ARROW EC INCOME ADVANTAGE ALTERNATIVE FUND
december 2024

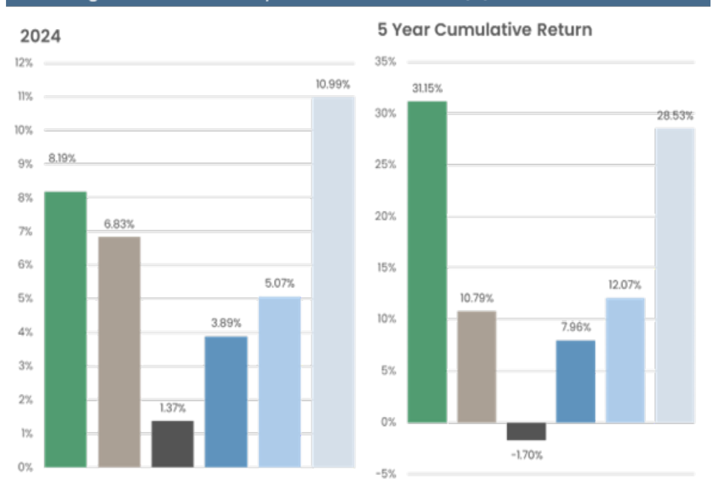
Arrow Capital Management Inc.

Equity markets struggled in the final month of the year, as attention remained firmly fixed on the Federal Reserve (FED). During its December meeting, the Fed implemented the widely anticipated 25bps reduction in policy rates. However, the accompanying Q&A and press release were more hawkish than markets had expected. A key point of focus was the statement that the committee had revisited the “extent and timing” of potential future cuts. As a result, equity markets sold off sharply, with the S&P 500 recording its second-largest daily decline of 2024 (-2.9%). While equity markets posted impressive returns for the year, December results were disappointing. The U.S. equity market (S&P 500) closed down -2.4%, while the Canadian equity market (TSX Composite) finished -3.3% lower.

As East Coast PMs expected, the FED rate cut did little to help interest rates, as longer-term rates sold off and interest rate yield curves continued to steepen dramatically in December. In Canada, the 2s-10s curve steepened 25bps as 2yr rates moved 11bps lower (rallied) and 10yr rates rose (sold off) 14bps. US 2s-10s curve steepened 31bps with 2yrs rising 9bps and 10yr rising a much more significant 40bps. The steepening of curves, and overall rise in rates, is the result of markets re-pricing rate cutting expectations (fewer and pushed farther out in time) as well as the potential inflationary pressure and additional supply that could result from the incoming Trump administration.

The equity market rally led risk asset performance in 2024; however, December served as a stark reminder of the importance of quality in the current market environment. As assets, including credit, have become increasingly expensive, the team has continued to emphasize the growing need to focus on quality. For example, high-yield (HY) credit risk premiums relative to investment-grade (IG) credit, approached 10yr low levels in Q4 – a clear indication investors were not being adequately compensated for the additional risk. During December’s modest sell-off, lower-quality exposures were hit harder, with U.S. high-yield (HY) spreads widening by 21 basis points, while higher-quality U.S. investment-grade (IG) credit spreads only increased by 2 basis points.

Fixed Income Returns[1]
Morningstar: FY 2024 and 5yr Cumulative Returns (%)



Canadian investment-grade (IG) credit outperformed the U.S. market, rallying and tightening by 3 basis points in December. As the performance charts on the right highlight, AECIAA investors achieved significant returns relative to more traditional fixed income in 2024. The investment team achieved these returns without exposing investors to higher risk HY assets. While riskier assets performed well throughout the year, the strategy aims to maximize **risk-adjusted returns** for investors.

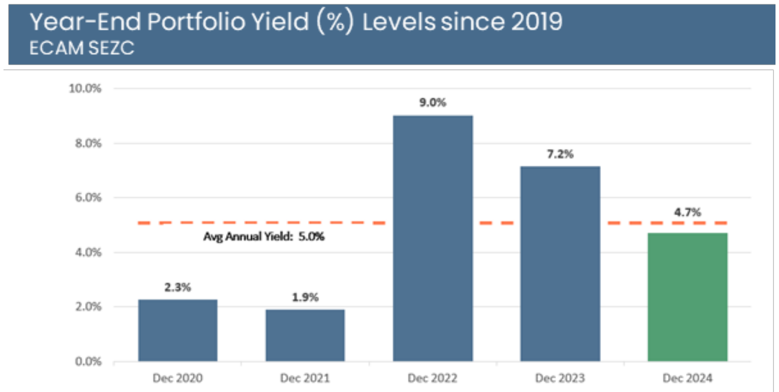
C$ Credit: 3yr Bank Bail-in Credit Spreads
BMO Capital Markets: Daily spreads

While all-in yields of corporate bonds remains compelling, the credit portion has rallied significantly in 2024 (as the blue line at left illustrates) and spreads are trading near historically expensive levels. Given current market levels, the portfolio is positioned with significantly less risk (credit exposure) as the PMs anticipate some credit spread weakness in early 2025.

The portfolio’s 12-mos break even (B/E) level is a key risk metric. Over the next year, given current positioning, the portfolio could sustain any spread weakness up to this B/E value and investors could still expect to experience a positive return. The ability of the portfolio to sustain a move of this magnitude without expected negative annual returns illustrates the current defensive positioning.

As the chart at bottom left of the previous page highlights, spreads could weaken to the orange dotted line (near the worst COVID-19 days) and investors would be flat, or break-even, over the 12-month period.

The current yield drives the investor “buffer” and creates the appealing 12-mos B/E level above. Even with substantially reduced risk exposure, the portfolio still offers investors a yield that is above the 5yr historic average. This yield, shown in the bar chart at right, is the annual return investors could expect to receive if spreads remain at current levels. This does not account for potential spread tightening, or more likely in this environment, the addition of risk at cheaper levels if spreads weaken.



	2021	2022	2023	2024	2025
Starting Yield	2.3%	1.9%	9.0%	7.2%	4.7%
Full Year Return	2.1%	2.3%	10.0%	8.2%	Target: 5-7%

The table below the chart highlights each year’s starting yield (the level at the end of the previous year on December 31st) alongside the actual full-year net return achieved over the 12 months period. As you can see from the two dotted lines, we have a historic track record of being able to create returns in excess of the portfolio yield since 2019 and we remain confident that the current portfolio positioning can generate returns within the target range of 6-8% for investors in 2025. The investment team believes a portfolio focused on higher-quality, lower-risk assets, along with the avoidance of interest rate volatility, will continue to provide an exceptionally compelling return profile for investors.

Historical Performance	1 yr	3 yr	5 yr	10 yr	ITD
Arrow EC Income Advantage Alternative Ser FD	8.19	6.78	5.57	4.70	4.13

Returns as of December 31, 2024

[1]Source: 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 redes¬ignated as Series FD Units.

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. 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 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 2025.