INVESTMENT FUNDS

BOND

MONTHLY COMMENTARY

February 28, 2021

The economic landscape was marked by a sharp decline in the number of new COVID-19 cases in North America. In the U.S., vaccine distribution has progressed significantly and the percentage of the population that has received at least one dose of the vaccine doubled in the past month (7.5% to 15.2%). The progress has been slower in Canada, as the country experienced setbacks in terms of vaccine deliveries.

In the U.S., the Biden administration advanced its agenda to provide a $1.9 trillion fiscal package to help the economy recover from the pandemic.

A combination of better COVID-19 news and more fiscal support sent bond yields sharply higher during the month: the U.S. 10-year rate went from 1.06% to 1.46%, with a few volatile trading sessions toward the end of the month (+15 bps on Feb 25th). The movement was initially led by increasing inflation expectations, but real yields also contributed. Various Federal Reserve (Fed) speakers had a chance to try to "talk down" the market, including Fed Chair Powell during his congressional testimony, but overall, they did not seem too concerned by the yield increases. Stock markets also experienced some volatility, but no significant correction. Markets are now pricing an earlier start of QE tapering and Fed interest rate liftoff, and we will see in the coming months whether the Fed also adjusts its forecasts and forward guidance.

Even with yields rising around the globe in February, we are still in a historically low rate environment, encouraging the search for yield. We have been overweight corporate credits since the start of the year and this has contributed positively to the overall performance of the fund, as corporate credits have outperformed the aggregate universe index. Even though spreads in this sector were near pre-pandemic levels by year-end, spreads have continued to tighten in the first few months of the year. February was set to repeat the trend until the last week of the month, where we saw some volatility in corporate spreads and equity markets due to the speed of the rise in federal yields. Corporate credit spreads closed the month roughly unchanged due to this volatility. We prepared for such a scenario by buying some protection and reducing the risk in our corporate credit holdings in February. Finally, February was marked by strong interest from buyers for municipal credit, particularly unrated ones. Overweighted in this sector as part of our basic strategy, the portfolios benefited from this tightening of spreads.

Going forward, with the faster deployment of vaccines in the United States, the economy is expected to reopen quickly, leading to a likely rise in inflation. For now, central banks seem to think this will be temporary and that they do not need to adjust their monetary policies accordingly. Although, as mentioned earlier, the rise in bond yields in February and the volatility involved were mainly caused by the markets predicting a move by central banks earlier than communicated. On one hand, a risk to watch closely would be a possible change of tone by the major central banks, which would follow the footsteps of the market's expectations. On the other hand, the large amount of new issuance funding the large budgetary government deficits coupled with the risk of inflation and uncertainty on central banks' view of the matter could create curve opportunities. Finally, the ongoing recovery should continue to support risk assets such as corporate credits, though the historically tight level of spreads warrants a close monitoring of the situation as we could see some volatility ahead. Nonetheless, we remain optimistic on the recovery and positive on credit for the coming months.

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Main funds managed by the team

- ✓ Money Market
- ✓ Short Term Bond
- ✓ Bond
- ✓ IA Clarington Bond Fund
- ✓ IA Clarington Money Market Fund
- ✓ IA Clarington Real Return Bond Fund

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- Major player in the asset management industry
- Manages $97 billion in general portfolios and segregated and mutual funds
- A team of 184 people, including 108 investment professionals (including 44 CFA charterholders)
- Composed of experienced managers who emphasize fundamental analysis, identification of value and long-term investing

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