REFLECTION

3rd QUARTER 2022 REVIEW

www.cristallin.ca

SUMMARY

AMETHYST ARBITRAGE FUND

The last quarter saw our hedge fund deliver on one of its primary roles: preserving our investors' capital. All the traditional asset classes once again posted negative returns in the third quarter, although the declines were less dramatic than in the first two quarters of the year. The Amethyst Arbitrage Fund produced a good positive return in the third quarter due to its diverse range of non-directional arbitrage strategies.

This was also the case in the first quarter. But it should be recalled that in the second quarter, the central banks admitted that they had underestimated the inflationary risks. This sent bond prices into a rarely seen downward spiral that forced us to chalk up some significant losses. We were confident that we could recover from much of that drop, given the nature of our arbitrage strategies, and this is what transpired. Much of the ground lost has now been regained. Although 2022 will probably be remembered for the losses incurred by many investors, we are confident that, in the end, the Fund will post positive results. Here follows a discussion of what happened in the third quarter, along with a sense of what the last quarter of the year may bring.

MARKET EVENTS

The high volatility in equity markets and interest rate hikes affected the spreads in M&A transactions, prompting us to be even more cautious and reduce the risk in our portfolio. We tightened our criteria for decisions on whether to participate in any new transactions. As a result, we were involved in fewer than 20 transactions during the quarter, compared to an average of close to 30. Despite having reduced our risk-taking, the M&A arbitrage strategy gave us a positive return for the quarter.

Despite having reduced our risk-taking, the M&A arbitrage strategy gave us a positive return for the quarter.

However, we were not completely spared the surprises that sometimes occur in such transactions, such as when a third player interfered with a deal, seeking to merge with a company that was itself in the process of merging with another. This new offer significantly widened the spread on the original deal, and because we were committed to it, we had to employ all our arbitrage skills to get out of it relatively unscathed.

Unexpected Second Offer

Initially, Unity Software had proposed to merge with IronSource in a stock-for-stock transaction. So we bought IronSource shares and sold Unity Software shares short, since we found the market spread attractive and it met our criteria. But then AppLovin Corporation made a bid for Unity Software. The spread on which we had placed our bet then widened considerably, as can be seen in the next page chart, and the value of the stock on which we were holding a short position rose sharply. As a result, much value was lost.

Sticking closely to our risk management rules, we then liquidated half of the position, obviously taking a substantial loss. But it soon became clear that AppLovin's proposal might not materialize, so we began to gradually rebuild our original position, taking advantage of the very wide spread created by AppLovin's involvement. And when it became clear that AppLovin's offer would be rejected and would not be followed by a higher offer, the spread on the original deal shrunk back as quickly as it had widened. In the end, we emerged from the experience unscathed.

FROM Jul. 1998 to Sep. 2022	ANNUALIZED RETURNS (%) *Net of all fees*							Volatil.	Correl.	% Mths > 0	Sharpe Ratio
	YTD	1 yr	3 yr	5 yr	10 yr	20 yr	Incep.				
Amethyst Arbitrage Fund - Cl. F	**-1.8%**	**-1.5%**	**1.4%**	**1.4%**	**4.4%**	**7.0%**	**7.7%**	**8.0%**	**-**	**74%**	**0.71**
HFRI - Global Fund Weighted	-6.2%	-6.1%	6.2%	4.5%	4.6%	5.7%	6.0%	6.9%	0.48	65%	0.57
S&P 500 (TR)	-26.9%	-18.8%	6.7%	8.4%	11.3%	9.6%	6.7%	15.8%	0.43	64%	0.30
S&P/TSX Composite (TR)	-11.1%	-5.4%	6.6%	6.5%	7.3%	8.6%	6.5%	14.8%	0.49	63%	0.30
EAFE World Equity (TR)	-28.9%	-27.4%	-4.2%	-3.4%	1.0%	3.1%	0.8%	16.8%	0.43	56%	-0.08
FTSE CAN Long Term Bond	-21.0%	-17.2%	-6.1%	0.1%	1.8%	5.2%	5.3%	7.7%	0.14	59%	0.42

CRYSTALLINE

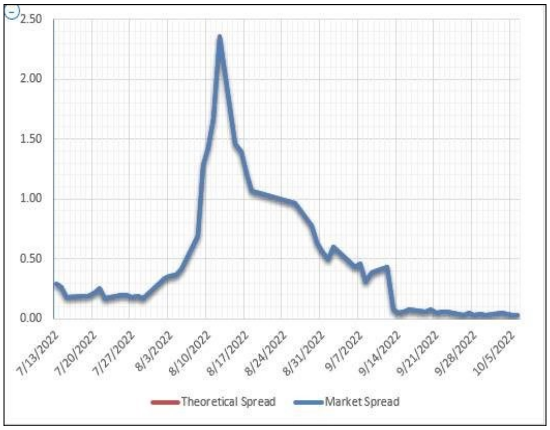
ans de passion et de rendement
years of passion and performance

CANADIAN MANAGER OF ALTERNATIVE FUNDS, SINCE 1998

1002 Sherbrooke Street West
Suite 1525
Montreal (Quebec)
Canada H3A 3L6

TEL. +1 514 284 0248
info@cristallin.ca

M&A Deal Spread
(IronSource - Unity Software)



CONVERTIBLE SECURITIES

We began the quarter on the heels of an absolutely horrendous month of June, marked by almost unprecedented volatility in the bond markets. Then some normalcy returned to markets in July. ***But the volatility quickly returned in August and September, with bond prices slipping even further.*** We were up against a long list of problems. This included higher sovereign bond curves, widening credit spreads, as well as the cost of borrowed capital and securities for short sales. And let's not forget all the geopolitical issues, which only added to the feeling that we should probably wait before buying, and not hesitate to sell anything that was looking riskier.

Convertible Bonds Take a Beating

In the third quarter, convertible bonds took a beating across the board. We sold those with little chance of recovering in the near to medium term. Our strategy is to replace them with securities that we believe offer better credit quality, when the interest coupons are more attractive and the shares sold in exchange provide greater capital protection. In M&A bonds, we tactically increase the positions we believe are the best when other transactions go through and capital has been freed up.

The important thing to understand about bonds is that they will inevitably mature and are bound to be worth $100 (provided, of course, that the issuer does not go bankrupt). Since bonds bear interest, their initial yield is captured at time of purchase. If a bond's price falls, the loss recorded at the end of the month is simply a reset of its yield to maturity. As a result, the future yield will necessarily be higher.

Well Positioned

In the end, our arbitrage strategies in the last quarter ensured that the bonds still held in the portfolio were safe, short-term investments in M&A bonds, as well as convertible bonds that were well hedged with a counterparty position and that gave us a positive carry. This portfolio is a good fit with our mission to protect capital and potentially provide a higher return once the market veers upwards.

This portfolio is a good fit with our mission to protect capital and potentially provide a higher return once the market veers upwards.

FIXED INCOME

The extreme volatility in the bond markets, exacerbated at the end of the quarter by the tax measures announced in the United Kingdom, did not prevent us from achieving an attractive positive return for the quarter. As in the previous quarter, the shifts in the yield curve and the changing durations continued to be sudden and substantial. ***In the U.S., rates on 10-year Treasuries reached 2.57% on August 1 and ended the quarter at 3.94%.*** Caution was everything in our arbitrage transactions in these two segments.

We realized some gains, mainly on our credit spread arbitrage transactions and on duration. Credit spreads were particularly volatile, especially those on corporate bonds. As in the previous quarter, the spreads on government agency bonds continued to ease back to more normal levels, something we had not seen since the third quarter of 2021. The lack of new issues, combined with the defensive nature of this type of bond, and rising rates across the board have allowed agency securities to outperform, as we had been expecting since last year. Our patience had served us well.

Good Opportunities in September

At the end of the quarter, our use of the risk envelope was at 57%, or much like it was three months earlier. However, we saw a particularly good opportunity at the end of August, after agency spreads had widened. We increased this weight to over 80% and then reduced it further at the end of the quarter, once we had realized the expected gains.

We enter the final quarter of the year favouring three- and seven-year agency securities in our credit spread positioning, and we have made a small addition to our positions on corporate bond spreads, since we see attractive opportunities as these spreads widen. On the yield curve, we are holding an albeit modest position, as we expect that the curve will flatten. ***As for duration, we favour short positions in both the Canadian and U.S. markets.***

THE ECONOMY AND FINANCIAL MARKETS

Stock markets continued to trend downward for a third consecutive quarter. In the U.S., the S&P 500 index fell 5.3% during the quarter, following a dramatic 9.3% drop in September. The year-to-date decline is 24.8%. The Toronto Stock Exchange S&P/TSX index was slightly less affected, dropping 2.2% during the quarter, for a total decline of 13.1% in 2022. As for bonds, the DEX Universe Index, despite a slightly positive return in the third quarter, is posting a negative return of 10.5% year-to-date. In the first three months of the year, the commodity market had its best quarter ever, but the value of the commodity basket then fell sharply, by about 14%, in the third quarter.

U.S. Treasuries - 10 Year Yield

So when Will the Recession Hit?

As for the economy, the debate carries on as to whether and when the global economy will slip into a recession. The International Monetary Fund (IMF) has again lowered its growth forecast for 2023, from 2.9% to 2.7%, thereby reinforcing fears of a recession. For the United States, the IMF now expects GDP to grow by 1.6% this year and only 1% in 2023. A recession in the U.S., which would have an impact on the Canadian economy, appears increasingly likely. Some U.S. observers, most notably Jamie Dimon, CEO of JPMorgan Chase, believe this is inevitable.

OUTLOOK

The U.S. will hold midterm elections on November 8 and, interestingly, this period is usually very favourable for equity markets. Should we expect the same this time around? One thing is certain, the big loser could be democracy. Above all, Republican majorities in both the House of Representatives and the Senate could make it difficult, if not impossible, for the White House to act in a difficult economic and geopolitical environment.

All Eyes on the Central Banks

The central banks will continue to hold centre stage in the next quarter. Both the Federal Reserve and the Bank of Canada are expected to raise interest rates again before the end of the year. The magnitude of such hikes may provide some indication of whether they will be the last, and whether the monetary authorities expect the surge in inflation to slow. For now, their rate hikes, combined with quantitative tightening, seem likely to ensure continued volatility in the bond markets. Before the volatility in both the equity and bond markets can subside, the markets appear to be looking for signals from the central banks that they will soon stop raising interest rates.

For now, their rate hikes, combined with quantitative tightening, seem likely to ensure continued volatility in the bond markets.

CRYSTALLINE

ans de passion et de rendement
years of passion and performance