HAF Quarterly Commentary

Horizons Active Global Fixed Income ETF

Q4 2023

Market Overview

During the fourth quarter (Q4), the global bond market experienced a significant rally following indications from central banks that the peak in rates was reached. The door was also left open for rate cuts in 2024 to help them manage a soft landing. The U.S. 10-year yield moved from 4.57% to 3.88%. On the credit side, the dovishness from central banks helped credit spreads compress further, even though some signs of cracks and weaknesses started to appear in the economy.

The U.S. Federal Reserve, after hiking rates in July, decided to stay on hold for the rest of the year to better assess the impact of monetary policy down the road. The European Central Bank and Bank of England also stayed on the sidelines during Q4 while central banks in Brazil, Chile, and Colombia decided to cut rates as inflation started cooling in these regions.

Quarter in Review

The Sub-Advisor's active approach to security selection and duration has proven to be a support during this period of higher interest rates.

During the quarter, HAF increased duration in U.S. dollars when the 10-year U.S. yield reached 5.0%, to reach an overall duration north of 6 years. When the 10-year U.S. yield broke lower than 4.00%, the Sub-Advisor decided to bring back the duration around 5 years. The portfolio has been trimming its exposure to credit in general as credit spreads tightened significantly and the Sub-Advisor considers the market is only pricing for a rosy outcome of a soft landing. The Sub-Advisor prefers to play more defence on the credit front.

Sector-wise, on the investment grade front, the Sub-Advisor still favours consumer, non-cyclical issuers operating in the Food industry, as well as issuers in the Communication Services industry. The Sub-Advisor remains selective with high-yield issuers and sector exposure is concentrated in Consumer Non-Cyclical, Energy, and Consumer Discretionary, where spreads are already reflecting the possibility of an economic slowdown. The Sub-Advisor favours quality issuers in the Energy sector as they are expected to continue generating significant free cash flow in this commodity-friendly environment. The portfolio has started to gradually reduce its exposure to Additional Tier 1 bonds to be slightly more defensive.

On the emerging market front, the portfolio remains overweight in Latin America considering expectations of the continuation of the easing cycle for central banks combined with attractive positive real interest rates. On the hard currency front, the portfolio remains overweight in Colombia. It also favours Mexico and Romania.

Outlook and Positioning

Global bond markets offer a lot of opportunities, and the asset class is attractive considering higher rates globally. With some leading indicators showing tighter financial conditions are beginning to bite and given the lagged impact of policy tightening, the Sub-Advisor expects a recession in 2024 and favours entering 2024 with some dry powder. Considering the economic outlook, the strategy is well positioned to encounter various market environments considering its strong yield carry protection provided by an overall diversified investment grade portfolio.

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