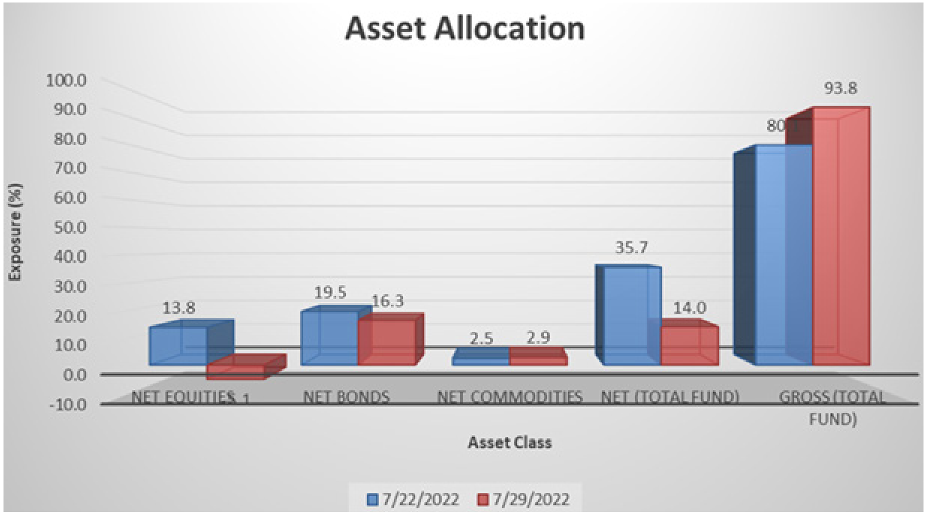
ARROW CANADIAN ADVANTAGE ALTERNATIVE CLASS
Week ending July 29, 2022

Arrow Capital Management Inc.



Monthly performance, macro context, current positioning and future expectations.

Performance
Week of July 29, 2022

Arrow Canadian Advantage Alternative Class (Series F):
WTD -0.07%
MTD (July) -0.87%
YTD 0.34%

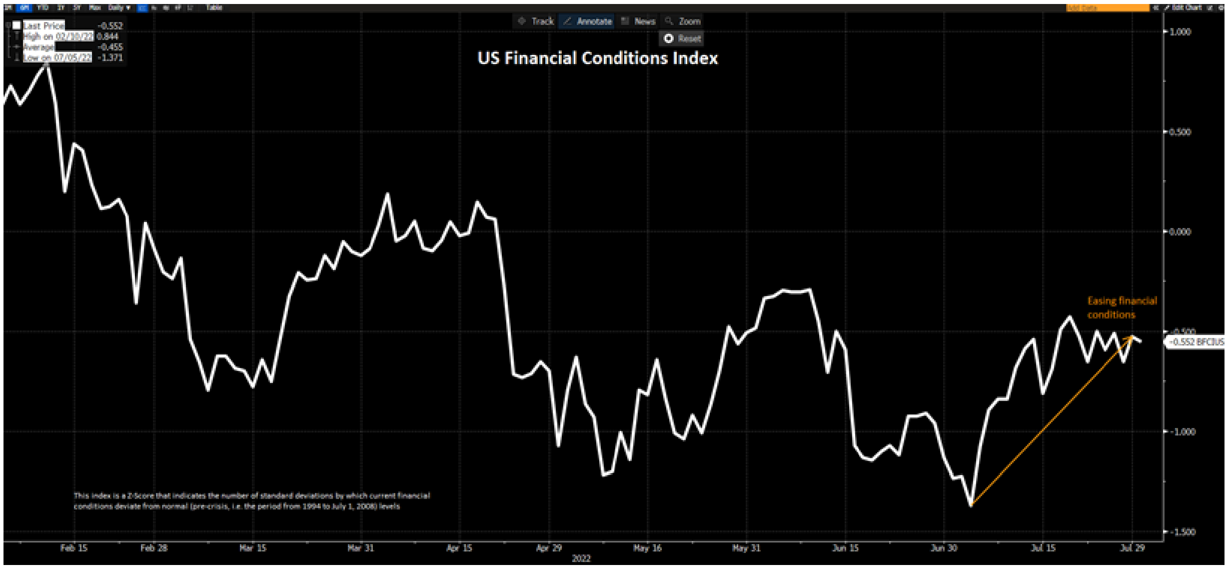
S&P TSX Composite:
WTD 3.74%
MTD (July) 4.41%
YTD -7.21%

S&P 500:
WTD 4.26%
MTD (July) 9.11%
YTD -13.34%

Fund Commentary
The Fund was flat on the week while the TSX was up 3.7%. While our 10yr bond position was a solid performer our equity shorts hurt. We have taken the opportunity with the ramp in equities to materially add to our shorts.

What a week and what a month for stocks especially in the US. The Nasdaq outperformed rising over 10% for the month! The fireworks came largely in the past two weeks as longer-term rates crashed aided by what the market interpreted as an easing post the FOMC presser. While sentiment has been very bearish, the trigger in our opinion was the comment by Chair Powell that the FFR is now in the range of what the FED believes is the “neutral rate” i.e. the rate at which inflation and growth are in balance. So, risk assets can therefore rally right? Not so fast - it is highly likely that either Powell made a mistake, or the market misinterpreted or a bit of both. Larry Summers speaking on BBG TV was quick to criticize the Chair: “Jay Powell said things that, to be honest, were analytically indefensible. There is no conceivable way that a 2.5% interest rate, in an economy inflating like this, is anywhere near neutral.” Remember the neutral rate was estimated by the same FED to be 2.5% in 2018, when inflation was much lower, so the implication is the inflation is all transitory...still!

We believe the FED was hawkish - it is still all about inflation and nothing that Powell stated (outside of neutral rate comment) contradicted his messaging. There has been no pivot. With credit, equity and rates rallying the FED Chair must be beside himself. As Powell said in his March FOMC presser, "Policy works through financial conditions. That's how it reaches the real economy." (h/t Cam Hui). If so, this is the wrong read by the markets.



The proof is also found in the reversal of real rates again. You cannot have your cake and eat it too. The FED has abandoned forward guidance for now - a good idea given their track record - and they should by implication stop talking about neutral rates too. We suspect this week that the FED Governors on tap to speak will try to jawbone down expectations for cuts early in 2023 and focus on the inflation fight. Our forecast for headline inflation is over 7% YoY for Q4 2022! The market will stop fighting the FED at some point.

	Jun-22	Mar-22
REAL GDP QoQ	(0.90)	(1.60)
REAL GDP YoY	1.60	3.50
GDP US Nominal Dollars	24,852	24,387
GDP US Chained Dollars	19,682	19,728
Contribution to % Change in GDP		
Real GDP, QoQ	**(0.90)**	**(1.60)**
Consumption	0.70	1.24
Investment	(2.73)	0.93
Government	(0.33)	(0.51)
Net Exports	1.43	(3.23)
Consumption	0.70	1.24
Durable Goods	(0.22)	0.49
NonDurable Goods	(0.85)	(0.56)
Services	1.78	1.31
Investment	(2.73)	0.93
Residential Investment	(0.71)	0.02
Nonresidential Investment	(0.01)	1.26
Inventories	(2.01)	(0.35)
- Inventory Nonfarm	(1.96)	(0.26)
Government	(0.33)	(0.51)
Federal	(0.20)	(0.46)
State and Local	(0.13)	(0.05)
Net Exports	1.43	(3.23)
Exports	1.92	(0.55)
Imports	(0.49)	(2.69)

We got Canadian GDP this week for May and the flash for June, which was looking okay- maybe 1.1% for Q2- so a bit better than the US, BUT this will change by year end as real estate projects fall off and residential housing deteriorates. In 1Q2022, residential investment rose to 10% of GDP- that is 3 standard deviations above the long-run average- and for some context, well above the 6.7% peak the US experienced in 2005. This week we also got the first cut on Q2 US GDP - it was negative and with back-to-back negative quarters many are calling this a recession. As you know, with our process this is not really important because regardless of definitions, falling real GDP is big negative for equities. While many won't bother to look under the hood, the table below shows the sub-components of GDP; remember your ECO 101 course Y=C+I+G+(X-M)?!

A final brief comment on equities. So far Q2 earnings season has produced a lot of dispersion in results which is not too surprising in an inflationary environment. Those companies with pricing power are flexing it even faster than their rising input prices (a.k.a. "gouging" in some circles) while others that cannot are disappointing. Once nominal GDP begins to fall, we expect that earnings will experience a more rapid ROC decline in Q3 / Q4. Our forecasts are for $200-$210 on SPX for '22 and $190-$200 for '23. As we have noted before, the P has come down but it is the E that is next in the P/E ratio.

Coming this week are more earnings announcements and in Canada, the economic data we are set to get manufacturing PMI data on Tuesday and employment data on Friday.

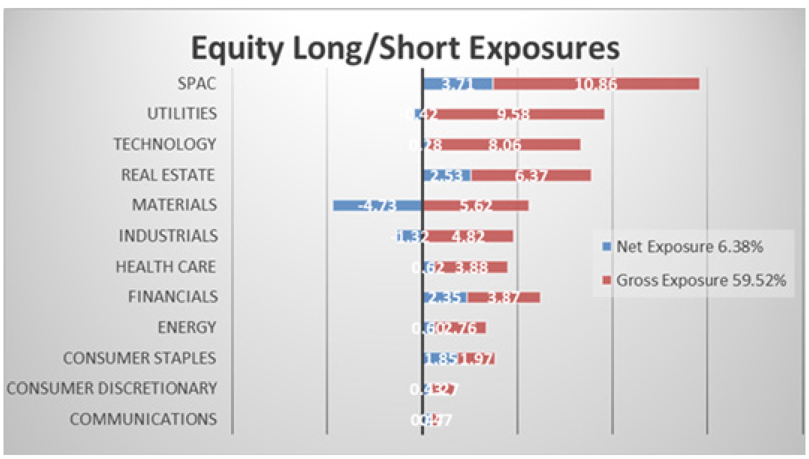
In the US we are getting ISM and PMIs, mortgage apps, durable goods, and employment data (claims, payrolls, hourly earnings, participation rate).

Geographic Equity Exposures (% Total Portfolio including Futures)

ASSET ALLOCATION	NET	GROSS	LONG	SHORT
Canada	3.7	34.9	19.3	-15.6
US	-11.0	34.4	11.7	-22.7
Rest of World	2.1	2.8	2.5	-0.3
Equities Total	**-5.1**	**72.1**	**33.5**	**-38.6**
Bonds	16.3	18.9	17.6	-1.3
Commodities	2.8	2.8	2.8	0.0
Total	**14.0**	**93.8**	**53.9**	**-39.9**

Net equity exposure was reduced from 13.8% to -5.1%.
Canada net exposure was reduced by 4.4%.
US net exposure was reduced from 3.3% to -11%.
Rest of World net exposure was reduced by 0.2%.
Net bond exposure was reduced by 3.1%.
Net commodity exposure was increased by 0.3%.
Total fund gross exposure was increased by 13.7%. Total fund net exposure was reduced by 21.7%.

Sector Exposures (% Long / Short Portfolio of individual companies)



Market Cap Breakdown:

FX Exposures:

FX EXPOSURE	%
CAD	64.8
USD	34.6
Other	0.6
DXY	0.0
Total Fund	100%

As a reminder, we view foreign exchange as active "bets" that are used to either generate alpha or act as a hedge to the overall portfolio. The Fund's reference currency (except for the USD class) is the Canadian dollar so any exposures other 100% Canadian dollars are considered "active" positions.
CAD was increased by 5.1%. USD was reduced by 5.1%.

We look forward to reporting back next week.

Historical Performance – As of July 29, 2022

	1-Year	3-Year	5-Year	10-Year
ACAA - Series F	3.30% 1	5.36%	11.38%	10.28%

Published August 2, 2022.

More information about the Fund can be found on our website www.arrow-capital.com.