barrage capital

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Currency Hedging Program

Barrage Fund

Since its inception in March 2013, the Barrage Fund largely took advantage of the Canadian dollar depreciation against the U.S. dollar since its assets were primarily invested in the United States. During this period, the loonie went from 97 US cents to 75 US cents, generating a return on the currency of about 29% on all assets held in U.S. dollars.

The Canadian dollar since the Fund's inception

Through our letters to unit holders, we have expressed our favourable opinion with regards to the exchange rate at the time:

> *"In addition, with an exchange rate close to parity, we see a great opportunity to acquire such securities (U.S.) without exposing ourselves to significant currency risk."*
>
> August 5 2013: 96 US cents

> *"We are pleased to have access to many investment opportunities south of the border at an exchange rate that we believe is still favourable."*
>
> February 5 2014: 90 US cents

But the continued deterioration of the Canadian dollar against its American counterparty since the beginning of 2015 is forcing us to re-evaluate our position. We now deem it prudent to reduce our exposure to the exchange rate on assets held in U.S. dollars for the following two reasons:

1- Purchasing Power Parity

The Purchasing Power Parity (PPP) is a technique used in economics to compare the purchasing power of consumers in different countries. This technique helps establish the exchange rate at which the cost of a basket of goods would be equal between two countries with a reasonably comparable standard of living.

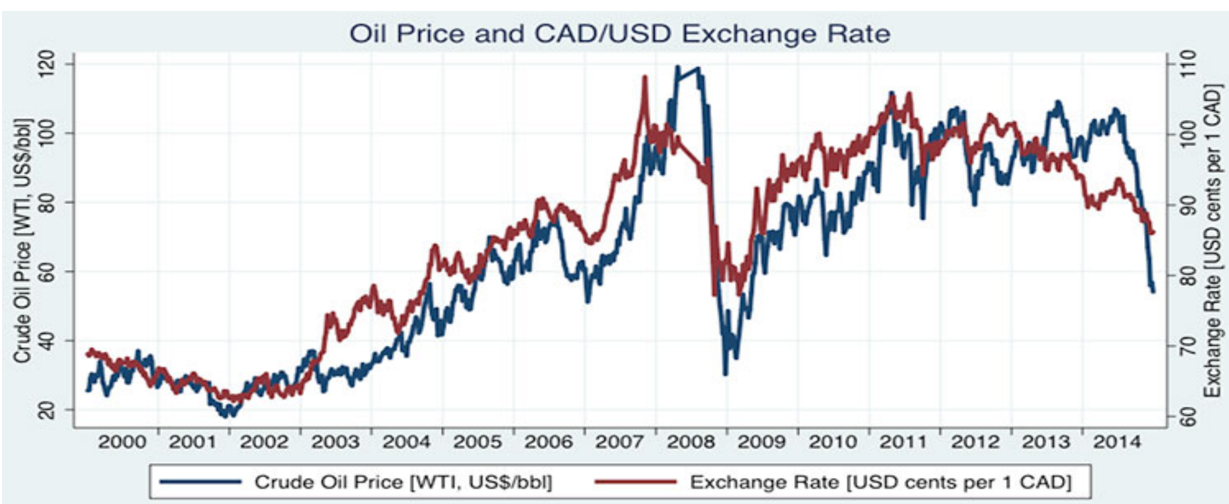
The Canadian dollar parity rate is around 84 US cents. When the exchange rate moves away from this equilibrium, we can observe behavioural changes from consumers wanting to benefit from this imbalance. For example, many Canadians took advantage of a strong Canadian dollar over the last few years by purchasing vehicles or real estate south of the border. On the flip side, a drop in the value of the Canadian dollar should raise Americans' interest for a condominium in Mont-Tremblant or a fishing trip in Quebec's north region. In theory, the long-term exchange rate between two currencies should fluctuate around the PPP.

Under this technique, the Canadian dollar was over-valued by 15% when the Fund was launched but would now be under-valued by roughly 10%.

2 - Oil

According to a study carried out by the University of British Columbia, every US$1 move in the price of a barrel of oil (WTI) translates into a 0.42 US cents variation in the Canadian dollar. Thus, a rise of US$20 in the price of a barrel would translate into a rise in the Canadian dollar of 8.4 US cents.

The following graph shows this correlation from 2000 to 2014, the blue line representing the price of a barrel and the red line representing the Canadian dollar exchange rate:



During the course of last year, the disequilibrium between the global supply and demand of crude led to a drop in the price of a barrel to an artificially low level. This lower price is currently bringing back the market to equilibrium by stimulating demand and curbing supply. We are already noticing adjustments at the consumers and producers' levels. While it is challenging to predict with precision when crude prices will return to higher levels, we believe economic forces will sooner or later bring back the price of a barrel in line with its marginal production cost of around US$100.

In the event where the historical correlation between the Canadian dollar and oil prices persists in the future, a rise in the price of crude would entail a rise in the Canadian dollar.

Currency Hedging Program

Although other factors can influence the exchange rate, the two mentioned above lead us to believe it is now timely to protect ourselves from a potential recovery in the Canadian dollar.

For these reasons, we have put in place a currency hedging program within the Barrage Fund, effective August 31, 2015. More precisely, the Fund is now hedged on the USD/CAD pair at a rate of 75.2 US cents, on approximately 70% (hedge ratio) of its exposure to the U.S. dollar. This hedge ratio could increase further in the event of a continued deterioration of the Canadian dollar. This protection is costing approximately 30 basis points per year (0.30%) on the portion that is effectively covered.

As you know, our priority is to maximize returns for our clients while minimizing risks. We believe this program will allow us to reach our objective. If you have questions pertaining to this hedging program, we invite you to communicate with us.

Kind regards,

Patrick Thénière　　　　Rémy Morel

Mathieu Beaudry　　　　Maxime Lauzière