JANUARY 2024

MONTHLY UPDATE

Evolve Active Core Fixed Income Fund

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.

NEO **FIXD**

ETF TICKER: FIXD (UNHEDGED)
MUTUAL FUND FUNDSERV CODE: EVF110 (CLASS F); EVF111 (CLASS A)
SUB-ADVISOR: ADDENDA CAPITAL

ADDENDA CAPITAL

Active management in Canadian preferred shares continues to be an attractive investment opportunity. Addenda Capital is one of Canada's largest multi-asset investment firms, with over $33.4 billion in assets under management*, including $21.7 billion in fixed income and over $829 million in preferred shares.

Source: Addenda Capital, as at June 30, 2023. *Excludes $1.8 billion in Advisory assets and $309 million in Overlay assets.

Market Review

While the bond market closed 2023 with a strong outturn, the momentum slowed in January as the market reassessed the rhetoric surrounding imminent rate cuts. Expectations of the first rate cut, being as early as March, were pared back as the Fed indicated that rates are likely to move lower in coming months but has pushed back on talk of a move as early as March.

Both the U.S Central Bank and the Bank of Canada (BoC) held rates steady in January. The BoC held its target for the overnight rate at 5%, with the Bank Rate at 5¼% and the deposit rate at 5%. The Bank is continuing its policy of quantitative tightening.

BoC-Monetary Policy Report

The Bank of Canada projections for global growth edged up to 3.0% in 2023 and 2.5% in 2024. The BoC revised materially up their US growth in 2024 to 1.7% (no landing) from 0.8% (soft landing).

For Canada, the central bank shows small downward growth revision for 2023 to 1.0% and 0.8% this year before a strong recovery to 2.4% in 2025.

On the inflation front, the Bank now expects the inflation rate to be 2.8% in 2024 before returning roughly to target in 2025.

Potential output in Canada is expected to increase by about 2% on average over 2023 to 2025.

Portfolio Positioning

The Evolve FIXD CorePlus strategy had negative absolute returns during the month of January, but strong relative performance with respect to benchmark. Duration contributed to performance, as well as security selection.

Perspective

Growth

Economic growth slows in 2024 but remains positive as domestic demand is supported by a fully employed labour market. In Canada, consumer spending is supported by strong population growth and investment income. Unemployment stays close to cyclical low levels as labour market rebalancing progresses and unit labour costs fall.

Restrictive monetary policy for a longer time increases the risk of recession.

Inflation

Inflation pressure declines in 2024 but achieving central bank targets may prove difficult without further economic deceleration.

Productivity gains in the US provide some relief to inflation pressures with unit labour costs growing below 2%. The US benefits more than Canada which may cause some divergence in the short term

Policy

Against the backdrop of slowing economic growth, and moderating inflation, central banks will now manage policy with a focus on economic growth.

The Fed has the opportunity for a mid-cycle ease in rates in the first half of 2024, while the BoC faces the risk of further tightening and will likely need to maintain higher rates for most of the year.

Expect continued steady reductions in balance sheet holdings which will reduce liquidity and support for risk assets.

Expectations are for no significant additional fiscal stimulus.

Risks

Uncertainty related to potential changes to monetary policy by central banks, as well as geopolitical risks and US election noise contribute to market volatility.

Fed waiting too long to ease and maintaining high real rates in a non-inflationary growth environment hurts economic growth.

The BoC easing too soon as it follows the Fed while still facing inflationary growth due to a labour market which keeps inflation elevated.

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