MONTHLY BOND LETTER

AlphaFixe Capital

ECONOMIC EVENTS

FEBRUARY 2018

- The Canadian economy grew at an annualized rate of 1.7 % in the fourth quarter of the year, bringing growth for 2017 to 3.0 %, 0.7 % more than in the US. Consumer spending slowed down in the last quarter (+ 2.1 %), while residential real estate increased sharply (+ 13.4 %) on the eve of the new mortgage rules which will be in effect in January 2018. Corporate investments were also strong (8.8 %), driven by significant gains in machinery and equipment (12.7 %). On the other hand, net exports reduced growth, mainly because imports (6.3 %) surpassed exports (3.0 %).

Similar to the United States, the weaker growth in the fourth quarter should not be worrisome, given that the strain on growth from higher imports was the result of a stronger domestic economy. In addition, labor shortages seems to encourage companies to invest in equipment in order to overcome production capacity constraints.

- The Trump administration has announced that the United States will impose a 25 % tariff on steel imports and 10 % on aluminum. However, Trump has opened the door to exempt Canada and Mexico if NAFTA is renegotiated. To justify this decision, the White House has invoked national security reasons allowing the President to act without Congress' approval. China is the world leader in aluminum production with 54 % market share, while Canada ranks third at 5 %.

This measure could affect particularly Canada as 54 % of US aluminum imports arrives from the north. As an American ally through NATO and NORAD, is Canada truly a national security risk? This announcement could open a trade war, as several countries say they are prepared to retaliate.

- Influenced by government spending and the resumption of international trade, China's economic growth accelerated in 2017 to 6.9 %, 0.2 % more than in 2016. However, China's leaders are expecting an economic slowdown this year, as the government will strengthen efforts to mitigate the shadow banking system risks and close inefficient and polluting factories.

While many question the accuracy of government's GDP data, maintaining a 6.5 % growth target like last year means that the economy will remain a priority despite financial and environmental reform announcements.

RATE TRENDS

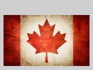
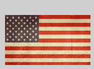
- The new Chairman of the Federal Reserve, Jerome Powell, delivered his first speech before the US Congress, drawing a rather bright picture of the economy which has improved since December, according to him. The economy should be supported by robust employment, consumer spending, global recovery that supports US exports and Trump's fiscal stimulus. In this perspective, inflation should reach the 2 % target during the year while wages should grow at a faster pace.

Powell focused on exports and government spending contributions to future growth. These factors were previously headwinds to the economy, but will be tailwinds in 2018. However, Trump's tariffs announcement may dampen the contribution of foreign trade.

- The minutes from the European Central Bank's (ECB) January meeting indicate that they could announce a review of their monetary policy at the beginning of the year on the back of more sustained inflation growth. Meanwhile, the ECB has expressed concern that the US administration is deliberately trying to engage in a currency war following Treasury Secretary Steven Mnuchin comments on economic benefits of a weak US dollar.

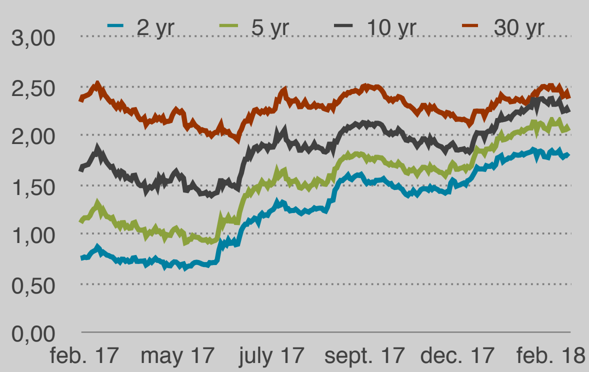
Since the asset purchase program has just been reduced to € 30 billion per month, the only change they could make would be to eliminate the part referring to an accélération of the program if the economic situation worsens. On the heels of a possible trade war with the United States, this announcement could however be delayed.

BOND RATES

Feb. 28, 2018		Monthly Change	Change 2018		Monthly Change	Change 2018
Key Interest Rate	1,25 %	0,00 %	0,25 %	1,50 %	0,00 %	0,00 %
3 months	1,15 %	-0,05 %	0,09 %	1,65 %	0,20 %	0,28 %
2 years	1,79 %	-0,05 %	0,10 %	2,25 %	0,11 %	0,37 %
5 years	2,05 %	-0,03 %	0,18 %	2,64 %	0,13 %	0,43 %
10 years	2,24 %	-0,05 %	0,19 %	2,86 %	0,16 %	0,46 %
30 years	2,38 %	0,02 %	0,11 %	3,12 %	0,19 %	0,38 %
RRB 30 years	0,60 %	0,01 %	0,02 %			

Source: Bloomberg

CANADIAN RATE TRENDS



1800 Ave. McGill College | Suite 2420 | Montréal (PQ) | H3A 3J6
514-861-3493
www.alphafixe.com
info@alphafixe.com

CREDIT BOND RISK PREMIUMS

ISSUER	Credit rating DBRS	Credit rating S&P	Spread 5 yrs	Spread 10 yrs	Spread 30 yrs	Change 5 yrs month	Change 5 yrs 2018	Change 10 yrs month	Change 10 yrs 2018	Change 30 yrs month	Change 30 yrs 2018
Royal Bank, deposit notes	AA	AA-	75	95	135	10	0	10	5	10	5
Manulife, Senior debt	A high	A+	90	120	165	10	0	15	5	15	0
Fortis Inc.	BBB high	BBB+	95	130	170	15	5	10	-5	15	5
Hydro One	A high	A	65	90	130	5	0	10	5	5	0
Enbridge Inc	BBB high	BBB+	115	160	225	15	0	15	-5	15	0
Encana Corp	BBB low	BBB	135	195	265	15	5	15	5	20	0
GTAA	---	A+	55	75	95	5	5	5	5	10	10
Bell Canada	BBB high	BBB+	95	140	205	5	0	0	-5	5	5
Rogers Communications	BBB	BBB+	85	135	200	5	-5	5	-5	5	0
Loblaw	BBB	BBB	105	150	210	15	10	10	5	15	10
Canadian Tire	BBB high	BBB+	110	155	215	15	10	10	5	15	10
Province of Québec	A high	A+	40	60	74	5	4	5	5	7	9
Province of Ontario	AA low	A+	41	63	76	3	3	5	4	7	9
CMHC	AAA	AAA	28	38	---	3	1	4	3		

Source: National Bank Financial

CREDIT MARKET

- Canadian corporate bond new issuance reached $ 5.6 billion in February, a decrease of $ 800 million from the previous month and $ 600 million less than in February 2017. The Province of Quebec issued a second green bond, the first one was issued back in February 2017. The $ 500 million bond matures in 2023 with a speed of 38 bps, equivalent to a standard provincial bond. Nearly 80 % of investors were considered "green" or signatories of the United Nations Principles for Responsible Investment (PRI). Proceeds from this issue will be used to finance the purchase of Azur trains for the Montreal Metro and hybrid buses.

- DBRS said it changed the outlook on New Brunswick's credit rating (A high) from stable to negative. This warning reflects a slow but steady deterioration in the province's credit profile over the last decade. A weak economic outlook and budget imbalances were also mentioned. DBRS is concerned about the lack of political will to restore public finances, which places the province in a position of vulnerability related to unexpected shocks. Initially planned in 2020/21, the Liberal government budget balance was pushed back by one year. For the next fiscal year (2018/19), the Finance Minister anticipates a deficit of $190 million due to additional expenses ($ 73 million) in this election year.

- Collectively, the six largest Canadian banks earned $ 10.5 billion in the first quarter of 2018, a level similar to the same period last year. These excellent results are fueled in part by their international businesses, particularly those in the United States. For example, TD Bank reported a net income of $ 952 million from its US division, up 19 % year-over-year. Their Canadian businesses also improved as all banks reported earnings growth ranging from 9 % to 19 % in Canada. For the coming quarters, banking executives have expressed concerns about the consequences of the new mortgage rules and NAFTA renegotiation.

FTSE TMX INDEX PERFORMANCE

Sector	Weight	Feb. 2018	2016
Universe	100 %	0,15 %	-0,65 %
Short Term	45,5 %	0,28 %	0,06 %
Mid Term	22,5 %	0,48 %	-0,65 %
Long Term	32,1 %	-0,26 %	-1,63 %
Federal	36,6 %	0,36 %	-0,41 %
Provincial	33,6 %	0,04 %	-1,23 %
Corporates	28,0 %	0,02 %	-0,23 %
RRB		0,31 %	-0,11 %

Source: ftse.com

The agencies are always wary about the lack of political will to restore public finances. In the case of New Brunswick, the demographic aspect also adds concern. The median age is five years older than in Canada, creating additional pressure on health care spending and reducing the province's potential for economic growth.

The new mortgage rules could reduce financing activities during the year, without however significantly increasing loan loss provisions. As long as the economy is expanding and the key rate remains low, households should not default on their mortgages.

STRATEGIC POSITIONNING

As the global economy turns the page on a stellar year, the US administration could be throwing cold water on growth by announcing punitive global tariffs on steel and aluminum imports. This measure is described by all as unacceptable and retaliation is emerging from the old continent. The European Union said it would defend member's interests by imposing tariffs on steel, clothing, shoes, bourbon and motorbikes. Thus, a future German Harley-Davidson owner wearing Levi's jeans and drinking Jack Daniels would see an increase on his invoice. President Trump's goal is to increase the production of metals in the United States, but the shortage of skilled labor in the United States will complicate his task. Meanwhile, metal imports are not expected to fall and these prices will be passed on to consumers. Since his inauguration, financial markets have only reacted to Trump's positive aspects from his economic plan, namely tax cuts and deregulation. Today, bond investors are discovering the negative side of his plan with the resurgence of protectionism and the increasing budget deficits. These rather inflationary measures come at a time when bond investors are already worried about wage and price increases.