

IA Clarington Loomis Global Multisector Bond Fund

Manager commentary – Q2 2024

The U.S. Federal Reserve (Fed) appears to believe that the U.S. is back on a disinflationary path, adjusting June's Federal Open Market Committee (FOMC) policy statement to note that 'modest' progress had been made towards their 2% inflation objective. Recently, there has been some weakening in economic data and supply/demand conditions in the labour market have continued to become better balanced. Further incoming data is likely needed to determine ongoing progress of the Fed towards their inflation goal. However, the Personal Consumer Expenditures (PCE) reading at the end of the quarter eased and supports the Fed's stance. Coming into the year, the market was pricing in six interest rate cuts from the Fed in 2024; however, as at the end of the second quarter, the market had shifted to two cuts. Investors now seem to be grappling with a more shallow and drawn out rate cutting cycle than the Fed previously indicated. During the quarter, investment-grade and high-yield spreads were slightly wider on a deceleration in economic data and interest rates moved higher as inflation data still remains stuck above the Fed's target and the probability of a 'no cut' scenario has increased.

For the second quarter of 2024, securitized credit was a contributor to the Fund's performance. The shorter duration of our securitized bucket relative to the index (1.9 years versus 6.0 years for the bench, on average) was helpful as interest rates moved higher during the quarter. The Fund benefitted from carry in this sector as well – as at June 30, the yield on the securitized bucket was 7.0%.

Investment-grade corporate credit allocation was positive to performance. Carry and shorter duration within investment-grade credit (5.9 years duration versus 6.6 years for the index, on average) was beneficial for excess returns as corporate yields rose 18 basis points (bps) in the second quarter (from 5.30% to 5.49%).

Emerging markets credit was beneficial as a result of our exposure to Teva Pharmaceutical Industries Ltd. and First Quantum Minerals Ltd. Teva continues to deliver on its balance sheet and we believe is moving closer to an upgrade. For First Quantum, though there has been no movement yet in the opening of the mine in Panama, we continue to believe its debt is covered by assets just in the Zambian mine alone.

High-yield corporate credit weighed modestly on returns. CSC Holdings LLC (CSCHLD) was the main detractor from the Fund's performance. Loomis is a member of the Steering Committee of the bondholder group. The group has led the process to put in place a Cooperation Agreement effective as of July 3rd (currently covers roughly 70% of all debt outstanding of CSCHLD). The goal of the Cooperation Agreement is to block/dissuade any transaction that would leak value away from creditors. Our view is that CSCHLD bonds are trading below recovery value (US\$25 billion of equity value versus

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US\$23 billion of debt). We see the Coop as a potential positive catalyst as well, with continued success in stabilizing and subsequently turning around the cable broadband internet business.

In our view, the credit cycle is firmly in the 'late cycle' stage. Monetary policy still remains in restrictive territory and lending standards have tightened. The economy appears to be losing some momentum, with first-quarter real gross domestic product (GDP) reported lower, at 1.3% quarter-over-quarter. We have seen a small amount of marginal weakness in the consumer, but the U.S. labour market continues to underpin consumer spending. Corporate fundamentals still remain stable and are also supportive of economic activity. Looking forward, our base case calls for trend, or slightly below trend, U.S. growth in 2024 consistent with an economic 'soft landing' scenario, and we do not anticipate a recession. On a global basis, we see gradual improvement in European growth, led by improving business activity broadly in periphery economies, but there is upside risk to inflation that forces the European Central Bank to hold after just one rate cut. China is showing signs of gradual recovery, with business activity picking up, but we are mindful of persistent risks associated with a weak housing market.

We believe that inflation has peaked and positive real rates should have the effect of slowing growth and continuing to lower inflation over time. The market's expectation for a 'soft landing' implies inflation continues, unabated, back to the 2% Fed target with growth holding up. Further progress on inflation requires lower wage and house price inflation. To accomplish that, the Fed likely needs to maintain high policy rates to slow demand, in our view. Current restrictive policy is leading to some initial signs of a moderating labour market with lower job openings and a lower quit rate, rather than lower payrolls. Our base case calls for 'unstable' inflation, meaning in the short term, inflation could persist, while over the long term we believe it will be a recurring problem based on structural themes, such as deglobalization, decarbonization and the "greenification" of energy sources, aging demographics and growing government deficits. We expect the path to 2% inflation to be a bit rocky and expect to see dips as cycles progress, but we also believe the economy is likely to experience higher lows than have been experienced over the last 15 years. As a result, we have moderated our view of future Fed cuts with the expectation that the cutting process will be more drawn out with fewer rate cuts in 2025 and a trough rate expectation of 3.50% to be hit in 2026.

Corporate fundamentals appear stable and, while there has been some recent weakness in broader fundamentals, we believe factors like leverage and interest coverage ratios continue to remain attractive in a historical context. Corporate profits are ticking back up and the rolling recessions that we have witnessed in technology, housing and manufacturing have seemingly come to an end. Our Credit Health Index (CHIN) suggests defaults/losses will remain relatively low, while slowly increasing to more normal levels associated with a 'late-cycle' environment. Technical factors remain supportive, with investment-grade issuance front-loaded in the first half of 2024, as corporations potentially tried to issue debt ahead of a volatile U.S. election period. In addition, specific to the high-yield market,

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fundamentals also look relatively healthy, defaults may have already peaked for this cycle and most signs of distress seem idiosyncratic, in our view. The high-yield maturity wall also seems manageable through 2025, not posing a major threat after a wave of refinancing earlier in the year.

We believe that long-term value has returned to fixed-income markets with a combination of discount-to-par (positive convexity) and favourable yields. In our view, bond markets will likely be supported with strong demand as investors sit on record levels of cash that will be seeking yield as the Fed potentially cuts interest rates on the front end. We see long-term fair value in the 10-year U.S. Treasury at 4.50%, and believe the current range is 3.75% (soft-landing scenario) to 5.00% (no-cut scenario). We believe the “belly” of the yield curve presents the best risk/return trade-off. In a declining rate environment – based on lower inflation and Fed cuts – the belly offers investors the ability to capture most of the upside return of the long-end without the potential volatility. The U.S. deficit and Treasury supply continue to be a topic of heavy discussion and will likely have a significant influence over long-end Treasury yields. Regardless of the U.S. presidential winner, we believe the fiscal deficit is structural in nature and neither party will risk taking a “hawkish” stance on fiscal responsibility. This may lead to continued growth in the deficit and more Treasury issuance, which we believe could lead to increased volatility and a floor under long-term Treasury yields.

We are mindful of the risks going forward, such as tighter financial conditions, geopolitical risk, further decline in the commercial real estate market, and the upcoming U.S. and global presidential elections. Although risks exist, spreads have moved to the tightest levels of this cycle. We are not surprised by how buoyant credit markets are these days – fundamentals are stable with the potential for losses to remain benign – and buyers are showing up with an almost-insatiable demand. Our view is that investors can feel comfortable going for the extra spread pick-up available in the credit markets. We feel that 2024 overall will likely be an environment where returns are driven by carry and it will be prudent to maintain a balanced risk profile between interest-rate and spread risk. Spreads will likely live in a range that is typical of a non-stressed market, which for high-yield corporates tends to be in the +300 to +450 bps range, and we are being patient and selective in deploying capital. Protectionism and isolationist policies could elevate volatility going forward and make for buying opportunities in credit, interest rates and currencies, for which we would consider redeploying additional reserves faster. We believe the best approach is to maintain a yield advantage in our portfolios rather than waiting on the sidelines for a ‘risk-off’ environment that may never materialize.

Over the quarter, we added approximately 2% weighting in bank loans. We have been adding to select bank loans where we like the credit and can pick up little more spread versus high-yield credit.

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Fund and benchmark performance, as at June 30, 2024	1 year	3 year	Since inception (Jul. 2020)
IA Clarington Loomis Global Multisector Bond Fund – Series A	3.8%	-3.2%	-1.9%
Bloomberg U.S. Aggregate Bond Index (CAD Hedged) ¹	1.7%	-3.6%	-3.1%

Non-traditional fixed income asset classes may carry higher risk, but generally provide higher yield than traditional fixed income asset classes. For definitions of technical terms in this piece, visit iaclarington.com/glossary and speak with your investment advisor.

¹Source: Bloomberg L.P. The Bloomberg U.S. Aggregate Bond Index (CAD Hedged) is a broad-based benchmark that measures the investment grade, U.S. dollar-denominated, fixed-rate taxable bond market. This includes Treasuries, government-related and corporate securities, mortgage-backed securities, asset-backed securities and collateralized mortgage-backed securities.

The performance data comparison presented is intended to illustrate the Fund's historical performance as compared with historical performance of widely quoted indices. There are various important differences that may exist between the Fund and the stated indices that may affect the performance of each. The Fund's market capitalization, geographic, sector and credit quality exposure and interest rate sensitivity may differ from that of the benchmark. The Fund's currency risk exposure may be different from the benchmark. The Fund may hold cash while the benchmark does not. It is not possible to invest directly in market indices. The performance comparison is for illustrative purposes only and does not imply future performance.

Indicated mutual fund rates of return include changes in share or unit value and reinvestment of all dividends or distributions and do not take into account sales, redemption, distribution or optional charges or income taxes payable by any securityholder that would have reduced returns. Returns are historical annual compounded total returns.

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