TSX EARN

MONTHLY COMMENTARY

Evolve Active Global Fixed Income Fund

EARN seeks to generate positive returns throughout the interest rate and economic cycles, firstly by allocating to different credit asset classes, and also through bottom-up individual security selection.

As at July 31, 2020

ETF TICKER: EARN (Hedged)
MUTUAL FUND FUNDSERV CODE: EVF130 (Class F); EVF131 (Class A)

SUB-ADVISOR: Allianz Global Investors (AllianzGI)

Allianz Global Investors

AllianzGI is one of the world's leading active investment managers, managing USD 601 billion in assets, including over USD 200 billion in global fixed income (as at March 31, 2019).

MARKET & PORTFOLIO UPDATE:

July was another good month for risk assets, despite spikes in coronavirus infections (especially in the US), strongly negative Q2 GDP prints, and escalating tensions between the US and China. In the meantime, we continue to get a drip feed of policy stimulus that is supporting asset markets. EU leaders finally came to an agreement on the Next Generation EU recovery fund and a multi-year budget; along with recent ECB policy measures, this helped to anchor peripheral Euro bond yields and suppress volatility in these markets. Meanwhile 10-year US Treasury yields continued to grind lower, ending the month at just 0.53% - around historic lows. Credit spreads responded positively and finished the month 19bps tighter for Investment Grade and 95bps tighter for high yield, with lower rated issues outperforming in spread terms, but BB issues were helped by their longer duration in total return terms. USD issues strongly outperformed European ones. Oil issues also continued their strong recovery, even as WTI crude traded sideways around $40/barrel.

In this context all credit sectors contributed positively but our high yield industrials were the strongest. The equity index hedge position detracted as stock markets continued to edge higher. Away from this, were only a couple of very mild detractors at the security level.

During the month we exited a position in communications, while adding a new name in capital goods. We also did an issuer rotation within consumer cyclical.

OUTLOOK:

Central banks have restored market functioning since the peak of the crisis and financial conditions have loosened considerably, but questions remain about market vulnerability to a re-emergence of downside global growth risks.

Our mantra has been that central banks have been providing liquidity, not solvency, so the key is to find good companies with bad balance sheets rather than bad companies in the more stressed bucket. It seems that companies with material direct impact from Covid-19 are finding traction hard – but away from that demand is strong even for cyclicals as long as they have a good rating.

Therein lies the next chapter, after 2nd Quarter results which were in line with moribund expectations and 3rd Quarter outlooks that are "seeing some upturn", we probably need to wait for the fourth quarter to see more directionality and rating agency action. Our credit research team still expects another wave of fallen angels and that should provide opportunities for canny investors.