Quarterly Report

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SECOND QUARTER
2017

FRIEDBERG
MERCANTILE
GROUP LTD.

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Second Quarter Report 2017

FRIEDBERG MERCANTILE GROUP LTD.

MESSAGE TO OUR INVESTORS

I am pleased to present you with a discussion of our Funds' performance for the second quarter of 2017.

Results continue to be positive, with the Global-Macro Hedge Fund edging a 0.5% gain for the quarter to bring year-to-date results to 3.9%. The Asset Allocation Fund performed just slightly better, gaining 0.7% for the quarter and capping off a 9.4% increase for the first half of the year.

The Global-Macro Hedge Fund's results do not as yet reflect the well-thought-out foundational work we have put in place over the past two to three years nor the gains that we expect from our value-laden ideas. With one exception, our portfolios have remained remarkably stable over the past half year, if not longer. Our convictions remain solidly entrenched, and with each passing day, evidence continues to mount to reinforce these convictions. Let me first deal with the exception, as it will shed important light on our thinking about the rest of the portfolio.

Until the very end of the first quarter, and for quite some time prior, we felt that accelerating inflation was in the cards. We expected commodity prices to rise from their depressed levels, driven by the very accommodative monetary stance taken by the world's largest central banks. By the same token, we expected labour costs to rise in line with strong employment growth, both here and abroad.

We waited rather patiently for many months but, surprisingly, saw little or no sign of that happening. The unique QE experiment of the past seven to eight years, as implemented by various world central banks but most notably the Fed and the ECB, upset the canons of monetary orthodoxy. Real interest rates were pushed down into negative territory, a first in the history of fiat money, and yet inflation never took off.

The solution to the riddle came to us in a belated epiphany: interest rates were negative but there was still not enough money growth to finance a pick-up in consumer prices. The payment of interest on banks' reserves and the imposition of capital-based formulas constraining bank credit expansion saw to it that money growth never accelerated enough to generate inflationary pressures. In fact, money growth remained quite moderate in the US, the Eurozone, Japan and the U.K. This monetary virtuosity yielded rising, one might say soaring, prices for (income-producing) assets and modest consumer price inflation. Modest price inflation allowed central banks in turn to continue expanding their balance sheets, which simply meant that it allowed them to maintain negative interest rates on government obligations maturing as far as 10 or even 20 years out.

Commodity prices experienced a sharp rise from their 2009 lows to early 2011, but the rise proved to be nothing more than a normal rebound from the 2008 collapse. The subsequent decline took prices well below the 2009 lows, proof of the severe disinflationary forces at work in the global economy. After a very brief and weak rebound from early 2016 to early 2017, commodity prices have again begun to fall back and are now challenging the post-2009 lows. As well, and atypically for this stage of the economic cycle, labour costs in the US have been rising at a crawling pace. A serious inflationary outbreak is not in the cards despite the multi-trillion-dollar expansion of central bank assets, simply because it has not translated into a rapid expansion of money in the hands of private economic agents.

We must, of course, remain attentive to a change in conditions in which the base money supply/base money multiplier begins to expand; it might still do that, especially if central banks fail to corral excess reserves by paying attractive rates. But rather than anticipate this occurrence, we have thought it appropriate to abandon our “inflation play” and moved to liquidate our commodity exposure.

If our reading is correct, the implications are momentous. Modest or nonexistent inflationary pressures should forestall aggressive tightening of monetary conditions. In due time, reasons will be conjured against reducing central bank balance sheets if and when interest rates threaten to exceed inflation by a wide margin. Very imprecisely, or rather, very impressionistically, Fed funds should not move beyond 2% nor should 10-year Treasurys exceed 3%, barring significant changes to labour costs and/or commodity prices. And, as we reasoned earlier, these variables should remain well behaved as long as money supply growth continues to run at the present pace.

At higher interest rates, the prospective equity risk premium will narrow from slightly in excess of 4% to around 3%. Nonetheless, investors will continue to find reason to own equities, perhaps until the prospective equity premium falls to 2%, a premium that may no longer justify owning assets with variable returns. But even this logic may break down years from now: will Treasurys continue to be considered risk-free? Will entitlement and the administrative state now overwhelm us with debt that will never be serviced?

It does not pay to speculate about events so far into the future. Near term, central banks have shown a strong determination to normalize rates. The dramatic rise of stock prices and income-producing real estate, along with the markets’ extreme complacency (as measured by historically low volatility), have reawakened an old central bank nightmare, that of a highly damaging boom-bust cycle. They feel it is better to snuff out boom conditions now by reintroducing fear and a heightened sense of risk, thus disturbing this widespread complacency.

Our inflation scenario provides us with the assurance (as assured as we can ever be) that the rate-rise phase engineered by central banks will not last long. Ergo, we will maintain our strong long positions in US homebuilders and

WHILE THE OVERALL TONE OF THE PORTFOLIO AND THE VARIOUS ALLOCATIONS HAVE NOT VARIED MUCH IN MANY MONTHS – A STRONG POINT, AS NOTED EARLIER – AN IMPORTANT ELEMENT HAS BEEN ADDED, ONE THAT I BELIEVE GIVES US A CRUCIAL EDGE AGAINST LONG-ONLY OR EVEN 70/30 FUNDS: A LIBERAL USE OF OPTIONS. OUR CONCERN IS NOT A DEVELOPING, CLASSIC, SLOW-MOVING BEAR MARKET CAUSED BY SHRINKING PROFIT MARGINS AND PERHAPS EVEN A RECESSION. NO. OUR CONCERN, AS DETAILED IN PREVIOUS LETTERS, IS WITH SUDDEN MILITARY OR FINANCIAL ACCIDENTS THAT ARE EMINENTLY POSSIBLE AND, IN OUR OPINION, MORE PROBABLE THAN CURRENTLY ASSESSED.

IF OUR PICKS ARE VINDICATED, AS WE BELIEVE THEY WILL BE, WE STAND TO HANDILY OUTPERFORM THE S&P 500 AND OTHER RELEVANT BENCHMARKS IN MONTHS TO COME.

Japanese stocks. The same goes for our beefed up position in Greek banks and a smattering (as the Greek market is painfully small) of industrial stocks. Earlier in the quarter we traded out of the long German bunds/short Italian bonds spread but have now reinstated it in the belief that rising rates will affect debt-laden Italy more than debt-free Germany. On the short side, we continue to ride the death spiral of many US retailers, caught flat-footed by the juggernaut of electronic commerce. Even for those retailers who are able to respond to the onslaught, success will come at the expense of shrinking profit margins and heavy legacy costs as they dispose of unwanted real estate.

During the quarter, revelations that Temer, Brazil's president, had been heard on tape accepting a $150,000 bribe caused an extremely severe selloff of 6% to 9% in Brazilian risk assets and in the currency. Temer was the motor behind all the reform initiatives, some already concluded and others to be shepherded through an extremely contentious Congress. Without Temer, labour reform and, more importantly, pension reform are in jeopardy. While he may be able to survive until next year's elections, political weakness has reduced chances of the passage of an already diluted piece of legislation to 50/50. We believe, however, that the market overreacted. Either Temer will manage to pass the present package or a new and more popular future administration will improve and pass it. Pension reform is seen as much too important an agenda to be abandoned without a huge effort.

Markets have managed to recover somewhat from the dramatic selloff. Still, the decline caused us to give up half of the gain we had earned on that position (240 basis points in the Global-Macro Hedge Fund and 180 basis points in the Asset Allocation Fund). In the interim, and pending the current risk-off phase, we have hedged the currency component. With inflation running between 2% and 4%, local-currency bonds yielding 10.5% represent excellent value. Our 7.5% target should yield an important capital gain. Still, we are seeking a total return, made up of capital gains on the bonds, income and currency gain. The currency hedge will need to be lifted or the entire position closed since capital gains expectations alone do not justify the current allocation.

While the overall tone of the portfolio and the various allocations have not varied much in many months – a strong point, as noted earlier – an important element has been added, one that I believe gives us a crucial edge against long-only or even 70/30 funds: a liberal use of options. Our concern is not a developing, classic, slow-moving bear market caused by shrinking profit margins and perhaps even a recession. No. Our concern, as detailed in previous letters, is with sudden military or financial accidents that are eminently possible and, in our opinion, more probable than currently assessed. For example, a shooting war between North Korea and the United States, initiated by North Korea as an act of defiance or preemptively by US forces. The potential manpower losses are incalculable, and the territories affected may reach not only South Korea but also Japan and mainland USA. Or a conflict in the Middle East, one that moves quickly enough to close the navigational lanes and/or destroys oil wells. Or a run on some major Chinese lenders, insurers or developers that spreads too quickly for the authorities to contain it and causes a significant reduction in key commodity prices. These concerns, incorrectly priced in our opinion by stock, bond, currency and commodity options, present limited-cost trading and hedging opportunities but represent a significant headwind to profitability.

At this moment, our portfolio – positioned in out-of-the-money near-term puts in Amazon, Netflix, Apple, Nikkei, and the S&P index, out-of-the-money near-term VIX calls, out-of-the-money crude oil long-term calls, at-the-money near-term Intel and Tesla puts, and long-term at- and slightly out-of-the-money calls in homebuilders – decays by roughly 30 basis points per week, representing a far-from-inconsiderable monthly cost of 120 basis points. These options, of course, expire rapidly, and there is no guarantee that they will "pay off" should one of the "accidents" occur.

If our picks are vindicated, as we believe they will be, we stand to handily outperform the S&P 500 and other relevant benchmarks in months to come. More importantly, our long held homebuilder position has begun to outperform the market: three of our stocks (plus the ITB ETF) made 52-week highs this past week. Our position represents a 70% exposure in the Global-Macro Hedge Fund's NAV (delta adjusted) and a 20.4% exposure, soon to be raised, in the Asset Allocation Fund's NAV.

We are entering uncharted waters, facing extremely high valuations, great political uncertainty on the domestic front, a combustible military situation present in a few corners of our global village, negative interest rates running for more than seven years, a group of hi-tech companies trampling giants of the old world order and literally remaking the business landscape (some barely making money).

Can one make money in such an environment? I believe one can. What is needed is discipline, a stubborn insistence on value, a vision that goes beyond noise and the daily headlines, a judicious use of options, and a firm cap on leverage. And a little bit of luck. I believe that we have worked very hard to achieve this winning formula. With God's help, 2017 should be an exciting year.

Thanking you for your continuing trust,

ALBERT D. FRIEDBERG

Friedberg Asset Allocation Funds

Friedberg Asset Allocation Fund Ltd.
Friedberg Asset Allocation Fund

The Fund is a multi-strategy fund whose investment objective is to seek significant total investment returns, consisting of a combination of interest income, dividend income, currency gains and capital appreciation. Allocations are reviewed periodically.

MODEST RISK: Absolute return.

Performance[1] as of June 30, 2017

	NAV	Quarterly	Year over Year	Two Years	Three Years	Five Years
Friedberg Asset Allocation Fund Ltd.	1,595.59	0.81%	0.74%	6.79%	2.68%	2.62%
Friedberg Asset Allocation Fund	16.95[2]	0.71%	1.92%	6.98%	2.89%	2.76%
CSFB/Tremont Hedge Fund Index[3]		N.A.	6.26%	0.27%	2.03%	4.49%

[1]Net of fees
[2]NAV adjusted to reflect distributions reinvested in the fund
[3]Compounded annual rate of return through May 2017

Friedberg Asset Allocation Funds

Capital allocation of the Friedberg Asset Allocation Fund Ltd. as of June 30, 2017 is as follows:

INVESTMENT		CURRENT ALLOCATION	TARGET
FIXED INCOME		31.20%	35.00%
Brazilian NTNF 10% Jan. 1/25	*17.50%*		
Brazilian NTNF 10% Jan. 1/27	*13.70%*		
EQUITIES		42.70%	57.50%
U.S. Homebuilders	*21.10%*		
U.S. and Australian Gold	*14.40%*		
Greek Banks	*7.20%*		
FUTURES		7.60%	7.50%
Silver	*7.60%*		
CASH / MONEY MARKET		18.50%	0.00%
		100.00%	100.00%

Friedberg Asset Allocation Fund Ltd.

Year	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Year
2017	6.57%	2.07%	-0.54%	-1.54%	-1.12%	3.55%							9.06%
2016	-3.94%	5.15%	3.28%	8.82%	-4.95%	7.51%	4.24%	-3.87%	1.15%	-4.46%	-5.46%	0.90%	7.18%
2015	3.45%	0.31%	-1.31%	-0.74%	-1.03%	-1.67%	0.74%	-2.21%	-2.67%	3.79%	0.91%	-2.86%	-3.49%
2014	3.55%	3.30%	-1.58%	0.25%	0.32%	3.29%	-2.41%	2.93%	-5.79%	-1.39%	2.06%	0.78%	4.94%
2013	0.91%	-1.21%	0.89%	1.47%	-5.07%	-7.09%	1.98%	-0.95%	1.22%	1.99%	-0.80%	-2.20%	-8.94%
2012	5.10%	-0.08%	-2.83%	-0.77%	-3.22%	1.21%	0.40%	0.72%	1.43%	1.24%	2.83%	-1.16%	4.70%
2011	-4.11%	4.18%	1.11%	5.56%	-1.67%	-1.98%	4.65%	5.15%	-2.86%	3.31%	-1.05%	-1.58%	10.52%
2010	-0.27%	0.99%	0.56%	3.47%	1.10%	0.99%	-2.23%	3.36%	3.91%	2.57%	-0.06%	0.83%	16.14%
2009						0.38%	2.62%	0.09%	2.91%	0.53%	7.15%	-3.63%	10.13%

*** PAST PERFORMANCE IS NOT INDICATIVE OF FUTURE RESULTS ***

Friedberg Global-Macro Hedge Funds

Friedberg Global-Macro Hedge Fund Ltd.
Friedberg Global-Macro Hedge Fund

A multi-strategy fund. Allocations are reviewed periodically.

Performance[1] as of June 30, 2017

	NAV	Quarterly	Year over Year	Three Years	Five Years	Ten Years
Friedberg Global-Macro Hedge Fund Ltd.	3,077.16	0.47%	-14.82%	-1.77%	-11.83%	5.38%
Friedberg Global-Macro Hedge Fund	17.89[2]	0.51%	-14.16%	-1.85%	-12.12%	6.24%
CSFB/Tremont Hedge Fund Index[3]		N.A.	6.26%	2.03%	4.49%	3.30%

[1]Net of fees
[2]NAV adjusted to reflect distributions reinvested in the fund
[3]Compounded annual rate of return through May 2017

Friedberg Global-Macro Hedge Funds

Friedberg Global-Macro Hedge Fund Ltd.

Monthly Performance (%) Net of Fees

Year	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Year
2017	0.23%	3.14%	-0.44%	-1.76%	1.05%	1.22%							3.41%
2016	4.54%	9.86%	-9.79%	0.72%	-3.39%	1.30%	3.67%	-6.83%	-1.93%	-10.13%	-3.70%	0.49%	-15.94%
2015	4.75%	-1.16%	2.73%	-14.00%	3.14%	0.08%	11.12%	6.69%	-0.21%	0.16%	5.70%	-2.68%	15.09%
2014	17.06%	0.30%	-17.58%	-3.84%	-3.35%	1.27%	-12.07%	5.19%	-4.38%	-1.53%	7.09%	1.60%	-13.70%
2013	7.65%	-3.74%	3.04%	-1.90%	-5.62%	-13.17%	-14.23%	-1.28%	-11.27%	-4.80%	4.84%	1.87%	-34.43%
2012	-15.04%	-5.20%	1.64%	8.84%	11.22%	-2.12%	-0.69%	1.00%	0.84%	0.70%	-2.43%	-5.29%	-8.72%
2011	-10.28%	7.67%	-0.71%	9.53%	-5.06%	-3.23%	15.96%	16.22%	18.69%	-21.76%	11.47%	4.60%	40.86%
2010	2.99%	0.36%	-7.34%	3.76%	13.22%	4.75%	-13.76%	6.95%	9.11%	1.69%	-1.61%	-6.16%	11.36%
2009	-5.85%	-3.88%	3.65%	-7.15%	14.97%	-7.85%	9.47%	1.97%	5.02%	-2.21%	9.56%	-3.34%	12.02%
2008	7.18%	9.57%	-1.04%	-6.48%	4.51%	8.58%	-0.24%	-6.85%	4.18%	-5.96%	5.85%	19.06%	41.52%
2007	-1.01%	1.07%	-3.44%	-1.28%	-0.80%	1.57%	10.06%	2.80%	-1.33%	5.89%	7.91%	3.00%	26.27%
2006	1.88%	1.06%	-1.81%	2.07%	-0.75%	1.27%	2.04%	-0.09%	-0.56%	3.10%	2.43%	0.54%	11.64%
2005	1.04%	0.84%	-1.13%	1.31%	1.06%	2.47%	0.08%	0.95%	2.75%	-1.38%	2.56%	2.20%	13.41%
2004	4.03%	3.44%	1.36%	-7.84%	-0.39%	0.27%	1.02%	1.90%	1.45%	1.67%	2.76%	3.24%	13.09%
2003	3.11%	3.06%	-4.58%	-1.15%	9.26%	-3.77%	-8.04%	2.91%	5.49%	1.69%	1.49%	1.10%	9.76%
2002	-1.46%	2.04%	-2.22%	4.41%	5.41%	6.16%	-2.42%	4.45%	2.80%	-6.70%	0.32%	7.56%	21.17%
2001											0.00	-0.40%	-0.40%

*** PAST PERFORMANCE IS NOT INDICATIVE OF FUTURE RESULTS ***

Friedberg Global-Macro Hedge Funds

Global-Macro Hedge Fund Ltd. (Cayman)

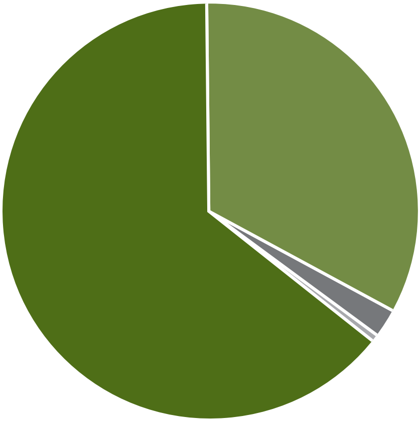
Breakdown as a Percentage of Total Assets

AS OF JUNE 30, 2017

U.S. and Global Equities*	64.43%
Fixed Income	33.05%
Currency Program	2.13%
Commodities	0.39%

Total Exposure per dollar of capital: 2.46x

* Contains long/short equities



Global-Macro Hedge Fund Ltd. (Cayman)

Breakdown as a Percentage of Total Assets

AS OF MARCH 31, 2017

U.S. and Global Equities*	35.95%
Fixed Income	35.64%
Currency Program	18.00%
Commodities	10.41%

Total Exposure per dollar of capital: 2.78x

* Contains long/short equities

Closed Funds

Fund	Inception Date	Inception NAV	Liquidation Date	Liquidation NAV	Size of Fund at Liquidation	Annual % Rate of Return
Friedberg Diversified Fund	13-Sep-96	10.00	31-Oct-06	48.43	$4,642,228	16.90%
Friedberg Global Opportunities Fund Ltd.	13-May-97	1000.00	28-Feb-05	501.89	$5,700,000	-8.46%
Friedberg Equity Hedge Fund L.P.	15-Feb-98	10.00	31-Oct-06	22.12	$6,784,836	9.50%
Friedberg International Securities Fund	31-Mar-98	10.00	30-Nov-05	11.49	$4,500,000	1.83%
Friedberg Futures Fund	8-May-98	10.00	31-Oct-06	19.59	$1,126,409	8.10%
Friedberg Global-Macro Hedge Fund L.P.	31-May-02	10.00	31-Oct-06	19.00	$30,691,202	15.64%
Friedberg Equity Hedge Fund Ltd.	16-Oct-96	1000.00	30-Apr-07	2951.78	$31,540,284	10.81%
Friedberg Currency Fund II Ltd.	6-Mar-97	1000.00	30-Jun-08	1019.23	$35,599,879	0.17%
Friedberg Total Return Fixed Income Fund Ltd.	2-Oct-96	1000.00	31-Jul-09	2155.93	$94,686,020	6.17%
First Mercantile Currency Fund	7-Sep-85	10.00	30-Dec-09	8.29	$848,443	N.A.
Friedberg Foreign Bond Fund	19-Aug-96	10.00	30-Jul-10	9.84	$13,336,465	6.91%
Friedberg Total Return Fixed Income Fund L.P.	19-Feb-97	100.00	28-Dec-11	325.47	$11,776,462	8.27%
Friedberg Forex L.P.	13-Jun-91	10.00	28-Dec-11	11.78	$2,558,382	2.66%
Friedberg Currency Fund	3-Jan-95	10.00	30-June-13	8.41	$1,932,936	-0.93%

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