Market Commentary
Third Quarter 2018

Signature Corporate Bond Fund

Investment-grade corporate bonds outperformed Government of Canada bonds as interest rates rose and spreads tightened a few basis points during the third quarter. Capital markets were concerned with U.S. trade tensions with China as announced tariffs went into effect. Emerging market weakness led to some volatility in the quarter as tighter U.S. monetary policy and a stronger U.S. dollar had a negative impact on countries that rely on external funding. Global risky assets were volatile and mostly lower but the S&P 500 Index was up 7.7%, and West Texas Intermediate (WTI) oil traded sideways, ending the quarter down 1.2% to close at US$73.25 per barrel.

Credit fundamentals were stable in the quarter as U.S. earnings grew, supported by higher revenue and lower corporate taxes. Earnings are expected to continue higher in the second half of 2018. Issuance was stable in the U.S. and down 17% in Canada. U.S. investment-grade non-financial gross debt to EBITDA dropped slightly to 3.0 times as of Q2 2018, due to higher earnings. The ratio has fallen slowly from 3.4 times a year ago.

The U.S. Federal Reserve raised rates by 25 basis points at its September meeting, signalling one more increase in 2018 and three in 2019. The Canadian bond market continued to flatten in the third quarter with the two-year to 30-year spread falling eight basis points to 21 basis points.

The Canadian Investment Grade Index returned -0.45% in the quarter, outperforming Canadian government bonds as spreads tightened two basis points. In Canada, investor appetite for credit remained balanced as spreads have been fairly stable over the past two quarters compared to U.S. spread volatility. The highest returning sectors over the quarter were short financials and securitization, while the lowest returning sectors were long-term infrastructure and energy, mostly due to the move in rates.

Over the course of the quarter, high-yield bond spreads tightened 44 basis points to +338 basis points, effectively absorbing the impact of higher underlying government bond yields. Investment-grade bond spreads continued to widen through the spring, before finishing the quarter four basis points tighter to +112 basis points, with Canadian bonds less volatile than the U.S. market.

The defensive positioning that helped us earlier in the year worked against us at the margin during the quarter. Offsetting this, developments in the Western Canadian energy patch had a positive effect on performance. Investment-grade rated Husky Energy's hostile bid for lower-rated MEG Energy saw those bonds trade materially higher. Baytex Energy's acquisition of lower-levered Raging River Exploration set Baytex up for credit ratings upgrades. Also material to Western

Canada was the decision by Royal Dutch Shell and its consortium partners to proceed with their LNG export facility in B.C. This should support natural gas prices, and by extension, the many oil producers who produce associate gas.

The term loans of DHX Media and Digicert were sold. Re-pricings in that market are providing us a cost-effective opportunity to gradually reduce exposure. The US Foods 5.875% bonds due 2024 were re-added to the Fund. We also materially added to our position in New Gold bonds on recent weakness. Our thesis on this gold producer, as with select copper producers like First Quantum Minerals, another material position, is that years of underinvestment in mining has set the stage for supply deficits in coming years, making the industry ripe for consolidation.

At the end of the quarter, the fund consisted of approximately 51% high-yield bonds, 46% investment-grade bonds and 3% cash and other.

The outlook for Canadian investment-grade bonds is mixed for the next quarter, as we believe the Canadian and Global economies will post modest growth, as various geo-political issues and trade tariffs slow growth. Additionally, the Fed and the Bank of Canada are expected to tighten financial conditions further. Corporate spreads are fair, so prudence is necessary. However, credit quality is expected to remain intact, demand is good, and we don't see any signs for concern at this point. Therefore, we remain cautiously overweight in corporate bonds.

Class F Returns (in %) as at September 30, 2018	Year-to-date	1 year	3 year	5 year	10 year
Signature Corporate Bond Fund	1.6	2.7	5.2	5.1	6.6

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