Everything Everywhere All At Once | March 2025

'Chaos, when left alone, tends to multiply.'
Stephen Hawking

In true game show fashion, President Trump unveiled his administration's reciprocal tariffs with a 'family feud'-style board (survey says 34%). The aim of 'Liberation Day' was to emancipate America from the economic oppression of its global trading partners.

So far, the only liberation to note is investors being freed from their money. Since that fateful afternoon in the Rose Garden, equities have declined by over 10%, and high-yield credit spreads are 80 bps wider.

The silver lining for Canadians is that we are out of Trump's crosshairs (for now). But every silver lining has a cloud. And before we start popping bottles of sparkling ice wine and maple syrup, we need to consider the existing tariffs and the implications of 'Liberation' for the US and global economy.

Oh, Canada?

Thus far, Canada has escaped reciprocal tariffs. However, sectoral tariffs on autos, aluminium, steel, energy, potash, lumber, and non-CUSMA-compliant goods remain. The drag on these export-heavy industries is estimated to have a 1.5-2% impact on growth (i.e., flirting with a recession). And this is just the tariffs in and of themselves and does not factor in the increasing potential for a global economic slowdown.

While it is impossible to pinpoint the odds of a recession, it is safe to assume the probability is much higher today than it was a week ago. The shocking scope and magnitude of the tariffs have radically changed the outlook for the US and global economies.

The land of the freed.

The weighted average tariff on imports into the US has risen over 20%. The natural consequence is rising prices, with US inflation potentially hitting 3.5-4% in the coming months. Estimates put the cost to the average household at $3,000-$4,000, implying reduced discretionary spending in an economy heavily dependent on consumer spending.

Furthermore, the tariffs upend global trade and supply chains, and the uncertainty reduces business investment. Thus, while a recession might be avoided, it is hard to foresee escaping a slowdown in GDP.

Central bank tug-of-war.

This puts central bankers in the stagflation quagmire of higher inflation and slower growth. For now, markets are betting that lower growth will win the tug-of-war. The perception is that tariff-induced inflation will be 'transitory' and that the bigger concerns are a recession and higher unemployment.

As we type, the bond market has priced in five cuts from the Fed and three from the BoC over the next twelve months. It seems reasonable for them to cut rates, but it might not have the desired effect that investors are seeking.

The Fed put.

The problem is that monetary policy is a blunt instrument and ill-equipped for a trade war. Lower rates can dull economic pain but are ineffective in combating tariffs. The only real solution to tariffs is removing them, which seems unlikely in the near term.

In 2022, we wrote that 'the Fed put was kaput'. We will not go so far this time. There is certainly room for lower rates to provide some relief, but their impact will be limited. Unfortunately, this implies that the V-shaped recovery equity investors have grown accustomed to might be harder to manufacture this time around.

The Month of March.

Credit.

The tariff two-step led to significant market confusion and volatility, with recession fears ultimately leading to a sell-off in risk assets. US equities hit correction territory mid-month, declining more than 10% from their February peak. The sell-off in credit was orderly, with spreads leaking wider.

The broad investment-grade indices show spreads to have widened by 4-7 bps. On the ground, we saw bigger moves and greater dispersion, with spreads 5-40 bps higher, depending on the sectors and issuers (autos being the standout underperformer).

Investment grade credit spreads:

- Canadian spreads widened 4 bps to 113 bps.
- US spreads widened 7 bps to 94 bps.

In Canada, CIBC was a notable issuer, coming to market with an institutional preferred share, LRCNs, and NVCCs. In telcos, BCE brought a hybrid to market as it seeks to progress in deleveraging via partial equity treatment of these securities. Furthermore, BCE conducted and upsized a tender process for some of their long bonds, which was positively received by the market. Late in the month, Telus announced it is pursuing a partial sale of its wireless towers, which is expected to raise $1 to $1.5 bn to repay debt. Overall, it appears the telcos have received the message from rating agencies and are looking to monetize infrastructure assets to accelerate their deleveraging efforts. This will likely be a theme through Q2, which bodes well for spread performance in the sector.

Interest Rates.

The BoC delivered another 25 bps cut, bringing the overnight rate to 2.75%. The Bank acknowledged that the economic data did not warrant the cut, but with 'pervasive uncertainty' surrounding tariffs, they felt that further easing was prudent. With inflation still running hot south of the border, the Fed held rates steady, opting for a 'wait and see' approach.

Overall, fears of a tariff-induced slowdown led bond traders to increase the odds of additional rate cuts from the Fed and BoC, resulting in a rally in short-end rates. Longer-dated yields traded in a contained range and ended the month flat to 7 bps higher, steepening both US and Canadian yield curves.

Sovereign yields:

- Canadian 2y finished at 2.46% (-11 bps) and the 10y at 2.97% (+7 bps)
- US 2y finished at 3.90% (-10 bps) and the 10y at 4.21% (unchanged)

The Funds.

Algonquin Debt Strategies Fund.

The Fund maintained its defensive risk posture, with credit exposures at the lower end of our historical range. Over the month, we continued to rotate the portfolio to higher-quality, liquid issuers and dynamically managed credit hedges. Ultimately, the yield and active trading were not enough to offset the losses from the credit spread widening, leading to a slight loss in the month.

Portfolio Metrics:

- 5-6% yield
- Average credit rating: BBB+
- Average maturity: 2.4y
- IR Duration: 1.5y

	1M	3M	6M	YTD	1Y	3Y	5Y	10y	SI
X Class	-0.07%	0.27%	2.88%	0.27%	8.62%	8.15%	9.39%	7.92%	8.29%
F Class	-0.11%	0.14%	2.47%	0.14%	7.55%	7.20%	8.51%	NA	NA

* As of March 31st, 2025

The Algonquin Debt Strategies Fund LP was launched on February 2, 2015. Returns are shown on 'Series 1 X Founder's Class' since inception and for 'Series 1 F Class' since May 1st, 2016, and are based on NAVs in Canadian dollars as calculated by SGGG Fund Services Inc. net of all fees and expenses. For periods greater than one year, returns are annualized.

Algonquin Fixed Income 2.0

The sell-off in credit was a headwind for the Fund, but having reduced exposures, the losses from spread widening were contained and offset by the portfolio yield, duration management, and active trading.

Portfolio Metrics:

- 4-6% yield
- Average credit rating: BBB+
- Average maturity: 3y
- IR Duration: 2.3y

	1M	3M	6M	YTD	1Y	2y	3y	5y	SI
F Class	0.05%	1.18%	3.05%	1.18%	9.49%	8.94%	6.30%	7.34%	5.02%

* As of March 31st, 2025

Algonquin Fixed Income 2.0 Fund is an Alternative Mutual Fund and was launched on December 9, 2019. Returns are shown for Class F since inception and are based on NAVs in Canadian dollars as calculated by SGGG Fund Services Inc., net of all fees and expenses. Investors should read the Simplified Prospectus, Annual Information Form, and Fund Facts Documents and consult their registered investment dealer before making an investment decision.

Commissions, trailing commissions, management fees, and operating expenses all may be associated with mutual fund investments. An Alternative Mutual Fund is not guaranteed, its value changes frequently and its past performance is not indicative of future performance and may not be repeated. Payment of quarterly distributions is not guaranteed and paid at the discretion of the manager; therefore, it may vary from period to period and does not infer fund performance or rate of return.

Looking Ahead.

Trump's tariff policy has ignited a global trade war. Last month, we wrote that markets not only underestimated the probability of tariffs but also the impact of them.

Confronted with the reality that Trump was not joking, people are now scrambling to determine appropriate risk premiums for various asset classes. Given the complex nature of global trading flows and the potential for further escalation, it could take weeks, if not months, to arrive at appropriate valuations.

The current market moves are all based on speculation and fear. Over time, the economic data will start reflecting the impact of trade policy, which will result in further market adjustments.

With the odds of a recession increasing, central bankers are expected to respond with monetary stimulus. While rate cuts are likely to occur, Messrs Powell and Macklem have clarified that monetary policy does little to ameliorate the effects of a trade war. As a result, should growth weaken significantly, the chances of a sharp recovery seem low.

This creates a difficult environment for equities, which are sensitive to growth prospects. Trade confusion makes it difficult to see how and when a return to sustained growth could emerge. It is possible that once stock markets find a comfortable level, they just muddle sideways for a long time.

As credit investors, we see an opportunity brewing. Credit funds do not require a recovery and narrowing of spreads to generate attractive returns. Higher spreads translate into higher yields, improving the performance prospects in the medium term.

We reduced exposures by over 50% late last year and continue to actively manage the portfolios from a defensive posture. We have not changed our view yet; however, as valuations become cheaper, it will make sense to gradually add exposure. We will look to the hard data, central bank guidance, and further changes to tariff policies to inform our decision.

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