NEO FIXD

Evolve Active Core Fixed Income ETF

FIXD invests primarily in domestic and international high quality fixed income securities, and to a lesser extent, adding yield or enhancing returns on the portfolio by opportunistically investing in international fixed income securities, emerging market debt, preferred shares, convertible bonds and non-investment grade bonds.

For the month ending February 28, 2019

TICKER: FIXD

SUB-ADVISOR: Foyston, Gordon & Payne, Inc.

FOYSTON, GORDON & PAYNE INC.
INVESTMENT COUNSEL

Fixed income allocations remain a core component of many investor portfolios as a source of income and portfolio diversification. Foyston, Gordon & Payne Inc. has managed the FGP Core Plus Bond Fund since December 31, 2015.

OVERVIEW:

Financial markets continued to respond positively in February to the now-neutral Fed and a growing expectation for a resolution to the U.S./China trade negotiations. The S&P 500 has surged by over 11% in the first two months of the year (the TSX has done even better – up over 12%) making this the best start to the year since 1991. While several factors contributed to these results – growing optimism over U.S.-China trade talks, continued decent economic growth, as well as a return of risk appetite in markets that appeared to be oversold by the end of the year - the primary reason is the market's belief that the Federal Reserve intends to leave short-term interest rates unchanged while it takes some time to assess the impact of its previous interest rate hikes on an economy that still is not faced with meaningful inflationary pressures. The Bank of Canada too has indicated, although less clearly than the Fed, that it expects the pace of their expected rate hikes to slow at least for the first half of 2019. Interest rates were mostly unchanged at the front end of the yield curve while longer-dated maturity yields rose modestly, steepening the yield curve. The domestic five year bond yield increased by about 5 basis points in February while the equivalent rate in the U.S. increased by 7 basis points. For the year, the five yield is lower by 7 basis points in Canada and is unchanged in the U.S.

It was not just common equities that rebounded strongly in the first two month of 2019 as Canadian corporate bonds also retraced much of the significant widening we witnessed in credit spreads during the fourth quarter of last year. The funds above-index exposure was a positive contributor to performance during the month although the very high-quality nature of our individual holdings somewhat limited our full upside participation as it was some of the riskier names in our market that performed best. We remain comfortable with this trade off as we would rather maintain our focus on longer-term quality and value within the portfolio rather than performance chasing in the short run.

Even though risk assets (equities, corporate bonds, etc.) performed strongly to start the year, the preferred share market in Canada has been a little slower to rebound. We anticipate that in the coming months the market will gradually recognize the increasing dividend levels of preferred shares (even in the absence of moves higher in key interest rates) and the further improved valuation relative to more widely followed asset classes that have rebounded strongly this year. When viewed with a longer-term investment time horizon we remain quite comfortable with an increased allocation to preferred shares as the asset class is attractively valued and offers a significant yield advantage over other fixed income options available in the market today.

Evolve ETFs
Brookfield Place, 161 Bay Street, Suite 2700, Toronto ON M5J 2S1
416.214.4884 | 1.844.370.4884 | www.evolveetfs.com

OUTLOOK AND PORTFOLIO STRATEGY:

Overall portfolio strategy was little changed from the end of 2018. The fund continues to hold increased allocations to both corporate bonds and preferred compared to Q4 2018. Additionally, the ETF currently has minimal exposure to high yield bonds. While the domestic economy is moderating from the highs in previous years, we continue to expect to see positive growth in the near term which should work to support risk assets going forward. Further, we remain confident in the credit quality of the individual investments we have made in each of these asset classes. Portfolio duration remains below the benchmark's duration as FGP continues to have an unfavorable long-term view of the bond market's risk/reward characteristics. FGP continues to believe that interest rates remain at a level inconsistent with Canada's economic fundamentals. The portfolio is positioned to perform well against its benchmark in a stable to rising rate environment.