CUMBERLAND
Private Wealth

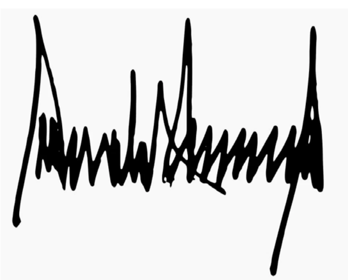
FIXED INCOME
THIRD QUARTER REVIEW

"Fed" Up with the Volatility?

As the days go by, it feels like weeks have passed – only because they are so jammed packed with news. These are the days of our lives (*yes - it does feel like a soap opera*). Intraday moves feel more violent. Like the chart on the left vs. the chart on the right below. What happened on those days?

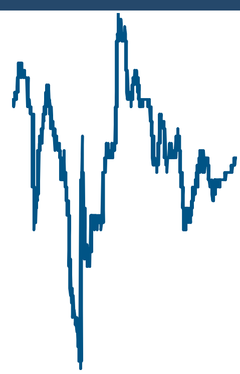
Look at that Volatility!

Exhibit 1: Volatility?



Source: qz.com - Trump's signature

Exhibit 2: Volatility!



Source: Bloomberg

Both charts exhibit a very stressed-liked environment, sensitive to daily news with a lot of volatility. However, the left is actually President Donald Trump's signature - that is how compressed it is. While the right is the intraday swing of the Government of Canada 10-year index on September 4, 2019. Needless to say, the markets are indeed following the leader south of us in style. We hit many extremes this quarter.

Peaks

- S&P 500 hit a record all-time high during the quarter at 3,026 on July 26, 2019
- At the beginning of August, US/China trade wars were escalated with a new round of tariffs imposed by the US and then retaliated by China.
- Hong Kong protests continued to escalate during the quarter that caused more uncertainty in global financial markets until the Anti-Extradition Law Amendment Bill was withdrawn on September 4th.
- On September 15th, WTI Crude prices jumped to US$62.90/bbl, up almost 15% in one day when Saudi Arabia's oil plant was attacked. WTI ended the quarter at US$54.07/bbl.
- Overnight Repo rates (SOFR) peaked at 5.25% in the quarter vs. an average of 2.43% from Q2/19 due to concerns of liquidity in the banking system.

Troughs

- On August 14, the Dow dropped by more than 800 points, followed by another 700- point day drop on August 23rd.
- US 10-year government yields hit a 3-year low at 1.45% in the quarter.
- Government of Canada 30-year bond auction cleared at a coupon of 1.36% - the lowest ever in its history.
- Sweden joined the negative yield club issuing 10-year bonds at -0.295%.
- The whole German bunds yield curve moved fully into negative territory!

Other News in the Quarter Still Lingering

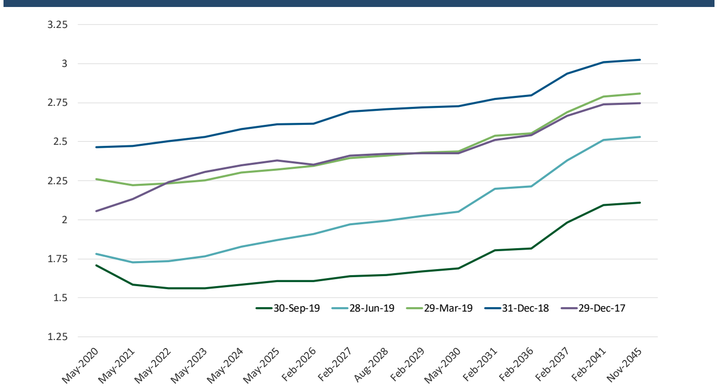
- Brexit - still the potential of a "no-deal" exit with the target date set at October 31, 2019.
- President Trump impeachment talks circle.
- US and tariffs on other countries (potential).
- Central banks around the world cutting interest rates and waiting to see how far the US cuts theirs.

Quarter Review

During the quarter the Fed cut interest rates twice (once in July and once more in September). The Fed did indicate in their September meeting there would be no more cuts in the near term. While these rate cuts were widely expected as they started motioning them in mid-July, 3 voters dissented in the vote: 1 voter thought there should be a bigger cut than just the 25bps and 2 who voters wanted to maintain rates status quo.

In the US, with a pivot from holding rates to a cut, interest rates for the quarter moved anywhere between 7 bps to 42 bps lower. The 2-year and 5-year part of the curve ends the quarter inverted.

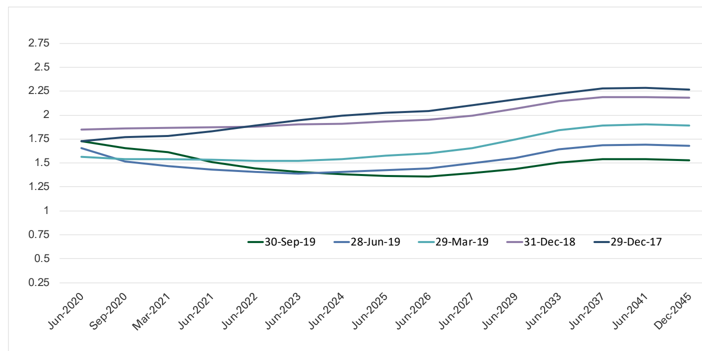
Exhibit 3: US Yield Curve



Source: Bloomberg

On the Canadian side, because the Bank of Canada (BOC) was firm in holding rates through the quarter, the yield curve reacted differently: short end rates (1 to 3 years) actually moved higher anywhere between 2bps to 15bps. Meanwhile rates greater than 3 years moved anywhere between 2bps to 16bps lower.

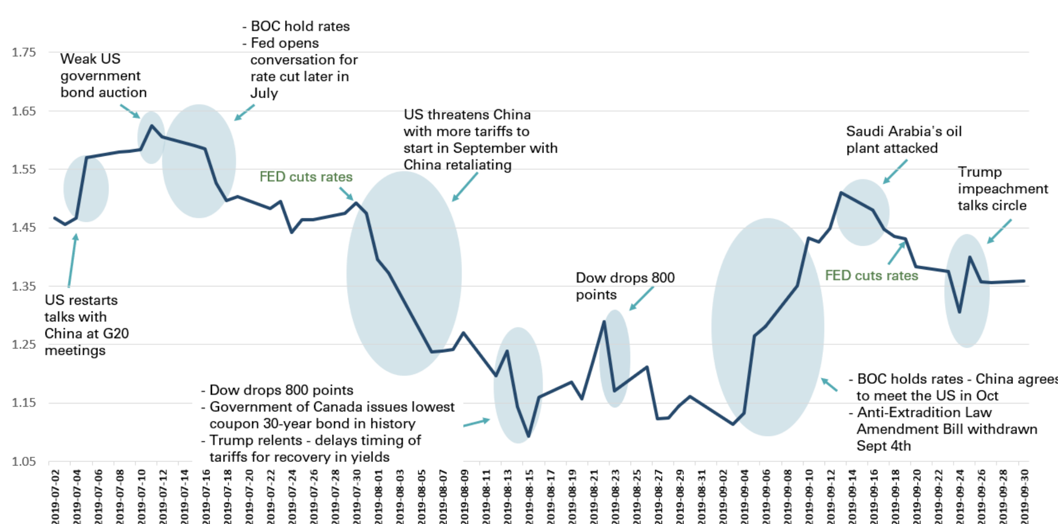
Exhibit 4: Canada Yield Curve



Source: Bloomberg

The volatility of the 10-year Government of Canada bond moved from peak to trough 32% during the quarter (higher than in Q2 at 21%) mainly from the news linked to our southern neighbours. This continues to be interesting to see such big moves.

Exhibit 5: 10-Year Government of Canada Bond Yield



Source: Bloomberg

CUMBERLAND
Private Wealth

Canadian investment grade corporate spreads were wider anywhere between 3bps to 6bps across the curve and rating categories during the quarter, as a result of the risk-off tone during August due to the trade-war escalation between China and US. Spreads in August moved wider anywhere between 6bps to 11bps and could not be fully recovered in the month of September.

Returns for various fixed income asset classes are in the table below. During the quarter, long government bonds outperformed as heightened uncertainty from the escalation of tariffs between the US/China in their trade war lead investors to safe assets.

Asset class returns	Q3/19	Q3/18	2018	2017
Bond Universe Index	1.19%	-0.96%	1.41%	2.52%
Corporate Bond Index	1.08%	-0.46%	1.1%	3.38%
FTSE High Yield Canadian Index	2.01%	1.04%	2.15%	9.94%
S&P/TSX Preferred Index	-0.09%	1.72%	-12.21%	13.44%

Outlook: Stabilizing Income during Volatile Times

With the yield curve so flat, we continue to be cautious as we lock in yield for income and continue to defer where the most risk vs. rewards make sense.

Due to the daily volatility of these markets, we continue to be patient and opportunistic as we add to existing and new positions into our funds.

At the end of Q2, there were 95% of the bonds in the Canadian Bond Universe trading above par. With a slug of new issuance over the quarter and some market selloff, we have now just over 92% of the bonds trading above par (still a lot of premium bonds out there).

We continue to stay disciplined and focused on preserving capital and managing the risk for our unitholders. We enter the final leg of the year optimistic of our positionings in our funds.

Take Care,

Diane Pang
Lead Manager,
Cumberland Fixed Income*
October 1, 2019

*Cumberland refers to Cumberland Private Wealth Management Inc. (CPWM) and Cumberland Investment Counsel Inc. (CIC). CIC acts as sub-advisor to certain CPWM investment mandates including the CPWM Fixed Income mandate with Diane Pang as its lead Portfolio Manager. Diane Pang is a Portfolio Manager at CIC.