INVESTMENT FUNDS

BOND

MONTHLY COMMENTARY

January 31, 2021

The main macro drivers of January 2021 included the U.S. politics on one side and the stabilization in new COVID-19 cases and vaccine rollout progress on the other side. The U.S. Senate went to Democrats on January 5th after two runoff elections. This means that President Biden will have more leeway to implement his program with a blue Congress, although his majority in the Senate is the narrowest possible (50-50 with the tie-breaking vote by Vice-President Harris). Rates sold off and curves steepened on the news as markets priced more fiscal stimulus than under a gridlocked Congress.

After a strong increase in December and early January, new infections of COVID-19 started to decrease materially both in Canada and the U.S., which bodes well as it should open the door for a lifting of some of the lockdown measures. The vaccination campaign had a relatively slow start but gained pace toward the end of January in the U.S. Canada experienced more difficulties getting vaccines delivered, and this could persist for weeks, so the U.S. might experience a stronger economic recovery as restrictions could be lifted earlier. The Robinhood/Reddit saga brought a little bit of volatility to the markets, but it was concentrated in specific single-name stocks. The impact on rate markets was minimal. The main risk that could emerge from this would be more stringent regulations on leverage and margin trading, but it is not clear at this point whether this will happen.

The fund has a strategic overweight position in corporate bonds, the latter offering a better yield than federal bonds while having a shorter average duration which partly protects against a possible rise in interest rates. In addition, positions in some higher-yielding assets such as preferred shares as well as high-yield and emerging market bonds received a small allocation. Although we do not anticipate a strong compression of credit spreads in general in 2021, we believe that they should remain well supported, due to the programs put in place by central banks and the search for yield from Canadian and international investors.

The overweighting in corporate bonds is funded through a significant underweighting in federal government bonds, on both the Canadian and U.S. sides. We believe the federal government bonds should underperform in an environment of economic recovery where the risk on credit spreads is relatively moderate.

In the context of low interest rates and an ongoing economic recovery, we believe that credit spreads should continue to slightly tighten in the coming months due to the search for yield from investors, the support from central banks and the fiscal stimulus offered by governments. With vaccines being efficient, the inflation set to rise, and the large amounts of new issuance funding never seen before budgetary deficits, we could see higher rates in the coming months. As a result, it will pay to deviate from the benchmark duration to capitalize on those moves.

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We will see massive fiscal stimulus and quantitative easing programs continue as the year progresses, while overnight rates will be kept at the zero-lower bound for a long time. Those will likely create curve opportunities and relative value trades.

Green bonds are becoming increasingly popular. We believe that the ESG trend could continue to perform in the months/years to come and we intend to increase our allocation on opportunities.

The ongoing economic recovery could cause differentials in the speed at which yields increase around the world, creating opportunities for foreign investment.

The COVID-19 pandemic is not over yet and slower-than-expected vaccination campaigns or new virus strains around the world could hamper economic recovery. Governments will pass new stimulus packages, which will have to be financed and absorbed by the financial markets. More bonds available could put pressure on interest rates and steepen yield curves. Central banks will have to be cautious on how they manage their quantitative easing programs and how they communicate their intentions to the financial markets in order to avoid repeating some mistakes of the past.

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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

iAIM snapshot

- Principal asset manager for iA Financial Group
- 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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