glc asset management

Mortgage Diversified
Portico Investment Management

Q2 2020

Diversify fixed-income holdings with less interest-rate sensitivity

What's the strategy?

The Mortgage Diversified (Portico) portfolio strategy has a unique design – a hybrid of commercial and Canadian residential mortgage investments, which seeks to generate more income than government bonds of a similar term, while creating a portfolio that is less interest-rate sensitive because of its shorter duration.

What's the approach?

This portfolio strategy leverages the expertise and experience within the Canada Life Commercial Mortgage team. The Canada Life Commercial Mortgage team sources, underwrites and manages the commercial mortgage deals. The Portico Investment Management team offers capital market expertise, portfolio management oversight and liquidity management. Both portfolio managers pursue tested and strongly vetted processes within a culture of strong risk management.

Why invest in this portfolio strategy?

This unique portfolio strategy is a good complement to traditional bond investments, offers greater diversification through mortgages not typically available to investors and access to highly specialized and experienced portfolio management. Ideal for investors seeking to diversify their fixed-income exposure with a portfolio of high quality mortgages geographically diversified across Canada.

Typical portfolio characteristics

Here's what you can expect to see from Portico's Mortgage Diversified fixed-income strategy when compared to its Canadian benchmark:

- Shorter duration and less interest rate sensitivity than the broad Canadian bond market
- Higher interest income than bonds of a similar term because of the higher yield premium on mortgages
- A very low delinquency rate on its mortgages, which is a testament to the team's rigorous risk management process
- Typical mix of 50% residential, 35% commercial and 15% bonds.

Wo Strategy snapshot

Asset class
Fixed Income

Inception date
1969

Assets in mandate
$1,610.4 million

Benchmark
10% FTSE Canada 91 Day T-bill Index
65% FTSE Canada Short Term Overall Bond Index
25% FTSE Canada Mid Term Overall Bond Index

Investment team
Portico Investment Management

Portfolio manager(s)
Dale Haynes
Vice-President, Fixed Income

About GLC

GLC Asset Management Group Ltd. (GLC) is a leading investment management firm that manages more than $55 billion in assets.

GLC has 5 investment management divisions:

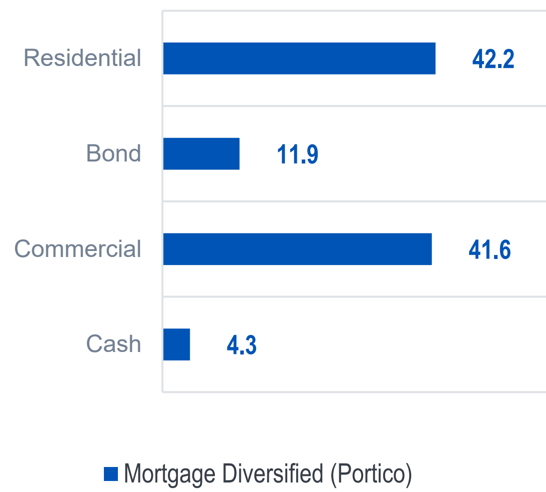
- GWL Investment Management
- London Capital Management
- Laketon Investment Management
- Portico Investment Management
- Global Multi-Asset Strategy team (including Portfolio Solutions Group)

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 30, 2020

	Portfolio[1]
Average term (years)	3.92
Modified duration (years)	3.22
Market yield (%)	2.08
Number of Bonds	13
Regulatory Liquidity (%)	14.9

Sector Allocation %



Source: GLC, FTSE Global Debt Capital Markets │1. Fund: LL - Mortgage Diversified Fund (Portico) │2. Index: 10% FTSE Canada 91 Day T-bill Index, 65% FTSE Canada Short Term Overall Bond Index, 25% FTSE Canada Mid Term Overall Bond Index

Portfolio manager's quarterly commentary

As at June 30, 2020

Market review

The COVID -19 pandemic remains the focal point in all areas of the market, in terms of the commercial mortgage space, borrowers across the country have faced mounting pressure to provide payment assistance to beleaguered tenants. Lenders in turn have seen the number of requests from borrowers for loan concessions grow rapidly. The extent to which the national shutdown will ultimately affect real estate investment cashflows remains to be seen. This uncertainty has led to increased challenges in valuation as investors and borrowers try to determine if the impact to NOI will persist or correct itself in the short term. Government regulators have attempted to ease operational stress on the financial system with several policies. In March, the Office of the Superintendent of Financial Institutions (OSFI) announced it will allow banks to continue to classify loans with deferred payments as performing for borrowers affected by COVID-19. The announcement means banks will not be forced to hold additional capital on their books to offset these loans. OSFI also announced a reduction in the domestic stability buffer of 125bps, bringing it down to 1.00% to end the quarter. OSFI estimates the reduction will support more than $300 billion of additional lending capacity by Canada's largest financial institutions. Grocery anchored, needs based retail has demonstrated resiliency in the current pandemic, while enclosed malls continue to experience negative pressure; e- commerce in Canada continues to eat into bricks-and-mortar sales at a rapid pace. Data from statistics Canada shows e-commerce sales have grown by 13% annually since 2016. Its share of total retail sales has grown by more than 9% annually over that same period. The implementation of social distancing and quarantine measures have had negative impacts on retail in general; it has proven to be beneficial to industrial real estate.

The critical role of industrial assets in the omnichannel and global supply chains is forecasted to increase and will ensure the sector remains well supported by strong fundamentals, on a relative basis.

Portfolio performance

During a period that concluded with the ongoing global health crisis and global market volatility, the fund generated a small positive return, but underperformed its benchmark (Commercial Mortgage Composite Index) for the quarter on a gross return basis. As evidence of the conservative underwriting standards applied to this fund's holdings, no commercial loans were in arrears.

Portfolio activity

During the second quarter of 2020, one renewal loan was maintained in the fund for approximately $3.7 million at a spread of 300 bps for a term of one year. There were no new commercial loans added to the fund. The portfolio's bond component continues to be maintained to ensure the liquidity of the fund.

Positioning & outlook

The portfolio remains defensively positioned with a focus on high-quality, conservatively underwritten Canadian commercial mortgages that are diversified across Canada by location, property type and borrower. Reflecting the high-quality bias, we seek to opportunistically add commercial mortgage loans located in major Canadian markets secured by institutional-quality real estate with full recourse to the borrowers. The portfolio management team believes the portfolio is well-positioned to acquire and maintain a high-quality, diversified portfolio of commercial mortgages and insured residential mortgage pools to produce stable and predictable income with minimal default risk. In view of the deteriorating economic conditions in Alberta, the portfolio management team will cautiously approach potential near-term lending opportunities in that province. Instead, the team will look to other areas of the country that are performing well and providing good lending opportunities.