MONTHLY BOND LETTER

AlphaFixe Capital

NOVEMBER 2017

ECONOMIC EVENTS

- Canadian employment in Canada jumped 80,000 in November, after gaining 35,000 in the previous month. As a result, the unemployment rate fell by 0.4 % to 5.9 %, a low since February 2008. The majority of jobs are from the private sector (72,000) and are geared toward part time workers (50,000). However, full-time jobs were predominant in the last year (441,000), while part-time positions decreased slightly (-51,000). Geographically, Ontario dominates (44,000) followed by British Columbia (18,000) and Quebec (16,000). Labor market robustness has resulted in average wage growth of 5.6 % over the past year.

The upturn in the labor market is starting to become a problem for some companies. More than 41 % of small business owners believe that the labor shortage is an impediment to increased production and sales. The example of Fleury Michon, who had to close a production line due to lack of staff, is a good illustration of the challenges facing small businesses which in turn would lead to higher wages to attract employees, thus creating inflationary pressures.

- In the United States, the gap between the number of unemployed (6.5 million) and the number of job vacancies (6.1 million) has reached its lowest level since January 2001. During the height of the financial crisis, there was 13 million more unemployed people than available jobs. On the other hand, the number of workers who quit their jobs was 3.2 million, up 100,000 in one year. Generally, workers leave their jobs to improve conditions, such as wages.

Given the shortage of skilled workers in the United States, companies could turn to investment projects to increase production. In this regard, company investments in equipment has greatly improved in the last three quarters.

- Economic activity in the euro zone has improved. In November, Markit's manufacturing activity index has reached its highest level in 17 years (60.1). This is the second highest reading in the index' history. Production and new orders continue to grow, including exports. This trend has led to the strongest job growth since the survey's inception back in June 1997.

The upturn in manufacturing activity in 2017 is beginning to feel its effects on inflation. The price index component has been at its peak for six and a half years, while sales prices are at a level which has not been seen since June 2011. Therefore, the ECB could fritter redire its QE program in 2018.

RATE TRENDS

- During his confirmation as Chairman of the Federal Reserve in front of the US Senate, Jerome Powell said the policy rate would increase a little, continuing Janet Yellen's path. This continuity allowed the 2-year US rate to reach a record high in the last nine years at 1.78 %. On the other hand, Mr. Powell mentioned that the authorities "will continue considering appropriate ways of easing regulatory burden", setting himself apart with the former President.

- Short-term rates continue to rise since September due to restrictive monetary policy bias, while long-term rates remained stable. As a result, the curve flattened with the US 30-year and 2-year yield spread falling below the 1 % mark for the first time in 10 years. In Canada, this spread closed the month at 80 bps, also a record low since before the financial crisis.

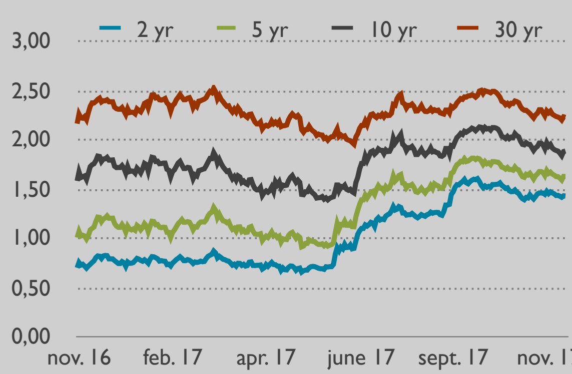
The US economy strength will force the Fed to raise its policy rate, and a rate hike is expected in December. Yield curve flattening is a result of a change in the monetary policy, as inflation expectations remain stable. However, the curve's flattening recession indicator does not have the same scope as before. The Fed's three quantitative easing programs and the twist operation have created a downward pressure on rates. The Fed has estimated that the cumulative effect of these efforts has reduced the 10-year rate by 105 bps.

BOND RATES

Nov. 30 2017		Monthly Change	Change 2017		Monthly Change	Change 2017
Key Interest Rate	1,00 %	0,00 %	0,50 %	1,25 %	0,00 %	0,50 %
3 months	0,88 %	0,01 %	0,43 %	1,26 %	0,12 %	0,76 %
2 years	1,43 %	0,04 %	0,69 %	1,78 %	0,18 %	0,59 %
5 years	1,63 %	0,01 %	0,52 %	2,14 %	0,12 %	0,21 %
10 years	1,89 %	-0,06 %	0,17 %	2,41 %	0,03 %	-0,03 %
30 years	2,23 %	-0,07 %	-0,08 %	2,83 %	-0,05 %	-0,24 %
RRB 30 years	0,61 %	-0,08 %	0,12 %			

Source: Bloomberg

CANADIAN RATE TRENDS



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CREDIT BOND RISK PREMIUMS

ISSUER	Credit rating DBRS	Credit rating S&P	Spread 5 yrs	Spread 10 yrs	Spread 30 yrs	Change 5 yrs month	Change 5 yrs 2017	Change 10 yrs month	Change 10 yrs 2017	Change 30 yrs month	Change 30 yrs 2017
Royal Bank, deposit notes	AA	AA-	75	90	130	5	-20	0	-20	0	-25
Manulife, Senior debt	A high	A+	90	115	165	5	-25	0	-20	5	-20
Fortis Inc.	BBB high	BBB+	90	135	170	0	-30	0	-30	0	-55
Hydro One	A high	A	65	85	135	0	-15	0	-20	5	-15
Enbridge Inc	BBB high	BBB+	115	165	230	-5	-15	-5	-15	-5	-10
Encana Corp	BBB low	BBB	135	195	275	-10	-80	-15	-90	-20	-70
GTAA	---	A+	50	70	90	0	-20	0	-25	0	-45
Bell Canada	BBB high	BBB+	95	145	200	0	-20	0	-20	-5	-25
Rogers Communications	BBB	BBB+	90	140	195	0	-25	0	-25	-10	-40
Loblaw	BBB	BBB	100	150	205	-5	-20	-5	-20	-5	-20
Canadian Tire	BBB high	BBB+	105	155	210	0	-20	-5	-20	-5	-20
Province of Québec	A high	A+	42	60	70	-3	-13	-6	-18	-7	-22
Province of Ontario	AA low	A+	43	62	71	-4	-13	-6	-17	-6	-18
CMHC	AAA	AAA	31	40	---	-3	-7	-5	-8		

Source: National Bank Financial

CREDIT MARKET

- Canadian corporate bond new issuance reached $ 13.0 billion in November, an increase of $ 5.2 billion compared to the previous month and $ 3.8 billion more than in November 2016. Since the beginning of the year, corporate bond issuance amounted to $ 100.1 billion, up 27.2 % from the same period last year. Among the borrowers, grocery store chain Metro has issued three bonds totalling $ 1.2 billion in order to finance the acquisition of Jean Coutu. Beforehand, Metro had divested about 85 % of its Alimentation Couche Tard shares and proceeded with a common share issuance to complete its acquisition. Metro's debt is now 3 times higher than EBITDA, a comfortable level for agencies as cash flow will reduce debt.
- The rating agency DBRS downgraded Alberta's credit rating from AA (high) to AA while maintaining a negative outlook. According to DBRS, the deterioration of the budget balance and the increase in the Province's debt ratio no longer warrants such a high rating. In fact, indebtedness should reach 17.5 % of GDP at the end of this fiscal year, nearly 2 % more than last year. The negative outlook reflects the lack of a credible plan to return to a balance budget in the near future. The province is still counting on higher growth as well as hiring and wage increase freezes. DBRS estimates that the debt ratio will reach 24 % by 2020-21 or earlier. With this decline, DBRS's rating is approaching that of S&P (A +).
- The Quebec government has made an economic update which now forecasts a budget surplus of $ 2.4 billion for fiscal year 2016-17 after the $ 2 billion transfer to the Generations Fund. Last spring, the forecast surplus was $ 250 million. This improvement is due to higher revenues from a stronger economic growth and the deferral of certain infrastructure expenses. A portion of this leeway will be redistributed to taxpayers in the form of a $ 1 billion tax cut for 2017. Additional spending will also be made on health, education and poverty alleviation measures. As a result, Quebec will again present a balanced budget with the objective of reducing debt from 52 % to 45 % of GDP by 2026.

FTSE TMX INDEX PERFORMANCE

Sector	Weight	Nov. 2017	2017
Universe	100 %	0,79 %	2,94 %
Short Term	44,2 %	0,13 %	0,54 %
Mid Term	23,5 %	0,62 %	1,87 %
Long Term	32,3 %	1,83 %	7,04 %
Federal	37,1 %	0,43 %	0,76 %
Provincial	34,2 %	1,24 %	4,56 %
Corporates	26,8 %	0,68 %	3,76 %
RRB		1,37 %	0,60 %

Source: ftse.com

Although the debt ratio of the oil producing province is less than half of Quebec's, what worries agencies is the lack of political will to restore a balanced budget. However, the province has a significant taxation possibility, including the implementation of a sales tax, but the decision is politically difficult.

It is reasonable that the entire surplus expected this year will not be applied to reduce the debt burden. Currently, the rating agencies are comfortable with the plan put forward by the government to achieve the goal in 2026. Since the tax rate for taxpayers is still among the highest in Canada, it is normal for them to benefit.

STRATEGIC POSITIONNING

The Canadian and US economies are in full swing, supported by a full-employment which is fuelling household spending. Improved economic conditions in Europe and Japan are also reducing global excess capacity. In sum, the global economy is strengthening against the backdrop of monetary and fiscal stimulus, but inflation is beginning to worry bond investors. However, the situation could worsen in 2018. The US dollar has depreciated by 9 % against a currency basket since the end of 2016, pushing up the price of imports, but boosting the manufacturing industry. In Canada, the labor shortage is starting to create wage pressures, not to mention raising the minimum wage in Ontario to $ 15 / hour as of January 1, 2018. Placed with workforce constraints, business leaders could turn to investment projects that would raise their level of productivity. Although short-term rates will respond more to restrictive monetary policies, long-term rates will react to inflation expectations and supply and demand for capital. Increased demand for investment coupled with a shortage of skilled labor is expected to put upward pressure on long-term rates in the near future.