



# Horizons Active Ultra-Short Term Investment Grade Bond ETF (HFR)

## Market Review

North American bond yields have adjusted higher, and the yield curve steepened over the first quarter (Q1). The theme for Q1 in the U.S. was a resilient economy and continued elevated inflation. The U.S. Federal Reserve (Fed) said it will likely cut interest rates later in the year, but they need to see further evidence that inflation is moving lower. As a result, investors reduced their expectations for the total number of rate cuts this year and pushed the start of the easing cycle further out. At the end of 2023, investors were looking for the Fed to reduce rates by 158 basis points (bps) in 2024 to 3.75% with the first 25 bps ease built in by March. At the end of Q1, forecasted cuts had been reduced to just 74 bps for the year with the first cut now expected in July.

Softening global growth and inflation added to the view that financial conditions are tight and are working their way through the global economy. The Swiss National Bank has already started to loosen monetary policy and the table is now set for the Bank of Canada (BoC), the European Central Bank, and the Fed to start modestly cutting rates. The U.S. backdrop supports the view of slowing inflation and heightened risks of keeping rates too high for too long. The Canadian economy has been operating below potential and although inflation is still above the BoC's 2% target, it has come down considerably. Over 2023, headline inflation declined from 5.2% to 2.8% and core inflation fell 170 bps to 3.2%. The market is expecting the BoC to cut rates by 70 bps in 2024 to 4.35%, with the first cut also anticipated in July. Adding to this dynamic is ongoing quantitative tightening, strong wages, and an increase in the net supply of government bonds. In this environment, short-term Provincial spreads declined four bps to 27 bps and corporate spreads narrowed 24 bps to reach 103 bps.

## Quarter in Review

While a typical short-term universe portfolio generated a return of -0.15% and a universe bond portfolio delivered -1.22%, HFR maintains a very low total duration kept generally between 0 and 1 year. Portfolio duration ended the quarter at around 0.93 years. The bond market was trading in a range through most of the quarter. Rates were being pulled up and down as participants tried to determine the timing of interest rate cuts. This volatility gave us opportunities to have both short and long-duration positions, which contributed to performance.

HFR took profits from several expensive corporates that had performed well. The primary corporate market was highly active, but the HFR only participated in a few select issuers, which included CIBC, Dream Industrial REIT, RioCan Real Estate, Crombie, Ford, National Bank, and two asset-backed securities issues. In the quarter, our selection of Banks, Real-Estate, Communications and Energy issuers provided added value.

## Outlook and Positioning

The Sub-Advisor is awaiting interest rate cuts in North America, but more evidence of falling inflation is still required before this can begin. Monetary policy is restrictive and will lead to softer growth in Canada and the United States. Inflation has declined from very elevated levels over the past year and if it continues to fall the BoC will become more confident in hitting its 2% inflation target, which will allow it to eventually begin the process of loosening monetary policy. The Sub-Advisor expects this to start in the summer and several rate cuts will be needed this year and next to support the economy and help avoid a hard landing. During the year, interest rates and credit spreads are expected to stay low, but the Sub-Advisor expects to see volatility and opportunities as central banks transition to interest rate cuts, elevated bond supply and geopolitical risks.

Short-term investment grade credit spreads are now slightly below long-term historical averages. A decent economy along with expected rate cuts and asset allocation into fixed income have all contributed to recent corporate performance. HFR has a modest overweight to credit with a focus on high-quality names. Over the past year, HFR has been taking profits and reducing exposure as spreads narrowed.



Commissions, management fees and expenses all may be associated with an investment in the Horizons Active Global Fixed Income ETF ("HAF" or the "ETF") managed by Horizons ETFs Management (Canada) Inc. The ETF is not guaranteed, its value changes frequently and past performance may not be repeated. The prospectus contains important detailed information about the ETF. **Please read the relevant prospectus before investing.**

Certain statements may constitute a forward-looking statement, including those identified by the expression "expect" and similar expressions (including grammatical variations thereof). The forward-looking statements are not historical facts but reflect the author's current expectations regarding future results or events. These forward-looking statements are subject to a number of risks and uncertainties that could cause actual results or events to differ materially from current expectations. These and other factors should be considered carefully and readers should not place undue reliance on such forward-looking statements. These forward-looking statements are made as of the date hereof and the authors do not undertake to update any forward-looking statement that is contained herein, whether as a result of new information, future events or otherwise, unless required by applicable law.

This communication is intended for informational purposes only and does not constitute an offer to sell or the solicitation of an offer to purchase exchange traded products (the "Horizons Exchange Traded Products") managed by Horizons ETFs Management (Canada) Inc. and is not, and should not be construed as, investment, tax, legal or accounting advice, and should not be relied upon in that regard. Individuals should seek the advice of professionals, as appropriate, regarding any particular investment. Investors should consult their professional advisors prior to implementing any changes to their investment strategies. These investments may not be suitable to the circumstances of an investor.

All comments, opinions and views expressed are generally based on information available as of the date of publication and should not be considered as advice to purchase or to sell mentioned securities. **Before making any investment decision, please consult your investment advisor or advisors.**

Published April 30, 2024