DECEMBER 2018

Debt Market Monitor

Debt Capital Markets Services

A poorly performing stock market can affect short bond yields

The Canadian and U.S. stock markets look like they may have given up all, or most, of their 2018 gains during the year. As a result, investors are flocking to the short end of the bond market for safe shelter. Large-bond fund managers, such as PIMCO and BlackRock, are urging turmoil-weary investors to direct funds to short-maturity bonds as higher interest rates push front-end yields to more attractive levels. The thought being: Although front-end bond yields will not likely match the returns of the equity market, they may end up among the few positive yielding assets for 2018.

For investors that are seeking a haven from volatility, front-end bonds have a strong record during stock market drawdowns. Managers of corporate cash accounts have complained of the growing challenge to source short-end bonds – partly due to non-traditional buyers entering the bond buying market previously largely occupied by wholesale buyers, thus adding to the demand.

The increasing demand for short-term bonds coincides with the Federal Reserve's expectations of rate hikes – which, in theory, leaves these bond holders poorly positioned for further monetary tightening in general. However, BlackRock's chief investment officer of global fixed income believes that the impact of two or three further rate hikes next year, is already baked into the yields we are presently seeing. He goes on to say that short-dated yields have overstretched their climb, insulating investors from further rate increases. BlackRock indicates that the income earned from holding bonds with a two-year maturity time line can withstand a further yield increase of approximately 1.4% without incurring a negative return over a one-year period.

Although the Federal Reserve is sending strong signals that multiple rate increases are in the offing, there may not be as immediate an impact on the short end of the bond market as some people think.

Fiscal Snapshot

Bank of Canada

	Bank Rate	Bank Prime Lending Rate
November 2018	2.00	3.95
One month ago	2.00	3.95
One year ago	1.25	3.20

Government of Canada Benchmark Bond Yields

	5-Year	10-Year	Long
November 2018	2.20	2.27	2.39
One month ago	2.42	2.49	2.52
One year ago	1.63	1.89	2.23

Indicative Commercial Mortgage Spreads* Over Government of Canada Bond Yields

Conventional	5-Year	10-Year
November 2018	1.40 - 1.90	1.60 - 2.00
One year ago	1.50 - 2.00	1.65 - 2.25
Insured	**5-Year**	**10-Year**
November 2018	0.80 - 1.10	0.80 - 1.10
One year ago	0.95 - 1.15	0.95 - 1.25

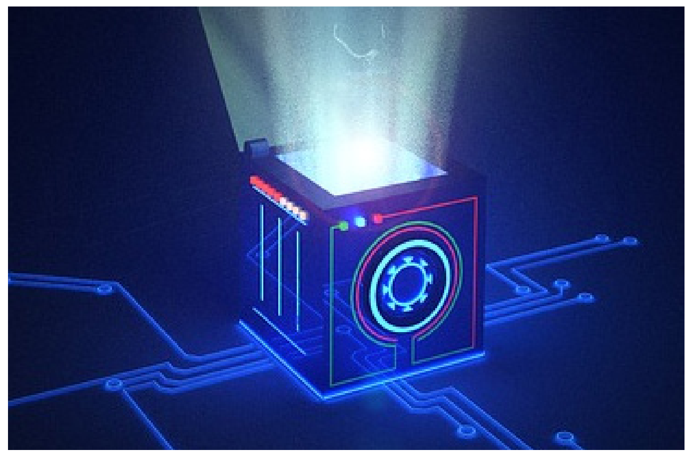
*Spreads are indicative of high quality real estate in major Canadian markets.

Highlighted Transaction

Asset Type	Multi-tenanted flex office
Location	Major Canadian city
Facility Details	A $20M non-recourse, committed non-revolver to assist with the future development of additional density. The facility is for a 3 year term with an extension option of a further 2 years. The structure includes a floating interest rate with the ability to swap to a fixed rate at the borrower's option.

Intelligent Debt Financing Solutions

The Avison Young Debt Capital Markets dedicated team is focused on providing innovative North American-wide debt and equity solutions to accomplish goals. We originate debt and equity for all types of real estate and all types of clients. Debt origination includes fixed and floating rate structures, permanent and construction financing, structured finance, bridge and mezzanine debt and insured agency financing - CMHC and Fannie Mae / Freddie Mac.



Our years of combined debt/equity capital markets experience has created meaningful relationships that we can put to work for you.

Please contact our Debt Capital Markets team for more details related to debt financings or real estate transactions.

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