First Asset Long Duration Fixed Income ETF
First Quarter 2019

Market Overview

- The U.S. Federal Reserve (the "Fed") pivoted abruptly on the direction of U.S. monetary policy in what became the defining action of the first quarter of 2019. In response to the financial market shocks in the fourth quarter of 2018, the Fed halted interest rate hikes indefinitely, averting a (potential) policy error. Furthermore, the Fed is ending earlier its balance sheet reduction, and has brought renewed focus on correcting for past inflation shortfalls. Markets responded with a risk rally that recaptured the highs of October 2018.

- In spite of the credit and equity rally during the quarter, government bond yields made substantial new lows as anticipated hikes in interest rates were repriced into interest rate cuts and recession fears emerged in response to weak growth data primarily in Japan and Europe. The lack of room for policy support sparked concern as the European Central Bank postponed its plans to return interest rates to zero from negative territory.

- Prospects for interest rate cuts from the Bank of Canada took root in market pricing for the first time since 2016 amid lingering risks of renewed trade tensions and concerns of a global economic slowdown, to which Canada would not be immune.

- Chinese stimulus progressed in measured fashion at the meeting in March of the country's National People's Congress where tax cuts and fiscal spending were announced, while further Chinese tariffs were postponed by the Trump administration and meaningful negotiations appear to be progressing. Such outcomes helped ease concerns of a potential hard landing for the Chinese economy that would exacerbate a global economic downturn.

Performance Summary

- Over the first quarter of 2019, First Asset Long Duration Fixed Income ETF (TSX:FLB) (the "Fund") returned 6.7%, slightly underperforming its benchmark, the FTSE Canada Long Term Government Bond Index, which was up 6.9%.

- The total return outcome of the Fund's portfolio was primarily driven by a significant decline in Canadian interest rates, with further gains coming from a narrowing of Canadian government credit spreads.

- Relative to the benchmark, duration positioning was the most significant contributor to the Fund's performance, while government credit exposure was the main detractor.

- Duration and yield curve positioning added to the Fund portfolio's active return, coming primarily from our overweight duration position in Canadian bonds maturing in seven to 10 years relative to longer maturities, as interest rates fell and the yield curve steepened during the reporting period. The Government of Canada 10-year bond yield fell by about 35 basis points (bps) over the quarter, while the 10-year to 30-year segment of the yield curve steepened by 6 bps in the same time-frame.

- An underweight exposure to government credit reduced the Fund's active return as spreads tightened in this sector by 10-14 bps across the curve over the quarter.

Portfolio Activity

- The Fund's portfolio duration is about in line with the benchmark, featuring an overweight in the seven-year to 10-year area and an underweight in the 20-year portion of the yield curve.

- In the spread product domain, the Fund is overweight in provincial credit and underweight in municipal and Canadian government agency debt.

- During the quarter, we added to the Fund's exposure to yield-curve steepening by selling duration-equivalent quantities of 30-year bonds in favour of 10-year bonds. Our concern was that evidence of an economic slowdown domestically and abroad would accumulate and drive the market toward expectations of interest rate cuts from the Bank of Canada.

- In addition, we closed the Fund's underweight position in government credit as the idling of policy interest rates among major central banks provided a more supportive environment for credit spreads in the absence of substantial further deterioration in the outlook for the global economy.

Outlook

- During the quarter, the powerful rally in government bond prices briefly pushed long-term bond yields below short-term bond yields – a so-called inversion of the yield curve. This development was attributable to Fed policy changes and soft economic data. This extreme circumstance has prompted comparisons of global bond markets, particularly in the case of low-growth Europe, to Japan where real interest rates and government bond yields are already negative. Over the near term, however, we believe lower yields should serve as a stabilizing force for growth rather than a precipitator of a deflationary contraction.

- Given the near-zero interest rate starting point, policy-makers and politicians are promoting fiscal tools to counter future downturns. We anticipate low interest rates and low growth to persist, resulting in lower returns across many asset classes.

- The rise of populism, far from fading away, is becoming the norm globally. Populist policies tend to be protectionist, rely on increased fiscal spending and lean on currency markets as an element of national competitiveness. This trend is disruptive to markets in the short term, but the long-term effects may defy historical norms. While populist policies have typically resulted in meaningfully higher inflation in the past, secular disinflationary forces currently in play – including demographic trends, technological change and record-high negative-yielding debt – may challenge that narrative.

Performance (in %)	**Year-to-date**	**1 year**	**3 year**	**5 year**	**Since inception (5/11/2016)**
First Asset Long Duration Fixed Income ETF	6.7	6.9	–	–	2.7
FTSE Canada Long Term Government Bond Index	6.9	7.6	–	–	4.4

Source: First Asset, as at March 31, 2019.

The indicated rates of return are the historical annual compounded total returns, including changes in unit value, and do not take into account sales, redemption or optional charges or income taxes payable by a security holder that would have reduced returns.

Use of Benchmark: FTSE Canada Long Term Government Bond Index is designed to track the performance of long-term (over 10 years) Government of Canada bonds denominated in Canadian dollars. The index is used as a benchmark to help you understand the Fund's performance relative to the general performance of long-term Canadian government fixed income.

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