

MONTHLY BOND LETTER

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ECONOMIC EVENTS

MAY 2025

- Canada's GDP grew at an annualized rate of 2.2% in the first quarter, following 2.1% growth in the previous quarter. However, this overall result masks certain weaknesses. Growth was mainly driven by a 6.7% rise in exports, as US companies rushed to get ahead of the Trump tariffs. Imports also rose, but at a more moderate pace (+4.4%). Some of these imports were stockpiled by companies, contributing to an inventory build-up that added 1.4% to GDP growth. Household consumption also increased (+1.2%), as did business investment (+4.0%), but investment in the residential sector fell (-10.9%).
- Economic uncertainty has prompted US households to manage their budgets more cautiously. In April, personal income rose by 0.8%, bringing annual growth to 5.5%. Spending, on the other hand, rose more modestly, by just 0.2% during the month. Since the beginning of the year, monthly income growth has outstripped expenditure growth, reversing the trend observed in 2024. As a result, households have strengthened their cushion: the savings rate, expressed as a proportion of disposable income, now stands at 4.9%, compared with 3.5% last December. The PCE price index rose by 0.1% in April, both in its overall and core version (excluding food and energy).
- In a bid to stimulate an economy weakened by the trade dispute with the United States, the People's Bank of China has announced new monetary support measures. It reduced its policy rate by 0.1% to 3.0%, its first cut since October 2024. It also lowered the reserve requirement rate by 0.5% to an average of 6.2% for banks. This reduction will free up some \$138 billion to be injected into the economy in the form of loans.

While the overall growth figure is impressive, it is largely tainted by temporary effects linked to trade tensions. Excluding trade and inventory changes, final domestic demand fell by 0.1% in the first quarter, compared with average quarterly growth of 3.6% over the previous four quarters. In addition, private-sector employment posted two consecutive months of decline, particularly in manufacturing. The economy is therefore more fragile than GDP would suggest.

This is a slowdown in consumption growth, not a contraction, as the job market and incomes continue to grow. For the time being, consumers have not seen their bills rise as a result of tariffs, largely because many companies had built up inventories in anticipation. However, once these inventories of products not subject to tariffs are exhausted, companies will either have to adjust their prices upwards, or reduce their profit margins to reflect the new commercial reality. Both will have a negative impact on employment and GDP growth.



Faced with major trade obstacles, China needs to stimulate domestic demand. It will surely take more than a 0.1% cut in the financing rate to encourage households to spend more. Households are still feeling the effects of the real estate slump, and the absence of a comprehensive social safety net is pushing families to save even more in uncertain times.

RATE TRENDS

- At its meeting on June 4, the Bank of Canada once again maintained its policy rate at 2.75%. It reiterated its intention to support economic growth while ensuring that inflation remains well under control. It is precisely because of this price stability objective that the Bank preferred to adopt a cautious approach. The Bank's core inflation measures have recently risen above 3%. Uncertainty surrounding tariffs is putting pressure on the Canadian economy. On the face of it, GDP growth remains robust, but this is largely due to a temporary rise in trade and inventory accumulation. At the same time, employment in sectors directly affected by tariffs is declining. Against this backdrop, the Bank of Canada prefers to give itself more time to assess economic developments.

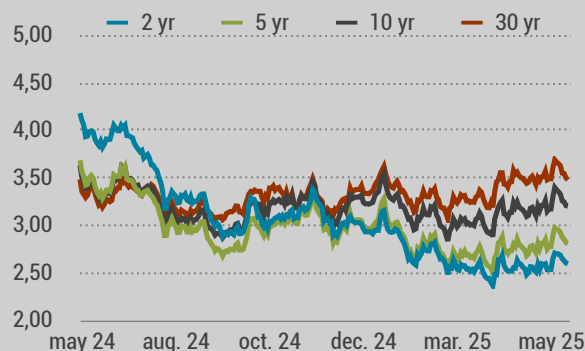
The implicit message of the press release is that the Bank of Canada would like to offer additional support to the economy, but remains concerned about rising inflation. The Canadian economy is feeling the negative effects of tariffs, but it's not collapsing. For the time being, the slowdown is concentrated in the sectors directly affected by these tariff measures, and has not yet spread to the economy as a whole. This pause will enable the Bank to assess the resilience of the Canadian economy after a major easing, and to obtain greater visibility on the federal government's budgetary intentions. If there is a widespread downturn in the job market, the Bank could then get the green light to lower its key rate again.

BOND RATES

		Monthly Change	Change 2025		Monthly Change	Change 2025
May 30, 2025						
Key Interest Rate	2,75 %	0,00 %	-2,25 %	4,50 %	0,00 %	-1,00 %
3 months	2,66 %	0,00 %	-0,48 %	4,33 %	0,04 %	0,02 %
2 years	2,59 %	0,11 %	-0,34 %	3,90 %	0,30 %	-0,34 %
5 years	2,81 %	0,13 %	-0,16 %	3,96 %	0,23 %	-0,42 %
10 years	3,20 %	0,11 %	-0,03 %	4,40 %	0,24 %	-0,17 %
30 years	3,48 %	0,04 %	0,14 %	4,93 %	0,25 %	0,15 %
RRB 30 years	1,56 %	-0,02 %	0,11 %			

Source: Bloomberg

CANADIAN RATE TRENDS



CREDIT BOND RISK PREMIUMS

Issuers	Credit Rating DBRS	Change								
		Spread			5 yrs		10 yrs		30 yrs	
		5 yrs	10 yrs	30 yrs	month	2025	month	2025	month	2025
Royal Bank, Bail-in-debt	AA	85	110	140	-10	5	-10	5	-10	0
Royal Bank, NVCC	A	130	165	205	-20	5	-20	5	-20	0
Sun Life, subordinated debt	A	100	135	175	-25	5	-25	0	-25	0
Hydro One	A high	60	90	115	-10	0	-10	0	-5	-5
Enbridge Inc	A low	95	135	175	-20	5	-20	10	-20	0
Altalink LP	A	60	90	115	-10	0	-10	0	-5	-5
GTAA	A high	55	85	110	-10	0	-10	0	-5	-5
Bell Canada	BBB	100	135	170	-15	0	-15	-10	-20	-20
Rogers Communications	BBBL	105	140	170	-15	0	-15	-10	-25	-20
Loblaw	BBB high	80	115	150	-20	5	-20	0	-20	-10
Canadian Tire	BBB	105	140	180	-20	0	-20	-5	-20	-15
Province Québec	AA low	22	67	91	-4	-2	-1	2	-7	1
Province Ontario	AA low	23	66	87	-4	-1	-1	4	-7	1
CMHC	AAA	13	32	---	-2	0	-3	-4		

Source: National Bank Financial

CREDIT MARKET

● Canadian corporate bonds new issuance totaled \$14.3 billion in May, up \$11.2 billion on the previous month and \$2.3 billion more than in May 2024. Year-to-date, bond financing totals \$49 billion, 2% less than at the same time last year. After an uncertain April in terms of international trade, financial markets recovered the ground lost in the previous month. Corporate bond spreads narrowed by 0.14%, returning to their lows of 0.99% at the start of the year. Long-term provincial bonds moved in the same direction, but the decline in spreads was less pronounced (-0.06%).

● Ontario has presented its budget for the 2025-2026 fiscal year and, as expected, the Minister of Finance has had to deviate from his most recent deficit projection published in the fall in order to take into account the risks associated with U.S. tariffs. Ontario's deficit will be \$14.6 billion, \$13.1 billion higher than in the recent economic update, and \$8.6 billion higher than in the previous fiscal year (2024-2025). Revenues are expected to decline by 0.8%, mainly due to lower corporate tax revenues. On the other hand, spending will increase by 2.2% due to the implementation of various support programs for workers and businesses affected by tariff threats. The trade dispute is also delaying the return to a balanced budget, now scheduled for fiscal 2027-2028, a year later than originally planned.

● DBRS Morningstar has downgraded Bell Canada's credit rating by one notch to BBB and BCE Inc's credit rating from BBB to BBB(low), each with a stable outlook. This downgrade comes despite the announcement of a dividend cut from \$3.99 to \$1.75. Although the dividend cut is a step in the right direction, the agency justifies its decision by pointing to a deterioration in BCE Inc.'s financial profile, characterized by rising indebtedness and increased pressure on cash flow. The planned acquisition of Zipy Fiber, a fiber-optic Internet service provider in the northwestern U.S., for around \$7 billion, is a key factor in this deterioration. DBRS expects gross leverage to remain in a high range of 3.50x to 3.75x EBITDA over the next three years.

FTSE TMX INDEX PERFORMANCE

Sector	Weight	May 2025	2025
Universe	100 %	0,02 %	1,38 %
Short Term	39,7 %	0,09 %	1,91 %
Mid Term	31,1 %	-0,31 %	2,07 %
Long Term	29,2 %	0,26 %	-0,16 %
Federal	41,3 %	-0,36 %	1,44 %
Provincial	32,7 %	0,09 %	0,88 %
Corporates	24,2 %	0,58 %	1,98 %
RRB		0,23 %	1,82 %

Source: ftse.com

This budget is marked by the risks associated with trade with the United States, as Ontario is the most exposed province, given the size of its industrial base and the high concentration of the automotive sector within its borders. The recent increase in tariffs on steel and aluminum from 25% to 50% will also deal a heavy price to Ontario's steel mills.

Telecommunications companies have benefited from the accommodating immigration policies put in place under the Trudeau era. However, the slowdown in population growth is intensifying competition and reducing average revenue per user. Telecommunication companies will have to adapt and manage their finances more carefully.

STRATEGIC POSITIONNING

The anxiety that pervaded investors in April gradually dissipated after the USA and China agreed a 90-day truce in their trade war that was damaging their respective economies. Trump also threatened the European Union with 50% tariffs, only to grant a reprieve until July to make way for negotiations. This strategy of tariff threats followed by backtracking when a negative reaction from financial markets occurs has earned him the nickname TACO, for Trump Always Chickens Out. Investors have realized that they can reverse certain unfavorable decisions if they exert sufficient pressure on the markets. This partly explains why risk premiums on credit bonds have returned to their lows of the beginning of the year. Stung by this image of weakness, Trump is likely to adopt a firmer stance in future trade negotiations. The next breaking point, beyond which his administration will have to backtrack, could therefore be much more painful for investors. This aggressive approach to international trade could also resurface if he succeeds in getting his tax-cutting plan through Congress. As presented, this budget would increase the deficit by \$472 billion for fiscal 2025. At over 6% of GDP, the budget deficit will have to be cut in half to be sustainable, especially as its trade war will limit its access to foreign capital.