CURVATURE MARKET NEUTRAL FUND

Commentary - November 2011

Experience. Intelligent Investing.

The Curvature Market Neutral Fund net return was +1.0% in November.

REFLEXIVE CHANGE REVIEW

After seeing a fast move higher off the lows in October, dispersion returned to the markets in November. As a result, Curvature's reflexive changes strategies were able to generate significant gains on both long and short positions. Lumina Copper and Auto Canada were two top contributors to the long side of the strategy while Cash Store Financial and Imperial Sugar continued to generate alpha on the short side.

EVENT DRIVEN AND ARBITRAGE REVIEW

Curvature's Event Driven Strategy posted positive returns in the month of November.

Even as the "risk-off" army is winning the battle of beta, a significant amount of M&A is occurring in the Canadian small cap space. Metal mining developers and producers continue to be consolidated as deals in November were announced for the acquisition or mergers of Iberian Minerals and Quadra FNX. Emerge Oil and Gas and Twin Butte Energy announced a friendly merger, which we view as a sensible strategic transaction requiring two sets of shareholder votes. Canmark Reit, was the subject of a hostile bid by Cominar, hoping to wrap up some attractive Quebec real estate properties. We view the Cominar bid as far too low, too hairy (Cominar will have to issue hundreds of millions of dollars of units going forward), and executed poorly on the part of Cominar.

Although it could be construed as a positive sign for the market that M&A is active, upon closer inspection, a different conclusion can be reached. A number of hostile deals have emerged in the first two weeks of December, in addition to a handful in November. In addition, a number of companies under strategic review (a for sale sign planted in their respective front lawns) have ended the process without bids satisfactory to their special committees. As we have discussed in prior missives, low share prices may attract bidders looking for a bargain, but shareholder and board opposition to these types of deals can be heightened. This has to do with the misalignment of long term fundamental asset value versus current share prices, reflecting in many cases high costs of capital and concerns regarding Chinese commodity demand growth (decline?) as well as European financial discombobulation. This "reality gap" (as the current share price is, well, the price, whereas the potential long term fundamental asset value is simply an opinion) which is common in bear markets, can increase the risk of hostile take-overs disintegrating.

At Curvature, we try to be bullet dodgers. As hard as it may be to do this in the matrix we call the capital markets, simple rules such as remaining diversified, avoiding speculative "arbitrage" and highly overbid arb situations has helped us avoid being shot by the likes of Connacher Oil and Gas, Ivanhoe Mines and Lundin Mining, just to name a few.

MARKET OUTLOOK

Curvature's change-based market neutral strategies were created to provide real alpha that is not correlated to risk assets. The past three years has proven that to be possible, even in a highly volatile macro environment. Due to the continued deleveraging impacts of the end of the global credit bubble, we believe that the volatility of the recent past is here to stay, and thus continue to create unique opportunities for change-based market neutral investing to protect capital and add alpha. As we entered 2011, the QE 2 rally was still in full effect and cyclical companies led the market.

Entering the summer, those QE liquidity effects began to falter, and the market was once again driven by sovereign debt concerns both in the US and Europe. Risk assets began to decline with the only holdout being precious metals and stable non-financial dividend paying vehicles as safe havens. It became clear to us that the gold trade was very overowned through the summer and when the US Fed did not in fact embark on QE 3 in September, that bastion of "safety" proved that there is really no place to hide if one is a long only investor.

Going forward, it seems clear that the impact of austerity programs continued sovereign debt downgrades (and possible defaults) in Europe and a significant slowdown in Chinese commodity demand is going to dominate the economic landscape in 2012, leading to a new global recessionary environment. It also seems clear that the political support of QE programs has been weakened globally as the side-effects of the medicine may be worse than the debt illness. Curvature thus remains quite cautious in our Fundamental Change portolio, preferring to be long companies that can experience positive change even through a recession and short companies that will be hurt the most by such an environment and who depend on access to capital markets to continue operating. Of course, at some point as the new recession becomes reality, another round of QE will likely be enacted, and our fundamental stance will certainly change as the macro liquidity picture ultimately improves. Watching the reaction of gold and related precious metal equities to ongoing economic weakness will likely provide an excellent clue as to when QE will be enacted.

And so it will go on for at least another decade in our view. Deleveraging cycles interspersed with short bouts of QE intervention until the credit bubble is ultimately inflated away and/or debt is defaulted upon. Companies that are experiencing negative fundamental change that rely on consistent access to external capital are likely to die, regardless of "valuation". Companies with positive fundamental change that can grow organically though the volatile economic cycles will outperform and even thrive.

I wish it were not so, but capital preservation with modest alpha expectations are the best investors can reasonably strive for in such an environment. Curvature continues to aim for an 8%-12% Total Return while protecting capital and delivering volatility less than half of broader risk assets with our market-neutral change strategies.

On a personal note I'd like to thank all of our partners, investors and service providers for helping to make Curvature the success it is today.

Cheers and Happy Holidays.

Thank you for your continued interest in the Fund. For further information, please contact your regional Arrow Capital representative.

^ Indices are denoted in US dollars.

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