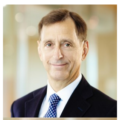
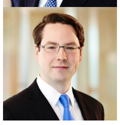
Ninepoint Diversified Bond Fund

October 2018 Commentary

Investment Team



Mark Wisniewski,
Partner, Senior Portfolio Manager



Etienne Bordeleau-Labrecque, MBA, CFA
Vice-président, gestionnaire de portefeuille

Chris Cockeram,
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After ignoring the fixed income carnage of September, in October the equity market finally got spooked by higher rates; equities went down globally, lead by the U.S. What was most surprising to us was the muted reaction across credit, commodities and foreign exchange. Typically, a risk off event such as the ~10% S&P 500 drawdown that we saw in October elicits a more violent reaction in other asset classes. For example, High Yield, which traditionally moves in unison with equities, only realized half of its usual beta.

The reasons cited for this selloff are varied, but they coalesce around a few themes. First, and most importantly, weak earnings (or weaker than expected future earnings) were a catalyst for the U.S. market to finally price in slower global growth, something the rest of the world had already realized this past spring with the Emerging Markets selloff. So, in a way, it was the U.S. equity market that had yet to catch up. Second, the market is finally pricing in a Federal Funds rate that is in line with the Fed dot plots (rates around 3.25% by the end of 2019); making the risk-free asset increasingly more attractive, particularly with the prospect of slower growth. Finally, after the October FOMC meeting, it is more and more clear that the Fed under Chair Powell will be less data dependent, more aggressive and less predictable. All else equal, this means more volatile financial asset prices, particularly long-term interest rates.

In the fund, although we maintain a low duration & higher quality bias, we were not spared by the global sell-off. As the table below shows, the Diversified Bond Fund (F) was down 38bps in October, taking our year-to-date performance to 46bps. While the fund's performance in October was below our expectations, it pales in comparison with the shellacking suffered by the major benchmarks. For example, the Canadian broad bond ETF XBB was down 72bps, while US Investment Grade and High Yield ETFs were both down 2%.

	October Return	***Year-to-date Performance***
Ninepoint Diversified Bond Fund (F)	-0.38%	0.46%
XBB (iShares Core Canadian Universe)	-0.72%	-1.15%
LQD (iShares US Investment grade)	-2.05%	-5.14%

HYG (iShares US High Yield)	-1.98%	1.05%

Source: Bloomberg, Ninepoint Calculations

This month's underperformance, relative to our expectations, come mostly from our preferred shares holdings, which detracted 13bps from performance. While it is a small weight (~5%), price action was very disorderly and as a result the overall preferred share market declined by much more than its usual relationship with equities and rates. At this juncture, the market has rebounded from the lows, but still not as much as equities. Ironically, early in October we had started the process of reducing our preferred shares positions. We managed to close two positions before the selloff started. Our strategy at this point is to be patient, wait for better price levels and continue our progressive exit from the asset class; we do not want to own preferred shares going into what we think are the last innings of this economic expansion.

With interest rates now up meaningfully and credit spreads mildly higher, we are now reinvesting at much more attractive all-in-yields. For example, our investment grade holdings have a yield of 3.9% with duration of only 3 years. In the coming months, we intend to continue to migrate the portfolio towards low duration, higher quality investment grade bonds. Although we think recession is still some ways away, we are getting to the point where adding some government bond exposure might be prudent.

Until next month,
The Bond Team: Mark, Etienne and Chris

Diversified Bond Fund Portfolio Characteristics:

	Limits	Sept 2017	Dec 2017	Mar 2018	Jun 2018	Sept 2018	Oct 2018	Outlook
Government Bonds	**100%**	3%	-2%	0%	-4%	2%	-0.5%	↑
Investment Grade	**80%**	15%	37%	56%	66%	73%	77%	↔
High Yield	**40%**	48%	32%	24%	17%	16%	16%	↔
Emerging Market Governments	**10%**	0%	0%	0%	0%	0%	0%	↔
Preferred Equities	**10%**	4%	6%	6%	6%	6%	4%	↓
Common Equities & ETFs	10%	0%	0%	0%	0%	1.5%	1.5%	↔
Derivatives	**+/- 2.5%**	0.0%	-0.1%	+0.5%	-0.1%	-0.05%	0.0%	**N/A**
Cash and Equivalents		29%	28%	14%	15%	1.5%	2%	↔
Total		100%	100%	100%	100%	100%	100%	
Duration	**1 to 8 years**	1.7	2.4	2.1	2.3	1.0	2.5	↔
Geographic (% North America)	**>75%**	78%	89%	90%	89%	93%	91%	↔

Current Net Foreign Currency Exposure: 0%

NINEPOINT DIVERSIFIED BOND FUND - COMPOUNDED RETURNS[1]

	1M	YTD	3M	6M	1YR	3YR	5YR	INCEPTION
Fund	1.3%	1.3%	0.7%	1.6%	4.8%	3.6%	3.2%	4.5%