MONTHLY BOND LETTER

AlphaFixe Capital

ECONOMIC EVENTS

JUNE 2023

- After a year of correction, the Canadian real estate market seems to have bottomed out and is now on the road to recovery. At least, that's what real estate sales figures for the Toronto area suggest. Sales rose by 20% month-on-month in May, bringing the annual change to 25%. The same is true of real estate sales in Calgary (+7.9%), Vancouver (+12.5%) and Montreal (+21.9%). New listings are progressing at a slower pace, with the median price of homes sold recovering over the past 3 months after 9 consecutive months of decline. This recovery in Canadian real estate goes hand in hand with the growth in Canada's population, which reached 40 million in June. In the first quarter alone, the population grew by 292,232, the highest first-quarter increase in history.

This upturn in Canadian real estate is one of the factors that contributed to raising the policy rate in June. Over the past year, Canada's population has grown by more than 1.2 million or 3.1%, mainly due to immigration. These new arrivals need to be housed, and the construction sector is unable to keep up with demand. What's more, the robust employment situation is not forcing households to sell their property, even though inflation and higher interest rates affected their budget over the past year. In short, of the 3 factors supporting real estate (demographics, employment and financing costs), two are still favorable.

- The US economy added 339,000 jobs in May, far surpassing investor expectations of 200,000. Job creation was spread across different industries, reflecting the strength of the economy. In fact, only the manufacturing (-2,000 jobs) and information (-9,000 jobs) industries posted slight declines last month. What's more, April's job creation was boosted by 41,000 to 294,000. As a result, the monthly average of job gains over the past year is 338,000, more than double what it was in 2019 (163,000) when the economy was considered strong.

ADP paints a similar picture, with an increase of 278,000 jobs in the private sector. On average, employees who stayed in their current jobs saw their salaries rise by 6.5% over the year, while those who switched jobs saw their salaries increase by 12.1% over the year. This rise in employment and wages, combined with the surplus savings accumulated during the pandemic, partly explains the economy's resistance to highre interest rates.

- Despite recent increases in policy rate, inflation in the UK remains persistent and difficult to control. The consumer price index rose by 0.7% in May, leaving the year-over-year unchanged at 8.7%. All 12 major categories making up the index posted gains in the last month. Excluding changes in energy and food prices, the core CPI index rose by 0.8% last month and by 7.1% over 12 months, the fastest pace of growth in 31 years. This increase is attributable to the fastest rise in 31 years in the price of services (+7.1%).

There has also been a marked rise in prices for discretionary spending such as airline tickets (+31.4%), as well as for leisure and culture (+6.7%). Considering the resilience of the British economy, the strength of the labor market of late, and the wage increases agreed to reduce the loss of household purchasing power, the Bank of England appears to have no respite.

RATE TRENDS

- The Bank of England has followed in the footsteps of the Bank of Canada and the Bank of Australia by stepping up monetary tightening. It has raised its key rate by 0.50% in order to stem the pressure on prices, which seems difficult to control. The economy is more resilient than expected and the labor market is strong, forcing wages up by over 7% in the past year. The Bank is therefore concerned about a second-round effect, where wage growth feeds inflation, creating a vicious circle that is difficult to break. The Bank was not the only one tightening monetarv policy. Norway's central bank (+0.50%) and the Swiss National Bank (+0.25%) also restricted credit. The European Central Bank also raised its rate by 0.25%, while indicating that there was still ground to cover to control inflation.

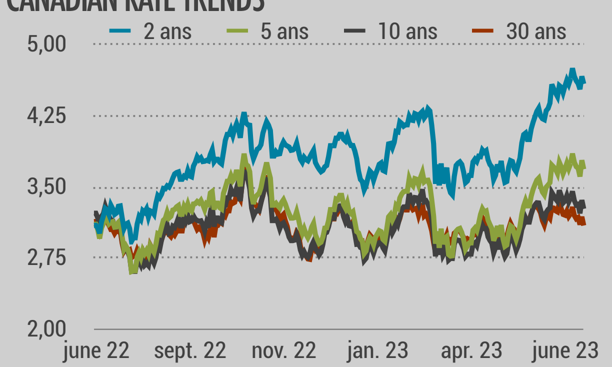
Inflation seems to be more persistent in Europe than in North America, requiring a restrictive monetary policy for longer. Central bankers on the Old Continent were also late to start tightening monetary policy, and are therefore playing catch-up with Canada and the USA. Nevertheless, they will eventually enter a phase of monetary policy adjustment, as is the case in Canada and Australia. The Federal Reserve seems to have reached this stage at its June meeting. It preferred to assess the impact of previous hikes on the economy before deciding whether further tightening was required.

BOND RATES

June 30, 2023	Canada	Monthly Change	Change 2023	USA	Monthly Change	Change 2023
Key Interest Rate	4,75 %	0,25 %	3,25 %	5,25 %	0,00 %	3,50 %
3 months	4,92 %	0,27 %	0,66 %	5,28 %	-0,11 %	0,94 %
2 years	4,59 %	0,37 %	0,53 %	4,90 %	0,50 %	0,47 %
5 years	3,69 %	0,24 %	0,28 %	4,16 %	0,41 %	0,15 %
10 years	3,27 %	0,08 %	-0,03 %	3,84 %	0,20 %	-0,04 %
30 years	3,09 %	-0,06 %	-0,18 %	3,86 %	-0,00 %	-0,10 %
RRB 30 years	1,37 %	0,05 %	0,17 %			

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	155	190	220	0	-10	0	-10	0	-10
Royal Bank, NVCC	A	215	260	300	0	-10	0	-10	0	-10
Sun Life, subordinated debt	A	190	225	250	-5	-10	-5	-15	-5	-20
Hydro One	A high	100	130	150	0	-10	0	-10	0	-10
Enbridge Inc	BBB high	155	205	245	0	-20	0	-10	0	-15
Altalink LP	A	100	130	150	0	-5	0	-5	0	-5
GTAA	A high	90	120	140	-5	-15	-5	-15	-5	-15
Bell Canada	BBB high	145	185	215	0	-15	0	-10	0	-10
Rogers Communications	BBBL	175	225	260	0	-5	5	0	0	-10
Loblaw	BBB high	135	170	195	0	-15	0	-15	0	-15
Canadian Tire	BBB	155	195	235	0	-15	0	-15	-5	-20
Province Québec	AA low	48	70	90	0	2	-2	-2	-3	-4
Province Ontario	AA low	50	71	91	1	2	-2	-3	-1	-4
CMHC	AAA	42	46	---	4	6	2	0		

Source: National Bank Financial

CREDIT MARKET

- Canadian corporate bonds new issuance totalled $13 billion in June, up $3.9 billion on the previous month and $5.6 billion more than in June 2022. Year-to-date, bond financing totals $49 billion, down 25% from the same period last year. This is the third-busiest June on record in terms of amounts issued. Issuers were also highly diversified, with 26 different issues from 19 companies. These included Northland Power Inc, with a $500 million hybrid green bond issue, the proceeds of which will be used to finance energy projects that meet the eligibility criteria of their green financing framework.

- The Office of the Superintendent of Financial Institutions (OSFI), the body that regulates our Canadian banks, has announced that it is raising the domestic stability reserve rate by 0.50% to 3.5% of risk-weighted assets, effective November 1. This reserve applies only to systemically important banks, and affects the 6 major Canadian banks only. With this increase, the minimum Tier 1 capital ratio will be 11.5% of assets. This announcement is aimed at strengthening the Canadian banking system in the face of multiple current and future vulnerabilities. Rising interest rates could make highly indebted households more vulnerable to bankruptcy, resulting in loan losses for financial institutions.

- Canadian provinces have issued a total of $6.6 billion as of June, which is 30% less than in June 2022, and brings the sum of issues in the current fiscal year (2023-2024) to $22.9 billion. With only one quarter completed this fiscal year, the province of Quebec has already executed 47% of its $27.5 billion financing program. Ontario has the same amount to fund, but has only completed 27% of its program. The situation is more difficult in British Columbia. Although the western province has completed 28% of its program, its funding requirements are significantly higher than last year. For the current fiscal year, British Columbia needs to borrow $18.9 billion in bonds, $14.3 billion more than last year.

FTSE TMX INDEX PERFORMANCE

Sector	Weight	June 2023	2023
Universe	100 %	0,04 %	2,51 %
Short Term	42,8 %	-0,34 %	1,00 %
Mid Term	28,2 %	-0,48 %	1,85 %
Long Term	29,1 %	1,09 %	5,39 %
Federal	38,0 %	-0,30 %	1,42 %
Provincial	34,3 %	0,29 %	3,32 %
Corporates	25,8 %	0,21 %	2,97 %
RRB		0,08 %	-0,27 %

Source: ftse.com

This decision does not change the picture for our 6 Canadian banks, which already have a Tier 1 capital level equal to the new required standards (11.5%). The banks' objective is to raise this to 12% by the end of the year. In the wake of the recent crisis surrounding U.S. regional banks, OSFI is sending a clear message to the rest of the world: our banking system is solid and well supervised.

Investors will have to get used to seeing new issues from the province of British Columbia, as it will borrow close to $40 billion over its next two fiscal years. This year, it plans to finance 63% of its needs with foreign currency bonds, more than double the Canadian average. Let's hope that foreign investors will be keen to invest.

STRATEGIC POSITIONNING

Central banks are doing everything they can to bring inflation back to target without triggering a severe recession. Having aggressively raised rates over the past year, central bankers must now assess the effect of these rate hikes on economic and price trends. Some banks, such as the Bank of Canada, the Bank of Australia and even the Federal Reserve, which paused in June, are now in an adjustment phase. What complicates central banks tasks is that this expansion is more the result of income growth than credit growth, as was the case in the USA prior to the 2008 financial crisis. The debt-to-disposable income ratio of American households has fallen from 135% in 2008 to 100% today. This period of deleveraging is unprecedented in recent American history. As a result, monetary tightening is no longer as effective at slowing the economy as it once was. On the other hand, Canada's indebtedness has not stopped growing, and the effect of monetary policy could be more direct. However, a surge in immigration over the past year has partly offset the restrictive effect of rising interest rates. New immigrants have to find housing and consume independently of the cost of money. It is therefore arguable whether key rates are high enough to slow down the economy, and whether the cuts anticipated in the US next year are not premature.