

# **Canso Select Opportunities Corporation**

## **Annual Management's Discussion and Analysis For the Year Ended December 31, 2022**

Management's Discussion and Analysis ("MD&A") provides a review of Canso Select Opportunities Corporation's ("CSOC" or the "Corporation") audited financial results for the years ended December 31, 2022 and December 31, 2021 and assesses factors that may affect future results. The financial condition and results of operations are analyzed noting the significant factors that impacted the statements of financial position, statements of comprehensive income (loss), statements of changes in equity, and statements of cash flows of CSOC. As such, this MD&A should be read in conjunction with the audited financial statements and notes thereto. The audited financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") to provide information about CSOC.

The following MD&A is the responsibility of management and is dated March 28, 2023. The Board of Directors carries out its responsibility for the review of this disclosure through its Audit Committee, comprised of independent directors and CSOC's Chief Financial Officer. The Audit Committee has reviewed and recommended approval of the MD&A by the Board of Directors. The Board of Directors has approved this disclosure.

### **Business of the Corporation**

CSOC is an Ontario-based investment corporation. CSOC's investment objective is to provide capital gains and dividend income to its shareholders. Consistent with these objectives, the Corporation evaluates potential investments in debt, public and private equity and other securities. The deployment of funds to new investments depends on both the attractiveness of new investment opportunities and the availability of capital as generated from the realization of value from existing portfolio investments. The investment portfolio consists of public and private equity and debt investments primarily in North America, however, there is no geographic constraint on the investment portfolio.

### **Recent Developments**

#### *Acquisition of Lysander Shares*

Subsequent to year end, on January 13, 2023, CSOC announced the acquisition of 70,000 Class A common shares of Lysander Funds Ltd. at a purchase price of \$12.25 million. The Corporation issued 2,440,239 Class B subordinate voting shares as consideration for the Lysander shares purchased.

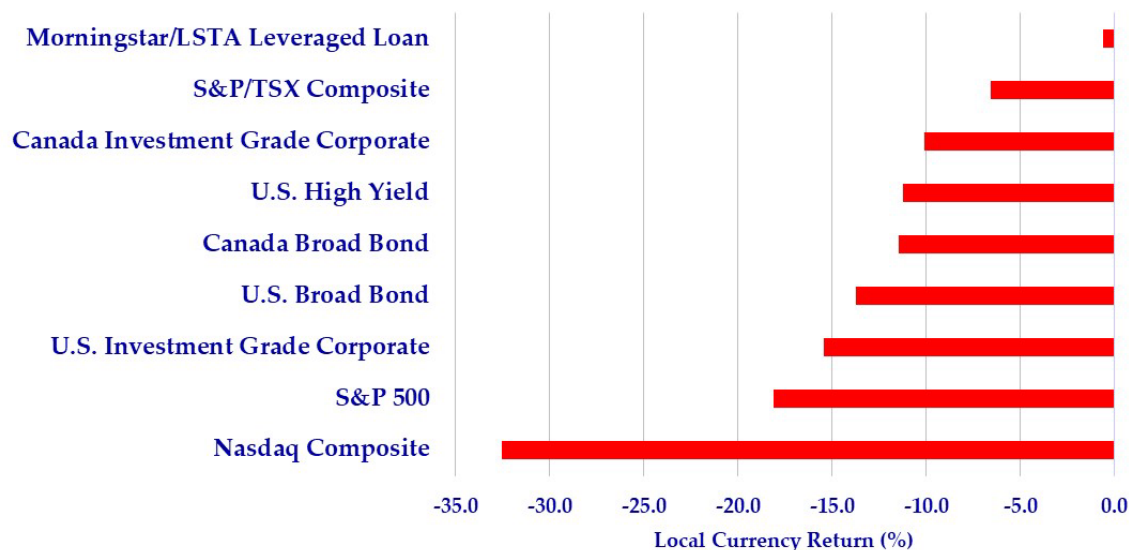
Lysander's most recent quarterly dividend was \$1.50 per share. If the current dividend is maintained, CSOC should receive approximately \$420,000 in annual dividends from Lysander per annum.

## Market Performance

2022 was a bruising year for both equity and bond markets as short term interest rates were raised globally, effectively repricing all risk assets. Central bankers were forced to play catch up in 2022 following an overly sanguine view that the inflation surge in 2021 surge would prove transitory. Instead, price pressures were exacerbated by Russia's invasion of Ukraine, which sent oil and gas prices soaring in the early part of the year. Although energy prices moderated in the second half of 2022, food and residential rents soared and workers aggressively demanded higher wages, resulting in stubbornly high inflation throughout the year. In an attempt to curtail inflation back to targeted levels, both the Federal Reserve and Bank of Canada embarked on the most aggressive interest rate increases since the 1980s. Both central banks increased overnight rates from 0.25% at the start of 2021 to 4.25% at the end of the year.

Tighter monetary policy led investors to effectively flee all assets classes, with the highest risk assets taking the worst downturn. Bonds had their worst performance in history with Canadian and U.S. bond indices down anywhere between 10% and 15%. The main U.S. equity indices were also down between 18% and 33%, while the S&P/TSX index was down only about 7% on the year due to higher exposures in natural resources, which had a fairly strong year.

Table 1: Major Benchmark Returns 2022



Private markets had an extremely difficult year as well. A lack of venture capital available funding, coupled with often tenuous business models caused devastation in early stage companies resulting in a near complete collapse in values for many companies. A series of scandals and bankruptcies in cryptocurrencies and related exchanges added fuel to the fire.

## Outlook

The full effect of higher interest rates will take time to filter through the economy, leaving investors wondering how the series of rate increases will eventually affect the behaviour of businesses and

consumers. The Bank of Canada has indicated that it may soon be time to pause increasing rates, whereas the Fed Chairman has signaled that their fight against inflation is not done, and the unemployment rate has remained at a historically low level. However, the markets are pricing in something entirely different. Bond traders are betting on the Fed pivoting from raising rates to cutting them later this year. Given the pace of monetary tightening, many economists suspect that a U.S. and possibly a global recession is imminent and will dent corporate earnings and erode the attractiveness of company bonds and shares.

We will continue to focus on the long-term prospects for income and capital appreciation for the investments in the portfolio. We currently believe there to be reasonable value in corporate bonds in Canada and the U.S. For the first time in several years government yields are above 4% and corporate bond spreads are at reasonable long term averages. Floating rate bonds are also attractive. We are invested in companies that we believe will outperform the market in the long-term and will ignore short term equity price volatility.

## **Overall Performance**

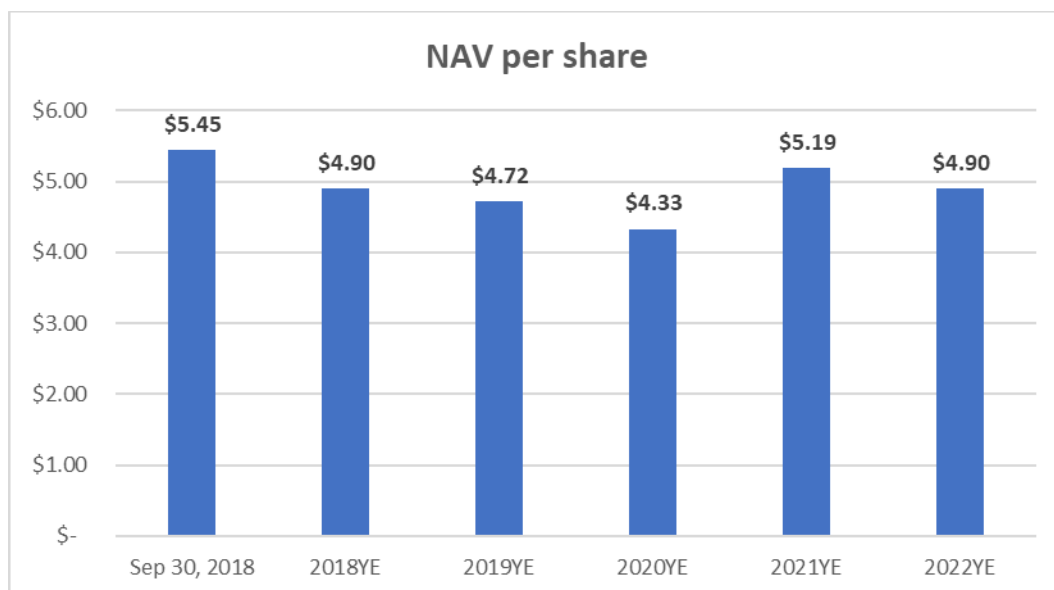
The Corporation's ability to generate income and to pay dividends depends on the performance of the holdings in its portfolio. Each fixed income and equity investment in the portfolio is unique. Portfolio companies vary from early stage start-up enterprises, to private companies in more advanced stages of development and publicly traded companies operating in mature industries.

Investments in corporate bonds and preferred shares are based on relative value analysis of the security compared with other securities trading in the market available in the market. CSOC will invest in corporate bonds and preferred shares where the yield spread above the relevant government benchmark is attractive given the relative risk of the investment.

The performance of equity securities in the investment portfolio depends on a variety of factors, which include but are not limited to, economic conditions, interest rates and investor confidence as indicated by equity market performance. In addition, for private equity investments factors such as access to capital and improving performance are key factors to long-term success.

## ***Specific Factors***

For the year ended December 31, 2022, CSOC shareholders' equity decreased by \$804,472 (\$0.29 loss per Class A or B share) versus a net increase in 2021 of \$2,376,970 (\$0.86 gain per Class A or B share). The decline in value per share was 5.6% on the year, as compared with a gain of 19.9% in 2021. While the portfolio does not have a specific benchmark against which its performance is measured, it outperformed all major North American bond and equity and bond indices for the past years.



Management is pleased with the performance of the portfolio in the past two years having outperformed all major indices in 2022, and performing very well in 2021 with an absolute return of almost 20%. We believe the portfolio is well positioned to generate attractive investment returns in 2023 and beyond.

CSOC's portfolio performance had a difficult start after its conversion to an investment fund in September 2018, due primarily to oversized positions in certain equity investments on the conversion date. The position sizes were appropriate at the time of the initial investment into the predecessor fund, however, given sizable fund redemptions just prior to the conversion date certain positions became oversized. Poor performance in some of those investments led to a decline in equity value per share for the period through the end of 2020. We have since right sized those positions.

### **Summary of Investment Portfolio**

CSOC's corporate structure provides a permanent capital base allowing the realization of value from its existing portfolio over time. CSOC's investments with a market value in excess of 10% of portfolio market value are described below.

#### ***Yellow Pages Limited***

Yellow Pages (TSX: Y), is a digital media and marketing solutions provider in Canada, offering targeted tools to local businesses, national brands and consumers allowing them to interact and transact within today's digital economy. At year end CSOC held 124,487 common shares with an initial purchase of October 25, 2013. In October 2022, Yellow completed a substantial return of capital to shareholders via a pro rata share repurchase. CSOC sold 53,036 shares of Yellow for total consideration of \$667,191. It remained the largest holding of the corporation at approximately 13% of the investment portfolio at year end.

## *Investment Strategy and Activity in 2022*

Given our view on interest rates heading into 2022, we began building liquidity in the portfolio in the first quarter. We had already reduced our exposure to corporate bonds to effectively zero by the end of 2021, and began selling preferred shares in the first quarter of 2022. Given the relative long duration of preferred shares they were particularly exposed to increases in interest rates. CSOC holdings in preferred shares were reduced from almost 25% of the portfolio at the end of 2021, to about 8% at the end of the first quarter 2022.

Our second major change to the portfolio in the first quarter was in the holding of Hertz Global common equity which we reduced from approximately 13% of the portfolio at the beginning of the year to just under 5% by the end of the first quarter.

Proceeds from these sales were invested in short term government of Canada instruments and U.S. treasury bonds. At the end of the first quarter we had built a decent sized liquidity pool of just over 21% of the investment portfolio.

We held the portfolio relatively unchanged for the second quarter and much of the third quarter other than a few small adjustments to the portfolio. In June we sold the Cenovus Energy common share warrants, which represented about 2% of the portfolio at the time. In September we increased our weight in Bird Construction back to almost 8% of the portfolio as the stock had sold off significantly which was unwarranted in our view. Bird shares rallied strongly into year end as well into the first quarter of 2023.

In October, we began to deploy the liquidity that had been built up in the portfolio in the first quarter of 2022. We purchased equity stakes in Credit Suisse (CS) and Manulife Financial. We also purchased fixed income securities in each of CS, BNS, LATAM Airlines and Air Canada. On the CS and Air Canada bonds we purchased, we shorted U.S. Treasury and Government of Canada bond respectively, in order to lock in attractive credit spreads while limiting exposure to further interest rate risk. Other than the CS common equity, all of these investments performed well heading in to year end.

On the private investment side the only addition to the portfolio was a small additional investment in Hashtag Paid which was part of a larger equity round by the company. Brill Power raised equity in June 2022 and as a result we increased the price of the Class A shares in the portfolio reflecting the higher valuation of the company. Lastly, at year end we reduced the value of the Smooth Commerce convertible bonds by 50% of their face value given our concerns over their ability to raise new capital, as well as issues with respect to operational performance.

## *Detailed Investment Portfolio*

The table below consolidates CSOC's investments into Marketable and Private.

December 31, 2022

<b>Description</b>	<b>Average Cost \$</b>	<b>Fair Value \$</b>	<b>% of Portfolio</b>
<b>Marketable Investments</b>			
<b>Bank Indebtedness</b>	<b>\$ (88,025)</b>	<b>\$ (89,494)</b>	<b>-0.7%</b>
<b>Fixed Income Held Long</b>	<b>\$ 3,320,810</b>	<b>\$ 3,260,469</b>	<b>25.4%</b>
Air Canada convertible	\$ 767,600	\$ 757,696	5.9%
AMC Entertainment Holdings	\$ 237,219	\$ 138,090	1.1%
Bank of Nova Scotia	\$ 623,000	\$ 605,598	4.7%
Credit Suisse Group AG 144A	\$ 811,813	\$ 819,066	6.4%
Government of Canada	\$ 239,969	\$ 252,116	2.0%
Latam Airlines Group	\$ 641,209	\$ 687,903	5.3%
<b>Fixed Income Held Short</b>	<b>\$ (718,787)</b>	<b>\$ (722,772)</b>	<b>-5.6%</b>
US Treasury Note	\$ (718,787)	\$ (722,772)	-5.6%
<b>Common Equity Held Long</b>	<b>\$ 10,506,100</b>	<b>\$ 5,838,565</b>	<b>45.1%</b>
Aegis Brands Inc. (previously Second Cup Ltd.)	\$ 3,400,936	\$ 566,494	4.3%
Bird Construction Inc.	\$ 1,011,165	\$ 1,213,550	9.3%
Flint Corp (previously ClearStream Energy SVCS Inc.)	\$ 2,012,939	\$ 210,897	1.6%
Credit Suisse Group AG	\$ 657,679	\$ 512,821	4.0%
Hertz Global Holdings Inc.	\$ 424,452	\$ 502,555	3.9%
Manulife Financial Group	\$ 649,320	\$ 734,450	5.7%
MDA Ltd.	\$ 879,998	\$ 402,285	3.1%
Yellow Pages Limited	\$ 1,469,611	\$ 1,695,513	13.2%
<b>Preferred Shares</b>	<b>\$ 1,779,584</b>	<b>\$ 1,499,397</b>	<b>11.7%</b>
Bombardier Inc.	\$ 379,277	\$ 515,819	4.0%
Canadian Life Companies Split	\$ 78,572	\$ 84,588	0.7%
M-Split Corp	\$ 838,474	\$ 529,067	4.1%
Sun Life Financial Corp	\$ 483,261	\$ 369,923	2.9%
<b>Total Marketable Investments</b>	<b>\$ 14,799,682</b>	<b>\$ 9,786,165</b>	<b>75.9%</b>
<b>Private Investments</b>			
<b>Common Equity Held Long</b>	<b>\$ 1,291,079</b>	<b>\$ 1,419,067</b>	<b>11.1%</b>
Brill Power Limited	\$ 105,559	\$ 284,215	2.2%
Fibracast	\$ 800,000	\$ 840,000	6.6%
Nordstar Capital LP	\$ 5	\$ 37,483	0.3%
Reformulary Group Inc.	\$ 200,000	\$ 250,000	1.9%
X-Spectrum 2 Inc. (previously Xplornet Mobile Inc.)	\$ 51,792	\$ 1	0.0%
X-Spectrum 1 Inc. (previously Xplornet Wireless Inc.)	\$ 133,723	\$ 7,368	0.1%
<b>Fixed Income Held Long</b>	<b>\$ 944,000</b>	<b>\$ 744,000</b>	<b>5.8%</b>
Nordstar Capital LP	\$ 144,000	\$ 144,000	1.1%
Our Home and Miniature Land Inc.	\$ 400,000	\$ 400,000	3.1%
Smooth Payment Inc.	\$ 400,000	\$ 200,000	1.6%
<b>Preferred Shares</b>	<b>\$ 928,567</b>	<b>\$ 933,617</b>	<b>7.2%</b>
BZ Holdings Inc.	\$ -	\$ 2	0.0%
Flint Corp - Preferred (previously ClearStream Energy Services - Preferred)	\$ 729,400	\$ 486,002	3.7%
HashTag Paid Inc.	\$ 199,167	\$ 447,613	3.5%
<b>Total Private Investments</b>	<b>\$ 3,163,646</b>	<b>\$ 3,096,684</b>	<b>24.1%</b>
<b>Total Marketable and Private Assets</b>	<b>\$ 17,963,328</b>	<b>\$ 12,882,849</b>	<b>100.0%</b>
Other Assets, Net of Liabilities		\$ 98,673	
<b>CSOC's Investments at Fair Value</b>		<b>\$ 12,981,522</b>	

### *Purchase of Shares in Lysander Funds Ltd.*

Subsequent to year end, on January 13, 2023, CSOC announced the acquisition of 70,000 Class A common shares of Lysander Funds Ltd. at a purchase price of \$12.25 million. The corporation issued 2,440,239 Class B subordinate voting shares as consideration for the Lysander shares purchased.

Lysander's most recent quarterly dividend was \$1.50 per share. If the current dividend is maintained, CSOC should receive approximately \$420,000 in annual dividends from Lysander per annum. In our view, the long term business and financial prospects for Lysander are very positive, in large part due to the investment returns of its partner portfolio managers (PPMs).

Market outperformance for the key funds at the PPMs should result in higher assets under management for Lysander over time, which will translate into higher revenues, profitability and cash flows over time. Given the positive outlook for the business, we believe Lysander could increase dividends in time. The expected dividends from Lysander should more than cover the current normalized operating expenses of CSOC estimated at less than \$250,000 per annum.

### **Selected Annual Information**

The following table shows selected annual information about CSOC for the two most recently completed financial years of the Corporation:

<b>Description</b>	<b>2022 (CAD\$)</b>	<b>2021 (CAD\$)</b>
Total Revenue (Loss)	(\$721,274)	\$2,941,299
Net Income (Loss)		
Total	(\$804,472)	\$2,376,970
Per Share	(\$0.29)	\$0.86
Diluted Per Share	(\$0.29)	\$0.86
Total Assets	\$13,784,659	\$14,453,066
Equity per Class A Share	\$4.90	\$5.19
Equity per Class B Share	\$4.90	\$5.19

During the year ended December 31, 2022, CSOC reported net loss of \$804,472 or (\$0.29) per Class A or B share versus a 2021 gain of \$2,376,970 (\$0.86 per Class A or B share). In 2022, total assets decreased by approximately 4.6% and equity per share decreased by approximately 5.6%.

### **Discussion of Operations**

See "Investment Strategy and Activity" above.

## CSOC Tax Status

On September 4, 2018, Canso Select Opportunities Fund (the “Fund”) completed a plan of arrangement (the “Arrangement”) with the Corporation whereby the Corporation issued Class A Multiple Voting Shares and Class B Subordinate Voting Shares of CSOC in exchange for the outstanding units of the Fund and the Fund became a wholly-owned investment of CSOC.

The Fund has a pool of tax loss carry forwards that can be utilized to shelter gains of the Fund so long as the trust continues to be maintained and certain other conditions are met. If the Fund were to be wound-up into CSOC at a time when it had losses, such losses would expire unutilized. Consequently, the current intention is to maintain the continued existence of the Fund until such time as all or substantially all of the losses of the Fund are utilized, or so long as the benefits associated with maintaining and utilizing such losses (e.g. current and potential cash tax savings) outweighs the cost of maintaining the Fund. As the holding period for many of these investments of the Fund is measured in years, and the Fund has tax losses, the “transitional period” could be a year or more. Any new investments will be made directly by CSOC.

## Liquidity

Liquidity risk is managed by maintaining a portion of the Corporation’s assets in investments traded in an active market that can be readily sold. All liabilities of the Corporation are due within one year.

The securities of the Corporation are listed on the TSX Venture Exchange under the ticker CSOC.A and CSOC.B.

## Summary of Quarterly Results

The following table shows selected financial information about CSOC for the most recently completed eight quarters of the Corporation:

Description	31-Dec-2022	30-Sep-2022	30-Jun-2022	31-Mar-2022	31-Dec-2021	30-Sep-2021	30-Jun-2021	31-Mar-2021
Total Revenue	\$71,413	(\$210,696)	(\$561,770)	(\$20,221)	\$314,395	(\$399,842)	\$1,370,532	\$1,656,214
Total Revenue Per Share	\$0.03	(\$0.08)	(\$0.20)	(\$0.01)	\$0.11	(\$0.14)	\$0.49	\$0.60
Realized Gains (Losses)	\$200,381	\$49,943	\$201,696	(\$5,921)	\$213	(\$87,668)	(\$85,362)	\$389,268
Realized Gains (Losses) Per Share	\$0.07	\$0.02	\$0.07	(\$0.00)	\$0.00	(\$0.03)	(\$0.03)	\$0.14
Unrealized Gains (Losses)	(\$121,315)	(\$255,414)	(\$787,177)	(\$36,762)	\$291,772	(\$334,319)	\$1,437,592	\$1,255,462
Unrealized Gains (Losses) Per Share	(\$0.04)	(\$0.09)	(\$0.28)	(\$0.01)	\$0.11	(\$0.12)	\$0.52	\$0.45
Shareholders' Equity	\$13,606,074	\$13,565,387	\$13,793,149	\$14,326,086	\$14,410,546	\$14,190,817	\$14,575,540	\$13,422,765
Equity per Class A Share	\$4.90	\$4.88	\$4.96	\$5.16	\$5.19	\$5.11	\$5.25	\$4.83
Equity per Class B Share	\$4.90	\$4.88	\$4.96	\$5.16	\$5.19	\$5.11	\$5.25	\$4.83

The variations shown in the table above relate to the timing of investment decisions and do not reflect any general trends or seasonality. For each quarterly period, the financial data has been prepared in accordance with IFRS and the Canadian Dollar has been the presentation and functional currency.

### **Subsequent Events**

In addition to the purchase of Lysander shares completed in January 2023 as described above, CSOC also added a private convertible bond investment in AdHawk Microsystems. AdHawk has developed laser eye tracking technology that is applicable for gaming headsets, smart glasses, as well as a host of related applications. We believe the technology has very strong potential.

Also, subsequent to year-end, CSOC continued its sales of preferred shares and Hertz. Proceeds from these sales has not yet been reinvested and CSOC's cash position was approximately 16% of assets at February 28, 2023.

### **Capital Resources**

CSOC has no commitments for any capital expenditures as of December 31, 2022.

### **Off-Balance Sheet Arrangements**

CSOC does not have any off-balance sheet arrangements.

### **Changes in Accounting Policies Including Initial Adoption**

There were no changes during the period ending December 31, 2022 to the Corporation's accounting policies. The Corporation's accounting policies for its financial instruments are disclosed in detail in Note 2 of the Annual Audited Financial Statements.

### **Financial Instruments and Other Instruments**

For the period ended December 31, 2022, CSOC continued to have the capability to hold derivatives and short positions in an investment portfolio in accordance with its investment mandate. However, at year-end no short positions were held and CSOC held two warrants that were issued by the respective companies. The list of all associated risks are disclosed in detail in Notes 3 and Note 10 of the Annual Audited Financial Statements.

### **Transactions between Related Parties**

On August 1, 2018, CSOC entered into an operational services agreement with Canso Investment Counsel Ltd. ("Canso"). The operational services agreement sets out that Canso will provide the day-to-day operational services to carry out the business affairs of CSOC. Under the terms of the agreement, until August 1, 2022, no fees are payable for services provided by Canso to CSOC. On August 1, 2022, this arrangement was extended for a further 12 months. There were no management fees charged for the year ended December 31, 2022 (December 31, 2021: \$0).

## **Disclosure of Outstanding Share Data**

As at December 31, 2022, there were 1,611,460 Class A Shares and 1,166,738 Class B Shares of the Corporation outstanding. Subsequent to year end the corporation issued 2,440,239 Class B common shares in consideration for the Lysander shares purchased as described above.

## **Litigation**

The Corporation may become party to litigation from time to time in the ordinary course of business which could adversely affect its business. Should any litigation in which the Corporation becomes involved be determined against the Corporation, such a determination could adversely affect the Corporation's performance and the market price for the Corporation's securities.

In August 2021, a proposed class action complaint was brought in the Superior Court of the State of California relating to the sale of BZ Holdings, Inc. ("**BZ**"), a Delaware corporation, to Centerfield Media Parent, Inc., which was accomplished by merger approved by BZ's board of directors in December 2020. The proposed representative plaintiffs are three former common shareholders of BZ, purporting to represent a class of other common shareholders. As a result of the merger transaction, which was managed and approved by a special committee of the BZ board of directors, who were advised by sophisticated U.S. legal counsel and an investment banking advisor, the preferred shareholders recovered some, but not all of their investments, and the common shareholders did not receive any compensation. The defendants named in the complaint are BZ's board of directors, certain officers of BZ, BZ's financial adviser, and certain preferred shareholders who the plaintiffs allege promoted and approved the merger. CSOC, was a preferred shareholder of BZ and CDS & Co. is named in the complaint as the registered holder of CSOC's preferred shares. CDS & Co. has not been served with the complaint. Upon motions by the other defendants, on February 22, 2022, the court stayed the lawsuit on jurisdictional grounds. The Corporation denies the allegations in the complaint and, if necessary, will vigorously defend the action.

## **Other MD&A Requirements**

Additional information relating to the Corporation is available on SEDAR at [www.sedar.com](http://www.sedar.com).

**FORWARD-LOOKING STATEMENTS**

*This report may contain forward-looking statements and information within the meaning of applicable securities legislation. Forward-looking statements can be identified by the words “seeks”, “expects”, “believes”, “estimates”, “will”, “target” and similar expressions. The forward-looking statements reflect the current expectations of CSOC regarding future results or events and are based on information currently available to it. Certain material factors and reasonable assumptions were applied in providing these forward-looking statements. All forward looking statements in this press release are qualified by these cautionary statements. CSOC believes that the expectations reflected in forward-looking statements are based upon reasonable assumptions; however, CSOC can give no assurances that the actual results or developments will be realized. These forward-looking statements are subject to several risks and uncertainties that could cause actual results or events to differ materially from current expectations. Readers, therefore, should not place undue reliance on any such forward-looking statements. Further, a forward-looking statement speaks only as of the date on which such statement is made. CSOC undertakes no obligation to publicly update any such statement or to reflect new information or the occurrence of future events or circumstances except as required by securities laws. These forward-looking statements are made as of the date of this report.*

*Additional information about CSOC is available under its SEDAR profile at [www.sedar.com](http://www.sedar.com).*