MONTHLY BOND LETTER

AlphaFixe Capital

ECONOMIC EVENTS

JULY 2019

- According to the Greater Toronto Real Estate Board, housing sales increased by 10.4% in June compared to the previous year. During the same period, new listings declined slightly, so that the average selling price of homes rose 3.0% to $832,703. During the first half of the year, sales increased by 8.5 % and new listings by 1.0 %, resulting in an average price increase of 2.4 %, but a 5 % increase for condominiums.

This is one of the reasons why the Bank of Canada will not stimulate the economy further by lowering the policy rate. The strength of the labour market and the decline in longer-term rates are stimulating the real estate market which the Bank has been trying to contain in recent years.

- The US economy grew at an annualized rate of 2.1% in the second quarter, a deceleration from the first three months of the year (3.1%). The trade dispute with China and the slowdown in global economic growth led to a 5.1% drop in exports. Companies have also contributed to the slowdown with reduced inventories and capital investments (-10.5%). In contrast, household spending recovered, rising 4.3%, after a small 1.1% gain in the first quarter. The end of the government's shutdown at the beginning of the year have contributed to consumer spending, but also to the rebound in government spending (+5.0%).

The publication of national accounts is a good illustration of the economic situation. The domestic economy is doing well, supported by a strong labour market. On the other hand, Trump's trade war has consequences for companies and exports. The US economy is still on solid ground and Trump does not want to cause a recession before the 2020 elections.

- According to data published by the CPB in the Netherlands, the volume of international trade is heading towards a third consecutive quarter of decline, a first since the Great Financial Crisis of 2008-2009. The trade dispute between China and the United States, which is changing global supply chains, and the risks of a hard Brexit since the appointment of Boris Johnson could explain the decline in trade.

Unless there is an open war between China and the United States, international trade could rebound by the end of the year. Stricter fuel standards next year will increase shipping costs. Companies could bring forward their orders to avoid these higher costs.

RATE TRENDS

- The Federal Reserve announced a 0.25% cut in its key policy rate to 2.25%, while indicating that it will complete its balance sheet reduction in August, two months in advance. This cut, the first since the 2008 crisis, is due to weakness of the global economy, trade tensions as well as subdued inflationary pressures. By stating that the timing and extent of future adjustments will depend on realized and expected economic conditions, the Fed leaves the door wide open for another cut.

So the Federal Reserve of Donald Trump delivered what everyone believed, except for the American President who is always looking for more. Peter Navarro, the president's economic adviser, recently called the Fed to call for cuts by a total of 1% this year. Definitely, the Fed has lost its political independence.

- For its part, the Bank of Canada maintained its key policy rate at 1.75% at its July meeting. "Recent data shows that the growth of the Canadian economy is returning to its potential. However, the outlook is clouded by persistent trade tensions. In view of these elements, the degree of monetary stimulus provided by the current director remains appropriate.». Trade tensions and energy price developments will be of particular interest to the Bank.

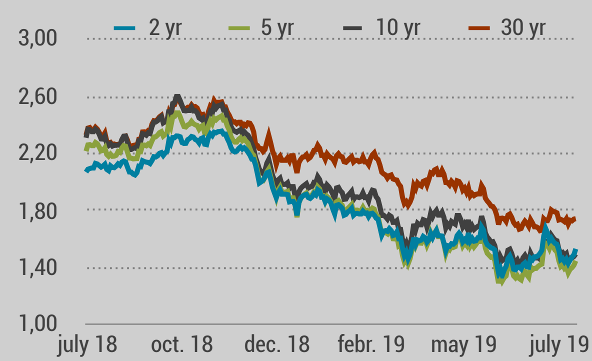
The Bank is facing two opposing forces. On the one hand, labour market strength has resulted in an increase of 3.8% in wages over one year last June. Real estate has also rebounded. On the other hand, exports represent almost 40% of GDP. Before following the Fed, the Canadian economy will have to show domectic signs of weakness.

BOND RATES

July 31 2019	Canada	Monthly Change	Change 2019	United States	Monthly Change	Change 2019
Key Interest Rate	1,75 %	0,00 %	0,00 %	2,25 %	-0,25 %	-0,25 %
3 months	1,65 %	-0,01 %	-0,00 %	2,06 %	-0,03 %	-0,29 %
2 years	1,55 %	0,07 %	-0,32 %	1,87 %	0,12 %	-0,62 %
5 years	1,45 %	0,06 %	-0,44 %	1,83 %	0,06 %	-0,68 %
10 years	1,48 %	0,01 %	-0,49 %	2,01 %	0,01 %	-0,67 %
30 years	1,70 %	0,01 %	-0,49 %	2,52 %	-0,00 %	-0,49 %
RRB 30 years	0,32 %	0,00 %	-0,44 %			

Source: Bloomberg

CANADIAN RATE TRENDS



CREDIT BOND SPREADS

ISSUER	Credit rating DBRS	Spread 5 yrs	Spread 10 yrs	Spread 30 yrs	CHANGE 5 yrs month	5 yrs 2019	10 yrs month	10 yrs 2019	30 yrs month	30 yrs 2019
Royal Bank, bail-in debt	AA	90	125	165	-10	-45	-10	-35	-10	-35
Manulife, sub debt NVCC	A	130	175	215	-15	-55	-15	-45	-15	-45
Fortis Inc.	BBB high	90	130	185	-10	-50	-10	-55	-10	-50
Hydro One	A high	70	100	145	-5	-45	-10	-40	-5	-35
Enbridge Inc	BBB high	110	155	225	0	-50	-5	-55	-5	-50
Encana Corp	BBB	160	225	280	0	-45	0	-45	0	-45
GTAA	---	60	85	115	0	-25	0	-20	0	-25
Bell Canada	BBB high	100	145	210	-10	-55	-10	-55	-10	-50
Rogers Communications	BBB	95	140	205	-10	-55	-10	-55	-10	-55
Loblaw	BBB	105	150	210	-10	-60	-10	-65	-10	-60
Canadian Tire	BBB high	100	145	205	-10	-60	-10	-65	-10	-65
Province of Québec	A high	43	65	76	0	-16	0	-19	0	-20
Province of Ontario	AA low	44	68	79	-1	-19	-1	-21	-1	-22
CMHC	AAA	31	41	---	0	-12	1	-15		

Source: National Bank Financial

CREDIT MARKET

- Canadian corporate bond new issuance totalled 6.0 billion in July, a decrease of $7.1 billion from June, but $1.1 billion more than in July 2018. Since the beginning of the year, corporate bond financings reached $54.4 billion, or 0.9% lower than at the same date last year. The major Canadian banks have dominated activity on the primary market in July with 3 of the 7 issues totaling $4.25 billion. In July 2018, the list of new issues was more diversified with 13 securities including only 2 for the major Canadian banks totalling $2 billion.

- SNC Lavalin's credit rating has been lowered one notch by DBRS from BBB to BBB(low), a notch above high-yield bonds. The agency also maintained a negative outlook on the engineering company's rating. This downgrade follows disappointing financial results in the second quarter which in turn will reduce SNC's expected earnings for the year and delaying the recovery of the company's financial ratios. In addition, "DBRS believes that there remains a significant business risk surrounding the company and uncertainty as to whether the current strategic plan will be achieved as planned and without significant financial volatility". SNC announced that it was withdrawing from the fixed price contract projects due to frequent cost overruns that undermine its profitability.

- Moody's downgraded Newfoundland and Labrador's rating from Aa3 to A1 and also changed the outlook from negative to stable. This downgrade is explained by the provinces' high level of debt and interest burden as well as the rating agency's expectations regarding continued consolidated deficits over the next two years. Moody's also points out that "the province's fiscal trajectory is based on a 7.3% decline in spending between 2019/20 and 2022/23, which is a very ambitious target for a Canadian province". Moody's is also concerned that the province may eventually have to deal with the financial difficulties at Nalcor Energy, a wholly-owned provincial company whose mission is to manage its energy resources, including the Muskrat Falls project.

FTSE TMX INDEX PERFORMANCE

Sector	Weight	July 2019	2019
Universe	100 %	0,17 %	6,70 %
Short Term	43,4 %	-0,01 %	2,66 %
Mid Term	22,5 %	0,13 %	6,06 %
Long Term	34,1 %	0,41 %	12,56 %
Federal	35,1 %	-0,09 %	3,95 %
Provincial	35,4 %	0,22 %	9,00 %
Corporates	27,5 %	0,42 %	7,27 %
RRB		0,45 %	9,30 %

Source: ftse.com

By withdrawing from the fixed-price project segment, SNC announces that it will reduce its revenues. This type of project is expected to continue, as taxpayers no longer want to bear the cost overruns of companies whose corruption has been part of their history for several years. SNC still must deliver the equivalent of $3.2 billion in fixed price contracts, including the REM.

There will be little impact of this downgrade since Moody's was out of step with other agencies that rate the province A- and A(low). The explosion in construction costs for the Muskrat Falls project and the volatility of the province's revenues from oil royalties largely explain Newfoundland's financial difficulties. These two elements are far from disappearing.

STRATEGIC POSITIONNING

The Federal Reserve finally caved to constant pressure from President Trump, who keeps saying that his central banker is damaging his country's economy with a high policy rate. Yet Jerome Powell points to the trade tensions between Donald Trump and China as a source of economic uncertainty that forced him to lower rates. Since the Fed has lost all political independence, further cuts in the key policy rate are to be expected, as the President would have preferred a 0.50% cut in July. Coincidentally, the day after the Fed's announcement, Trump announced that it would impose a 10% tariff as of September 1st on the equivalent of $300 billion worth of imports that had not yet been taxed. Trump therefore wants to increase the trade risk to force the Fed to further cut rates while putting pressure on China, which, unlike the United States, has no electoral constraints. Trump's plan is taking shape, orchestrating a monetary stimulus for the economy, under the pretext of trade tensions, which he will withdraw as the election timetable approaches. The new tariffs will mostly affect household consumption goods and he clearly does not want to erode his electoral base with a higher Christmas bill. Stimulating full employment is extremely rare and could create inflationary pressures in the future. Once the conflict is resolved, inflation indices and expectations will resume.