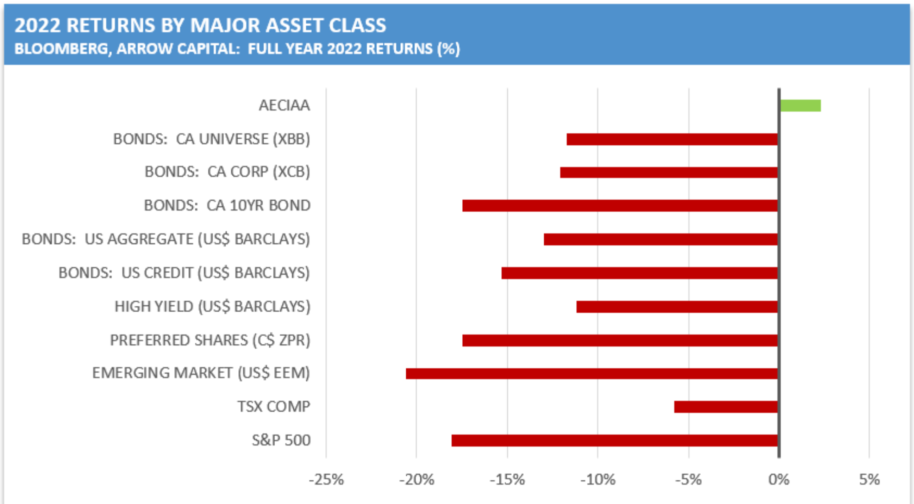
# EAST COAST MARKET COMMENTARY
December 2022



We doubt there is an investor out there who isn't glad to close the door to 2022. Volatility, weakness and reduced asset mix diversification from the increasingly positive correlation between rates and equities, resulted in losses virtually across the board. The chart below shows the full-year returns of major asset classes. East Coast is a beacon of green in a sea of red. This charts aims to highlight the diversification benefit afforded to investors who own investment grade credit (corporate bonds without interest rate exposure). It also highlights the success of our PMs who actively manage the portfolio through constantly changing market conditions. As our investors recall, the portfolio was extremely con-servatively positioned to start 2022, leaving the investment team with tons of dry powder to add risk as credit spreads cheapened (sold off) dramatically throughout the year. By end of Q3, the portfolio was very aggressively positioned – given our investment team's bullish view – and investors made approximately 2.75% in Q4, as spreads started to tighten (rally) into year end.




## THE FEAR THAT INTEREST RATES WOULD NOT BE ABLE TO OFFSET EQUITY LOSSES BECAME A CRUSHING REALITY IN 2022

**US 60/40 Portfolio Returns: 10 Worst Annual Returns of the 60/40 Portfolio on Record**
**NYU: 60% S&P 500 Return and 40% 10yr Treasury Return**

| Year | 60/40 Portfolio Return | Reason |
|---|---|---|
| 1931 | -27.3% | Great Depression |
| 1937 | -20.7% | 1937 Crash |
| **2022** | **-16.9%** | **The Great Inflation** |
| 1974 | -14.7% | 1973-74 Bear Mkt |
| 2008 | -13.9% | Great Financial Crisis |
| 1930 | -13.3% | Great Depression |
| 1941 | -8.5% | WWII |
| 2002 | -7.1% | Dot-Com Crash |
| 1973 | -7.1% | 1973-74 Bear Mkt |
| 1969 | -6.9% | Nifty Fifty Crash |

Interest rates weakened dramatically again in December (+36bps in 10yr Govt of Canada bond yields) capping off the weakest year on record for fixed income in both Canada and the US. In our Dec 2021 investor update we wrote:

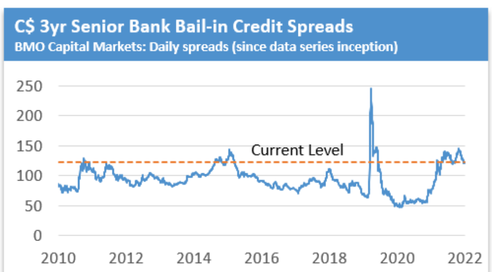
*"Interest rate volatility is likely to continue as central banks around the globe will be forced to raise rates to curb inflation, while simultaneously trying to ensure they do not derail growth prospects in the process. Ultimately, we believe 2022 will be another year of higher interest rates and disappointing returns from traditional fixed income."*

We were very nervous about inflation being higher and stickier than markets were expecting to start this year. We have also discussed our concerns about the increasingly positive correlation between equities and rates over the last 18mos. Throughout 2022, global central banks have increased interest rates dramatically, and their relentless fight against inflation has crushed both equity and fixed income markets.

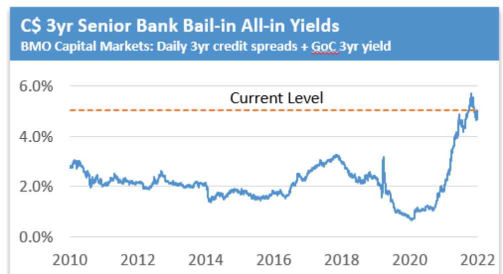
The balanced asset mix (60/40) originated when interest rates were much higher and their annual yield (average ~6.5%) could be expected to help offset equity weakness if risk markets had a bad year. With interest rates yielding between 1-1.5% to start 2022, there was limited yield to start, and the massive move higher in rates (prices lower) compounded the losses in investor's portfolios this year, rather than helping to offset them.

## WILL INVESTMENT GRADE CREDIT CONTINUE TO BE A TOP PERFORMER IN 2023? IT IS HIGHLY FAVORED BY WALL STREET STRATEGISTS

With continued uncertainty in the market, it was very hard to find a single upbeat forecast within Bloomberg's annual Wall Street strategist's survey results. Bloomberg summed it up quite nicely: "It may be one of the most anticipated recessions of all time, but that doesn't mean it won't hurt." Most strategists expect recessions on both sides of the Atlantic, dismal growth rates, increasing Fed fund rates and further weakness in equities (at least in the first half). While our Investment Team has been bullish on investment grade (IG) credit since mid 2022, as we now enter 2023, others have finally caught on. Strategists seem to be highly supportive of investment grade credit which appeared to be one of the few darlings within the Bloomberg strategist survey. Strategists also remain very wary of High Yield (HY), warning investors to "keep an eye on quality" and to focus on an "up-in-quality approach" within credit markets. It's nice that Wall street strategists are finally paying attention and seeing the benefit of IG credit; however, we believe the charts below (left), of historic IG credit spreads, and below (right), of all-in IG corporate bond yields, make the most salient arguments for the inclusion of credit within investor portfolios.




During Q4 2022, 3yr Senior bank bail-in credit spreads (left) cheapened to levels that have only been cheaper during COVID-19 (since data series inception date of Jan 1, 2010). Spreads have rallied slightly in December but remain cheaper than the vast majority of trading days in 12yrs of history. The chart at right is even more compelling as it shows the all-in yield of IG corporate bonds which is still at the cheapest levels seen over this 12yr period for which we have 3yr Senior bank bail-in data history.




The December podcast by our CIO, Mike McBain, goes into detail about 2022 year-end results, as well as our Investment Team's thoughts as we enter 2023. This-one pager serves only as a brief summary to highlight the strategy's success in a very difficult year for investments (2022) and outlines a few reasons we believe investment grade credit strategies should continue to outperform heading into 2023 in a highly uncertain, and likely volatile, environment.

| Historical Performance | 1 yr | 3 yr | 5 yr | ITD |
|---|---|---|---|---|
| Arrow EC Income Advantage Alternative FD | 2.30 | 3.29 | 3.64 | 3.22 |
| East Coast Investment Grade II Fund Cl F | 3.99 | 6.32 | 6.51 | 5.67 |

*Returns as of December 31, 2022*

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 redes¬ignated as Series FD Units. The inception date of the East Coast Investment Grade II Fund is April 1, 2013.

Commissions, trailing commissions, management and performance fees and expenses all may be associated with mutual fund and exchange-traded fund (ETF) investments. Please read the prospectus and Fund Facts for Arrow EC Income Advantage Alternative Fund carefully before investing before investing. Offering of securities in the East Coast Investment Grade II Fund are made pursuant to a Confidential Offering Memorandum (OM) only to those investors who meet certain eligibility or minimum purchase requirements. Important information, including this fund's fundamental investment objective is contained in the OM which may be obtained from Arrow Capital Management Inc. Please read the OM before investing. Unless otherwise indicated, the indicated rates of return are the historical annual compound total returns net of fees and expenses payable by the fund (except for figures of one year or less, which are simple total returns) including changes in security value and reinvestment of all 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. Mutual funds and ETFs are not guaranteed, their values change frequently and past performance may not be repeated. You will usually pay brokerage fees to your dealer if you purchase or sell securities of an ETF on recognized Canadian exchanges. If the securities are purchased or sold on these Canadian exchanges, investors may pay more than the current net asset value when buying securities of the ETF and may receive less than the current net asset value when selling them.

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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The comparison presented is intended to illustrate the historical performance of Arrow EC Income Advantage Alternative Fund and East Coast Investment Grade II Fund (the "Funds") as compared with the historical performance of a widely quoted market index or a weighted blend of widely quoted market indices or other investment funds. There are various important differences that may exist between the Fund and the stated indices or other investment funds that may affect the performance of each. The objectives and strategies of the Fund result in holdings that do not necessarily reflect the constituents of and their weights within the comparable indices. Indexes are unmanaged and their returns do not include any sales charges or fees. It is not possible to invest directly in market indices. Certain statements contained in this communication are based in whole or in part on information provided by third parties and Arrow Capital Management has taken reasonable steps to ensure their accuracy. Market conditions may change which may impact the information contained in this document. Published January 2023.