HFR Quarterly Commentary

March 2019

General Market Review

Bond markets were strong in the opening quarter of the year (Q1 – the first three months ending March 31, 2019). Weakening global economic growth caused markets to remove the risk of further rate hikes by monetary authorities and pushed longer-term yields lower. Ten-year Canada yields ended the quarter at 1.62%, down 35 basis points from the start of the year, and below the Bank of Canada's overnight target rate of 1.75%.

Sector spreads also performed well in Q1, reversing some of the risk-off spread widening that occurred at the end of 2018. As term yields fell, investors saw greater value in higher yielding corporate and provincial bonds. This was supported by more dovish messaging coming from central banks on the future path of policy rates which encouraged greater risk taking and improved market liquidity.

On average, spreads on provincial bonds narrowed by 12 basis points in the quarter while investment-grade corporate spreads narrowed by 22 basis points. Lower-quality BBB-rated securities outperformed. The average yield advantage of owning a BBB-rated mid-term corporate bond narrowed by 30 basis points and finished the quarter at 187 basis points.

Portfolio Review

Much of the Horizons Floating Rate Bond ETF's (HFR) negative performance was due to the interest rate hedge, as rates fell dramatically during the quarter, which was detrimental to performance. Our corporate bond holdings performed well, particularly in the Energy sector.

We continue to focus on the quality of issuing companies rather than taking undue credit risk since the fund is mostly exposed to corporate bonds. We constantly seek the best opportunities in a variety of industries and along the corporate term structure.

Heading into the second quarter of 2019, we are heavily invested in financial sector bonds and continue to have a very low net duration.

Outlook

Bond market sentiment has swung dramatically over the past several months in response to a slowing global expansion lead by weaker Chinese consumer demand and a post-tax reform let down in the U.S. This has been exacerbated in Canada by home grown headwinds facing Canadian households and business spending. We have lowered our expectations for growth and pushed out our expectations for further rate hikes in North America. In our view the timely recognition by policy makers of the weaker back drop combined with still moderate inflation pressure has reduced the risk of a policy mistake coming from rate hikes and could contribute to extend the current business cycle which is positive for riskier assets.

HORIZONS
EXCHANGE TRADED FUNDS

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