MONTHLY BOND LETTER

AlphaFixe Capital

ECONOMIC EVENTS

JANUARY 2022

- Inflation in Canada declined by 0.1% in December, bringing the annual change to 4.7%. This is the first monthly decline in prices since December 2020. Certainly, lower prices at the pump (-4.1%) last month were a contributing factor to the decline in the index, as were prices for clothing (-3.9%), recreation (-0.7%), and health and personal care (-0.5%). All in all, these are items that can be associated with the Omicron wave, which has prompted some to stay home. On the other hand, airline ticket prices (+24.7%) and home insurance premiums (+4.4%) pulled the index up.

Pressure on goods prices may ease as supply constraints ease. However, prices for services could rise. The labor shortage will not abate soon, while the pandemic has reduced the capacité in some service industries. Once the Covid measures are lifted, a supply/demand imbalance could push up prices for services as it did for goods last year.

- The U.S. economy recovered at the end of the year, rising from an annualized growth rate of 2.3% in the third quarter to 6.9% in the fourth. For the year 2021, the U.S. economy grew by 5.7%, the fastest pace since 1984. Personal consumption expenditures rose 3.3%, driven by spending on services (4.7%). Business fixed investment rebounded by 1.3%, while residential investment declined by 0.8%. Most of the GDP growth, 71% to be exact, was due to the increase in business inventories, especially in the automotive industry.

The increase in inventories is welcome, as the inventory-to-sales ratio is historically low. It is therefore possible that inventory rebuilding will continue in the coming quarters as businesses will want to guard against potential shortages. Consumer strength will therefore be critical to prevent inventory investments from hurting businesses.

- Eurozone GDP grew at an annualized rate of 1.2% in the fourth quarter, a slowdown from the previous quarter due to health measures imposed in various countries and supply problems, particularly in Germany where the economy contracted by 2.9%. In contrast, the French economy, which is more service-oriented, grew at an annualized rate of 2.9% over the same period. For Europe as a whole, growth in 2021 amounted to 5.2%, just returning to pre-pandemic levels.

Covid restrictions and continued supply chain bottlenecks are expected to hamper growth early in the year. However, the economic effect of Omicron is proving to be less damaging than previous waves, giving reason to believe in a rapid recovery.

RATE TRENDS

- The Bank of Canada has maintained its policy rate, but believes that excess capacity in the economy has been absorbed after a second half of strong growth in 2021. Now that the output gap has closed, the Bank can begin to raise the policy rate to fight inflationary pressures. In fact, it adjusted its inflation forecast for 2022 to 4.2%, up 0.8% from its October estimate.

- The Federal Reserve kept its policy rate at the floor while clarifying that the balance of risk between employment and inflation had shifted to the latter. In a press conference, Mr. Powell was more hawkish, mentioning that the committee had not agreed on the size of the rate hike, meaning that a 0.50% increase was not ruled out. He even mentioned that a rate rise at each meeting could be possible. This was more aggressive than expected.

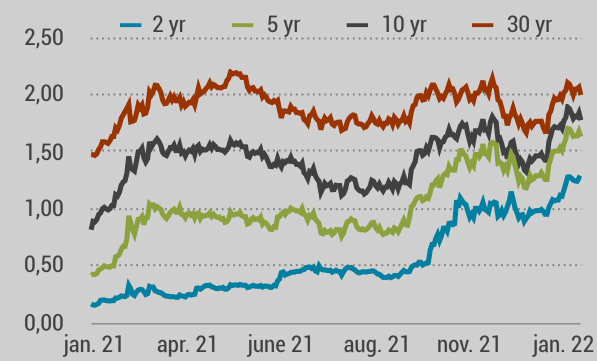
The stage is now set in both Canada and the United States for a rate hike starting in March. However, the reduction of central bank balance sheets to reduce the amount of monetary stimulus in place seems to have taken a back seat. Central bankers have been accommodating for too long and may be forced to step up their game in this tightening cycle to fight inflationary pressures. Considering that the Fed has never been able to orchestrate a soft landing for the economy, it seems hard to believe that they will be able to pull it off this time without breaking the economy's wings.

BOND RATES

Jan. 31 2022	Canada	Monthly Change	Change 2022	United States	Monthly Change	Change 2022
Key Interest Rate	0,25 %	0,00 %	0,00 %	0,25 %	0,00 %	0,00 %
3 months	0,34 %	0,17 %	0,28 %	0,18 %	0,15 %	0,13 %
2 years	1,28 %	0,32 %	1,12 %	1,18 %	0,45 %	1,07 %
5 years	1,63 %	0,37 %	1,20 %	1,61 %	0,35 %	1,19 %
10 years	1,77 %	0,35 %	0,88 %	1,78 %	0,27 %	0,71 %
30 years	2,05 %	0,37 %	0,57 %	2,11 %	0,20 %	0,28 %
RRB 30 years	0,33 %	0,45 %	0,43 %			

Source: Bloomberg

CANADIAN RATE TRENDS



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CREDIT BOND RISK PREMIUMS

Issuers	Credit Rating DBRS	Spread 5 yrs	Spread 10 yrs	Spread 30 yrs	Change 5 yrs month	Change 5 yrs 2022	Change 10 yrs month	Change 10 yrs 2022	Change 30 yrs month	Change 30 yrs 2022
Royal Bank, Bail-in-debt	AA	100	130	170	15	15	15	15	15	15
Royal Bank, NVCC	A	135	175	225	25	25	25	25	25	25
Sun Life, subordinated debt	A	115	155	205	15	15	15	15	15	15
Hydro One	A high	75	110	145	10	10	10	10	10	10
Enbridge Inc	BBB high	125	170	245	15	15	15	15	15	15
Altalink LP	A	75	110	145	10	10	10	10	10	10
GTAA	A high	75	110	140	5	5	10	10	10	10
Bell Canada	BBB high	115	160	220	15	15	15	15	15	15
Rogers Communications	BBB high	140	185	250	10	10	10	10	15	15
Loblaw	BBB high	105	150	200	15	15	15	15	10	10
Canadian Tire	BBB	110	160	240	15	15	15	15	10	10
Province Québec	AA low	39	63	82	6	6	7	7	8	8
Province Ontario	AA low	43	67	86	6	6	6	6	8	8
CMHC	AAA	33	45	---	2	2	4	4		

Source: National Bank Financial

CREDIT MARKET

- Canadian corporate bond new issuance totaled $10.2 billion in January, up $3.2 billion from the previous month and $3.3 billion higher than January 2021. Financing activity was concentrated in the first week of the year with a total of $7 billion, mostly bank debt. In fact, Canadian banks took advantage of favourable market conditions to issue a whopping $56 billion in January alone, spread across various currencies. The Canadian market welcomed a total of $7.3 billion in new issues, but Canadian banks preferred to borrow in the U.S. market ($24.9 billion) and the euro zone ($15.7 billion).

- Metro unveiled its financial results for the first quarter of 2022. Sales totaled $4,317 million in the first quarter, up 0.9% from the same period last year and 7.1% higher than the first quarter of 2019. However, same-store sales (excluding new stores) were down 1.4% from the same period last year. Considering that the food basket has seen inflation of about 3.5% over the past year, according to executives, Metro's actual sales are negative. However, Statistics Canada's latest reading of food inflation among grocers shows a 5.7% increase in prices in the past year. In addition, Metro's results were boosted by a strong performance from the pharmaceutical division, with a 7.7% increase in Jean Coutu's sales.

- The performance of provincial bonds in January was again negative, dragged down by rising long-term rates and widening yield spreads. With two months left in the fiscal year, the provinces have completed 82% of their $107 billion funding requirement for the year. Some provinces such as Manitoba (96%), Ontario (90%) and Quebec (88%) are slightly ahead of schedule. Alberta (41%), on the other hand, is struggling with $6.9 billion still to be borrowed. The province has benefited from higher oil prices in 2021, narrowing the difference between Alberta's and Ontario's yield spread to 5 bps. At the start of the pandemic, that difference was nearly 40 bps.

FTSE TMX INDEX PERFORMANCE

Sector	Weight	Jan. 2022	2022
Universe	100 %	-3,40 %	-3,40 %
Short Term	40,3 %	-0,95 %	-0,95 %
Mid Term	27,2 %	-2,65 %	-2,65 %
Long Term	32,4 %	-6,86 %	-6,86 %
Federal	34,9 %	-2,34 %	-2,34 %
Provincial	36,6 %	-4,66 %	-4,66 %
Corporates	26,4 %	-2,94 %	-2,94 %
RRB		-6,73 %	-6,73 %

Source: ftse.com

Metro's results will benefit from the new Covid restrictions imposed in Quebec, which shift the restaurant budget to food at home. On the other hand, the new trucker vaccination rule could affect the supply of food from the United States and accelerate food inflation again.

If oil prices hold up or continue to rise, Alberta could deliver a balanced budget for the next fiscal year, a first since 2014-15. During that period, Alberta's credit spread was lower than Ontario's by 20 bps, but the oil province did not have such a high debt level.

STRATEGIC POSITIONNING

2022 will be a transitional year for monetary policy across most of the industrialized world. The Bank of England has already begun its monetary tightening with 2 hikes totaling 0.40% while the Bank of Canada and the Federal Reserve have made it clear that the table is set for a withdrawal of monetary stimulus starting in March. Even the European Central Bank (ECB) is not ruling out a rate hike this year after recently defending the status quo for 2022. Inflation must be kept under control, that is the new objective of central bankers. However, a portion of the rise in prices stems from a supply problem where monetary policy has little effect. The increase in goods prices may slow this year, but the increase in services prices must be monitored. Public exasperation with Covid could lead to a rapid reduction in health measures and a return to more service-oriented consumption. Some service industries would not be able to respond to a sudden shift in demand, forcing prices up as was the case for goods in 2021. Nonetheless, highly expansionary monetary policies are no longer appropriate and a withdrawal is necessary. How fast and how strong will rates and balance sheets normalize? It is always difficult to take away candy from a child, especially when the child always wins. Will the Fed bend to investors who are unhappy about losing their stimulus candy?