

**LORICA CANADIAN FIXED INCOME FUND**

(Formerly MARQUEST CANADIAN FIXED INCOME FUND)

**ANNUAL MANAGEMENT  
REPORT OF FUND PERFORMANCE**

Year ended December 31, 2018

**LORICA** | INVESTMENT  
COUNSEL INC.



# LORICA CANADIAN FIXED INCOME FUND

(Formerly MARQUEST CANADIAN FIXED INCOME FUND)

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## **A NOTE ON FORWARD-LOOKING STATEMENTS**

*This report contains forward looking statements. These statements primarily relate to assessments of future economic and market conditions. Such information has been included to assist readers with assessing recent developments in the Fund's operating climate and possible future developments that may affect Fund performance. All forward looking statements are based on management's current beliefs and assumptions which are subject to numerous risks and uncertainties. Statements with respect to future economic and market conditions are based on management's beliefs and assumptions with respect to a range of factors, including market conditions generally and within the sectors in which the Fund's investments operate. While management considers such beliefs and assumptions to be reasonable based on information currently available to it, no assurance can be given that such beliefs and assumptions will prove to be correct. Events or circumstances may cause actual results to differ materially from those expressed or implied by such forward looking statements as a result of numerous known and unknown risks and uncertainties, including, but not limited to, those associated with economic and market conditions, political stability and other risks identified in the Fund's prospectus. Most of these factors are beyond the control of the Fund and its Manager. Neither the Fund nor its Manager assumes any obligation to update any of the forward-looking statements made in this report.*

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## ANNUAL MANAGEMENT REPORT OF FUND PERFORMANCE | For the Year Ended December 31, 2018

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This annual management report of fund performance contains financial highlights but does not contain the complete annual financial statements of the Lorica Canadian Fixed Income Fund (the "Fund"). You can get a copy of the annual financial statements at your request, and at no cost, from the manager Lorica Investment Counsel Inc. (the "Manager") by calling 647-776-8111, by writing to us at 130 Spadina Avenue, Suite 801, Toronto, Ontario M5V 2L4 or by visiting our website at [www.loricaic.com](http://www.loricaic.com) or SEDAR at [www.sedar.com](http://www.sedar.com).

Securityholders may also contact us using one of these methods to request a copy of the Fund's proxy voting policies and procedures, proxy voting disclosure record, or quarterly portfolio disclosure.

### ***Management Discussion of Fund Performance***

#### ***Investment Objectives and Strategies***

##### *Investment Objectives*

The Fund seeks to provide income by investing in a diversified portfolio of investment grade fixed-income assets, primarily denominated in Canadian dollars. The Fund's objective is to exceed, to the extent possible, the performance of the FTSE Canada Universe Bond Index.

##### *Investment Strategies*

An actively managed core fixed income strategy investing in government and investment grade corporate bonds. The investment strategy includes: duration and yield curve management; and sector, industry, issuer and individual security selection; with an emphasis on duration and credit risk.

#### ***Risks***

There are risks associated with investing in the Fund. There have been no changes to the Fund which affected the risks associated with investing in the Fund during the year. Specific risk information can be found in the Fund's prospectus available at SEDAR's website [www.sedar.com](http://www.sedar.com).

#### ***Results of Operations***

As at December 31, 2018, the Fund's total NAV was \$1,879,680, a decrease of 36.63% since the year end (December 31, 2017: \$2,966,230). This change was primarily the result of net redemptions of \$1,602,818.

The Lorica Canadian Fixed Income Fund ("Fund") Class A returned -3.01% returned net of fees and expenses for the 12 months period ending December 31, 2018. The benchmark, FTSE Canada Universe Bond Index ("Universe") returned 1.41% (no adjustment for fees or expenses) over the same period.

In the first half of 2018, the Canadian bond market was relatively directionless, with yields trading mostly in a narrow range. However, in Q3, bond yields moved higher and credit spreads moved gradually tighter as the US economy looked strong with steady employment gains and corresponding strong consumer confidence, enabling the Federal Reserve to stay on course "neutralising" rates. The prospects for the Canadian economy were more precarious than for the US, as weak energy prices continued to hurt economies of the oil producing provinces and uncertainty surrounding NAFTA negotiations took a toll on Canadian trade and business investment. The yield move in the US was more pronounced than for Canada reflecting the greater uncertainty surrounding the Canadian economy. Yield curves flattened in response to lower inflation expectations leading some market observers and participants to predict recession on the back of a Fed policy mistake. The Bank of Canada was more circumspect indicating a variety of economic risks including the housing market, consumer debt and notably trade negotiations, electing to avoid much in the way of forward guidance.

By Q4, the economic outlook changed significantly. The ongoing US-China trade conflict appeared to be taking a more worrying toll on US and Chinese growth, with no end in sight. Domestic US politics were also destabilising, as the budget battles surrounding the debt ceiling and Trump's "wall" escalated and the Mueller investigation surfaced with more vigor. In Canada, the effects of macro-prudential policies and consumer debt on the housing market were more evident causing housing prices to convincingly turn downwards. European growth, which had looked promising

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## ANNUAL MANAGEMENT REPORT OF FUND PERFORMANCE | For the Year Ended December 31, 2018

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late in 2017 and early this year, also slowed, prompting the ECB to back-away from tightening monetary policy. Yields responded by moving lower across the yield curve. The Fed, not wishing to make a policy error, quickly went from tightening guidance to data-dependency, ratifying and building upon the downward move in yields, while avoiding significant inversion of the yield curve. Markets went from pricing-in Fed rate increases throughout 2019 to momentarily pricing in a decrease at the March meeting. Overall, yields finished the year not far from where they began.

Credit was generally under pressure during the first half of 2018 with rising yields, volatile equity markets and issuance pressuring spreads. In Q3, demand for credit emerged as investors capitalized on the higher yields. However, credit was again under pressure in Q4 as economic fundamentals that troubled the sovereign markets again pushed yield spreads wider. That being said, Canadian investment grade credit remained solid in Q4 (outperforming riskier credit) due to Canada's sovereign strength – one of a handful of countries rated AAA by S&P, and the composition of Canada's investment grade corporate universe – largely regulated domestic-centric business models with little exposure to volatile, commodity and un-integrated energy businesses (many of which primarily issue in the high yield or US markets).

The portfolio was positioned defensively throughout the 2018, with a relatively short duration and no long-end exposure. Although yields only dropped by a small amount on average over the year, the bear flattening (rise in short term yields against fall in long term yields) negatively impacted performance. The portfolio was underweight provincial credit with a concentration of short-term provincial holdings which was positive for performance given provincial spread widening and the steepening of the provincial spread curve. The concentration of short-term corporate bonds was also positive for performance given the greater spread widening amongst mid-term corporate bonds. In terms of industry exposure, the portfolio was overweight industries that were positively impacted by rising interest rates, i.e. insurance and senior bank debt, which was positive for performance.

### ***Recent Developments***

We expect the US economy to deliver reasonable growth with tighter labour markets and higher wages throughout 2018. However, the challenging trade environment and consequent impact on global growth will ensure slower US growth. Canadian growth will be further impacted by a softer housing market and weak energy prices. We still think it possible that the Federal Reserve will deliver one rate hike later this year, although they have guided for caution and the sidelines; we don't expect the Bank of Canada to do anything this year. Real yields should eventually expand in the longer-end of the yield curve, resulting in a steeper yield curve. However, global sovereign flows will remain a wildcard factor, affecting longer-term US and Canadian real yields. Finally, we believe that tight labour markets should eventually push inflation expectations higher, but given recent experience, are hesitant to predict the timing of this move.

There are risks to both the US and Canadian economic outlooks which have been exacerbated by volatile capital markets. We are of the belief that the biggest driver behind recent Fed (and BoC) policy, has been the effort to normalise rates across the yield curve, not the threat of higher inflation. Although the effort to normalise rates would appear to have stopped short of the Fed's original goal, the Fed's primary concern was always to maintain positive economic growth. Consequently, given the prognosis for the economy has deteriorated from a year ago, we are not surprised that the Fed has moved to more accommodative policy by halting rate increases and tapering its balance sheet unwind. That being said, we expect the Fed to remain data dependant and responsive to changes to the economic and political environment.

In terms of credit markets, growth of both the proportion of long-term credit outstanding and the high-yield debt market have increased the risk of the domestic corporate bond market, making it more sensitive to higher interest rates and global event risks. Conversely, highly rated, liquid, short and mid-term credit are attractive on both an absolute and relative value basis. We continue to maintain a relatively defensive credit positioning in the portfolio, with an overweight in shorter duration, liquid, high quality corporate bonds, and exposure to longer-term provincials. We are well positioned to capitalize on relative value and yield enhancement opportunities.

# LORICA CANADIAN FIXED INCOME FUND

(Formerly MARQUEST CANADIAN FIXED INCOME FUND)

## ANNUAL MANAGEMENT REPORT OF FUND PERFORMANCE | For the Year Ended December 31, 2018

### Related Party Transactions

Lorica Investment Counsel Inc. is the manager of the Fund (“the Manager”), as of January 16, 2019. For the year ended December 31, 2018 Marquest Asset Management Inc. was the manager of the Fund (“the Former Manager”).

The Manager is responsible for managing all of the Fund’s activities, including investment advisory and portfolio management services under a Management Agreement. The Management Agreement is subject to automatic renewal for additional one-year terms. The Management Agreement may be terminated during its term if the Manager defaults in its performance of any of its duties or obligations thereunder and the if holders pass a resolution at a meeting of holders terminating the Management Agreement as a result of such default. Further, the holders of a Fund may, by resolution passed at a meeting of holders at least 180 days before the end of the initial term or each anniversary thereof, elect not to renew the Management Agreement, whereupon the Management Agreement will not be renewed beyond its existing term. The Manager must give the holders and the Trustee at least 180 days’ notice of its intention not to renew a Management Agreement. Management fees are paid by each class at the rates set out under “Management Fees” below.

During the year, \$18,978 in management fees (including HST) was paid to the Former Manager. The Former Manager was also the trustee of the Fund and was responsible for certain aspects of the day-to-day administration. The Fund reimbursed the Former Manager for operating costs incurred in administering the Fund of \$39,795.

As disclosed in the Fund’s prospectus, the Manager may voluntarily waive, absorb or pay a portion of the Fund’s fees and expenses, at its discretion. During the year the Former Manager did not absorb expenses of the Fund.

### Financial Highlights

The following tables show selected key financial information about the Fund and are intended to help you understand the Fund’s financial performance since inception. The information is derived from the Fund’s audited annual financial statements.

<b>LORICA CANADIAN FIXED INCOME FUND (Class A)*</b> <b>(formerly MARQUEST CANADIAN FIXED INCOME FUND (Class A))</b> <b>Net Assets per Unit (\$) <sup>(1)</sup></b>					
	<b>2018</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>	<b>2014</b>
<b>Net assets, beginning of the year <sup>(2)</sup></b>	<b>10.01</b>	<b>10.09</b>	<b>10.16</b>	<b>10.04</b>	<b>10.00</b>
<b>Increase (decrease) from operations:</b>					
Total revenue	0.29	0.26	0.28	0.29	0.01
Total expenses (excluding distributions)	(0.47)	(0.18)	(0.16)	(0.17)	-
Realized gains (losses) for the year	(0.21)	(0.17)	0.07	0.03	-
Unrealized gains (losses) for the year	0.04	0.09	(0.11)	(0.18)	0.03
<b>Total increase (decrease) from operations <sup>(2)</sup></b>	<b>(0.35)</b>	<b>-</b>	<b>0.08</b>	<b>(0.03)</b>	<b>0.04</b>
<b>Distributions:</b>					
From net investment income (excluding dividends)	(0.01)	(0.06)	(0.10)	(0.09)	-
From dividends	-	-	-	-	-
From capital gains	-	-	(0.08)	(0.11)	-
Return of capital	-	-	-	-	-
<b>Total annual distributions <sup>(3)</sup></b>	<b>(0.01)</b>	<b>(0.06)</b>	<b>(0.18)</b>	<b>(0.20)</b>	<b>-</b>
<b>Net assets at December 31st of year shown</b>	<b>9.70</b>	<b>10.01</b>	<b>10.09</b>	<b>10.16</b>	<b>10.04</b>

#### Notes:

<sup>(1)</sup> This information is derived from the Fund’s audited annual financial statements. The net assets attributable to holders of redeemable units per unit presented in the financial statements may differ from the net asset value calculated for fund pricing purposes. An explanation of these differences can be found in the notes to financial statements, if applicable.

<sup>(2)</sup> Net assets and distributions are based on the actual number of units outstanding at the relevant time. The increase/decrease from operations is based on the weighted average number of units outstanding over the financial period.

<sup>(3)</sup> Distributions were paid in cash or re-invested in additional units of the Fund, or both.  
\*Class A units were first issued on December 1, 2014 at \$10.00.

**LORICA CANADIAN FIXED INCOME FUND**  
(Formerly MARQUEST CANADIAN FIXED INCOME FUND)

**ANNUAL MANAGEMENT REPORT OF FUND PERFORMANCE | For the Year Ended December 31, 2018**

*Financial Highlights (continued)*

<b>LORICA CANADIAN FIXED INCOME FUND (Class F)*</b> <b>(formerly MARQUEST CANADIAN FIXED INCOME FUND (Class F))</b> <b>Net Assets per Unit (\$) <sup>(1)</sup></b>					
	<b>2018</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>	<b>2014</b>
<b>Net assets, beginning of the year <sup>(2)</sup></b>	<b>9.97</b>	<b>10.06</b>	<b>10.14</b>	<b>10.04</b>	<b>10.00</b>
<b>Increase (decrease) from operations:</b>					
Total revenue	0.29	0.25	0.28	0.28	0.01
Total expenses (excluding distributions)	(0.39)	(0.11)	(0.10)	(0.10)	-
Realized gains (losses) for the year	(0.19)	(0.14)	0.08	0.11	-
Unrealized gains (losses) for the year	0.05	0.04	(0.05)	(0.10)	0.03
<b>Total increase (decrease) from operations <sup>(2)</sup></b>	<b>(0.24)</b>	<b>0.04</b>	<b>0.21</b>	<b>0.19</b>	<b>0.04</b>
Distributions:					
From net investment income (excluding dividends)	(0.02)	(0.14)	(0.18)	(0.17)	(0.01)
From dividends	-	-	(0.08)	(0.10)	-
From capital gains	-	-	-	-	-
Return of capital	-	-	-	-	-
<b>Total annual distributions <sup>(3)</sup></b>	<b>(0.02)</b>	<b>(0.14)</b>	<b>(0.26)</b>	<b>(0.27)</b>	<b>(0.01)</b>
<b>Net assets at December 31st of year shown</b>	<b>9.72</b>	<b>9.97</b>	<b>10.06</b>	<b>10.14</b>	<b>10.04</b>

Notes:

<sup>(1)</sup> This information is derived from the Fund's audited annual financial statements. The net assets attributable to holders of redeemable units per unit presented in the financial statements may differ from the net asset value calculated for fund pricing purposes. An explanation of these differences can be found in the notes to financial statements, if applicable.

<sup>(2)</sup> Net assets and distributions are based on the actual number of units outstanding at the relevant time. The increase/decrease from operations is based on the weighted average number of units outstanding over the financial period.

<sup>(3)</sup> Distributions were paid in cash or re-invested in additional units of the Fund, or both.

\*Class F units were first issued on December 1, 2014.

# LORICA CANADIAN FIXED INCOME FUND

(Formerly MARQUEST CANADIAN FIXED INCOME FUND)

ANNUAL MANAGEMENT REPORT OF FUND PERFORMANCE | For the Year Ended December 31, 2018

## Financial Highlights (continued)

Ratios and Supplemental Data					
Class A*	2018	2017	2016	2015	2014
Total net asset value (000's) <sup>(1)</sup>	\$46	\$205	\$311	\$136	\$-
Number of units outstanding <sup>(1)</sup>	4,740	20,445	30,829	13,372	1
Management expense ratio <sup>(2)</sup>	4.72%	1.82%	1.62%	1.69%	-
Management expense ratio before waivers or absorption <sup>(5)</sup>	4.72%	4.14%	3.86%	4.79%	88.81%
Trading expense ratio <sup>(3)</sup>	-	-	-	-	-
Portfolio turnover rate <sup>(4)</sup>	371.59%	444.46%	467.23%	451.67%	13.04%
Net asset value per unit <sup>(1)</sup>	\$9.70	\$10.01	\$10.09	\$10.16	\$10.04
Class F**	2018	2017	2016	2015	2014
Total net asset value (000's) <sup>(1)</sup>	\$1834	\$2,762	\$4,732	\$4,225	\$538
Number of units outstanding <sup>(1)</sup>	188,666	277,108	470,450	416,756	53,595
Management expense ratio <sup>(2)</sup>	3.91%	1.11%	0.96%	0.94%	-
Management expense ratio before waivers or absorption <sup>(5)</sup>	3.91%	2.52%	2.29%	2.64%	88.81%
Trading expense ratio <sup>(3)</sup>	-	-	-	-	-
Portfolio turnover rate <sup>(4)</sup>	371.59%	444.46%	467.23%	451.67%	13.04%
Net asset value per unit <sup>(1)</sup>	\$9.72	\$9.97	\$10.06	\$10.14	\$10.04

### Notes:

<sup>(1)</sup> The information is provided as at December 31st of the year shown.

<sup>(2)</sup> Management expense ratio is based on total expenses (excluding commissions and other portfolio transaction costs) for the stated period and is expressed as an annualized percentage of daily average net asset value during the period.

<sup>(3)</sup> The trading expense ratio represents total commissions and other portfolio transaction costs expressed as an annualized percentage of daily average net assets during the period.

<sup>(4)</sup> The Fund's portfolio turnover rate indicates how actively the Fund's portfolio adviser manages its portfolio investments. A portfolio turnover rate of 100% is equivalent to the Fund buying and selling all of the securities in its portfolio once in the course of the year. The higher a Fund's portfolio turnover rate in a year, the greater the trading costs payable by the Fund in the year, and the greater the chance of an investor receiving taxable capital gains in the year. There is not necessarily a relationship between a high turnover rate and the performance of a Fund.

<sup>(5)</sup> Waivers and absorption of certain expenses associated with the Fund are at the Manager's discretion and may be terminated at any time.

\*Class A units were first issued on December 1, 2014.

\*\*Class F units were first issued on December 1, 2014.

## Management Fees

The Management fees for each applicable class are calculated daily and are based on the Fund's ending total NAV per class; cumulative daily totals are then paid on a weekly basis. The Manager uses these management fees to pay sales and trailing commissions to registered dealers on the distribution of the Fund units, as well as for the general investment management expenses.

	As a percentage of Management fees		
	Maximum Annual Management Fee Rate (%)	Sales & Trailer Commissions (%)	Investment Advisory and Portfolio Management Services (%)
Class A Units	1.40%	32.44%	67.56%
Class F Units	0.65%	0.00%	100.00%

## Past Performance

The performance information shown assumes that all distributions made by the Fund in the years shown were reinvested in additional securities of the Fund. The performance information does not take into account sales, redemptions, distributions or other optional charges that would have reduced returns or performance. How the Fund has performed in the past does not necessarily indicate how it will perform in the future. Performance differences between classes of units are mainly attributable to management fees charged to each class.

# LORICA CANADIAN FIXED INCOME FUND

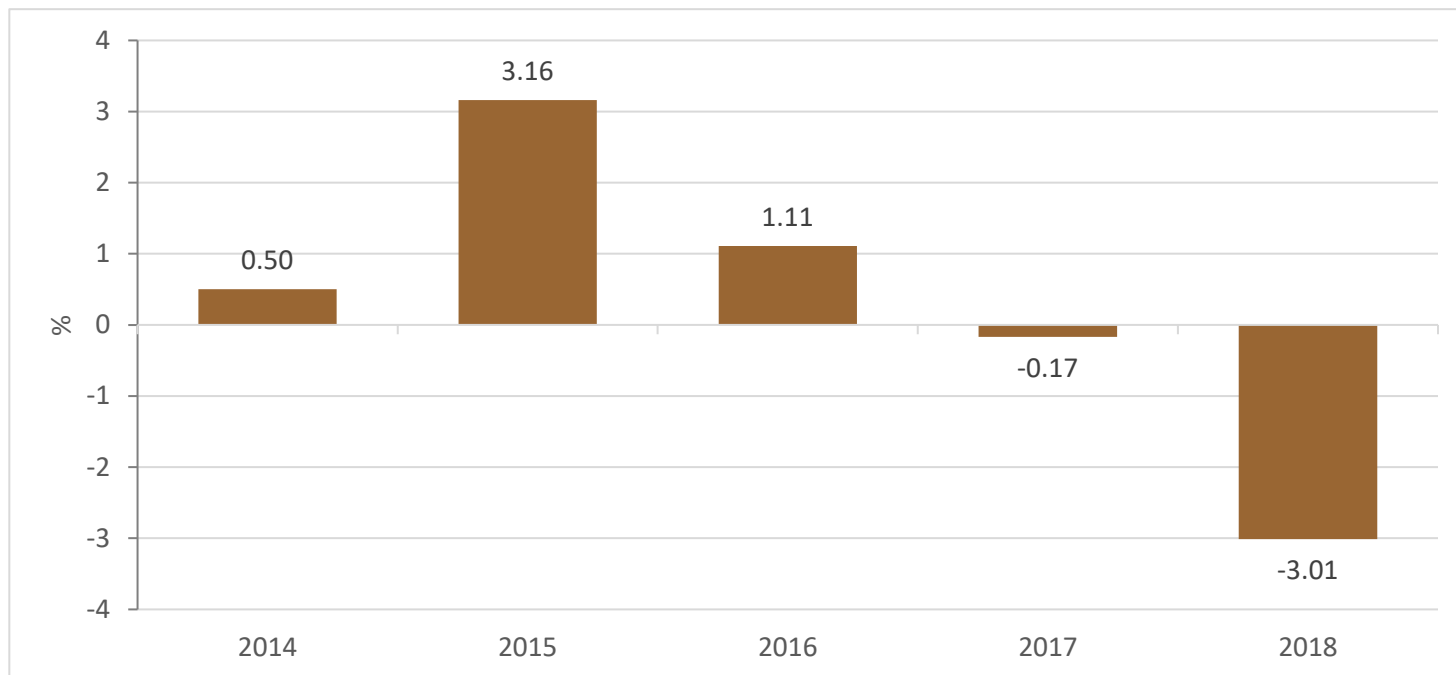
(Formerly MARQUEST CANADIAN FIXED INCOME FUND)

## ANNUAL MANAGEMENT REPORT OF FUND PERFORMANCE | For the Year Ended December 31, 2018

### Year-by-Year Returns

The following bar chart shows the Fund's annual Class A and F unit's performance for each of the years shown and illustrates how the Fund's performance has changed from year to year. In percentage terms, the bar chart shows how much an investment made on the first day of each financial year would have grown or decreased by the last day of each financial year.

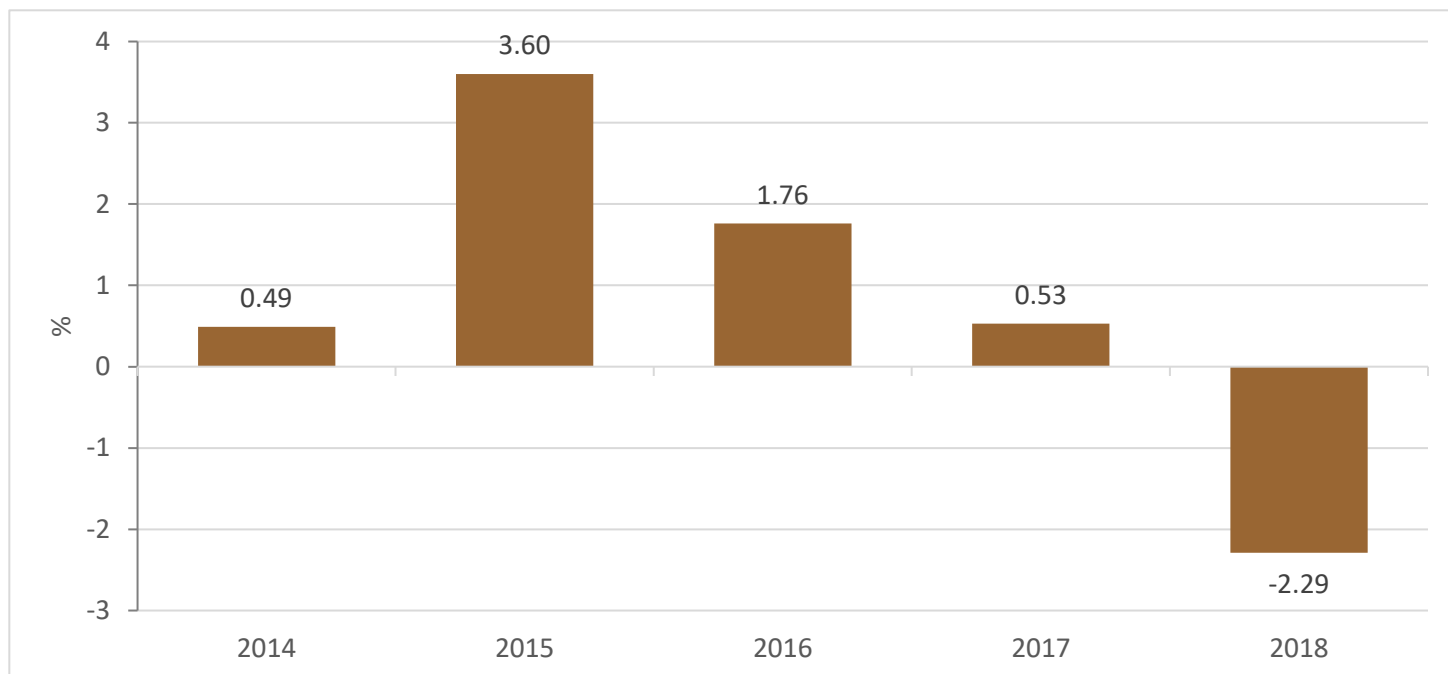
#### Class A



\*Inception date for Class A units was December 1, 2014.

#### Past Performance (continued)

#### Class F



\*Inception date for Class F units was December 1, 2014.



# LORICA CANADIAN FIXED INCOME FUND

(Formerly MARQUEST CANADIAN FIXED INCOME FUND)

**ANNUAL MANAGEMENT REPORT OF FUND PERFORMANCE | For the Year Ended December 31, 2018**

## *Annual Compound Returns*

The table below compares the annual compounded performance of the Class A and F units of the Fund against the FTSE Canada Universe Bond Index. This index is capitalization-weighted, with approximately 1500 Canadian Bonds. It includes the highest quality bonds with term-to-maturity of one to thirty years, designed to reflect the Canadian bond market.

As the index is made up of groups of fixed income securities from various duration periods and market capitalizations, it does not share the same holdings or the same weighted proportions as the Fund and compounded total returns figures between the two may differ. For greater in-depth discussion regarding the Fund's asset class holdings and performance over the year please see the "Results of Operations – Investment Portfolio" section of the MRFP.

	1 Year (%)	3 Years (%)	5 Years (%)	10 Years (%)	Since Inception (%)
<b>Class "A"</b>	-3.01	-0.71	-	-	0.37
<b>FTSE Canada Universe Bond Index</b>	1.41	1.86	-	-	2.41
<b>Class "F"</b>	-2.29	-0.02	-	-	0.98
<b>FTSE Canada Universe Bond Index</b>	1.41	1.86	-	-	2.41

# LORICA CANADIAN FIXED INCOME FUND

(Formerly MARQUEST CANADIAN FIXED INCOME FUND)

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## ANNUAL MANAGEMENT REPORT OF FUND PERFORMANCE | For the Year Ended December 31, 2018

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### Summary of Investment portfolio as at December 31, 2018

Total Net Asset Value: \$1,879,680

### Portfolio Allocation

	% of Fund's Net Asset Value
Corporate Bonds	83.36
Provincial Bonds	16.53
Net Other Assets (Liabilities)	0.00
Cash	0.11
Total	100.00

### Top 25 Holdings

	% of Fund's Net Asset Value
1 Province of Ontario 2.60% 6-2-2025	7.12
2 Telus Corp. 3.60% 1-26-2021	6.83
3 TransCanada PipeLines 3.69% 7-19-2023	6.61
4 CI Financial Corp 3.52% 7-20-2023	6.44
5 Loblaw Companies Ltd. 3.92% 6-10-2024	5.42
6 Saputo Inc. 1.94% 6-13-2022	5.35
7 Nissan Canada Fin Services 2.61% 3-5-2021	5.30
8 Sun Life Financial Inc 2.75% 11-23-2022	5.24
9 OMERS Realty Corp. 3.24% 10-4-2027	4.57
10 Bell Canada 3.00% 10-3-2022	4.51
11 Sun Life Financial Inc 3.05% 9-19-2023	4.35
12 Manulife Financial Corp. 3.05% 8-20-2024	4.14
13 Province of Ontario 2.85% 6-2-2023	4.06
14 Manufacturers Life Insurance 3.18% 11-22-2022	4.01
15 Honda Canada Finance 2.15% 2-18-2021	3.96
16 Canadian Western Bank 2.92% 12-15-2022	3.92
17 Enbridge Pipelines Inc. 3.00% 8-10-2026	3.74
18 Province of Alberta 2.55% 6-1-2027	3.12
19 HSBC Bank of Canada 2.54% 1-31-2023	2.84
20 National Bank of Canada 1.96% 6-30-2022	2.58
21 Telus Corp. 3.75% 1-17-2025	2.18
22 Province of Nova Scotia 2.10% 6-1-2027	2.12
23 Manufacturers Life Insurance 2.389 1-5-2021	1.33
24 Province of Ontario 2.60% 6-2-2025	7.12
25 Telus Corp. 3.60% 1-26-2021	6.83
	99.74

*The investments and percentages shown may change from time to time due to the ongoing portfolio transactions of the Fund. The weightings of the positions are calculated based on the total net asset value of the Fund as at December 31, 2018. The Fund does not hold short positions. To obtain a copy of the most recent annual report, semi-annual report, quarterly report or simplified prospectus of the Fund, please contact a member of our client services team or visit our website at [www.loricaic.com](http://www.loricaic.com) or SEDAR at [www.sedar.com](http://www.sedar.com).*

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