AGF Canadian Growth Equity Class[1]

FUND COMMENTARY FIRST QUARTER 2017 | **FOR ADVISOR USE WITH INVESTORS**

FUND FACTS

FUND CATEGORY:	BENCHMARK INDEX[2]:	DATE OF INCEPTION:	INVESTMENT STYLE:	PORTFOLIO MANAGER:
Canadian small- or mid-cap equity	60% S&P/TSX Composite Total Return Index / 40% S&P/TSX Small Cap Index	October 1964	Bottom-up growth	AGF Investments Inc. Peter Imhof, CIM

Market overview

During the first quarter of 2017, global equities continued to move higher, continuing a rally that followed the U.S. election in early November. However, leadership in the market shifted, as the reflation trade that followed the election of Donald Trump to the U.S. Presidency in late 2016 waned, with Financials and cyclical leadership giving way to secular growth sectors. As such, portfolios with growth investment styles performed relatively better in comparison to late-2016 when growth severely underperformed value.

From a macroeconomic perspective, economic data remained supportive and in some cases, saw acceleration. In the U.S., non-farm payrolls exceeded market expectations for the first two months of 2017, averaging gains of 231,000 per month, which was well above consensus, as well as the pace in 2016. Meanwhile, the ISM Manufacturing Index continued to accelerate well into expansion territory, hitting a high of 57.7 in February before settling at 57.2 in March. Similarly, the services sector remained robust, with the ISM Non-Manufacturing PMI at 57.6, signalling strong expansion conditions. In response to the strong macroeconomic data, the U.S. Federal Reserve raised the federal funds rate for a third time this cycle in March and telegraphed more rate hikes to come in 2017 while also mentioning that any future hikes would be “gradual”.

In Canada, equity markets continued their move higher as macroeconomic data remained supportive. Data released during the quarter showed that the Canadian economy grew faster than expected in January, up 0.6% on a monthly sequential basis and 2.3% on a year over year basis. In fact, seven out of the past eight months have reported monthly GDP gains of 0.3% or better, which is nearly double the 15-year average of 0.17%. Growth was broad-based, with 15 out of 20 major industries reporting gains, led by manufacturing, resources and wholesale trade. The strong GDP print, in addition to other improving Canadian data, is expected to result in upwardly revised growth forecasts, though the Bank of Canada remains dovish and is widely expected to keep rates on hold throughout the year.

Fund overview

As at Mar. 31, 2017	3 mo.	1 yr.	3 yr.	5 yr.	10 yr.	PSD*
AGF Canadian Growth Equity Class (%) (net of fees)	1.2	16.3	2.4	3.1	-0.6	8.6
Benchmark (%)	2.1	23.1	4.9	6.3	4.4	-
Canadian Small/Mid Cap Equity Category Average	0.8	17.2	3.2	8.0	4.6	-
Quartile Rank	3	3	3	4	4	-

Source: AGF Investment Operations.

* Performance start date (PSD): Apr. 30, 1965.

During the quarter, the Fund underperformed its benchmark, returning 1.2% versus 2.1% for the benchmark. Overall sector allocation effect was negative, as an underweight to Materials detracted from relative performance. This was partially offset by an underweight to Health care and the Fund’s allocation to private companies, which contributed to performance. Overall security selection effect was also positive and helped contribute to performance, as selection in Energy, Industrials and Real Estate more than offset negative selection effect in Materials and Consumer Staples.

In terms of individual holdings, the top contributors were CRH Medical Corp., Grande West Transportation Group and New Flyer Industries, while the top detractors were Seven Generations Energy, Whitecap Resources and Tahoe Resources.

The top contributor during the period was CRH Medical Corp. which saw its shares rise 51.6%. CRH Medical provides innovative products and services to gastrointestinal (GI) physicians. During the quarter, the company’s shares steadily climbed as it continued to grow through acquisitions, announcing the acquisition of a gastroenterology anesthesia practice in Kissimmee, Florida, as well as an agreement with Puget Sound Gastroenterology in Seattle, Washington to develop a “deep sedation” program. The deep sedation program development represents a new growth strategy to target GI practices that do not currently offer deep sedation services. We continue to believe that the company is well positioned for growth – with growing demand for colonoscopies given aging demographics, demand for anesthesia services has increased and with a fragmented GI-anesthesia segment, CRH Medical is well positioned for continued growth.

The top detractor during the period was Seven Generations Energy, which saw its shares decline 22.4%. Seven Generations is an oil company with a concentrated asset base in northwest Alberta. The company is expecting major growth in the coming years from the development of its Montney play. Since reporting its fourth quarter of 2016 results, Seven Generations stock has been under pressure, given the production shortfall in the quarter and softly articulated guidance that volumes will remain flat through the first quarter and see modest growth in the second quarter (due in part to a third-party plant outage). However, we believe that these are shorter-term issues and that the company should be able to reach its production guidance. As Seven Generations brings on material production volumes in the third quarter, we believe investor confidence will be regained in the company.

Outlook

The M&A environment in Canada has remained robust, as a weaker Canadian dollar and reasonable valuations for Canadian equities has resulted in U.S. companies coming in to buy Canadian companies. During the quarter there were two takeovers of holdings in the portfolio – Milestone Apartments REIT and RDM Corp. Both were acquired by U.S. based companies.

Looking ahead, we continue to believe Canadian equities are well positioned, despite a very strong 2016. Global growth is improving, Canadian economic growth is accelerating, the oil market continues to shift towards a balancing of supply and demand, and overall valuation multiples are in line with historical averages. Our belief is that the market will continue to reward pro-growth, pro-cyclical stocks, and Canada has one of the largest sector weightings to these groups of any index in the world. With that said, the global economic backdrop still has many risks, which leads us to believe tactical stock picking and sector rotation is likely to be rewarded this year. Our focus will remain on identifying those businesses in Canada with high growth opportunities, solid management teams and reasonable valuations that provide us with both upside participation and downside protection in uncertain times.

1 Effective April 1, 2016, AGF reduced the MF Series management fee from 2.50% to 2.25%. AGF Canada Class merged into AGF Canadian Growth Equity Class on May 20, 2016. On April 10, 2012, shareholders approved a change in the investment objective providing the Fund with greater flexibility to invest in stocks of all market capitalizations.

2 On May 1, 2012, the Fund's benchmark changed from a blended index of 60% BMO Small Cap Blended Total Return Index (Weighted) / 40% S&P/TSX Composite Index to a blended index of 60% S&P/TSX Composite Index / 40% BMO Small Cap Blended Total Return Index (Weighted). Then on July 1, 2014, the BMO Small Cap Blended Total Return Index was replaced with the S&P/TSX Small Cap Total Return Index. In both cases, the benchmark changes were applied from that date forward.

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