Quarterly Report

3

THIRD QUARTER
2016

FRIEDBERG MERCANTILE GROUP LTD.

Contents

Message to our Investors 1

Friedberg Asset Allocation Funds 8

Friedberg Global-Macro Hedge Funds 10

Closed Funds 13

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Past trading results are not indicative of future profits.

Third Quarter Report 2016

FRIEDBERG MERCANTILE GROUP LTD.

MESSAGE TO OUR INVESTORS

> "Central banks reasserted their sway over financial markets in recent months, after two quarters punctuated by bouts of sharp volatility. Markets proved resilient to a number of potentially disruptive political developments. *Nevertheless, questions lingered as to whether the configuration of asset prices accurately reflected the underlying risks.*"
>
> **(Bank for International Settlements, Quarterly Review, September 2016, my emphasis)**

Please find below a discussion of our funds' performance for the quarter ended September 30, 2016.

The Global-Macro Hedge Fund lost 5.3% for the quarter, bringing year-to-date losses to 3.3%, while the Asset Allocation Fund gained 1.4% for the quarter, bringing year-to-date gains to 17.6%. The single element that best explains the significant difference in performance — one down and the other up — is the loss experienced by the Global-Macro Hedge Fund in its Asian short exposure. Without it, the Global- Macro Hedge Fund would have recorded a similar gain. The ability to short equities, bonds and commodities (including buying options that are not direct hedges) and the ability to use leverage are the two features that differentiate one fund from the other, as explained in our last letter. Despite disappointing results in recent years, we are not contemplating changes to the Global-Macro Hedge Fund's range of activities, though we continue to fine-tune execution.

My discussion turns first to the Global-Macro Hedge Fund. Continuing and severe losses in its Asia short portfolio were finally brought under control but not before costing the Fund an additional 660 basis points for the quarter and 1,510 basis points year-to-date. The thundering herds, fed by gobs of new liquidity and enabled opaqueness, suffocated whatever notions of reasonableness we could muster.

Trampled and bloodied, we beat a slow and reluctant retreat and came to the unproven conclusion that risk assets, pushed and goaded by central banks gone mad, had nowhere to go but up. It appeared that negative real interest rates on sovereign and high-quality corporate debt were no match for cash distributions (dividends plus buybacks) equal to 4.7% for US equities, much less E/P yields of 5.5%.

This view encouraged us to build up the long side of the US equities portfolio, adding a junior biotechnology ETF and a number of airlines towards the end of the quarter. The US equities, composed principally of homebuilders and natural gas liquids and natural gas producers during most of the quarter, did well, outperforming the indices by a 5-1 margin. But this bullish conclusion, though perhaps well warranted (for where else would rational long-term investors put their savings?) may, on second thought, be recklessly dangerous. The fact is that the distortions created by central banks over the past seven years have blunted our navigating instruments. If a storm is approaching, we are unable to see it. We navigate by instruments, valuations, historical precedents, official opinions and reassurances. Even when a gigantic tsunami overwhelms one of the ships in a perversely calm sea, we reject the warning, chalking it up to its conductor's carelessness. That mighty sterling can collapse 6% in a few seconds says only that the Brexiters made a bad choice. Really? Our senses apprehend that all is not well, but we look around and can't see it.

Stepping back from the metaphors, I offer that vanishing liquidity (defined as the ability to rapidly execute large financial transactions at low cost with limited price impact) is the lonely indicator of serious trouble ahead. Liquidity to markets is the equivalent of air to humans. And permitting myself one more incursion into the figurative world, air gets thinner, more rarified, the higher one climbs. Historically, bull markets have always been accompanied by rising volumes and rising liquidity. They died when far-sighted, sophisticated sellers overwhelmed the throng of new, enthusiastic, short-sighted buyers. This seven-year-old bull market is different. Precious few buyers with conviction and enthusiasm can be spotted. It's a lack of sellers that has fortuitously allowed the paucity of buyers to drive up prices.

Retail investors have been leaving equity markets in droves for the past few years, exceeding by far the withdrawals experienced during the last bear market. The principal buyers in this bull market have been corporations buying back their own shares. This is seen as a way to distribute funds to shareholders in a tax-advantaged manner while offsetting dilution from executive compensation and, most important, as a way to goose up earnings per share even as operating earnings are on the decline. But to do this, corporations have been incurring debt at an increasing pace, as cash flow has barely been sufficient to cover normal capital expenditures and buybacks. So this source of "support" is seen as nearing exhaustion, which in turn should make for even less buyers. Liquidity is shrinking and, as I explain below, most likely will continue to do so unless and until an external event aligns prices more realistically.

This liquidity constriction is felt in our own skin. Positions that were easy to put on months ago have become increasingly difficult to exit. It now takes five to eight days to get out of positions if we do not wish to noticeably affect prices, compared with one to three days in months past. The loss of liquidity is not an empty term; it's real.

Many years ago, as a commodities futures trader, I became acquainted with a system whose name I now forget but which usefully focused on determining clearing prices. I learned then that thin volumes — generally accompanied by wider-than-normal bid/ask spreads — were a sign that markets were not clearing, a condition that describes markets still engaged in price discovery. Such markets do not offer a reliable guide to investment prospects nor do they indicate where, in fact, a significant number of buyers and sellers could meet.

Not until volume rises significantly above the recent pace will we be confident that risks are being properly priced in and that prices are indeed clearing. And such will not happen, I fear, until an outside event forces it. It may be in the manner of a known unknown event, such as a steep Chinese yuan devaluation, a military threat to the producing oil wells in the Middle East, a North Korean nuclear attack on a neighbouring country or on a US installation, a Russian move on the Baltics, or simply an all-out tax and regulatory attack on US capital by an incoming administration. Or

THIS LIQUIDITY CONSTRICTION IS FELT IN OUR OWN SKIN. POSITIONS THAT WERE EASY TO PUT ON MONTHS AGO HAVE BECOME INCREASINGLY DIFFICULT TO EXIT. IT NOW TAKES FIVE TO EIGHT DAYS TO GET OUT OF POSITIONS IF WE DO NOT WISH TO NOTICEABLY AFFECT PRICES, COMPARED WITH ONE TO THREE DAYS IN MONTHS PAST. THE LOSS OF LIQUIDITY IS NOT AN EMPTY TERM; IT'S REAL.

it may be in the manner of an unknown unknown event, which by definition, we cannot anticipate. Last, let's not forget the rising probability of a spurt in the rate of inflation. Already service inflation is running close to 3% per annum, while headline inflation no longer enjoys the benefit from falling gasoline prices and has moved decisively above 2% per annum. More ominously, breakevens have broken out of long downtrends, indicating that an important inflection in the rate of inflation is at hand. A "recognition" that this has begun to happen can come quite suddenly, as simply as a reaction to a one-month 0.3 print. Such events and developments can no doubt bring out motivated sellers; my guess is that they will be forced to offer deep price concessions to arrive at reasonable clearing levels.

So this has been part of our ordeal. On the one hand, equity risk premiums have been wide enough to justify an aggressive stance, as there are no reasonable investment alternatives; on the other hand, technical considerations have gnawed at us, alerting us to the possibility that the risk premium may not be wide enough, as it has not been validated by reasonably heavy volume. We have shifted back and

forth on this issue, moving net exposure from barely long (because of a relatively large short book in Asia) to heavily long (once these shorts were covered and new longs, like airlines and biotechnology, were added) and to more moderately long at this time of writing. Just as markets have been seeking price discovery, we too have been seeking that still elusive investment posture that will enable us to ride through thick and thin.

In the end, we have chosen to stay with longs of conviction, increasingly relying on index puts and precious metals to cover the high likelihood that prices for risk assets around the globe will need to clear at dramatically lower levels.

A word about precious metals: I am as certain as I have ever been that the $1050/oz. low for gold registered almost one year ago represents and will stand as the absolute low of the four-year bear market commenced in September 2011. This decline, essentially a correction to the dramatic 12-year liftoff that saw prices rise from $250/oz. to more than $1900/oz., did not signal a change in fundamentals. Supply in the form of new mining output did not increase in any material way, the supply of global fiat money was not reduced, global credit did not improve, international reserves did not contract, geopolitical tensions did not decrease, deflation did not spread beyond Japan and even in Japan it never accelerated. If anything, the reverse was true for each and every case. What did happen is that, thanks to central bank intervention, interest rates were forced down to historically low levels. This caused investment assets, that is, income-producing assets, to appreciate as investors chased returns.

Not enough is understood by financial observers of the role of momentum in markets. In this particular case, the upside momentum generated by the search for yields generated its own demand; stocks and bonds rose and the rise generated further buying. Contrariwise, non-income-producing assets, such as gold, did not participate in this rush for yields; here, negative momentum fed on itself. Precious metals were sold at first to make room for investment assets. In due course, selling generated more selling. The self-feeding process crested when an end to falling interest rates came into the market's sight and, as a result, prospective gains on investment assets became far less certain. This happened sometime towards the

end of 2015. Since then, precious metals have not only held their own but have shown signs of outperforming investment assets. Inflation and the inevitable rise of interest rates are likely to reverse the momentum effects of the past four to five years. We plan to continue to maintain a heavy exposure to precious metals in the strong belief that, going forward, momentum will favour precious metals, in particular gold and silver.

All investment categories contributed profitably to the Asset Allocation Fund. Our bet on local-currency Brazilian government bonds, a position that represents 34.5% and 20.8% of the net assets of the Global-Macro Hedge Fund and the Asset Allocation Fund respectively, continues to move our way. Yields on the 10-year bond have declined to the vicinity of 11.3%. Given our views that inflation will decelerate far more quickly than expected and possibly move below 5% on an annual basis before first quarter of next year, I now expect these bonds to trade up to yield less than 7.5%. Until a few weeks ago, we had hedged the currency component of the bond, unsure as to what effect falling interest rates would have on the real. More recently, we have begun to lift hedges, moving with the market, so to speak. The simple interpretation is that falling interest rates, as long as they fall more slowly than inflation, generally pose no threat to the currency. With inflation rates in Brazil receding quickly, real interest rates have become extremely attractive. Moreover, foreign capital of a long-term nature has taken a liking to the new administration and its pro-business and pro-growth agenda. In particular, President Temer has promised to carry out a fair number of privatizations and has promoted passage of a bill that would cap fiscal spending for 20 years.

The equities portion of the portfolio, represented by gold miners, homebuilders and natural gas liquids producers, made the most significant contribution to performance (110 basis points).

In all, we will be facing a far more complicated picture in the next few months than we had expected just a few months back. While equities remain attractive relative to fixed-income instruments, prospective returns don't appear to have taken into account the bewilderingly wide range of potentially wealth-destroying risks facing markets today. To make matters worse, the steady disappearance of liquidity across

all markets makes all pricing suspect and promises spikes and sustained levels of volatility that are far greater than those to which we have become accustomed in recent years. A resolution of some of these uncertainties is at hand, perhaps as early as the next few months. I believe that value investing coupled with a sizeable sprinkling of options and a firm attachment to high-quality assets should carry us profitably over these few months.

Thank you for your continued trust.

ALBERT D. FRIEDBERG

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 September 30, 2016

	NAV	Quarterly	Year over Year	Two Years	Three Years	Five Years
Friedberg Asset Allocation Fund Ltd.	1,605.27	1.35%	19.65%	7.29%	5.63%	2.70%
Friedberg Asset Allocation Fund	16.87[2]	1.44%	19.14%	7.13%	5.44%	2.68%
CSFB/Tremont Hedge Fund Index[3]		N.A.	-1.56%	-0.03%	2.92%	3.55%

PERFORMANCE ATTRIBUTION

Fixed Income	0.23%
Equities	1.11%
Commodities	0.10%
TOTAL	1.44%
S&P 500 (total return)	3.30%

[1]Net of fees
[2]NAV adjusted to reflect distributions reinvested in the fund
[3]Compounded annual rate of return through August 2016

Friedberg Asset Allocation Funds

Capital allocation of the Friedberg Asset Allocation Fund Ltd. as of September 30, 2016 is as follows:

INVESTMENT		CURRENT ALLOCATION	TARGET
FIXED INCOME		19.20%	19.00%
Brazilian NTNF 10% Jan. 1/25	*19.20%*		
EQUITIES		58.60%	59.00%
U.S. Homebuilders	*20.00%*		
U.S. and Australian Gold	*23.90%*		
U.S. Natural Gas	*9.40%*		
U.S. Biotech	*2.40%*		
Greek Banks	*2.90%*		
FUTURES		21.20%	22.00%
Platinum	*2.10%*		
Gold	*5.00%*		
Silver	*5.30%*		
Sugar	*6.00%*		
Lumber	*2.80%*		
CASH / MONEY MARKET		1.00%	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
2016	-3.94%	5.15%	3.28%	8.82%	-4.95%	7.51%	4.24%	-3.87%	1.15%				17.61%
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 September 30, 2016

	NAV	Quarterly	Year over Year	Three Years	Five Years	Ten Years
Friedberg Global-Macro Hedge Fund Ltd.	3,421.90	-5.27%	-0.40%	-0.80%	-12.12%	6.72%
Friedberg Global-Macro Hedge Fund	19.62[2]	-5.85%	-1.46%	-1.48%	-12.68%	N.A.
CSFB/Tremont Hedge Fund Index[3]		N.A.	-1.56%	2.92%	3.55%	4.21%

PERFORMANCE ATTRIBUTION

Fixed Income		0.83%
Equities		-3.37%
Longs	*3.81%*	
Shorts	*-6.58%*	
S&P Options	*-0.58%*	
CDS		-0.14%
Commodities		-1.71%
Gold		-0.20%
Currencies		-1.26%
TOTAL		-5.85%
S&P 500 (total return)		3.30%

[1]Net of fees
[2]NAV adjusted to reflect distributions reinvested in the fund
[3]Compounded annual rate of return through August 2016

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
2016	4.54%	9.86%	-9.79%	0.72%	-3.39%	1.30%	3.67%	-6.83%	-1.93%				-3.33%
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)

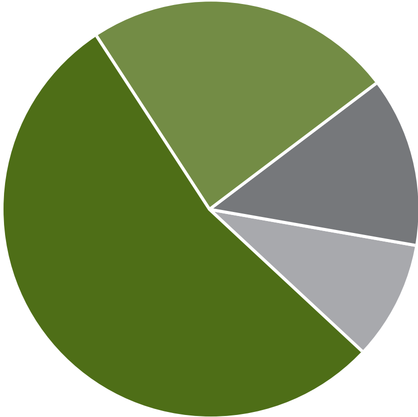
Breakdown as a Percentage of Total Assets

AS OF SEPTEMBER 30, 2016

U.S. and Global Equities*	54%
Commodities	24%
Fixed Income	13%
Currency Program	9%

Total Exposure per dollar of capital: 2.71x

* Contains long/short equities



Global-Macro Hedge Fund Ltd. (Cayman)

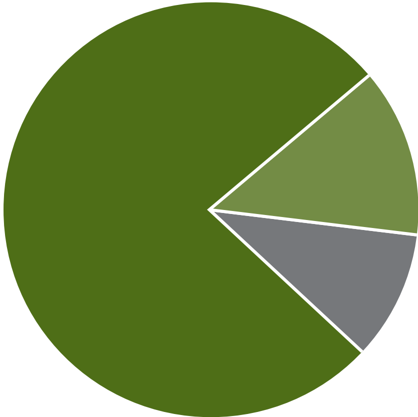
Breakdown as a Percentage of Total Assets

AS OF JUNE 30, 2016

U.S. and Global Equities*	77%
Commodities	10%
Fixed Income	13%

Total Exposure per dollar of capital: 2.47x

* 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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