and mortar.

Before we go through the numbers, we must be able to trust VEREIT's financial statements, especially in light of the recent accounting scandal. Following the fallout and with the eyes of the SEC and FBI watching, ARCP hired independent advisors, including Ernst & Young LLP, to conduct a thorough and independent investigation into their books. After the audit, the investigation revealed that there were no material changes related to ARCP's real estate ownership and value of the properties. In other words, the value of the properties stated were indeed the true value.

Using the re-audited financials, we find that the book value of the company (net of debt) is worth approximately $9.2B, while the current market value of the stock is $7.2B. This equates to a Price-to-Book of 0.78. Theoretically, today VER is worth more liquidated than operating as a company collecting rent. We believe this is a ridiculous assumption, as VEREIT has almost full occupancy (98.4%) with well-known (and well-capitalized) tenants like Red Lobster, CVS, Walgreens, Family Dollar, Dollar General, FedEx, Amazon, among many others. If VER can trade at a Price-to-Book multiple of only 1.0 (relative peers trade at an average of 1.5), that would represent a 28% upside in the share price.

Key to our decision has been recent moves by the new management team to deal with abnormal debt obligations maturing in 2016 and 2017. They have reduced the earnings payout from a traditional 80-90% level back to 64%, recycling cash into debt payments. Further, they have agreed to sell some joint venture properties to generate additional "delevering" cash.

Combining the favorable valuations with a completely new management team (CEO, CFO, COO, and Chairman, among others, were all replaced), re-audited financials, re-instated dividends (6.8% yield), and a re-formulated business plan, we believe this is an opportunity to buy into a stock that has a "bond-like risk, for an equity-like return".

QUBE INSIGHTS: Kaleo Holdings

Patrick Choi
Ian Quigley, MBA

Kaleo Full, A

Deere & Co.: John Deere is one of those rare brands that can immediately jog your memory of their product; in this case, an image of a green and yellow tractor. In addition to that ubiquitous tractor, Deere & Co. also operates broadly across the agriculture, turf, construction, forestry and financial segments. Despite the drop in farm stocks, we believe this company remains a hold for the following reasons:

1) **Brand Name:** John Deere was born in 1876, and their yellow and green corporate logo featuring a leaping deer represents one of the oldest and best-known brands in the business world. Deere & Co. is currently ranked #70 in Forbes' "World's Most Valuable Brands".
2) **Economic Fundamentals:** The agricultural market is cyclical, and despite being in the downturn of a cycle, economic fundamentals for the agricultural business remain strong. The amount of arable land is limited, while the demand for food is rising due to population growth and rapid industrialization in emerging markets. This should translate into the need for better machinery to help farmers become more productive.
3) **Valuations:** As of this writing, the company is trading at 12 times earnings, while the S&P 500 index is trading at 17. We believe this to be temporary, and the multiple will start to reverse itself once the agricultural business cycle turns upwards again.

"The No.1 thing people think of when they hear 'John Deere' is the color green. But some people, like in the urban areas, don't understand the strength of the color green or red. Farm families grow up with these different brands and the color is important. It's what they identify with." – Barry Nelson, manager of media relations for John Deere.

"It's share of mind, not share of market that counts." – Warren Buffett

Kaleo Full, B

The Walt Disney Company: Named after its founder Walter Disney in 1923, Disney is currently the 2nd largest media conglomerate in terms of revenue after Comcast, with operations in media networks (ESPN), theme parks, studio entertainment (movie segment), and consumer products. Since Bob Iger took the reins of CEO in 2005, he has transformed the company into one that places heavy emphasis on "brands". This includes acquiring new brands such as Marvel and Star Wars, as well as developing existing ones like Frozen in their "Princess" segment. We believe it is these brands that will help Disney transcend any kind of change in technology, and help fuel future growth for the company. To be sure, there are risks in our investment here, the greatest of which being ESPN and "cord cutting." We believe the conclusion is still up in the air, and will be monitoring the company closely to see how Bob Iger responds to this growing threat.

Vasily Karasyov (Analyst at Sterne Agee): "You mentioned that you now have three $1 billion franchise properties in consumer products revenue. I think I know two of them, Princess and Star Wars. Do you mind telling me what the third one is?"

Bob Iger (CEO of Disney): "The third one is followed by five others and we have eight. Pooh, Mickey Mouse, Monsters, Star Wars, Spider-Man, Cars, Disney Junior, and Princess ... And all over $1 billion in global retail sales in fiscal 2014."

(Q3 2014, The Walt Disney Company Earnings Conference Call, August 5, 2014)

QUBE INSIGHTS: Equity Research Snapshots

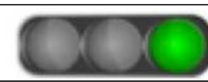
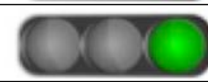
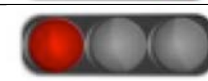
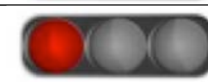
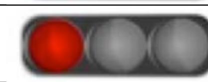
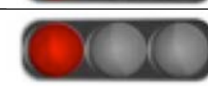
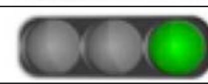
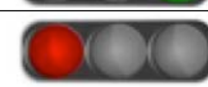
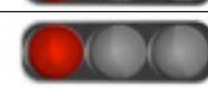
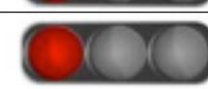
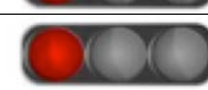
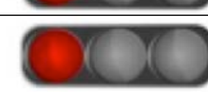
Patrick Choi
Ian Quigley, MBA

Our equity research is guided by a proven value-based approach pioneered by Benjamin Graham. Balancing traditional research techniques with modern portfolio science allows our team to find companies that demonstrate and maintain solid investing fundamentals. We look for less volatile and proven earnings combined with long-standing stable dividend policies. Share prices need to be justified on a combination of current earnings and reasonable earnings growth possibilities. Quality financial statements, coherent management and an operational business plan need to be in place before we rank a company “green”.

Do not hold

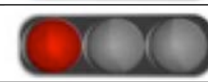
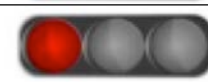
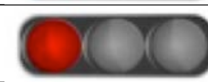
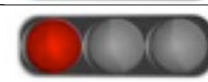
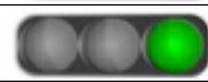
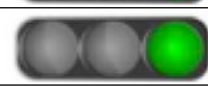
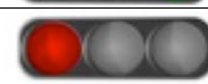
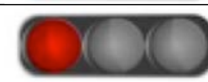
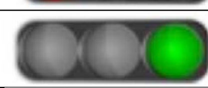
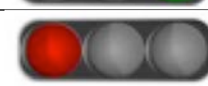
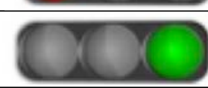
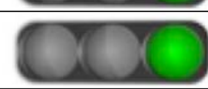
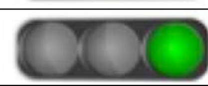
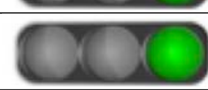
Considering a decision to hold

Hold

	INDUSTRY	Current Status
3M	Industrials	
Accenture	Information Technology	
Adobe Systems	Information Technology	
Aetna	Health Care	
AmerisourceBergen	Health Care	
Applied Materials	Information Technology	
ADP	Information Technology	
Becton Dickinson	Health Care	
Biogen	Health Care	
Broadcom	Information Technology	
CA Inc.	Information Technology	
Cardinal Health	Health Care	
Cisco Systems	Information Technology	
Citrix Systems	Information Technology	

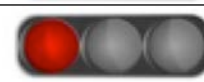
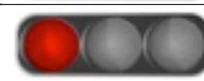
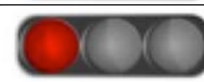
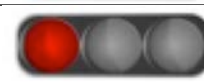
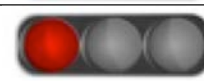
QUBE INSIGHTS: Equity Research Snapshots

Patrick Choi
Ian Quigley, MBA

	INDUSTRY	Current Status
Cognizant Technology Solutions	Information Technology	
Edward Lifesciences	Health Care	
Eli Lilly	Health Care	
EMC	Information Technology	
Gilead Sciences	Health Care	
Google	Information Technology	
Humana	Health Care	
IBM	Information Technology	
Intel	Information Technology	
Baxalta	Health Care	
Intuitive Surgical	Health Care	
Johnson & Johnson	Health Care	
Medtronic	Health Care	
Merck & Co.	Health Care	
Baxter	Health Care	
Microsoft	Information Technology	
VEREIT	Real Estate Investment Trust	
Western Digital	Information Technology	
Yahoo	Information Technology	

QUBE INSIGHTS: Equity Research Snapshots

Patrick Choi
Ian Quigley, MBA

	INDUSTRY	Current Status
Brookfield Asset Management	Real Estate Investment Trust	
First Capital Realty	Real Estate Investment Trust	
Micron Technology	Information Technology	
Motorola Solutions	Information Technology	
Omnicom Group	Consumer Discretionary	
Oracle Corp.	Information Technology	
Qualcomm	Information Technology	
Quest Diagnostics	Health Care	
Red Hat	Information Technology	
St. Jude Medical	Health Care	
Stryker	Health Care	
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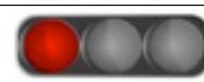
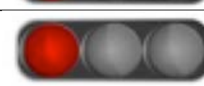
Teradata	Information Technology	
Chemours	Materials	

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Qube Investment Management Inc. is a registered portfolio management firm in the Provinces of Alberta and British Columbia and was registered as a portfolio management firm on June 25, 2012. Any return period cited before this date was prior to QIM being registered as a portfolio management firm. Inception was Jan 1, 2011 and all returns are for a modeled portfolio initiated at $500,000. Your actual returns may vary according to your individual portfolio. The modeled returns are calculated inclusive of dividends, adjusted to the Canadian currency, and are determined via the IRR (Internal Rate of Return) method. The gain/loss shown are simple (non-compounded) returns for periods up to one year. If the time since inception date is more than one year, then the return shown is an annualized return. For comparison purposes, the Kaleo model(s) are reported as gross returns before investment management fees. Individual investor level returns will differ as the fees agreed to in your Investment Management Agreement (IMA) are subtracted from the gross return.

At any one point in time, the composition of the Kaleo model may change. Currently, the focus for our models (Kaleo A, B and Full) is to invest in a globally diversified portfolio of liquid stocks with a minimum market capitalization of $1 billion. Our diversification strategy is to have similar industry weightings between our Kaleo models A, B and Full, which in turn will have similar weightings to the S&P 500. Our investment mandate is to not have any one industry sector or sub-group exceed 2.0 times the percentage weighting assigned to that group by the S&P 500 index unless the sector or sub-group composes less than 5% of the total index. Please refer to your Investment Policy Statement (IPS) for more details.

Index comparisons are based on the total return index provided by Standard & Poor's for both the S&P/TSX and the S&P 500. All index returns are inclusive of dividends, adjusted to the Canadian currency, and, similar to the modeled portfolio, determined via the IRR method. Please note that, as total return indices are not actual portfolios, these returns do not include the cost of management and/or trading fees.

Past performance is not indicative of future results and there is no assurance that our model portfolio will achieve its objectives or avoid significant losses

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