Market Commentary
Second Quarter 2018

Signature Global Income & Growth Fund

The second quarter of 2018 was dominated by rhetoric from the Trump administration on tariffs and trade wars. It began as a trade dispute but deteriorated into a trade war by the end of the quarter. The tariffs continue to be part of a tactic to drive concessions from U.S. trading partners, including China, Europe, Canada and Mexico.

Europe experienced a slowdown in economic activity from elevated levels and has stabilized at sustainable levels.

China is showing signs of slowing as its reform programs take effect, particularly on the deleveraging campaign of large corporations. This is having a negative impact on the domestic stock market which declined 15% in the past two months.

The slowdown in China and a weaker currency is causing havoc for emerging markets that generally depend on China for exports. They are negatively affected by the Chinese economic slowdown which reduces their imports, and the lower Chinese currency which increases the cost of those imports. Emerging economies are also negatively impacted by the rising U.S. dollar since U.S.-dollar debt is high in many of these emerging economies.

Growth in the U.S. remained robust, enabling the U.S. Federal Reserve (Fed) to continue tightening monetary policy by raising interest rates for a second time this year at its June meetings. As U.S. monetary policy continued to diverge from the rest of the world and put pressure on the global cost of capital, U.S. corporate bond spreads and emerging market bond spreads steadily widened. Despite these developments, the Fed signalled intentions to raise interest rates two more times before the end of the year.

The Bank of Canada hiked interest rates in January to 1.25% and in July to 1.50%. A combination of mixed economic data throughout the second quarter as well as business uncertainty induced by NAFTA re-negotiations persuaded the Bank of Canada to proceed with caution in its hiking cycle.

Inter-rating spread compression was a fixed-income theme in the second quarter as investment-grade bonds widened 13 basis points (ICE BofAML U.S. Corporate Index) and emerging market bonds gapped out 62 basis points (JP Morgan Emerging Market Bond Index) but high-yield bond spreads were unchanged (although yields were 18 basis points higher at 6.53% to end the quarter). For example, spreads on high-yield countries like Turkey, Argentina, and South Africa were at their widest levels since Q4 2016, while CCC spreads – the lowest rung of performing high-yield corporate bonds – were at their lowest levels since Q3 2014. Typically, these asset classes move together but the breakdown in correlation can be attributed to dramatic flows, supply and quality

differences. There is a note of caution warranted here about drawing conclusions from markets and indexes dominated by both large issuers and idiosyncratic risk.

Fund performance – equities

Consumer discretionary and financials were the main contributors to performance.

In consumer discretionary, our long-term position in Amazon continued to perform well as it moves into new industries, the most recent being pharmaceutical drug distribution. The company is continuing on a path of further disruptions in established industries.

Large leisure shoe manufacturer Nike performed well after strong quarterly results and the launch of an online offering which will directly target consumers, providing an alternative channel to classic distribution through stores.

Financials also performed well thanks to strong stock selection as the sector, in which we are overweight, did not do well as a whole. Synchrony Financial, the white-label credit card company, once part of GE Capital, performed well as the U.S. economy continued to grow and consumer confidence remained high, encouraging consumption and leading to higher credit card balances.

Brookfield Asset Management, the leading Canadian asset manager focused on property, infrastructure and private equity also performed well for the fund.

Industrials holdings as well as European holdings detracted from performance.

Fund performance – fixed income

Allocations to U.S. agency mortgage-backed securities and U.S. treasury inflation-protected bonds contributed to performance as did an underweight exposure to Italian government bonds and an overweight Canadian currency exposure at the expense of euro and Japanese yen currency exposures. However, the fund's allocation to U.S. dollar-denominated emerging market sovereign bonds detracted.

As a stronger U.S. dollar and higher U.S. interest rates put significant pressure on emerging market spreads, we decreased exposure to emerging market sovereigns. Furthermore, as the trade war rhetoric between the U.S. and its trade partners escalated, we maintained our exposure to U.S. inflation-linked bonds.

From a duration perspective, the renewed political uncertainty throughout the second quarter in Europe resulted in our decision to extend European duration by selling shorter-dated Spanish and Italian government bonds to buy longer-dated French and German government bonds. In addition, as the balance of risks have shifted further to the downside, we maintained an underweight in euro currency exposure relative to the benchmark but shifted to neutral Japanese yen currency exposure

relative to the benchmark. However, with respect to Japanese yen duration exposure, the fund remained underweight in favour of higher income-generating Canadian and U.S. dollar-denominated bonds.

Outlook

We continue to monitor developments in global trade wars although we would note that global growth remains constructive. Until there is more clarity on trade negotiations for NAFTA, Brexit, and U.S.-China, we expect volatility to remain elevated and note that the probability of downside risks across global capital markets has risen.

Class F Returns (in %) as at June 30, 2018	Year-to-date	1 year	3 year	5 year	10 year
Signature Global Income & Growth Fund	4.1	10.4	6.7	9.7	7.9

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