Actively managed Canadian corporate bond portfolio focused on generating an attractive yield while managing risk

What's the strategy?

The Corporate Bond (Portico) portfolio strategy invests primarily in investment-grade Canadian corporate bonds (rated BBB or higher), diversified across a wide range of both industry sectors and credit quality.

What's the approach?

The portfolio manager pursues a consistent, measured and disciplined approach to capture incremental gains through a multi-factor approach to analyzing interest rates, credit markets and yield curves. The portfolio manager of this actively managed fixed-income portfolio focuses on risk management and generating an attractive yield. Within well-defined risk parameters, the portfolio manager has the flexibility to add exposure to high-yield bonds and foreign-denominated bonds in select holdings when attractive market conditions exist.

Why invest in this portfolio strategy?

Ideal for investors seeking additional yield opportunity (above that of Canadian government bonds) through investment-grade corporate bonds scrutinized for their credit quality fundamentals and attractive relative value.

This actively managed portfolio also offers a reduced sensitivity (when compared to a core bond portfolio) to the negative effects of rising interest rates on bond prices; this is due to the additional yield cushion and typical shorter duration of the portfolio.

Typical portfolio characteristics

The Corporate bond (Portico) portfolio strategy offers investors a fixed income alternative that generates a higher income than a typical core Canadian bond fund. This portfolio strategy can offer:

- A diversified Canadian fixed income portfolio of corporate bond holdings across a wide range of industry sectors and credit quality.
- Additional yield opportunity (above that of Canadian government bonds) through investment-grade corporate, with the additional flexibility to invest in non-investment grade corporate debt and foreign-denominated debt in select holdings when attractive market conditions present.
- A reduced sensitivity (when compared to a core bond portfolio) to the negative effects of rising interest rates on bond prices.
- Active fixed-income portfolio management and proprietary credit analysis to capitalize on yield opportunities and minimize portfolio risk.

Strategy snapshot

Asset class
Fixed Income

Inception date
2001

Assets in mandate
$1,441.0 million

Benchmark
FTSE Canada All Corporate Bond Index

Investment team
Portico Investment Management

Portfolio manager(s)
Ian Whiteside
Vice-President, Fixed Income

About GLC

GLC Asset Management Group Ltd. (GLC) is a leading investment management firm that manages more than $50 billion in assets.

GLC has 5 investment management divisions:

- GWL Investment Management
- London Capital Management
- Laketon Investment Management
- Portico Investment Management
- Portfolio Solutions Group

Each division has a distinct investment approach that offers deep expertise within specialized areas of portfolio management, bringing unique perspectives to navigating capital markets through varying cycles.

As at June 28, 2019

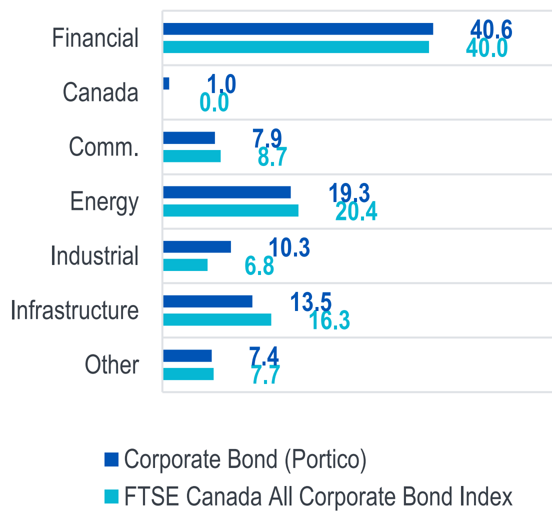
Portfolio attributes

	Portfolio[1]	Index[2]
Average term (years)	8.62	9.09
Modified duration (years)	6.42	6.59
Market yield (%)	2.73	2.69
Number of Bonds	155	973

Credit quality %

	Portfolio[1]	Index[2]
AAA	1.0	2.0
AA	19.5	24.0
A	33.1	31.9
BBB	44.6	42.2
<BBB	1.7	0.0

Sector Allocation %



Source: GLC, FTSE Global Debt Capital Markets | 1. Fund: LL - Corporate Bond Fund (Portico) | 2. Index: FTSE Canada All Corporate Bond Index

Portfolio manager's quarterly commentary

As at June 28, 2019

Market review

The FTSE Canada Universe Bond Index returned 2.5% (total return) for the second quarter of 2019, marking the third consecutive quarter of strong returns for Canadian fixed-income investors. North American bond yields moved lower, continuing a trend that began in October 2018. Canadian 10-year bond yields were down 15 basis points (bps) for the quarter, while U.S. 10-year bond yields fell 40 bps. The fall in bond yields coincided with a policy shift from various central banks, most notably the U.S. Federal Reserve, which abruptly shifted to a rate-cutting bias after hiking rates a quarter point last December. North American bond yields continue to be weighed down by negative interest rate policies on the part of central banks in Europe and Japan. The Bank of Canada left rates unchanged during the period and provided messaging that suggests rates are on hold for at least the rest of the year. The move in bond yields saw Canadian long-term bonds significantly outperform relative to short-term bonds. Canadian corporate bonds slightly outperformed government bonds. Provincial and municipal bonds outperformed within the government sector.

Portfolio performance

The fund delivered a positive return that modestly outperformed the FTSE Canada All Corporate Bond index on a gross return basis for the quarter. The key factors contributing to outperformance were the fund's security selection (notably in Sunlife, Hydro One and Loblaw Companies) and by having a higher average yield than the index as a whole. The fund had a shorter duration and therefore had less exposure to interest rates changes than the index. As interest rates fell during the quarter, bonds that had a higher sensitivity to interest rate changes performed better than bonds with lower sensitivity, thus the shorter duration offset some of the fund's gains. The fund was also negatively impacted by industry selection, most notably in long-term Energy and Infrastructure sector bonds.

Portfolio activity

We participated in several new issues during the quarter. Within the Communications sector, we added new ten-year Rogers and five-year Bell bonds (BBB rated) as the issues delivered an attractive new issue concession. We added several bonds issued from various domestic banks, including TD, CIBC, RBC, HSBC and BNS, as well as from Bank of America, a U.S.-based bank. Additionally, the fund participated in new issues from Suncor Energy (10-year, A rated), Alectra (30-year, A rated) and Aimco Realty (10-year, AA rated). These bonds came with an attractive discount. Lastly, the fund added a new high yield bond to the portfolio, Kruger Packaging Ltd. This bond came at an attractive coupon and added yield to the fund. From a credit-quality perspective, participating in new issues (as well as other changes) resulted in an increase in 'BBB'-rated exposure relative to the start of the quarter – particularly in the shorter end of the yield curve – to take advantage of the attractive spread-versus-risk profile of shorted-dated bonds.

Positioning & outlook

We remain cautious given continued geopolitical risks, foreign trade disputes and reduced global growth prospects (notably in Asia and Europe), which could result in a risk-off movement similar to the end of 2018. However, with the change in bias at the Bank of Canada and the Fed towards maintaining and lowering interest rates respectively, there may be room for corporate spreads to further compress, provided economic growth picks up in the latter half of the year and geopolitical missteps remain limited. In the longer-end of curve, the fund continues to have a bias towards high-quality bonds and will continue to switch to higher-quality bonds when valuations are attractive. In the mid- to shorter part of the curve, the fund continues to focus on higher-yielding bonds where the risk/reward profile is favourable. From a sector position, the fund has an overweight bias towards Financials, particularly Insurance issues, based on the attractive carry those bonds provide relative to other similar rated products. It also has an overweight position in Industrials, particularly within the Consumer segment (Grocery). The fund continues to maintain exposure to "Maple issuers" (non-Canadian corporations that issue Canadian-denominated bonds to the Canadian market) as these issuers offer an attractive pick-up relative to similarly rated domestic peers. We continue to be opportunistic in adding new issuers/issuances to the portfolio where credit quality and yield suggest they'll add value. We remain confident in the quality of the credit issues within the portfolio and believe the portfolio is well-diversified across sectors and industries.