

FORTIFIED INCOME FUND



**THINK AHEAD.
STAY AHEAD.**

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MANAGEMENT'S RESPONSIBILITY STATEMENT

The accompanying financial statements have been prepared by Picton Mahoney Asset Management, the Manager of the Picton Mahoney Fortified Income Fund (the "Fund"). The Manager is responsible for all of the information and representations contained in these financial statements.

The financial statements have been prepared in accordance with International Financial Reporting Standards and include certain amounts that are based on estimates and judgements. Management maintains appropriate processes to ensure that relevant and reliable financial information is produced.

The financial statements have been audited by PricewaterhouseCoopers LLP. They have audited the financial statements in accordance with Canadian generally accepted auditing standards to enable them to express to the unitholders their opinion on these financial statements. Their report is set out on the following page.

Picton Mahoney Asset Management

Toronto, Ontario

March 26, 2019

INDEPENDENT AUDITOR'S REPORT

To the Unitholders and Trustee of
Picton Mahoney Fortified Income Fund (the Fund)

Our opinion

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Fund as at December 31, 2018 and 2017 and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards (IFRS).

What we have audited

The Fund's financial statements comprise:

- the statements of financial position as at December 31, 2018 and 2017;
- the statements of comprehensive income (loss) for the years then ended;
- the statements of changes in net assets attributable to holders of redeemable units for the years then ended;
- the statements of cash flows for the years then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies.

Basis for opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial statements* section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We are independent of the Fund in accordance with the ethical requirements that are relevant to our audit of the financial statements in Canada. We have fulfilled our other ethical responsibilities in accordance with these requirements.

Other information

Management is responsible for the other information of the Fund. The other information comprises the Management Report of Fund Performance.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements of the Fund, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially

inconsistent with the financial statements of the Fund or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of management and those charged with governance for the financial statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with IFRS, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Fund's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Fund or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Fund's financial reporting process.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control.

INDEPENDENT AUDITOR'S REPORT

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Fund's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Fund to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

PricewaterhouseCoopers LLP

Chartered Professional Accountants, Licensed Public Accountants

Toronto, Ontario
March 26, 2019

PICTON MAHONEY FORTIFIED INCOME FUND

STATEMENTS OF FINANCIAL POSITION

As at

	December 31, 2018 \$	December 31, 2017 \$
Assets		
Current assets		
Long positions at fair value*	323,019,405	185,352,786
Cash	53,816,157	12,105,102
Options purchased	1,307,623	201,936
Unrealized gain on foreign exchange forward contracts at fair value	242,079	1,142,490
Deposits with brokers for securities sold short	12,899,755	18,380,644
Subscriptions receivable	90,762	426,857
Receivable for investments sold	1,388,566	-
Dividends receivable	3,375	7,254
Interest and other receivable	4,676,041	2,144,854
	<u>397,443,763</u>	<u>219,761,923</u>
Liabilities		
Current liabilities		
Short positions at fair value**	27,623,809	13,771,052
Options written	416,080	60,294
Unrealized loss on foreign exchange forward contracts at fair value	8,527,096	399,809
Management fee payable	272,169	126,181
Performance fee payable	-	40,448
Redemptions payable	168,838	173,805
Accrued liabilities	264,335	73,142
Payable for investments purchased	4,822,650	-
Interest payable	574,588	161,544
Distributions payable	1,585	81
	<u>42,671,150</u>	<u>14,806,356</u>
Net Assets Attributable to Holders of Redeemable Units	<u>354,772,613</u>	<u>204,955,567</u>
Net Assets Attributable to Holders of Redeemable Units per Class		
Class A	40,560,824	25,640,513
Class F	255,495,300	145,868,309
Class FT	26,074,599	10,492,359
Class T	1,846,871	1,232,182
Class I	30,795,019	21,722,204
Number of Redeemable Units Outstanding		
Class A	3,889,228	2,311,429
Class F	23,838,720	12,909,550
Class FT	2,759,230	1,009,003
Class T	202,353	121,518
Class I	2,699,650	1,838,343
Net Assets Attributable to Holders of Redeemable Units per Unit		
Class A	10.43	11.09
Class F	10.72	11.30
Class FT	9.45	10.40
Class T	9.13	10.14
Class I	11.41	11.82
* Long positions, at cost	324,274,441	184,707,613
** Short positions, at cost	(28,767,038)	(14,130,439)

The accompanying notes are an integral part of the financial statements.

Approved on behalf of the Manager

David Picton

Arthur Galloway




President

CFO

STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

For the years ended December 31

	2018 \$	2017 \$
Income		
Net gains (losses) on investments and derivatives		
Interest for distribution purposes	18,247,879	4,707,851
Dividends	10,457	29,799
Net realized gain (loss) on investments and options	3,016,264	781,120
Net realized gain (loss) on foreign exchange forward contracts	(13,784,878)	2,742,312
Change in unrealized appreciation (depreciation) on investments, options and foreign exchange forward contracts	(9,392,790)	1,235,003
Interest and borrowing expense	(2,158,348)	(239,698)
Dividend expense	(7,031)	(4,592)
Net gains (losses) on investments and derivatives	<u>(4,068,447)</u>	<u>9,251,795</u>
Other income		
Securities lending income	12,160	2,187
Foreign currency gain (loss) on cash and other assets and liabilities	2,088,941	(1,123,917)
Total Income	<u>(1,967,346)</u>	<u>8,130,065</u>
Expenses		
Management fees	3,434,026	972,907
Performance fees	839,345	20,307
Transaction costs	801,651	124,893
Harmonized sales tax	509,753	147,134
Securityholder reporting fees	241,160	51,661
Administrative fees	71,606	43,042
Audit fees	70,079	27,461
Legal fees	59,891	25,709
Custody fees	42,822	19,710
Independent Review Committee Expense	12,319	13,729
Withholding taxes	2,415	60
Total Expense after Manager Absorption	<u>6,085,067</u>	<u>1,446,613</u>
Less: Expenses Absorbed by Manager	-	-
Total Expense after Manager Absorption	<u>6,085,067</u>	<u>1,446,613</u>
Increase (Decrease) in Net Assets Attributable to Holders of Redeemable Units	<u>(8,052,413)</u>	<u>6,683,452</u>
Increase (Decrease) in Net Assets Attributable to Holders of Redeemable Units per Class		
Class A	(1,211,360)	667,274
Class F	(5,959,728)	4,329,913
Class FT	(595,898)	455,464
Class T	(58,242)	55,759
Class I	(227,185)	1,175,042
Increase (Decrease) in Net Assets Attributable to Holders of Redeemable Units per Unit		
Class A	(0.35)	0.62
Class F	(0.27)	0.75
Class FT	(0.31)	0.74
Class T	(0.32)	0.65
Class I	(0.09)	1.01

PICTON MAHONEY FORTIFIED INCOME FUND

STATEMENTS OF CHANGES IN NET ASSETS ATTRIBUTABLE TO HOLDERS OF REDEEMABLE UNITS

For the year ended December 31

	2018 \$	2017 \$
Net Assets Attributable to Holders of Redeemable Units at Beginning of Year		
Class A	25,640,513	2,971,249
Class F	145,868,309	15,691,846
Class FT	10,492,359	2,090,871
Class T	1,232,182	335,569
Class I	21,722,204	6,297,163
	<u>204,955,567</u>	<u>27,386,698</u>

Increase (Decrease) in Net Assets Attributable to Holders of Redeemable Units

Class A	(1,211,360)	667,274
Class F	(5,959,728)	4,329,913
Class FT	(595,898)	455,464
Class T	(58,242)	55,759
Class I	(227,185)	1,175,042
	<u>(8,052,413)</u>	<u>6,683,452</u>

Redeemable Unit Transactions

Proceeds from redeemable units issued

Class A	24,593,655	23,710,687
Class F	180,922,187	132,992,205
Class FT	21,395,370	9,060,946
Class T	1,270,168	1,059,593
Class I	9,300,000	14,250,000
	<u>237,481,380</u>	<u>181,073,431</u>

Reinvestments of distributions to holders of redeemable units

Class A	1,049,243	543,993
Class F	4,844,375	2,480,425
Class FT	-	752
Class T	-	-
Class I	921,085	643,212
	<u>6,814,703</u>	<u>3,668,382</u>

Redemption of redeemable units

Class A	(8,184,542)	(1,582,450)
Class F	(61,720,527)	(5,987,126)
Class FT	(3,682,758)	(519,194)
Class T	(460,275)	(138,118)
Class I	-	-
	<u>(74,048,102)</u>	<u>(8,226,888)</u>

Net Increase (Decrease) from Redeemable Unit Transactions

170,247,981 176,514,925

	2018 \$	2017 \$
Distributions to Holders of Redeemable Units		
Net investment income		
Class A	(1,312,917)	(377,480)
Class F	(8,371,527)	(1,980,804)
Class FT	(1,518,550)	(461,464)
Class T	(135,541)	(64,064)
Class I	(911,526)	(404,474)
	<u>(12,250,061)</u>	<u>(3,288,286)</u>

Capital gains

Class A	-	(287,186)
Class F	-	(1,628,901)
Class FT	-	(128,202)
Class T	-	(15,611)
Class I	-	(232,766)
	<u>-</u>	<u>(2,292,666)</u>

Return of capital

Class A	(13,768)	(5,574)
Class F	(87,789)	(29,249)
Class FT	(15,924)	(6,814)
Class T	(1,421)	(946)
Class I	(9,559)	(5,973)
	<u>(128,461)</u>	<u>(48,556)</u>

Net Increase (Decrease) in Net Assets Attributable to Holders of Redeemable Units

149,817,046 177,568,869

Net Assets Attributable to Holders of Redeemable Units at End of Year

Class A	40,560,824	25,640,513
Class F	255,495,300	145,868,309
Class FT	26,074,599	10,492,359
Class T	1,846,871	1,232,182
Class I	30,795,019	21,722,204

Net Assets Attributable to Holders of Redeemable Units at End of Year

354,772,613 204,955,567

The accompanying notes are an integral part of the financial statements.

PICTON MAHONEY FORTIFIED INCOME FUND

STATEMENTS OF CASH FLOWS

For the years ended December 31

	2018 \$	2017 \$		2018 \$	2017 \$
Cash Flows from Operating Activities			Cash Flows from Financing Activities		
Increase (decrease) in net assets attributable to holders of redeemable units	(8,052,413)	6,683,452	Distributions to holders of redeemable units, net of reinvested distributions	(5,562,315)	(1,961,045)
Adjustments for:			Proceeds from redeemable units issued	235,418,561	180,029,596
Unrealized foreign exchange (gain) loss on cash	(5,421,931)	135,465	Amount paid on redemption of redeemable units	(71,654,155)	(7,334,160)
Net realized (gain) loss on investments and options	(3,016,264)	(781,120)	Net Cash Generated (Used) by Financing Activities	158,202,091	170,734,391
Change in unrealized (appreciation) depreciation on investments, options and foreign exchange forward contracts	9,392,790	(1,235,003)	Unrealized foreign exchange gain (loss) on cash	5,421,931	(135,465)
(Increase) decrease in due from manager	-	116,918	Net increase (decrease) in cash	36,289,124	7,080,333
(Increase) decrease in interest and other receivables	(2,531,187)	(1,872,517)	Cash, beginning of year	12,105,102	5,160,234
(Increase) decrease in dividends receivable	3,879	(5,300)	Cash, End of Year	53,816,157	12,105,102
(Increase) decrease in deposits with brokers for securities sold short	5,480,889	(18,380,644)	Cash	53,816,157	12,105,102
Increase (decrease) in interest payable	413,044	161,544	Cash overdraft	-	-
Increase (decrease) in other payables and accrued liabilities	296,733	167,668	Net Cash (Overdraft)	53,816,157	12,105,102
Purchase of long positions and repurchases of investments sold short	(876,508,585)	(401,974,588)	Items classified as operating activities:		
Proceeds from sales of long positions and on investments sold short	758,030,078	253,330,067	Interest received, net of withholding tax	15,716,692	2,835,334
Net Cash Generated (Used) by Operating Activities	(121,912,967)	(163,654,058)	Dividends received, net of withholding tax	11,921	24,499
			Interest and borrowing expense paid	(1,745,304)	(78,154)
			Dividends paid	(7,031)	(4,592)
			<i>Net of non-cash transfers and switches of \$2,398,914 (2017 - \$718,923)</i>		

PICTON MAHONEY FORTIFIED INCOME FUND

SCHEDULE OF INVESTMENT PORTFOLIO

As December 31, 2018

CCY*	No. of shares/ units/ Face value	Security Description	Average cost (\$)	Fair value (\$)	CCY*	No. of shares/ units/ Face value	Security Description	Average cost (\$)	Fair value (\$)
LONG POSITIONS (91.4%)									
Canadian Debt (40.4%)									
Corporate Bonds (40.4%)									
USD	3,400,000	1011778 BC ULC / New Red Finance Inc. 4.625%, 2022-01-15	4,507,731	4,504,418	USD	5,125,000	Telesat Canada / Telesat LLC 8.875%, 2024-11-15	7,273,538	7,297,229
USD	1,400,000	1011778 BC ULC / New Red Finance Inc. 4.250%, 2024-05-15	1,702,130	1,763,935	CAD	7,050,000	Vesta Energy Corp. 8.125%, 2023-07-24	7,047,500	6,649,031
USD	1,700,000	1011778 BC ULC / New Red Finance Inc. 5.000%, 2025-10-15	2,094,063	2,141,921	Total Canadian Debt - Long				
USD	2,900,000	Bank of Nova Scotia 2.653%, 2085-08-31	3,280,425	3,208,271	144,600,547 143,367,851				
USD	3,500,000	Bausch Health Cos Inc. 9.000%, 2025-12-15	4,658,596	4,774,335	Global Debt (50.6%)				
CAD	275,000	Clarity Trust Series D Medium Term Note 6.889%, 2019-04-15	275,000	275,000	United States Corporate and Government Bonds (32.2%)				
CAD	10,400,000	Element Fleet Management Corp. 5.125%, 2019-06-30	10,132,525	10,356,528	USD	3,900,000	Albertsons Cos, LLC / Safeway Inc. / New Albertsons LP / 5.750%, 2025-03-15	4,571,484	4,687,436
CAD	10,600,000	Element Fleet Management Corp. 4.250%, 2020-06-30	9,974,603	10,210,450	USD	900,000	Allison Transmission Inc. 5.000%, 2024-10-01	1,152,520	1,184,663
USD	4,850,000	First Quantum Minerals Ltd. 6.500%, 2024-03-01	5,570,529	5,522,881	USD	5,250,000	Ascent Resources Utica Holdings LLC / ARU Finance Corp. 10.000%, 2022-04-01	7,653,443	7,369,805
USD	1,800,000	First Quantum Minerals Ltd. 6.875%, 2026-03-01	2,254,356	1,982,122	USD	2,400,000	Berry Global Inc. 5.500%, 2022-05-15	3,238,853	3,280,189
CAD	275,000	Fusion Trust Series D Medium Term Note 6.889%, 2019-04-15	275,000	275,000	USD	1,000,000	Berry Global Inc. 4.500%, 2026-02-15	1,256,644	1,257,768
USD	3,100,000	GFL Environmental Inc. 5.625%, 2022-05-01	3,915,453	3,927,025	USD	1,667,000	Cablevision Systems Corp. 5.875%, 2022-09-15	2,232,279	2,242,642
USD	3,700,000	GFL Environmental Inc. 5.375%, 2023-03-01	4,628,388	4,447,055	USD	1,000,000	Centene Corp. 5.625%, 2021-02-15	1,351,029	1,372,632
CAD	1,225,000	Gibson Energy Inc. 5.250%, 2024-07-15	1,218,875	1,192,078	USD	2,000,000	Centene Corp. 6.125%, 2024-02-15	2,764,854	2,803,311
CAD	6,000,000	Iron Mountain Canada Operations ULC 5.375%, 2023-09-15	6,154,108	5,992,500	USD	3,200,000	CenturyLink Inc. 7.500%, 2024-04-01	4,328,718	4,228,526
USD	8,450,000	MEG Energy Corp. 6.375%, 2023-01-30	10,451,481	10,949,558	USD	2,178,000	Coeur Mining Inc. 5.875%, 2024-06-01	2,783,661	2,628,908
USD	8,600,000	MEG Energy Corp. 7.000%, 2024-03-31	10,748,271	11,276,070	USD	3,000,000	CSC Holdings LLC 10.875%, 2025-10-15	4,614,707	4,614,707
USD	2,777,000	MEG Energy Corp. 6.500%, 2025-01-15	3,784,690	3,863,951	USD	3,500,000	CSC Holdings LLC. 7.750%, 2025-07-15	4,776,169	4,860,978
CAD	5,100,000	NuVista Energy Ltd. 6.500%, 2023-03-02	5,108,250	4,860,938	USD	603,000	Endeavor Energy Resources LP / EER Finance Inc. 5.750%, 2028-01-30	808,692	844,333
CAD	2,258,000	Parkland Fuel Corp. 5.750%, 2024-09-16	2,288,641	2,214,722	USD	5,150,000	Freeport Minerals Corp. 9.500%, 2031-06-01	8,476,062	8,299,985
CAD	7,400,000	Parkland Fuel Corp. 5.625%, 2025-05-09	7,454,294	7,054,667	USD	2,900,000	Great Lakes Dredge & Dock Corp. 8.000%, 2022-05-15	3,871,046	4,035,094
CAD	6,900,000	Parkland Fuel Corp. 6.500%, 2027-01-21	6,900,000	6,704,213	USD	450,000	Harland Clarke Holdings Corp. 8.375%, 2022-08-15	552,027	564,133
CAD	10,000,000	Quebecor Media Inc. 6.625%, 2023-01-15	10,809,365	10,425,000	USD	6,015,000	HCA Inc. 7.500%, 2023-12-15	8,649,186	8,831,453
CAD	4,950,000	Source Energy Services Canada LP 10.500%, 2021-12-15	5,404,804	4,950,000	USD	4,180,000	Horizon Pharma USA Inc. 8.750%, 2024-11-01	5,827,608	5,823,238
CAD	7,150,000	Superior Plus LP 5.125%, 2025-08-27	6,687,931	6,548,953	USD	6,700,000	Iridium Communications Inc. 10.250%, 2023-04-15	9,510,719	9,699,933
					USD	3,250,000	Iron Mountain Inc. 5.750%, 2024-08-15	4,110,120	4,228,014
					USD	897,000	Molina Healthcare Inc. 5.375%, 2022-11-15	1,201,701	1,177,701
					USD	1,300,000	New Albertsons LP. 7.450%, 2029-08-01	1,439,820	1,429,313
					USD	3,675,000	QEP Resources Inc. 6.875%, 2021-03-01	5,131,728	5,082,068
					USD	3,150,000	RBS Capital Trust II 6.425%, 2049-01-03	4,869,502	5,098,201
					USD	350,000	Sealed Air Corp. 4.875%, 2022-12-01	470,813	475,043

PICTON MAHONEY FORTIFIED INCOME FUND

APPENDIX A

OPTIONS (0.3%)

Issuer	Option Type	Number of Options	Strike \$	Expiry	Average Cost \$	Fair Value \$
Crude Oil OPT IPE	Call Option	187	\$85	January, 2019	91,946	2,554
Gold Futures OPT(CMX)	Call Option	373	\$1,450	March, 2019	163,531	198,683
S&P 500 E-Mini	Call Option	719	\$2,750	January, 2019	294,654	34,370
					<u>550,131</u>	<u>235,607</u>
CBT US Treasury Long-Term Bond	Put Option	181	\$142	January, 2019	115,082	38,626
iShares iBoxx High Yield Corporate Bond ETF	Put Option	4,000	\$78	January, 2019	245,844	60,095
iShares iBoxx High Yield Corporate Bond ETF	Put Option	8,270	\$75	January, 2019	429,216	79,066
iShares iBoxx High Yield Corporate Bond ETF	Put Option	3,627	\$75	February, 2019	94,121	79,260
iShares iBoxx High Yield Corporate Bond ETF	Put Option	7,258	\$79	February, 2019	342,750	708,778
Markel Corporation	Put Option	18	\$900	January, 2019	13,768	6,085
Mattel Incorporation	Put Option	750	\$10	January, 2019	16,390	51,218
MEG Energy Corporation	Put Option	942	\$7	January, 2019	46,832	25,905
MEG Energy Corporation	Put Option	317	\$8	January, 2019	8,242	22,983
					<u>1,312,245</u>	<u>1,072,016</u>
Total Purchased Options					<u>1,862,376</u>	<u>1,307,623</u>
Gold Futures OPT(CMX)	Written Call Option	(373)	\$1,560	March, 2019	(67,247)	(76,417)
S&P 500 E-Mini	Written Call Option	(359)	\$2,800	January, 2019	(52,710)	(8,581)
S&P 500 E-Mini	Written Call Option	(180)	\$2,900	January, 2019	(9,373)	(1,229)
					<u>(129,330)</u>	<u>(86,227)</u>
CBT US Treasury Long-Term Bond	Written Put Option	(181)	\$138	January, 2019	(24,320)	(7,725)
iShares iBoxx High Yield Corporate Bond ETF	Written Put Option	(4,000)	\$75	January, 2019	(87,466)	(29,118)
iShares iBoxx High Yield Corporate Bond ETF	Written Put Option	(8,270)	\$70	January, 2019	(225,903)	(64,397)
iShares iBoxx High Yield Corporate Bond ETF	Written Put Option	(7,258)	\$75	February, 2019	(436,171)	(227,998)
S&P 500 E-Mini	Written Put Option	(180)	\$2,950	January, 2019	(15,366)	(615)
					<u>(789,226)</u>	<u>(329,853)</u>
Total Written Options					<u>(918,556)</u>	<u>(416,080)</u>

APPENDIX B

FOREIGN EXCHANGE FORWARD CONTRACTS (-2.3%)

Purchased Currency	Sold Currency	Forward Rate	Maturity Date	Fair Value (\$)	Counterparty	Credit Rating
USD \$9,718,000	CAD \$13,015,123	1.33928	2019-02-14	242,079	Canadian Imperial Bank of Commerce	A-1
Unrealized gain on foreign exchange forward contracts at fair value				<u>242,079</u>		
CAD \$265,205,777	USD \$200,601,168	1.32206	2019-02-14	(8,444,842)	Canadian Imperial Bank of Commerce	A-1
CAD \$5,418,202	USD \$4,032,000	1.34380	2019-02-14	(82,254)	Canadian Imperial Bank of Commerce	A-1
Unrealized loss on foreign exchange forward contracts at fair value				<u>(8,527,096)</u>		
Net unrealized gain (loss) on foreign exchange forward contracts at fair value				<u>(8,285,017)</u>		

PICTON MAHONEY FORTIFIED INCOME FUND

FUND SPECIFIC NOTES

As at December 31, 2018 and December 31, 2017

1. FAIR VALUE MEASUREMENT OF FINANCIAL INSTRUMENTS

The following tables illustrate the classifications of the Fund's financial instruments within the fair value hierarchy as at December 31, 2018 and 2017.

ASSETS (LIABILITIES) AT FAIR VALUE AS AT DECEMBER 31, 2018				
	Level 1 \$	Level 2 \$	Level 3 \$	Total \$
Bonds - Long	-	293,984,217	29,035,188	323,019,405
Options - Long	1,307,623	-	-	1,307,623
Bonds - Short	-	(27,623,809)	-	(27,623,809)
Options - Short	(416,080)	-	-	(416,080)
Forward Contracts, net	-	(8,285,017)	-	(8,285,017)
Total	891,543	258,075,391	29,035,188	288,002,122

ASSETS (LIABILITIES) AT FAIR VALUE AS AT DECEMBER 31, 2017				
	Level 1 \$	Level 2 \$	Level 3 \$	Total \$
Equities - Long	3,303,132	-	-	3,303,132
Bonds - Long	-	181,499,654	550,000	182,049,654
Options - Long	201,936	-	-	201,936
Equities - Short	(1,093,322)	-	-	(1,093,322)
Bonds - Short	-	(12,677,730)	-	(12,677,730)
Options - Short	(60,294)	-	-	(60,294)
Forward Contracts, net	-	742,681	-	742,681
Total	2,351,452	169,564,605	550,000	172,466,057

2. RECONCILIATION OF LEVEL 3 FAIR VALUE MEASUREMENTS

The following tables reconcile the Fund's Level 3 fair value measurements for the years ended December 31, 2018 and 2017.

December 31, 2018	Debt Instruments - Long \$	Debt Instruments - Short \$	Total \$
Balance at Beginning of Year	550,000	-	550,000
Investment purchases during the year	-	-	-
Proceeds from sales during the year	-	-	-
Transfers in during the year	28,485,188	-	28,485,188
Transfers out during the year	-	-	-
Net realized gain (loss) on sale of investments	-	-	-
Change in unrealized appreciation (depreciation) in value of investments	-	-	-
Balance at End of Year	29,035,188	-	29,035,188
Total change in unrealized appreciation (depreciation) for assets held as at December 31, 2018			-

December 31, 2017	Debt Instruments - Long \$	Debt Instruments - Short \$	Total \$
Balance at Beginning of Year	-	-	-
Investment purchases during the year	\$550,000	-	\$550,000
Proceeds from sales during the year	-	-	-
Transfers in during the year	-	-	-
Transfers out during the year	-	-	-
Net realized gain (loss) on sale of investments	-	-	-
Change in unrealized appreciation (depreciation) in value of investments	-	-	-
Balance at End of Year	\$550,000	-	\$550,000
Total change in unrealized appreciation (depreciation) for assets held as at December 31, 2017			-

PICTON MAHONEY FORTIFIED INCOME FUND

FUND SPECIFIC NOTES (CONTINUED)

During the year ended December 31, 2018, certain securities held long were classified as Level 3. The Fund's long Level 3 securities consist of debt instruments which were measured at the transaction price as determined at the time of purchase. If there was a 5% increase or decrease in the price of level 3 securities, with all other variables held constant, net assets attributable to holders of redeemable units would have increased or decreased, respectively, by approximately \$1,451,760 as at December 31, 2018 (December 31, 2017 - \$27,500).

December 31, 2018							
Security Name	Fair Value	Valuation Technique	Unobservable Inputs	Reasonable Shift (+)	Reasonable Shift (-)	Change in Valuation (+)	Change in Valuation (-)
Clarity Trust Series D Medium Term Note 6.889%, 2019-04-15	275,000	Private valuation	Broker quote	5%	5%	\$13,750	\$(13,750)
Fusion Trust Series D Medium Term Note 6.889%, 2019-04-15	275,000	Private valuation	Broker quote	5%	5%	\$13,750	\$(13,750)
Royal Bank of Scotland Group PLC 3.058%, 2049-12-31	7,824,412	Private valuation	Broker quote	5%	5%	\$391,221	\$(391,221)
Standard Chartered PLC 2.625%, 2049-12-31	3,942,254	Private valuation	Broker quote	5%	5%	\$197,113	\$(197,113)
Standard Chartered PLC 3.125%, 2049-12-31	9,567,177	Private valuation	Broker quote	5%	5%	\$478,359	\$(478,359)
Standard Chartered PLC 1.650%, 2049-12-31	7,151,345	Private valuation	Broker quote	5%	5%	\$357,567	\$(357,567)

December 31, 2017							
Security Name	Fair Value	Valuation Technique	Unobservable Inputs	Reasonable Shift (+)	Reasonable Shift (-)	Change in Valuation (+)	Change in Valuation (-)
Clarity Trust Series D Medium Term Note 6.889%, 2019-04-15	\$275,000	Recent financing	Purchase price	5%	5%	\$13,750	\$(13,750)
Fusion Trust Series D Medium Term Note 6.889%, 2019-04-15	\$275,000	Recent financing	Purchase price	5%	5%	\$13,750	\$(13,750)

3. OFFSETTING OF FINANCIAL ASSETS AND LIABILITIES

As at December 31, 2018 and 2017

The following table shows the net impact of the Fund's statement of financial position if all set-off rights were exercised.

Financial Assets and Liabilities	Amounts Eligible for Offset			
	Gross Assets / (Liabilities) \$	Financial Instruments \$	Collateral received/paid \$	Net \$
December 31, 2018				
Derivative assets - Foreign exchange forward contracts	242,079	(242,079)	-	-
Derivative liabilities - Forward exchange forward contracts	(8,527,096)	242,079	-	(8,285,017)
December 31, 2017				
Derivative assets - Foreign exchange forward contracts	1,142,490	(399,809)	-	742,681
Derivative liabilities - Forward exchange forward contracts	(399,809)	399,809	-	-

4. SECURITIES LENDING TRANSACTIONS

The Fund has entered into a securities lending program with its custodian, RBC Investor Services Trust. The aggregate market value of all securities loaned by the Fund cannot exceed 50% of the assets of the Fund. The Fund will receive collateral of at least 102% of the value of the securities on loan. Collateral consists primarily of fixed income securities. As at December 31, 2018, there was \$15,378,629 (Collateral - \$15,686,202) of securities on loan (December 31, 2017 - \$6,857,245 (Collateral - \$6,994,392) of securities on loan).

Securities lending income reported in the Statements of Comprehensive Income is net of a securities lending charge which the Fund's custodian is entitled to receive. For the years ended December 31, securities lending income were as follows:

	December 31, 2018 (\$)	December 31, 2017 (\$)
Gross securities lending income	18,709	3,114
Securities lending charges	(6,549)	(927)
Net securities lending income	12,160	2,187
Withholding taxes on securities lending income	(2,415)	(60)
Net securities lending income received by the Fund	9,745	2,127
Security lending charges percentage of gross securities lending income	35%	30%

PICTON MAHONEY FORTIFIED INCOME FUND

FUND SPECIFIC NOTES (CONTINUED)

5. OTHER PRICE RISK

Using Beta as a measure of the relationship of the Fund's performance versus its index, if the blended index consisting of 75% BofA Merrill Lynch Global High Yield Index (hedged to Canadian dollars) and 25% BofA Merrill Lynch Global Corporate Index (hedged to Canadian dollars) were to increase or decrease by 10%, net assets would have increased or decreased by approximately \$38,443,160 (December 31, 2017 - \$23,418,282). In practice, the actual results may differ from this sensitivity analysis and the difference could be material.

6. CURRENCY RISK

Foreign currencies to which the Fund had exposure as at December 31, 2018 and 2017 were as follows:

FINANCIAL INSTRUMENTS					
December 31, 2018 Currency	Monetary \$	Non-Monetary \$	Forwards Currency Contracts \$	Total \$	Percentage of Net Assets %
United States Dollar	270,319,872	-	(266,215,136)	4,104,736	1.2%
European Euro	(7,889)	-	-	(7,889)	0.0%
British Pound	(195,795)	-	-	(195,795)	-0.1%
Net Exposure	270,116,188	-	(266,215,136)	3,901,052	1.1%

FINANCIAL INSTRUMENTS					
December 31, 2017 Currency	Monetary \$	Non-Monetary \$	Forwards Currency Contracts \$	Total \$	Percentage of Net Assets %
United States Dollar	143,395,301	855,260	(143,370,057)	880,504	0.4%
European Euro	3,518,022	-	(4,202,187)	(684,165)	-0.3%
Net Exposure	146,913,323	855,260	(147,572,244)	196,339	0.1%

If the Canadian dollar had strengthened or weakened by 5% in relation to all other currencies held in the investment portfolio, net assets would have decreased or increased by approximately \$195,053 (December 31, 2017 - \$9,817). In practice, the actual trading results may differ from this sensitivity analysis and the difference could be material.

The Fund may enter into forward currency contracts to manage currency risk.

7. INTEREST RATE RISK

If the yield curve had shifted in parallel by 1%, with all other variables held constant, net assets will increase or decrease by \$10,588,740 (December 31, 2017 - \$6,129,527). In practice, the actual trading results may differ from this sensitivity analysis and the difference could be material.

As at December 31, 2018 and 2017, the Fund's exposure to debt instruments by maturity were as follows

Debt Instruments by Maturity Date	December 31, 2018 (\$)		
	Long Positions	Short Positions	Total
Less than 1 year	10,906,528	(2,688,774)	8,217,754
1-3 years	21,615,150	(1,864,321)	19,750,829
3-5 years	96,583,204	(8,270,947)	88,312,257
Greater than 5 years	193,914,523	(14,799,767)	179,114,756
Total	323,019,405	(27,623,809)	295,395,596

Debt Instruments by Maturity Date	December 31, 2017 (\$)		
	Long Positions	Short Positions	Total
Less than 1 year	6,427,328	-	6,427,328
1-3 years	1,109,625	-	1,109,625
3-5 years	33,859,543	(1,582,156)	32,277,387
Greater than 5 years	140,653,158	(11,095,574)	129,557,584
Total	182,049,654	(12,677,730)	169,371,924

PICTON MAHONEY FORTIFIED INCOME FUND

FUND SPECIFIC NOTES (CONTINUED)

8. CREDIT RISK

The following table below shows debt as a percentage of net assets attributable to holders of redeemable units held under each credit rating. All counterparties to derivative contracts had a credit rating of A-1 or higher as at December 31, 2018 and December 31, 2017.

December 31, 2018				December 31, 2017			
Bond Ratings	Net	Long	Short	Bond Ratings	Net	Long	Short
A-	0.90%	0.90%	0.00%	AAA	-2.85%	0.00%	-2.85%
BBB+	5.83%	5.83%	0.00%	A	1.62%	1.62%	0.00%
BBB	3.05%	3.71%	-0.66%	BBB+	1.68%	1.68%	0.00%
BBB-	1.55%	1.55%	0.00%	BBB	4.74%	4.74%	0.00%
BB+	5.60%	5.95%	-0.35%	BBB-	5.75%	5.75%	0.00%
BB	15.29%	15.58%	-0.29%	BB+	3.65%	3.65%	0.00%
BB-	5.12%	5.12%	0.00%	BB	13.42%	13.42%	0.00%
B+	9.85%	10.19%	-0.34%	BB-	12.81%	13.79%	-0.98%
B	8.56%	10.57%	-2.01%	B+	7.11%	8.47%	-1.36%
B-	16.32%	18.68%	-2.36%	B	14.95%	15.24%	-0.29%
CCC+	0.12%	1.13%	-1.01%	B-	12.43%	13.36%	-0.93%
CCC	4.34%	5.08%	-0.74%	CCC+	3.39%	3.70%	-0.31%
NR	5.94%	5.94%	0.00%	NR	3.95%	3.95%	0.00%

The above credit ratings are obtained and disclosed from the rating services in the following hierarchical order: 1) Moody's; 2) Standard & Poor's; 3) Fitch; 4) Dominion Bond Rating Service, using first available. All cash is held with a financial institution with a minimum credit rating of A-1+.

9. CONCENTRATION RISK

The table below summarizes the Fund's concentration risk as a percentage of net assets attributable to holders of redeemable units as at December 31, 2018 and 2017.

Jurisdiction	% of Net Assets	
	December 31, 2018	December 31, 2017
Equities		
Canada	0.0%	0.7%
United States	0.0%	0.5%
Debt		
Canada	40.4%	23.9%
United States	25.8%	30.0%
International	17.0%	25.5%
Derivatives	-2.0%	0.5%

PICTON MAHONEY FORTIFIED INCOME FUND

FUND SPECIFIC NOTES (CONTINUED)

10. LIQUIDITY RISK

The tables below categorize the Fund's financial liabilities into relevant maturity groupings based on the remaining period to the contractual maturity date. The amount in the tables are the contractual undiscounted cash flows. Amounts due to holders of redeemable units are disclosed as net assets attributable to holders of redeemable units on the statement of financial position and are due on demand.

December 31, 2018 Financial Liabilities	On Demand \$	< 3 months \$	> 3 months \$	Total \$
Short positions	27,623,809	-	-	27,623,809
Distributions payable	1,585	-	-	1,585
Redemptions payable	168,838	-	-	168,838
Accrued liabilities and other payables	-	5,933,742	-	5,933,742
Derivative liabilities	8,943,176	-	-	8,943,176

December 31, 2017 Financial Liabilities	On Demand \$	< 3 months \$	> 3 months \$	Total \$
Short positions	13,771,052	-	-	13,771,052
Distributions payable	81	-	-	81
Redemptions payable	173,805	-	-	173,805
Accrued liabilities and other payables	-	461,609	-	461,609
Derivative liabilities	460,103	-	-	460,103

11. FUND UNIT TRANSACTIONS

For the years ended December 31

	2018					2017				
	Class A	Class F	Class FT	Class T	Class I	Class A	Class F	Class FT	Class T	Class I
Units issued and outstanding, beginning of year	2,311,429	12,909,550	1,009,003	121,518	1,838,343	278,228	1,458,367	202,954	33,059	569,046
Units issued	2,231,192	16,072,743	2,122,815	128,598	782,524	2,126,147	11,761,139	854,984	101,736	1,214,584
Units reinvested	97,143	438,461	-	-	78,783	48,980	219,746	72	-	54,713
Units redeemed	(750,536)	(5,582,034)	(372,588)	(47,763)	-	(141,926)	(529,702)	(49,007)	(13,277)	-
Units issued and outstanding, end of year	3,889,228	23,838,720	2,759,230	202,353	2,699,650	2,311,429	12,909,550	1,009,003	121,518	1,838,343
Weighted average number of units held during the year	3,459,626	21,952,123	1,902,741	179,592	2,421,474	1,079,888	5,742,334	614,050	86,356	1,158,507

12. COMMISSIONS

For the years ended December 31 (in \$000)

	2018	2017
Brokerage commissions	802	125
Soft Dollar commissions	20	1

13. TAX LOSS CARRY FORWARDS

As at December 31 (in \$000)

	2018
Net capital losses carry forward	8,070
Non-capital losses carry forward	-

PICTON MAHONEY FORTIFIED INCOME FUND NOTES TO THE FINANCIAL STATEMENTS

As at December 31, 2018 and December 31, 2017

1. GENERAL INFORMATION

Picton Mahoney Fortified Income Fund (the "Fund") is an open-ended mutual trust established under the laws of the Province of Ontario pursuant to a trust agreement dated October 21, 2015 (the "Trust Declaration"). The Fund commenced operations on October 29, 2015. Picton Mahoney Asset Management acts as manager (the "Manager"), portfolio advisor (the "Portfolio Advisor"), and trustee (the "Trustee") for the Fund pursuant to the Trust Declaration. The Manager is responsible for the day-to-day business of the Fund, including the management of the Fund's investment portfolio. The address of the Fund's registered office is 33 Yonge Street, Suite 830, Toronto, Ontario, M5E 1G4. The financial statements are presented in Canadian dollars (CAD). These financial statements were authorized for issue by the Manager on March 26, 2019.

On October 29, 2015, 15,001 Class A units of the Fund were issued to the Manager of the Fund, for cash consideration of CAD \$10.00 per unit.

The Fund may issue an unlimited number of classes or series and may issue an unlimited number of units of each class or series. The Fund has created Class A, Class F, Class FT, Class T and Class I units.

Class A units are available to all investors. Class F units are available to investors who are enrolled in a dealer sponsored fee for service or wrap program and who are subject to an annual asset based fee rather than commissions on each transaction or, at the discretion of the Manager, any other investor for whom the Manager does not incur distribution costs. Class FT units are available to investors who are enrolled in a dealer sponsored fee for service or wrap program and who are subject to an annual asset based fee rather than commissions on each transaction or, at the discretion of the Manager, any other investor for whom the Manager does not incur distribution costs. Class FT units are also designed to provide cash flow to investors by making monthly distributions of cash. Class T units are available to all investors and are designed to provide cash flow to investors by making monthly distributions of cash. Class I units are available to institutional investors or to other investors on a case-by-case basis, all at the discretion of the Manager.

As at December 31, 2018 and 2017, the Fund currently has 5 Classes of Units: Class A, Class F, Class FT, Class T, and Class I. The investment objective of the Fund is to maximize total return to unitholders through income and capital appreciation by investing primarily in global income securities while mitigating capital loss by engaging in hedging strategies for downside risk protection.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The following is a summary of the significant accounting policies of the Fund.

(a) Basis of Preparation

These financial statements have been prepared in accordance with those requirements of International Financial Reporting Standards. The financial statements have been prepared under the historical cost convention, as modified by the revaluation of financial assets and financial liabilities (including derivative financial instruments) at fair value through profit or loss.

(b) Classification

(i) Assets

The Fund classifies its investments based on both the Fund's business model for managing those financial assets and the contractual cash flow characteristics of the financial assets. The portfolio of financial assets is managed and performance is evaluated on a fair value basis. The Fund

is primarily focused on fair value information and uses that information to assess the assets' performance and to make decisions. The Fund has not taken the option to irrevocably designate any equity securities as fair value through other comprehensive income. The contractual cash flows of the Fund's debt securities are solely principal and interest, however, these securities are neither held for the purpose of collecting contractual cash flows nor held both for collecting contractual cash flows and for sale. The collection of contractual cash flows is only incidental to achieving the Fund's business model's objective. Consequently, all investments are measured at fair value through profit or loss.

(ii) Liabilities

The Fund makes short sales in which a borrowed security is sold in anticipation of a decline in the market value of that security, or it may use short sales for various arbitrage transactions. Short sales are held for trading and are consequently classified as financial liabilities at fair value through profit or loss. Derivative contracts that have a negative fair value are presented as liabilities at fair value through profit or loss. As such, the Fund classifies all of its investment portfolio as financial assets or liabilities as fair value through profit or loss. The Fund's policy requires the Manager to evaluate the information about these financial assets and liabilities on a fair value basis together with other related financial information.

(c) Fair Value Measurements

The Fund utilizes a three tier hierarchy as a framework for disclosing fair value based on inputs used to value the Fund's investments. The three levels of the fair value hierarchy are as follows:

- Level 1 - Quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 - Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices); and
- Level 3 - Inputs for the asset or liability that are not based on observable market data (unobservable inputs).

Fair values are classified as Level 1 when the related security or derivative is actually traded and a quoted price is available. If an instrument classified as Level 1 subsequently ceases to be actively traded, it is transferred out of Level 1. In such cases, instruments are reclassified into Level 2, unless the measurement of its fair value requires the use of significant unobservable inputs, in which case it is classified as Level 3. The Fund's policy is to recognize transfers into and out of the fair value hierarchy levels as of the date of the event or change in circumstances giving rise to the transfer.

(d) Valuation of Investments and Derivatives

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value of financial assets and liabilities traded in active markets, which include equities, bonds, options, warrants, and exchanged traded funds are based on quoted market prices at the close of trading on the reporting date. The Fund uses the last traded market price for both financial assets and financial liabilities where the last traded price falls within that day's bid-ask spread. In circumstances where the last traded price is not within the bid-ask spread, the Manager determines the point within the bid-ask spread that is most representative of fair value based on the specific facts and circumstances.

Securities not listed on any recognized public securities exchange are valued in the same manner based on available public quotations from recognized dealers in such securities. If market quotations are not readily available, securities will be valued at fair value as determined in good faith by or under the

PICTON MAHONEY FORTIFIED INCOME FUND

NOTES TO THE FINANCIAL STATEMENTS

As at December 31, 2018 and December 31, 2017

supervision of the Manager. The cost of investments represents the amount paid for each security and is determined on an average cost basis.

The fair value of financial assets and liabilities that are not traded in an active market, including over-the-counter derivatives, is determined using valuation techniques. The Fund uses a variety of methods and makes assumptions that are based on market conditions existing at each reporting date. Valuation techniques include the use of comparable recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis, option pricing models and others commonly used by market participants and which make the maximum use of observable inputs.

Models use observable data, to the extent practicable. However, areas such as credit risk (both own and counterparty), volatilities and correlations require the Manager to make estimates. Changes in assumptions about these factors could affect the reported fair values of financial instruments. The Fund considers observable data to be market data that is readily available, regularly distributed and updated, reliable and verifiable, not proprietary, and provided by independent sources that are actively involved in the relevant market.

Investment fund units held as investments are valued at their respective Net Asset Values on the relevant valuation dates as reported by the investment fund manager, as these values are the most readily and regularly available.

Warrants, options, and futures that are not listed on any recognized public securities exchange are valued using the Black-Scholes model and based on observable market inputs.

Foreign exchange forward contracts are valued on each valuation day based on the difference between the value of the contract on the date the contract originated and the value of the contract on the valuation day.

The difference between fair value and the average cost is shown as the change in unrealized appreciation (depreciation) on investments, options and foreign exchange forward contracts.

Other financial assets (held for collection) and other financial liabilities are measured at amortized cost. Under this method, financial assets and liabilities reflect the amount required to be received or paid, discounted, where appropriate at the contract's effective interest rate. Due to their short-term nature, the fair value of other financial assets and financial liabilities carried at amortized cost approximates their carrying amount.

Receivable for investments sold and payable for investments purchased

Receivable for investments sold and payable for investments purchased represent trades that have been contracted for but not yet settled or delivered on the statements of financial position dates. These amounts are recognized initially at fair value and subsequently measured at amortized cost. At each reporting date, the Funds measure the loss allowance on receivable for investments sold and payable for investments purchased at an amount equal to the lifetime expected credit losses if the credit risk has increased significantly since initial recognition. If, at the reporting date, the credit risk has not increased significantly since initial recognition, the Funds measure the loss allowance at an amount equal to 12-month expected credit losses. Significant financial difficulties of the counterparty, probability that the counterparty will enter bankruptcy or financial reorganization, and default in payments are all considered indicators that a loss allowance may be required. If the credit risk increases to the point that it is considered to be credit impaired, interest income will be calculated based on the gross carrying amount adjusted for the loss allowance. A significant increase in credit risk is defined by the Manager as any contractual payment which is more than 30 days past due or a significant deterioration in a counterparty credit quality. Any contractual payment which is more than 90 days past due is considered credit impaired.

(e) Cash

Cash is comprised of cash on demand deposit with a Canadian financial institution and is stated at fair value.

(f) Investment Transactions and Income Recognition

Investment transactions are accounted for as of the trade date. Expenses are recorded on an accrual basis. Dividend income is recorded on the ex-dividend date. The interest for distribution purposes shown on the statement of comprehensive income represents the coupon interest received by the Fund accounted for on an accrual basis. The Fund does not amortize premiums paid or discounts received on the purchase of fixed income securities except for zero coupon bonds which are amortized on a straight line basis. Realized gains and losses on sale of investments and unrealized appreciation and depreciation in investments are determined on an average cost basis. Average cost does not include amortization of premiums or discounts on fixed income securities with the exception of zero coupon bonds. Income, common expenses and gains (losses) are allocated to each Class of the Fund based on the Class' prorated share of total Net Asset Value.

Distributions received from investment fund holdings are recognized by the Fund in the same form in which they were received from the underlying funds and are recognized on the distribution date.

(g) Valuation of Fund Units

The Fund's net asset value is calculated at the close of regular trading, normally 4:00pm (Eastern Time), on a day the Toronto Stock Exchange ("TSX") is open (a "Valuation Day"). The net asset value of the Fund will be calculated in Canadian dollars and the units of the Fund are denominated in Canadian dollars.

The Fund's units are divided into the Class A, Class F, Class FT, Class T and Class I units. Each class is divided into units of equal value. When you invest in the Fund, you are purchasing units of a specific class of the Fund.

A separate net asset value per unit is calculated for each class of units (the "Unit Price"). The Unit Price is the price used for all purchases, switches, re-classifications and redemptions of units of that class (including purchases made on the reinvestment of distributions). The price at which units are issued or redeemed is based on the next applicable Unit Price determined after the receipt of the purchase or redemption order.

The Unit Price of each class of the Fund is calculated by taking the fair value of all the investments and other assets allocated to the class and subtracting the liabilities allocated to that class. This gives us the net asset value for the class. The Unit Price for the class is obtained by dividing the net asset value for the class by the total number of units of the class that investors in a Fund are holding.

Although the purchases and redemptions of units are recorded on a class basis, the assets attributable to all of the class of a Fund are pooled to create one fund for investment purposes.

Each class pays its proportionate share of fund costs in addition to its management fee and performance fee. The difference in fund costs, management fees and performance fees between each class means that each class has a different Unit Price.

Any purchase, switch, reclassification or redemption instruction received after 4:00pm (Eastern Time) on Valuation Day will be processed on the next Valuation Day.

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(h) Foreign Currency Translation

The Fund's functional and presentation currency is Canadian dollars. The fair value of foreign investments and other assets and liabilities are translated into Canadian dollars at the exchange rates prevailing at the close of each valuation day. Purchases and sales of foreign securities and the related income and expenses are translated into Canadian dollars at rates of exchange prevailing on the respective dates of such transactions.

Foreign exchange gains and losses relating to cash and other assets and liabilities are presented as 'Foreign currency gain (loss) on cash and other assets and liabilities' and those relating to other financial assets and liabilities are presented within 'Net realized gain (loss) on investments, options, and foreign exchange forward contracts and 'Change in unrealized appreciation (depreciation) on investments, options, and foreign exchange forward contracts.

(i) Increase (decrease) in Net Assets Attributable to Holders of Redeemable Units per Unit

Increase (decrease) in net assets attributable to holders of redeemable units per unit of each Class of the Fund is determined by dividing the net increase in net assets attributable to holders of redeemable units from each Class of Units by the weighted average number of Units outstanding of that Class during the year.

(j) Transaction Costs

Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of an investment, which include fees and commissions paid to agents, advisors, brokers and dealers, levies by regulatory agencies and securities exchange, and transfer taxes and duties. Such costs are expensed and included in "Transaction costs" in the Statement of Comprehensive Income.

(k) Securities Lending Transactions

The Fund may enter into securities lending transactions. These transactions involve the temporary exchange of securities as collateral with a commitment to deliver the same securities on a future date. Income is earned from these transactions in the form of fees paid by the counterparty and, in certain circumstances, interest paid on securities held as collateral. Income earned from these transactions is recognized on an accrual basis and included in the Statements of Comprehensive Income.

The Fund has entered into a securities lending program with their custodian, RBC Investor Services Trust. The aggregate market value of all securities loaned by the Fund cannot exceed 50% of the assets of the Fund. The Fund will receive collateral of at least 102% of the value of the securities on loan. Collateral will generally be comprised of cash and obligations of, or guaranteed by, the Government of Canada or a province thereof, or a permitted supranational agency as defined in National Instrument 81-102. Securities lending income reported in the Statements of Comprehensive Income is net of a securities lending charge which the Fund's custodian, RBC Investor Services Trust, is entitled to receive.

(l) IFRS 9, Financial Instruments

IFRS 9 'Financial Instruments' addresses the classification, measurement and derecognition of financial assets and liabilities and replaces the multiple classification and measurement models in IAS 39.

Classification and measurement of debt assets is driven by the entity's business model for managing the financial assets and the contractual cash flow characteristics of the financial assets. A debt instrument is measured at amortized cost if the objective of the business model is to hold the financial asset for the collection of the contractual cash flows and the contractual

cash flows under the instrument solely represent payments of principal and interest (SPPI). A debt instrument is measured at fair value through other comprehensive income if the objective of the business model is to hold the financial asset both to collect contractual cash flows from SPPI and to sell. All other debt instruments must be recognized at fair value through profit or loss. An entity may however, at initial recognition, irrevocably designate a financial asset as measured at fair value through profit or loss if doing so eliminates or significantly reduces a measurement or recognition inconsistency. Derivative and equity instruments are measured at fair value through profit or loss unless, for equity instruments not held for trading, an irrevocable option is taken to measure at fair value through other comprehensive income. IFRS 9 also introduces a new expected credit loss (ECL) impairment model.

IFRS 9 has been applied by the Fund and did not result in a change to the classification or measurement of financial instruments. The Fund's investment portfolio continues to be classified as fair value through profit or loss and other financial assets which are held for collection continue to be measured at amortized cost. There was no material impact on adoption from the application of the new impairment model.

(m) Structured Entities

A structured entity is an entity that has been designed so that voting or similar rights are not the dominant factor in deciding who controls the entity, such as when any voting rights relate to administrative tasks only and the relevant activities are directed by means of contractual arrangements. The Manager has determined that all of the underlying funds in which the Funds invest are unconsolidated structured entities. In making this determination, the Manager evaluated the fact that decision making about the underlying funds' activities is not governed by voting or similar rights held by the Funds and other investors in any underlying funds. The Fund invests in mortgage-related and other asset-backed securities. These securities include mortgage pass-through securities, collateralized mortgage obligations, commercial mortgage-backed securities, asset-backed securities, collateralized debt obligations and other securities that directly or indirectly represent a participation in, or are secured by and payable from, mortgage loans on real property. The Manager has determined that such securities are also unconsolidated structured entities. The debt and equity securities issued by these securities may include tranches with varying levels of subordination. These securities may provide a monthly payment which consists of both interest and principal payments.

Mortgage-related securities are created from pools of residential or commercial mortgage loans, including mortgage loans made by savings and loan institutions, mortgage bankers, commercial banks and others. Asset-backed securities are created from many types of assets, including auto loans, credit card receivables, home equity loans, and student loans.

The carrying value of mortgage related and other asset-backed securities are disclosed in the Schedule of Investment Portfolio. The fair value of such securities as at December 31, 2018 represents the maximum exposure in losses at that date. The change in fair value of mortgage related and other asset backed securities are included in the Statement of Comprehensive Income and Change in unrealized appreciation (depreciation) on investments, options, and foreign exchange forward contracts.

(n) Offsetting

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis or realise the asset and settle the liability simultaneously. The legally enforceable right must not be contingent on future events and must be enforceable in the normal course of business and in the event of default, insolvency or bankruptcy of the company or the counterparty.

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3. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

These financial statements, include estimates and assumptions by management that affect the reported amounts of certain assets and liabilities at the date of the financial statements and the reported amounts of certain revenue and expenses during the period. Actual results could differ from these estimates. The following discusses the most significant accounting judgments and estimates that the Fund has made in preparing the financial statements.

Fair value measurement of derivatives and securities not quoted in an active market

The Fund holds financial instruments that are not quoted in active markets, including derivatives. Fair values of such instruments are determined using recognized valuation techniques and may be determined using reputable pricing sources or indicative prices from market makers.

Where no market data is available, the Fund may value positions using its own models, which are based on valuation methods and techniques generally recognized as standard within the industry. The models used to determine fair values are validated and periodically reviewed by the Manager, independent of the party that created them.

Models use observable data, to the extent practicable. However, areas such as credit risk (both own and counterparty), volatilities and correlations require the Manager to make estimates. Changes in assumptions about these factors could affect the reported fair values of financial instruments. The Fund considers observable data to be market data that is readily available, regularly distributed and updated, reliable and verifiable, not proprietary, and provided by independent sources that are actively involved in the relevant market.

4. FINANCIAL INSTRUMENTS RISKS

The Fund is exposed to various financial risks, including market risk (which includes currency risk, interest rate risk and price risk), credit risk and liquidity risk. The investment team reviews and rebalances the portfolio on a regular and ongoing basis to maintain the risk reward targets. Portfolios within each strategy are reviewed relative to each other and to their benchmark. Active industry and security allocations are analyzed. All investments may result in a risk of loss of capital.

Please refer to the Fund Specific Notes for details of the Fund's financial instruments risks.

Price risk:

The Fund trades in financial instruments, taking positions in traded and over-the-counter instruments which may include derivatives. As of December 31, 2018 and December 31, 2017, the Fund held or had exposure to long and short equity positions in publicly traded companies whose securities are actively traded on a recognized public exchange. Equities are susceptible to price risk arising from uncertainties about future prices of those instruments (other than those arising from interest rate risk or currency risk).

Short sales entail certain risks, including the risk that a short sale of a security may expose a Fund to losses if the value of the security increases. A short sale creates the risk of a theoretically unlimited loss, in that the price of the underlying security could theoretically increase without limit, thus increasing the cost to the Fund of buying those securities to cover the short position. In addition, a short sale by a Fund requires the Fund to borrow securities in order that the short sale may be transacted. There is no assurance that the lender of the securities will not require the security to be paid back by a Fund before the Fund wants to do so, possibly requiring the Fund to borrow the security elsewhere or purchase the security on the market at an unattractive price. Moreover, the borrowing of securities entails the payment of a borrowing fee. The borrowing fee may increase during the borrowing period, adding to the expense of the short sale strategy. There

is also no guarantee that the securities sold short can be repurchased by a Fund due to supply and demand constraints in the equity markets. Finally, in order to maintain the appropriate ratios between the long portfolio and the short portfolio of a Fund, the Manager may be required to buy or sell short securities at unattractive prices. The maximum risk resulting for financial instruments held long is determined by the fair value of the instrument.

Currency risk:

Currency risk is the risk that the cash and securities held by the Fund as well as due to and due from broker balances may be valued in or have exposure to currencies other than the Canadian dollar which is the functional currency of the Fund. The prices of the foreign securities are denominated in foreign currencies which are converted to the Fund's functional currency for determining fair value and, accordingly, each Class Net Asset Value will be affected by fluctuations in the value of such foreign currencies relative to the Canadian dollar. The Fund may enter into forward currency contracts to manage currency risk.

Interest rate risk:

Interest rate risk arises when a fund invests in interest-bearing financial instruments and from the possibility that changes in the prevailing levels of market interest rates will affect future cash flows or fair values of such financial instruments. There is minimal fair value sensitivity to interest rate fluctuations on any cash and cash equivalents invested at short-term market interest rates. Market prices may also be affected by changes in market interest rates. Also, changes in the market interest rate may affect the borrowing expenses of the short positions held by the Fund. Refer to Note 7 within the fund specific notes for the fund exposure.

Credit risk:

Credit risk is the risk that the counterparty to a financial instrument will fail to discharge an obligation or commitment that it has entered into with the Fund. All transactions in listed securities are settled/paid for upon delivery using approved brokers. The risk of default is considered minimal, as delivery of securities sold is only made once the broker has received payment. Payment is made on a purchase once the securities have been received by the broker. The trade will fail if either party fails to meet its obligation. However, there are risks involved in dealing with custodians or prime brokers who settle trades and in rare circumstances, the securities and other assets deposited with the custodian or broker may be exposed to credit risk with regard to such parties. In addition, there may be practical problems or time delays associated with enforcing the Fund's rights to its assets in the case of an insolvency of any such party.

The Fund is exposed to credit risk. For other financial assets at amortized cost, the Manager considers both historical analysis and forward looking information in determining any expected credit loss. At December 31, 2018 and 2017, all amounts receivable for investments sold, subscriptions receivable, dividends receivable, interest and other receivable, deposits with brokers for securities sold short, and cash are held with counterparties with a good credit quality and are due to be settled within one week. The Manager considers the probability of default to be close to zero as these instruments have a low risk of default and the counterparties have a strong capacity to meet their contractual obligations in the near term. As a result, no loss allowance has been recognized based on 12-month expected credit losses as any such impairment would be wholly insignificant to the Fund.

The Fund primarily invests in fixed income securities and is therefore exposed to the credit risk of the underlying fixed income portfolio. Refer to Note 8 within the fund specific notes for the fund exposure.

Liquidity risk:

Liquidity risk is the risk that a Fund will not be able to generate sufficient cash availability to execute its payment obligations. The Fund primarily invests in liquid securities that are readily realizable in an active market which is essential if the Fund is required to fund daily redemptions in the

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course of operations. The Fund from time to time may invest in restricted securities through private placements. However, this type of investment does not constitute a significant percentage of the Fund's Net Asset Value. The Fund may also maintain a cash reserve to accommodate normal-type redemptions. All liabilities of the Fund mature in one year or less with the exception of bonds sold short. At the Manager's discretion, bonds sold short can be repurchased to settle the liability immediately. Redeemable units are redeemable on demand at the holder's option. However, the Manager does not expect that the contractual maturity will be representative of the actual cash outflows, as holders of these instruments typically retain them for a longer period.

Concentration risk:

Concentration risk arises as a result of the concentration of financial instrument exposures within the same category, whether it is geographic region, asset type or industry sector.

5. CAPITAL MANAGEMENT

The capital of a Fund is represented by the issued and outstanding units and the net asset value attributable to participating unitholders. The Manager utilizes the capital of the Fund in accordance with the Fund's investment objectives, strategies and restrictions, as outlined in the Fund's prospectus, while maintaining sufficient liquidity to meet normal redemptions. The Fund does not have any externally imposed capital requirements.

6. REDEEMABLE UNIT TRANSACTIONS

The Fund is permitted to have an unlimited number of Classes of Units having such terms and conditions as the Manager may determine. Additional Classes may be offered in future on different terms, including having different fee and dealer compensation terms and different minimum subscription levels. Each Unit of a Class represents an undivided ownership interest in the Net Asset Value of the Fund attributable to that Class of Units.

Investors may be admitted to the Fund or may acquire additional Units on a daily basis. Units of the Fund are offered at the Class Net Asset Value per Unit calculated as of the applicable Valuation Date. The minimum initial investment in the Fund is \$2,000 for all Classes and the Manager has the discretion to accept a lesser initial subscription, provided, in each case, that the issuance of Units in respect of such subscription shall otherwise be exempt from the prospectus requirements of applicable securities legislation. Subsequent investments are subject to an additional minimum investment of CAD \$500 subject to applicable securities legislation.

The capital of the Fund is represented by issued redeemable Units with no par value. The Units are entitled to distributions, if any, and to payment of a proportionate share based on the Fund's Net Asset Value per Unit upon redemption. The Fund has no restrictions or specific capital requirements on the subscriptions and redemptions of Units other than as described above. The relevant movements are shown on the Statement of Changes in Net Assets Attributable to Holders of Redeemable Units and in the Fund Specific Notes of each Fund.

IAS 32, *Financial Instrument – Recognition and Measurement*, requires that units of an entity that include a contractual obligation for the issuer to repurchase or redeem them for cash or another financial asset be classified as financial liability. The Fund's units have been classified as financial liabilities. The Fund has multiple series of units that carry different management fee rates and therefore do not have identical features. As all units are equally subordinate, the units also would not meet the requirements of IAS 32 and therefore do not meet the conditions to be classified as equity.

7. DISTRIBUTIONS

The Fund intends to distribute net income and net realized capital gains, if any, to Unitholders at the end of each taxation year to ensure that the Fund is not liable for income tax under Part I of the Income Tax Act (Canada) (the "Act"), after taking into account any loss carry forwards and capital gains refunds.

All annual distributions paid on Class A, Class F and Class I units will be automatically reinvested in additional units. For Class FT and Class T units, unitholders will receive a target monthly distribution at an initial rate of 5% per annum. The target rate of monthly distribution will be reset at the beginning of each calendar year to provide a target yield based on the net asset value per Class FT unit or Class T unit as at December 31 of the prior year. Throughout the year, such monthly distributions to unitholders will be composed of net income, net capital gains and/or a return of capital. All distributions on Class FT and Class T units will be paid in cash.

8. TAXATION

The Fund qualifies as a "mutual fund trust" and will be subject to tax in each taxation year under Part I of the Act on the amount of its income for the year, including net realized taxable capital gains, less the portion thereof that it claims in respect of the amount paid or payable to Unitholders in the year. The Fund deducts, in computing its income in each taxation year, the full amount available for deduction in each year and, therefore, provided the Fund makes distributions in each year of its net income and net realized capital gains, it will generally not be liable in such year for any tax on its net income or profit under Part I of the Tax Act. As a result, the Fund does not record income taxes. Since the Fund does not record income taxes, the tax benefit of capital and non-capital losses has not been reflected in the Statement of Financial Position as a deferred tax asset.

Non-capital losses have expiry periods of up to 20 years and can be offset against future taxable income. Net capital losses can be carried forward indefinitely and offset against future taxable capital gains. For tax loss carry forward information, please refer to Note 13 in the Fund Specific Notes.

The Fund is required to include in income for each taxation year any dividends received by it in a taxation year and all interest that accrues to it to the end of the year, or becomes receivable or is received by it before the end of the year, except to the extent that such interest was included in computing its income for a preceding taxation year. In computing its income, the Fund will take into account any loss carry-forwards, any capital gains refund and all deductible expenses, including management fees.

Gains and losses realized by the Fund on the disposition of securities will generally be reported as capital gains and capital losses. The Fund has elected under section 39(4) of the Tax Act so that all gains or losses realized on the disposition of securities that are "Canadian securities" (as defined in the Tax Act), including Canadian securities acquired in connection with short sales, are deemed to be capital gains or losses to the Fund. Generally, gains and losses realized by the Fund from derivative securities and in respect of short sales of securities (other than Canadian securities) will be treated as income and losses of the Fund, except where a derivative is used to hedge securities held on capital account provided there is sufficient linkage and subject to detailed rules in the Tax Act. Whether gains or losses realized by the Fund in respect of a particular security (other than a Canadian security) is on income or capital account will depend largely on factual considerations. Losses incurred by the Fund in a taxation year cannot be allocated to unitholders, but may be deducted by the Fund in future years in accordance with the Tax Act.

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9. OPERATING EXPENSES

The Manager is responsible for the day-to-day operations of the Fund. The Fund pays its own operating expenses, other than advertising costs and costs of dealer compensation programs, which are paid by the Manager. Operating expenses include, but are not limited to, brokerage commissions and fees, taxes, audit and legal fees, fees of the members of the Independent Review Committee ("IRC"), costs and fees in connection with the operation of the IRC, safekeeping and custodial fees, interest expenses, operating, administrative and systems costs, investor servicing costs and costs of financial and other reports to investors, as well as prospectuses, annual information forms and fund facts.

With the exception of Class specific expenses, all other expenses are allocated to each Class of the Fund based on the Class' pro-rated share of total Net Asset Value of the Fund. The Manager may from time to time waive any portion of the fees and reimbursement of expenses otherwise payable to it, but no such waiver affects its right to received fees and reimbursement of expenses subsequently accruing to it.

10. RELATED PARTY TRANSACTIONS

(a) Management Fees

The Manager receives a management fee payable for providing its services to the Fund. The management fee varies for each class of units. The management fee is calculated and accrued daily based on a percentage of the net asset value of the class of units of the Fund, plus applicable

taxes, and is payable on the last business day of each calendar quarter. This fee differs among the classes of units of the Fund. The annual management fee payable by the Fund to the Manager on Class A units is 2.00%, on Class F units is 1.00%, on Class FT units is 1.00%, and on Class T units is 2.00%. The management fee for Class I units of the Fund is negotiated by the investor and paid directly by the investor, and would not exceed the management fee payable on Class A units of the Fund.

(b) Performance Fees

The Manager receives a performance fee payable in respect of each class of units of the Fund. The performance fee is equal to the daily net asset value of the class of units of the Fund during the calendar quarter multiplied by 20% of the amount by which the total return of the class of units exceeds the total percentage increase or decrease in the blended benchmark consisting of 75% BofA Merrill Lynch Global High Yield Index (hedged to Canadian dollars) and 25% BofA Merrill Lynch Global Corporate Index (hedged to Canadian dollars) (the "Performance Fee Index") since the end of the period for which the last performance fee was paid. If at any time the total return of the class of units of the Fund is less than its Performance Fee Index, then no performance fee will be payable until the total return of the class of units of the Fund relative to its Performance Fee Index has exceeded the amount of the deficiency calculated on a percentage basis. Investors in Class I units may negotiate a different performance fee than the one described herein or no performance fee at all. Any performance fee for Class I units will be paid directly to the Manager.

**THINK AHEAD.
STAY AHEAD.**



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