

ARROW EC INCOME ADVANTAGE ALTERNATIVE FUND

october 2025



Following strong monthly gains since May, risk assets moderated slightly in October as the pace of the rally began to slow. That said, U.S. equities (S&P 500) managed to eke out a +2.3% return, while Canadian equities (TSX Composite) finished mostly flat, posting a modest +0.8% gain for the month. October marked a period of consolidation following strong summer gains, as investors balanced improving inflation dynamics against signs of slower growth. Both central banks cut rates at the end of the month as expected, but each struck a hawkish tone — the Bank of Canada noting that the current policy level is likely appropriate to keep inflation trending toward target, and Chair Powell emphasizing that a December cut was “not a done deal.”

In the U.S., data reflected a gradual cooling in labour conditions, with slower job hiring and signs of moderation in core inflation. Canadian inflation remained slightly higher at 2.6%, supported by persistent strength in shelter and food categories. Interest rates fluctuated throughout the month, initially rallying sharply before giving back some gains following central bank policy meetings. Ultimately, yields ended modestly lower, with U.S. 10yr Treasuries rallying 6bps and Canadian 10yr GoC yields rallying 5bps. Central banks maintained a cautious, data-dependent tone, and the team expects continued volatility as markets reassess the likely pace of future cuts.

U.S. investment-grade (IG) credit weakened in October, with the Barclays U.S. Aggregate Credit Index widening by +4bps, while the iShares LQD ETF widened by +9bps, suggesting that the full magnitude of the move has not yet been fully reflected in the cash market index. The LQD ETF captures shifts in sentiment more quickly, including the late-month weakness in TMT (Technology, Media and Telecommunications) following Meta’s \$30 billion debt offering — one of the largest ever. In contrast, Canadian IG credit outperformed, rallying 1bp on the month, as limited new issuance was insufficient to offset the strong technical bid driven by continued investor demand for attractive all-in yields.

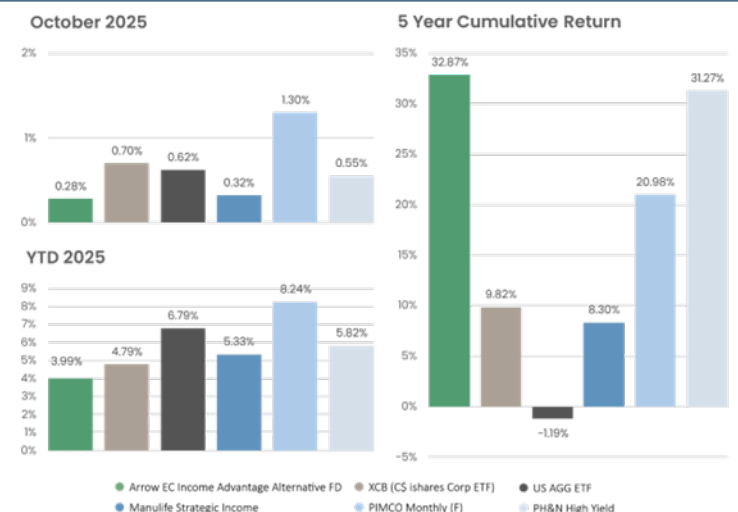
Index and traditional fixed-income funds - particularly those overweight rate duration - delivered stronger results on the back of the October rate rally. Following the October rate cuts, North American central bank rhetoric led markets to reprice expectations for additional cuts. Markets have currently assigned roughly a 65% probability of a single 25bps cut at the December Fed meeting, down from market expectations in early October that had full pricing (100%) for a single 25bps Dec Fed cut and a 20% probability of a 50bps move.

The current environment appears driven more by greed than risk assessment. Investor confidence remains elevated as capital continues to chase returns, even as risk premiums remain compressed, and valuations stretch higher. Markets today seem “priced for perfection” – leaving little margin for error and raising the question: how long before fear overtakes greed? History shows that both emotions—greed and fear—have repeatedly fueled significant market mispricing, from the dot-com bubble to 2020’s COVID-19 volatility. Once sentiment dominates, rational analysis gives way to emotion, and it becomes increasingly difficult for fundamentals, logic, or valuation discipline to reassert control.

Concentration risk in the equity market is approaching record levels. The current AI-driven cycle has created a self-reinforcing dynamic: chipmakers fund cloud providers, cloud providers reinvest in chipmakers, and both direct significant capital toward data center expansion. This feedback loop amplifies growth expectations and valuations across a narrow

Fixed Income Returns¹

Morningstar: Monthly, YTD 2025, and 5yr Cumulative Returns (%)



Source: Morningstar Direct, ArrowEC Income Advantage Alternative FD, Blackrock: Index iSharesETFs (XCB, AGG), PIMCO Monthly Fund (F), Manulife Strategic Income Fund (F), PH&N High Yield Bond Fund (F)

segment of the market, increasing systemic vulnerability should the AI investment cycle lose momentum.

While AI remains the dominant theme and the highest potential risk factor for equity markets, the table at left highlights several additional factors that could disrupt the current market euphoria. Private credit generated headlines in October, reaffirming the investment team's long-standing concern regarding funds that do not employ mark-to-market valuations. While the ongoing government shutdown appears to be nearing an end, the risk it stalls in the House remains. Potential economic and market consequences increase the longer it persists.

As a note, the table does not account for an exogenous shock - a black swan-type event - that could undermine investor confidence almost instantly (e.g., COVID-19).

Theme	Likelihood (6-12mos)	Systemic Impact	Risk	Trigger	Impact
AI & Mega-Cap Tech Valuations	High	High	- Extreme concentration - Stretched valuation / (P/E) multiples	- Sentiment shift - Slower than expected monetization - Earnings misses	- Sizeable tech correction / broad equity weakness - Risk-asset spillover
Private Credit / Shadow Banking	Med – High	Very High	\$2 trillion+ opaque, illiquid lending sector - Weak transparency - Leveraged borrowers & bank funding lines	- Borrower defaults - Redemption pressure in private-credit funds	- Private credit funds collapse - Liquidity contagion to banks and wider credit markets
Credit Market Over-Reach (HY & structured credit)	Med	High	- Record-tight spreads and low risk premium - Weak underwriting in structured & leveraged credit	- Economic slowdown - Rising defaults	- Liquidity stress - Widening spreads - Forced liquidations
AI Infrastructure & Data-Centre Debt	Med	Med-High	- Massive debt-financed build out of data centers, chips and utilities - Long return on investment (payback) timelines	Cost overruns, energy constraints, ROI shortfalls	Credit losses and project-finance stress (spilling into capital markets)
US Government Shutdown Risk	Low-Med	Med	- Treasury bill issuance pauses or is delayed - Faith in US fiscal governance - Economic slowdown/ impact if continues	- Short term liquidity squeeze (bills/MM) - Investors de-risk amid headline noise - Payment delays	- Short term funding stress - Collateral scarcity spikes T-bill yields and repo spreads

Historical Performance	1 yr	3 yr	5 yr	10 yr	ITD
Arrow EC Income Advantage Alternative Ser FD	5.03	8.29	5.85	5.47	4.17

Returns as of October 31, 2025

¹Source: Morningstar Direct: Arrow EC Income Advantage Alternative (Series FD), iShares Core Canadian Corporate Bond Index ETF (XCB), iShares U.S. Aggregate Bond Index ETF (AGG), PIMCO Monthly Fund (F), Manulife Strategic Income Fund (F), PH&N High Yield Bond Fund (F).

The inception date of the Arrow EC Income Advantage Alternative Fund (formerly East Coast Investment Grade Income Fund) was April 26, 2012. On June 26, 2020, the East Coast Investment Grade Income Fund (TSX: ECF.UN) was converted from a closed end fund into an open-end alternative mutual fund, renamed Arrow EC Income Advantage Alternative Fund and delisted from the TSX. Details of the conversion are outlined in the information circular which is available at www.sedar.com. Unitholders of Fund had their units redesignated as Series FD Units.

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The rates of return are used only to illustrate the effects of the compound growth rate and are not intended to reflect future values or returns on investment in an investment fund.

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