

PALOS

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Weekly Commentary

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By Charles Marleau, CIM

Quebecor: The Kings of Quebec Content

Quebecor Inc. (TSX: QBR/B) is a Montreal based communications giant that holds assets of Quebecor Media (QMI). Operations are heavily concentrated in Quebec. The company has a market cap of roughly \$7.5 billion and is focused on three distinct segments.

The Telecommunications segment, which operates under the Videotron moniker, is the company's largest source of free cash flow (FCF). Videotron provides internet, wireless, telephone, and cable services to the Quebec marketplace. In 2017, internet revenues topped its traditional cable revenues for the first time. The company intends to capitalize on service bundling, expansion into the discount internet market, migration to internet protocol TV (IPTV), and the adoption of 5G technology. At a recent conference on Quebec based companies, management stated that mobility and 5G adoption will be primary drivers of growth while further stating that market share in the Quebec wireless market has reached 19%. Whole home connectivity is being driven by Videotron's "Helix" platform.

Media, which includes conventional television through ownership of the TVA French language network and the magazine publishing business, is facing a challenging environment as advertising transitions away from traditional TV and print. The newspaper segment sees similar challenges. It is given that a consumer driven preference for streaming and internet-based content will be sustained. This is evidenced by the incredible growth in companies like Netflix, Spotify, and Apple TV. However, its not just the technology that has changed. To succeed, these companies require an extensive library of quality content in order to satisfy customer appetites. In this regard, QBR is in the enviable position of owning an impressive amount of top notch, French language content. We recently saw the launch of "Culture d'ici" which aims to strengthen a loyal customer base and monetize QBR's domination in Francophone cinema, programming, books, magazines, and music. As the saying goes; "content is King!"

There has been recent speculation surrounding a potential Quebecor investment in another iconic Quebec brand - The Cirque de Soleil (CdS). In 2019, private equity interests which includes the Caisse de dépôt et placement du Québec (CDPQ) were considering an initial public offering for CdS. However, the likelihood of an IPO in 2020 remains questionable as the pandemic and shutdown have been particularly damaging for the Cirque's financials. Vanishing revenues and questionable growth initiatives have seen the Cirque's fortunes

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in decline for years. While Quebecor may view a CdS acquisition as an opportunity to diversify outside of Quebec, investors have a legitimate concern that QBR might “overpay” and I believe this has weighed on the recent price of QBR shares.

The question at hand is not so much whether the CdS is an attractive asset (it is), but whether an interest could be acquired at a good price? This concern is understandable as we have previously seen companies “overpay” for assets and when this happens, it often takes years to recover. However, after speaking to Hugues Simard, CFO of QBR, I am assured that management will not overbid for Cirque du Soleil. Management is aware of investor concerns and QBR seems committed to moving forward with a conservative approach. This could potentially center on acquiring an interest through a debt arrangement rather than an outright purchase. This makes sense as owning debt would provide primary creditor protection while allowing for some form of ownership, a win-win scenario.

With growth in consumer demand for wireless streaming and high-quality content, I believe Quebecor is in a strong position to capitalize on this generational trend.

Disclaimer: Palos Funds are shareholders of QBR/B.

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Chart 1: Palos Domestic Funds versus Benchmarks (Total Returns) ¹	FundServ	NAVPS	YTD Returns
Palos Income Fund L.P.	PAL100	\$7.08	-13.92%
Palos Equity Income Fund - RRSP	PAL101	\$5.02	-11.63%
Palos Merchant Fund L.P. (Dec 31, 2019) ²	PAL500	\$1.71	20.15%
Palos WP Growth Fund - RRSP	PAL210	\$7.27	-5.02%
Palos-Mitchell Alpha Fund ³	PAL300	\$7.92	-23.69%
S&P TSX Composite (Total Return with dividends reinvested)			-9.52%
S&P 500 (Total Return with dividends reinvested)			-5.96%
S&P TSX Venture (Total Return with dividends reinvested)			3.87%
Chart 2: Market Data ¹			Value
US Government 10-Year			0.64%
Canadian Government 10-Year			0.51%
Crude Oil Spot			US \$38.49
Gold Spot			US \$1,780.30
US Gov't 10-Year/Moody BAA Corp. Spread			291 bps
USD/CAD Exchange Rate Spot			US \$0.7305

¹ Period ending June 26, 2020. Data extracted from Bloomberg

² Fund is priced annually

³ Fund is priced weekly on Tuesdays

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