

CI Investment Grade Bond Fund First-quarter 2019 Commentary

Market Overview

In the first quarter of 2019, central banks, across developed markets, made an abrupt “U” turn to a dovish monetary policy bias. Concern about declining global economic growth, trade tensions, muted inflation and an inconclusive Brexit process were the factors behind the change in central bank forward guidance. Naturally, government bond yields rallied on these developments, with 10-year rates declining 28, 35, 31 and 28 basis points (bps), respectively, in the U.S., Canada, Germany and the U.K. during the quarter.

Risk assets (i.e., credit and equities) also responded positively to the change in central bank sentiment. Prospects of weaker economic growth were ignored in favour of more accommodative interest rate policy in developed markets and stimulative growth initiatives in China. Major developed market equity indices had high single-digit to low double-digit returns over the quarter.

Investment-grade corporate credit spreads rallied, buoyed by strong foreign buying, a requirement for yield, reduced new issue supply and a reversal in fund flows from outflows to inflows. As measured by Bloomberg Barclays Aggregate Corporate Average indices, investment-grade corporate credit spreads tightened by 34, 22, 29 and 21 bps, respectively, in the U.S. Canadian, European and U.K. markets over the quarter. This represented about a 65% to 75% reversal of the widening in credit spreads that took place in the final quarter of 2018.

Performance Summary

CI Investment Grade Bond Fund (the “Fund”) derives its return from the movement in government bond yields and credit spreads. In the first quarter of 2019, the Fund returned 2.9% while its benchmark, the FTSE Canada All Corporate Bond Index, was up 4.0%.

The Fund’s relative underperformance versus the benchmark during the quarter was due to duration levels, the Fund’s weighting in Canadian- and U.S.-dollar-denominated securities and exposure to corporate credit. All three of these created a drag on Fund performance. Specifically:

- The Fund’s portfolio, on average, maintained a duration of approximately 1.0 years below that of the benchmark (5.22 versus 6.30 years) during a period of declining yields.

- Currency exposure (fully hedged) of the Fund portfolio's invested portion was 50% to the Canadian dollar and 13% to the U.S. dollar. The benchmark is 100% Canadian-dollar-denominated and benefited from the outperformance of Canadian government bonds yields versus U.S. Treasuries over the quarter. Also, the portfolio's level of cash during the quarter was higher than we would have liked.
- On average over the quarter, the Fund maintained a 3.4% exposure to corporate bonds. The benchmark comprises 100% corporate bonds. Given the tightening of credit spreads over the quarter, the benchmark generated greater excess return from credit than the Fund.

Outlook

The dovish turn by central banks early in 2019 prompted not only a rally in government bond yields but simultaneously triggered an aggressive "risk-on" tone. Yet, the slowdown in global economic growth has not stabilized, corporate leverage remains elevated and corporate earnings continued to be revised lower. In our view, risk markets appear to be putting a lot of hope in an economic recovery in the second quarter of 2019 and throughout the second half of the year based on 1) a timely and positive outcome to U.S.-China trade negotiations, 2) stimulative fiscal and monetary measures in China, 3) an approved Brexit, 4) a revival in euro-zone growth prospects, and 5) the ability of central banks to keep the global economy growing.

We expect the U.S.-China trade negotiations to be completed successfully (although much of this may already be priced into markets), and we do not believe there will be a hard Brexit. The key to the outcome that risk markets appear to be hoping and pricing for is China. The collective measures taken by the Chinese government to promote domestic growth and demand are pivotal. They must not only stimulate domestic demand but provide an economic growth impulse that reverberates externally. This may be a high bar as the current level of Chinese stimulus is well below the levels of 2009 and 2016, it is much more targeted and is largely focused on stimulating domestic demand. As a result, it may be less additive to global economic growth than anticipated.

Based on the above, we continue to have a below-consensus view on global economic growth, and we believe the price recovery in risk assets is a market correction, not a resumption of the bull trend. Accordingly, we believe it is prudent, late in the economic cycle, to increase the quality of the Fund's portfolio quality; that is, reduce credit, increase exposure to government bonds and actively manage duration.

In terms of interest rates, we believe the tenuous global growth backdrop keeps central banks biased to leave interest rates unchanged or to provide additional accommodation should market volatility rise. However, as markets are already starting to price in interest rate cuts and central banks are in data-dependent mode, we expect government bond yields to trade in broad ranges. This will increase opportunities to generate alpha through active duration management.

Sources used: Marret Asset Management Inc. and Bloomberg L.P.

Class F returns (in %) as at March 31, 2019	Year-to-date	1 year	3 year	5 year	Since inception (12/30/2014)
CI Investment Grade Bond Fund	2.9	3.5	3.2	N/A	4.1

Sources: Marret Asset Management Inc. and Bloomberg L.P. Data is as at March 31, 2019.

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