MONTHLY BOND LETTER

AlphaFixe Capital

NOVEMBER 2021

ECONOMIC EVENTS

- The Canadian economy grew at an annualized rate of 5.4% in the third quarter after contracting more than initially reported in the previous quarter (-3.2% vs. -1.1%). The easing of health measures boosted consumer spending by 17.9%, particularly for previously restricted activities such as food and beverage, accommodation, recreational and cultural services, and personal care. International trade also contributed to growth with an increase in exports (especially oil) coupled with a decrease in imports (automotive industry). On the other hand, investment declined, especially residential real estate and business inventories.

However, the situation could become more serious starting in November as British Columbia experienced significant flooding which should slow down the Canadian supply chain. Oh yes, let's not forget the outbreak of the Omicron variant and the possible risk of a slowdown at the end of the year if the authorities tighten up public health measures.

- The U.S. consumer price index (CPI) rose 0.9% in October and 6.2% over the past year, a pace not seen since November 1990. If we remove food and energy prices, the core index rose by 0.6% in one month and by 4.6% YoY. Again, not seen since August 1991. Energy prices jumped 4.8% last month, including gasoline (+6.1%) and fuel oil (+12.3%), but inflationary pressures are also evident elsewhere. New car prices rose 1.4% last month, bringing annual growth to 9.8% and 26.4% for used vehicles. Housing is also up 0.5% last month and 3.5% year-over-year.

It took only 17 months for inflation to go from 0.1% in May 2020 to 6.2% today, a pace of acceleration rarely seen. The rise in prices is worrisome enough to force the Federal Reserve to drop the temporary label it has attached to inflation this year, despite the presence of the Omicron variant. Is the Fed falling behind in its assessment again?

- Japan's economy contracted 0.8% quarter-over-quarter in September or -3.0% annualized. This is the second contraction in three quarters this year. The resurgence of Covid cases over the summer, coupled with ongoing supply chain disruptions, have dampened the Japanese economy. Aside from government spending, all other sectors of the economy declined.

The acceleration of the vaccination campaign in recent months suggests that consumer spending will improve in the last quarter of the year. In addition, the government has announced a new US$265 billion stimulus package, including a cheque for families with children.

RATE TRENDS

- Some central banks have chosen to tighten credit conditions in order to calm their overheating economy, inflation and real estate prices. This is the case for the central bank of New Zealand and South Korea, which each raised their key rate by 0.25% to 0.75% and 1.00% respectively. This was the second rate hike this year for these two banks. On the other hand, the European Central Bank (ECB) continues to defend the patient approach in the face of inflation, which it still describes as temporary despite a new peak in November (4.9%). According to the ECB, it would be inappropriate to raise rates at this time since price pressures should ease by the time the effect of the rate hike is felt in the economy, i.e. in 12 to 18 months.

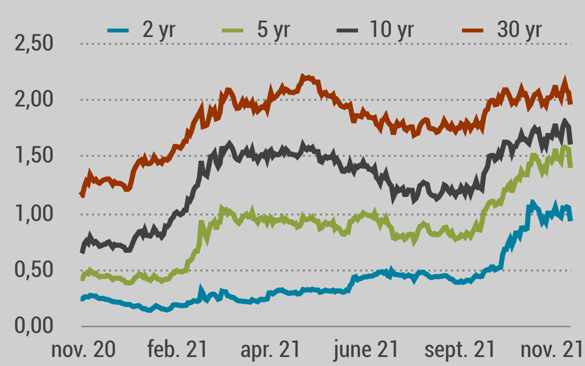
We may be entering a new chapter in this pandemic from a central bank perspective. Previously, the explosion of new Covid cases as we are seeing in Europe now or the emergence of a new variant (Omicron today) would prompt central banks to adopt a more dovish monetary policy. Currently, the increase in cases in South Korea has not kept the central bank from removing some of the stimulus in place. For its part, the Fed believes that the new variant could add to existing inflationary pressures. A return of the measures would increase demand for goods and intensify disruptions in supply chains.

BOND RATES

Nov. 30 2021		Monthly Change	Change 2021		Monthly Change	Change 2021
Key Interest Rate	0,25 %	0,00 %	0,00 %	0,25 %	0,00 %	0,00 %
3 months	0,07 %	-0,09 %	0,00 %	0,05 %	-0,00 %	-0,01 %
2 years	0,98 %	-0,11 %	0,78 %	0,57 %	0,07 %	0,44 %
5 years	1,40 %	-0,12 %	1,00 %	1,16 %	-0,02 %	0,80 %
10 years	1,57 %	-0,16 %	0,89 %	1,44 %	-0,11 %	0,53 %
30 years	1,89 %	-0,12 %	0,67 %	1,79 %	-0,14 %	0,15 %
RRB 30 years	0,05 %	-0,22 %	0,34 %			

Source: Bloomberg

CANADIAN RATE TRENDS



CREDIT BOND RISK PREMIUMS

Issuer	Credit Rating DBRS	Spread 5 yrs	Spread 10 yrs	Spread 30 yrs	Change 5 yrs month	Change 5 yrs 2021	Change 10 yrs month	Change 10 yrs 2021	Change 30 yrs month	Change 30 yrs 2021
Royal Bank, Bail-in-debt	AA	85	115	160	10	20	10	10	10	5
Royal Bank, NVCC	A	115	155	205	10	15	10	15	10	10
Sun Life, subordinated debt	A	105	145	195	15	15	15	15	15	10
Hydro One	A high	65	100	135	5	15	5	15	5	5
Enbridge Inc	BBB high	110	155	235	15	15	10	5	10	0
Altalink LP	A	65	95	130	5	15	5	15	5	5
GTAA	A high	65	100	135	5	15	5	15	5	5
Bell Canada	BBB high	95	140	210	10	15	10	10	10	10
Rogers Communications	BBB high	125	170	240	15	45	15	40	15	40
Loblaw	BBB high	90	135	190	10	15	10	10	5	-5
Canadian Tire	BBB	95	145	230	5	0	5	-10	0	-25
Province Québec	AA low	30	56	73	3	0	2	-1	3	-6
Province Ontario	AA low	34	61	77	3	-1	2	-1	2	-4
CMHC	AAA	27	40	---	3	6	2	8		

Source: National Bank Financial

CREDIT MARKET

- Canadian corporate bond new issuance reached $13.9 billion in November, up $3.4 billion from the previous month and $10 billion more than in November 2020. The green bond market continued its strong run this year with four new issues, including Bruce Power L.P.'s $500 million issue. The proceeds of this green bond will be used to finance or refinance nuclear facilities, a world first for this type of energy. Nuclear power is one of the options for achieving lower-carbon electricity generation, but it remains controversial given the management of nuclear waste and the environmental risks associated with an accident like Fukushima.

- Quebec's Minister of Finance has released his economic update. As is the case in many provinces, the projected deficit for the current fiscal year has fallen by 45% to $6.8 billion after the payment of $3.3 billion to the Generations Fund. The improvement in public finances is explained by an increase in revenues due to stronger-than-expected economic growth (6.5% compared to 4.2% forecast in March). The government therefore has budgetary leeway to help middle- and low-income people facing a rising cost of living. Thus, 3.3 million Quebecers will receive a cheque ranging from $200 to $275 to help them with the increase in inflation. The government also wants to invest to solve the labour shortage ($3 billion over 5 years), using incentive grants to train workers in various crucial sectors.

- U.S. high-yield bonds fell during the month of November as investors worried that the spread of the Omicron variant would affect the ability of companies to repay their debts. Yield premiums for these bonds jumped 52 bps in one month to close November at 3.67%, which translates into a decline of just over 1% in market value. This is the second month of negative returns this year and their worst result since September 2020. Lower rated companies (CCC) and those in the leisure industries were most affected by this flight to safety. Airline bonds also suffered.

FTSE INDEX PERFORMANCE

Sector	Weight	Nov. 2021	2021
Universe	100 %	0,87 %	-4,14 %
Short Term	39,9 %	0,23 %	-1,29 %
Mid Term	26,0 %	0,94 %	-3,79 %
Long Term	34,1 %	1,57 %	-7,88 %
Federal	34,2 %	0,87 %	-3,76 %
Provincial	37,4 %	1,14 %	-5,38 %
Corporates	26,2 %	0,47 %	-2,80 %
RRB		4,45 %	-1,74 %

Source: ftse.com

Wouldn't it have been more viable to offer a higher amount, but only to low-income people and exclude middle-income people? There aren't 3.3 million low-income people in Quebec. This cheque will only fuel demand in an environment where supply is still limited, so it will do nothing to curb inflation.

Despite widening in the last month, spreads still remain 19 bps below the year-end 2020 level. In addition to health risks, investors must also weigh inflationary risks that could prompt central banks to raise policy rates. Highly leveraged companies will have more difficulty meeting their obligations in such an environment.

STRATEGIC POSITIONNING

Inflation was considered the number one enemy, but Covid has just shown that it is not done yet. New cases of Covid have exploded in Europe, forcing the imposition of new restrictive measures in some countries where vaccination rates remain low. Already a concern, the situation has worsened with the arrival of the Omicron variant. The economic consequences remain unclear, as we still do not know the virulence of the variant and its resistance to vaccines. While there are risks to the economic recovery and employment, said Jerome Powell at the end of the month, inflation could accelerate. Did I hear stagflation from the Federal Reserve? Powell's logic is based on households spending more on goods and less on services and leisure. This increased demand will put additional pressure on global supply chains as the production environment is still disrupted. Remember Vietnam and China, which are closing factories at the sight of Covid cases. This is a change in the Federal Reserve's attitude toward health risk. Previously, each episode of variant and exploding cases was accompanied by cautious commentary and monetary policy support for the economy. Today, inflation is becoming more of the public enemy number one that central banks want to fight, even in the face of the health uncertainty that is keeping us on our toes.