CAPSTONE PRIVATE HIGH INCOME POOL

Q1 Commentary

MARCH 31, 2024

AT A GLANCE

- Non-traditional debt and equity income strategies
- Globally diversified
- Monthly liquidity*
- Low correlation to bond and stock markets
- $86 MM AUM
- Current price: $10.7232 (Series IH)

MARKET & POOL UPDATE

2024 started strong for the equity markets with the S&P/TSX Composite TR Index returning 6.6% YTD while the bond market (represented by the iShares Core Canadian Universe Bond Index ETF) is down 1.33% YTD. The rhetoric going into 2024 is that the Bank of Canada is prepared to cut rates in response to encouraging inflation data from the last two months and while this hasn't yet happened, we expect it to be a strong possibility, perhaps as early as June. How this may play out in the highly correlated traditional markets is difficult to predict. For this reason, there remains a compelling argument for the inclusion of uncorrelated non-traditional assets such as the Capstone Private High Income Pool (CPHIP) in order to enhance true portfolio diversification.

CPHIP returned 0.57% for the month of March (before fees) and 1.74% YTD of which our investment in US mortgages, approximately 65% of the Fund, was the principal contributor. While this large exposure has been a benefit to the Pool, the Investment Management Team is aware of the risks associated with over-concentration and as such are currently looking to other opportunities that would increase diversification while not detracting from the intended long-term annualized target rate of return of 8% before fees. Whereas some borrowers within the strategy have experienced technical defaults due to breaches in debt service ratio covenants, equity sponsors have been forthcoming in injecting additional capital ensuring that even those technically impaired loans have contributed positively to performance..

The capitalization rate ("cap rate"), is the measure of a property's income over its total value, and these increased across North America in 2023. Despite elevated cap rates, property prices increased in both the US and Canada in 2023 given the surge in demand for housing. Yet, the risk of further increases in cap rates persists, hinging on central banks' willingness or ability to lower or maintain interest rates. In CPHIP's largest investment, a stress test of the portfolio was conducted to quantify the impact of an elevated cap rate environment. It found that given a 100-bps increase in cap rates from December 2023 levels, loan-to-values (the percentage of debt secured on a property as a percentage of its total value), did not exceed an average of 73% in any of the real estate segments where the portfolio is exposed. In short, there is a sufficient equity cushion within each of the properties to recover values in the event of default. Moreover, default rates within the asset continue to remain low at 6.8% at year-end. Outside of one isolated instance, the strategy experienced no defaults in its real estate investments in 2023.

Our aviation and marine positions continue to perform in line with expectations amidst increasing materials costs related to the building of new ships and planes. These strategies are currently fully committed, and the leases have been stable. We remain confident that these positions will provide good value to this Pool through 2024.

If you are interested in investing, please contact your Portfolio Manager directly.

PERFORMANCE (Gross of Fees)

Performance figures are those of Series IH units as of March 31, 2024. Performance is annualized for periods longer than one year.

1 MO.	3 MO.	6 MO.	1 YR.	2 YR.	3 YR.	INCEPTION*
0.57%	1.74%	3.99%	8.06%	7.83%	8.19%	8.10%

*Annualized as of first trade date September 30, 2019.

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