MONTHLY BOND LETTER

AlphaFixe Capital

OCTOBER 2024

ECONOMIC EVENTS

- Demographics have been a driving force behind the Canadian economy in recent years, and the new immigration targets announced by the federal government will have a significant impact on our economy. The government has announced an annual target of 395,000 new permanent residents in 2025 and 365,000 in 2026. This is a significant drop from previously projected levels of around 500,000 per year. The federal government will also reduce the weight of temporary residents from the current 7% of the Canadian population to 5% by 2026. This means a drop of 445,000 temporary residents per year for the next two years. In total, immigration will reduce the size of the population over the next two years, rather than adding more than 3%, as was the case in 2023 and 2024.

The economic consequences are significant. Canada's GDP has managed to grow by 1.9% since the end of 2022, as the population has increased by 5% over this period. A drop in immigration could lead to an economic slowdown next year. On the other hand, these new targets will alleviate pressure on housing and rental prices, and will also help to rebalance the labor market, which has suffered an imposing influx of job seekers. This comes at a time when the Bank of Canada is accelerating its monetary easing, which will help to absorb shocks.

- The pace of growth in the US economy eased slightly over the summer, but the sources of growth are more robust. US GDP grew at an annualized rate of 2.8% quarter-on-quarter in the third quarter, down 0.2% on the previous quarter. However, consumer spending accelerated, rising by 3.7% compared with 2.8% in the spring. Investment rose slightly (+0.3%), particularly business investment (+3.3%). On the other hand, investment in residential property fell by 5.1% over the summer. International trade hampered expansion, but government spending contributed (+5%), notably military spending (+14.9%).

For the past 7 quarters, US GDP has been growing at an average rate of 2.9%, well above its potential level (1.8%), despite a higher rate structure. The job market has slowed, but is still expanding, with wages rising faster than inflation. If restrictive monetary policy fails to slow the economy considerably, the neural policy rate is therefore likely to be higher than the Federal Reserve and investors estimate.

- Eurozone GDP grew at an annualized rate of 1.5% in the third quarter, double the previous quarter's growth and economists' expectations. France led the way with a 1.5% gain, propelled by the Paris Olympics and consumer spending. Spain also posted robust growth this summer (+3.3%). However, the surprise came from Germany, where the economy avoided recession with annualized growth of 0.7% in the third quarter. Government and household spending drove the economy upwards.

Nevertheless, Europe's leading economy is still going through a difficult period. Since the third quarter of 2023, german GDP has failed to stick to two consecutive quarters of expansion, and it's possible that this sequence will continue in the fourth quarter. Volkswagen is currently undergoing a restructuring process that could culminate in plant closures in Germany and major layoffs.

RATE TRENDS

- The Bank of Canada caused no surprise by cutting its key rate by 0.50% to 3.75%. The monetary authority is pleased to have tamed inflation, which is now close to the Bank's target. The aim now is to keep inflation low and stable, and to achieve a soft landing for the economy. However, the economy is showing signs of weakness, growing at a moderate pace that is not keeping pace with population growth. Given the cuts announced this year and others to come, the Bank expects GDP growth to rise from 1.2% this year to 2.1% next year and 2.3% in 2026. If the economy evolves in line with the Bank's projections, it expects to cut its key rate again at future meetings, but the pace and timing will depend on economic conditions.

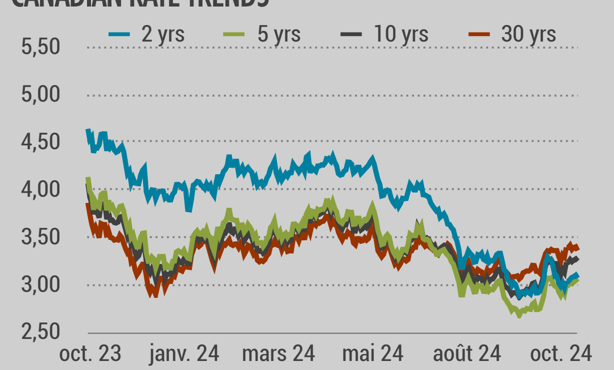
The tone of the Bank's press release does not suggest that it will continue this aggressive approach in the future. Upward and downward pressure on inflation appear increasingly balanced. The U.S. economy is stronger than expected and will require more moderate rate cuts. For the moment, the ingredients are not in place to justify another 0.50% cut in December. However, the Bank's work is not done, as the current policy rate is still above the neutral rate estimated by the Bank of Canada (2.25% to 3.25%).

BOND RATES

Oct. 31, 2024	Canada	Monthly Change	Change 2024	United States	Monthly Change	Change 2024
Key Interest Rate	3,75 %	-0,50 %	-1,25 %	5,00 %	0,00 %	-0,50 %
3 months	3,55 %	-0,67 %	-1,50 %	4,54 %	-0,08 %	-0,79 %
2 years	3,07 %	0,16 %	-0,82 %	4,17 %	0,53 %	-0,08 %
5 years	3,02 %	0,28 %	-0,16 %	4,16 %	0,60 %	0,31 %
10 years	3,22 %	0,26 %	0,11 %	4,28 %	0,50 %	0,41 %
30 years	3,29 %	0,15 %	0,26 %	4,48 %	0,36 %	0,45 %
RRB 30 years	1,48 %	0,04 %	0,18 %			

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 2024	Change 10 yrs month	Change 10 yrs 2024	Change 30 yrs month	Change 30 yrs 2024
Royal Bank, Bail-in-debt	AA	90	115	150	-5	-40	-15	-50	-10	-45
Royal Bank, NVCC	A	135	170	215	-5	-50	-15	-60	-10	-55
Sun Life, subordinated debt	A	110	150	190	-5	-55	-5	-55	0	-45
Hydro One	A high	65	100	130	-5	-20	-5	-15	-5	-10
Enbridge Inc	A low	100	140	195	-10	-30	-15	-35	-10	-25
Altalink LP	A	65	100	130	-5	-20	-5	-15	-5	-10
GTAA	A high	60	95	125	-5	-20	-5	-15	-5	-5
Bell Canada	BBB high	110	145	200	0	-15	-5	-20	5	0
Rogers Communications	BBBL	115	150	205	-10	-30	-15	-35	-5	-25
Loblaw	BBB high	90	125	170	-5	-15	-10	-15	-5	-5
Canadian Tire	BBB	120	160	210	-5	0	-10	0	-5	5
Province Québec	AA low	27	68	93	-4	-11	-4	2	-4	5
Province Ontario	AA low	29	67	90	-3	-11	-4	-1	-4	0
CMHC	AAA	18	41	---	0	-10	0	-3		

Source: National Bank Financial

CREDIT MARKET

- Canadian corporate bonds new issuance totalled $14.3 billion in October, up $1.8 billion on the previous month and $11.8 billion more than in October 2023. Year-to-date, bond financing totals $111.4 billion, up 45% on the same period last year. With two months of activity left in the calendar year, the primary market is $7.6 billion short of the record set in 2022. It is therefore highly likely that 2024 will become the new peak. The banking sector was a major contributor in October, with 7 issues accounting for 61% of the total amount.

- The decision of the American regulatory authorities has been announced. TD Bank has pleaded guilty to not having an adequate system in place to combat money laundering in the United States, and will have to pay a fine of US$3 billion. Last quarter, TD had taken a $3.57 billion provision in connection with this charge, thereby crippling its quarterly earnings. This is the largest fine ever imposed on a bank by US anti-money laundering authorities, eclipsing the nearly US$2 billion fine paid by HSBC in 2014 for transferring billions of dollars on behalf of Mexican drug cartels. In addition, as part of the agreement reached with the regulator, TD will have an asset cap imposed on its U.S. banking operations. The bank will not be able to grow beyond its current $370 billion in assets as long as the cap remains in place.

- In its fall fiscal update, the Province of Ontario now expects a deficit of $6.6 billion (0.6% of GDP) for the current fiscal year, $3.2 billion less than the original budget plan. This improvement is due to a $6.9 billion increase in revenues from personal and corporate income tax, as well as sales tax. The economy is progressing better than expected in the spring. This improvement prompted the government to increase spending (+$3.8 billion) by offering all Ontarians and children a (pre-election) cheque for $200. The budgetary upturn should also continue in subsequent years, with a deficit of $1.5 billion next year, $3.1 billion better than forecast.

FTSE TMX INDEX PERFORMANCE

Sector	Weight	oct 2024	2024
Universe	100 %	-1,01 %	3,21 %
Short Term	41,7 %	-0,30 %	4,70 %
Mid Term	29,4 %	-1,44 %	3,57 %
Long Term	29,0 %	-1,59 %	0,53 %
Federal	40,6 %	-1,13 %	2,77 %
Provincial	32,7 %	-1,25 %	2,18 %
Corporates	24,9 %	-0,50 %	5,35 %
RRB		-0,65 %	2,74 %

Source: ftse.com

This non-monetary constraint will limit the expansion of the bank's U.S. operations and the growth of its earnings. TD generates just over 25% of its revenues from its U.S. divisions. Despite this historic fine, spreads on TD Bank bonds have increased little. This testifies to investor confidence in the Bank's balance sheet strength and capitalization.

Changes in Canada's immigration thresholds over the next few years could also help the province's finances. Ontario has welcomed a significant number of new residents in recent years, putting pressure on spending on public services such as health, education and social services.

STRATEGIC POSITIONNING

The Federal Reserve began its monetary easing with a bang, but the strength of economic data seems to be slowing the Fed's ardor for future meetings. The election of Donald Trump and the possibility of a Republican sweep in Congress could also alter the trajectory of monetary policy. If he wins the support of both houses, Trump could carry out his policy promises unhindered, as he has surrounded himself with political allies who, unlike his first term, will not oppose him. He wants to cut taxes for corporations and the whealthy, and extend the tax cuts established in 2017 during his first term. He will tackle trade with tariffs, but the extent remains uncertain. Immigration is also at the heart of his promises, with his intention to deport many illegal immigrants. Is this possible or even economically feasible? It's doubtful. A stimulated economy, impediments to world trade and worsening labor shortages raise fears of a resurgence of inflation. The exploding budget deficit is also at the forefront of investors' minds, as they demand higher yields for holding US Treasury fixed-income debt. This election also has consequences for Canada, where the Canada-U.S.-Mexico Agreement will be renegotiated in 2026, and it's highly likely that further concessions will have to be made. What will be the impact on our currency and the Bank of Canada? Many questions await the final results in Congress.