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 January 29, 2021.

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).

PERFORMANCE ANALYSIS:

Markets started 2021 where they left off in 2020, in buoyant mood. The reflation theme that has characterised market sentiment over the past six-to-nine months was given a further boost after Democrats took slim control of the US Senate after the State of Georgia run-off elections, raising hopes of another large US fiscal stimulus in early 2021. Markets also looked through the subsequent political tensions in the US Capitol ahead of the Biden inauguration, with 10-year US Treasury yields rising to 1.15% - their highest levels since March 2020. However, in the second half of January, risk sentiment deteriorated somewhat as expectations of a very strong cyclical global growth rebound in 2021 were pared back, Italian political risks resurfaced and as equity markets also exhibited some volatility. Nonetheless, the US Federal Reserve and ECB re-iterated their highly accommodative policy stance, with Fed Chair Powell clearly indicating that the Fed is in no hurry to taper its asset purchase programme until the economic recovery is firmly established. 10-year US Treasury yields ended the month at 1.07%. Oil prices continued to climb, with WTI futures breaking the $50/barrel threshold for the first time since February 2020.

At the end of the month, the VIX index of equity volatility recorded its third largest ever 1-day percentage increase. This was caused by retail investors squeezing various short positions of hedge funds, who were then forced to unwind risk as they faced margin calls. This activity resulted in the S&P 500 dropping 2.5% and a ~0.20% drop in High Yield bond prices. The markets do seem to have put this issue behind them for now and have largely recovered. However, we believe that this illustrates that markets are in an uneasy equilibrium at the moment.
Performance in the credit markets was mixed; spreads were flat overall for the month with lower rated issues generally outperforming in total return terms thanks to their higher income and shorter duration. Energy issuers performed well on the strengthening crude price.

PORTFOLIO STRATEGY AND ACTIVITY:

During the month we increased our overall risk, adding new positions in energy, chemicals, consumer staples, and technology; we funded these out of some EM government energy companies and an insurer.
There is a balance of offsetting factors keeping the overall direction of credit markets uncertain at this point. Our view remains that monetary policy will remain loose well into 2021. Central bank efforts to reflate the economy should be supportive for commodities in general, while greater OPEC discipline and pivoting US energy policy should be beneficial for oil prices in particular. The flow of credit issuance is expected to ease, adding a positive technical factor.

While the approval of several Covid vaccines is positive, there will be logistical challenges in implementation and continued infections for the near term. Vaccines should in turn help economic recovery, but this may be offset by persistent unemployment and idiosyncratic company issues. Another potential risk is that as companies become more confident as vaccines are rolled out, they use their large cash balances for share buy-backs, thus increasing leverage, or that vaccine roll-out is slower than currently expected.
Overall, our base case for 2021 is that credit returns should be driven by income, with selectivity required at both the sector and issuer level.