Sun Life Wellington Opportunistic Fixed Income Private Pool

FUND COMMENTARY | Q4 2021

Opinions and commentary provided by Wellington Management.

Portfolio review

Global fixed income sectors generated mixed results over the fourth quarter of 2021 as market participants grappled with renewed COVID uncertainty. Most sovereign yield curves flattened as central banks pursued tighter monetary policies in response to sustained inflationary pressures. Most fixed income spread sectors outperformed government bonds, boosted by their income advantage and ongoing fundamental improvement amid limited spread movements. The US dollar (USD) finished higher versus most currencies in 2021.

Central bankers further progressed on their paths toward policy normalization during the period as inflation broadened out across more goods and services. The US Federal Reserve (Fed) accelerated the timeline for tapering its large-scale asset purchase program and projected three rate hikes in both 2022 and 2023. The Bank of England (BOE) hiked rates for the first time since the onset of the pandemic, citing persistent price pressures. While it expects to keep its policy rate on hold through the end of 2022, the European Central Bank (ECB) announced it would conclude its purchases under its pandemic emergency purchase program by March. The Norges Bank once again lifted its policy rate and indicated more hikes were likely, depending on the evolution of the pandemic. The Swiss National Bank and Bank of Japan diverged from many of their peers and maintained their policy rates.

Global sovereign yield curves flattened driven by increasing short-term yields following a hawkish pivot by major developed market central banks. Policymakers announced plans to dial back monetary stimulus as inflation concerns persisted into Q4. Omicron concerns did not delay monetary policy tightening plans, as most central banks remained focused on upside inflation risks. The inflation momentum in part led US Senator Joe Manchin to scale back his support for President Biden’s signature Build Back Better legislation in its current form. The ECB delivered a marginal hawkish surprise by announcing that its Asset Purchase Programme will only be raised to €40 billion per month when PEPP ends. The Bank of Canada pushed back against March rate hike expectations, reiterating a lift-off is not to be expected until the “middle quarters” of 2022. Within Emerging Markets (EM), select central banks in Latin America and Central and Eastern Europe, Middle East, and Africa continued to hike rates. The Peoples Bank of China eased policy, cutting the reserve ratio and the policy rate as weak growth persisted, driven by regulatory clampdown on sectors like real estate and technology.

The portfolio realized mixed total return contributions from its three components during the fourth quarter including, strategic sector, market neutral and tactical.

Sun Life Wellington Opportunistic Fixed Income Private Pool

FUND COMMENTARY | Q4 2021

Strategic sector positions contributed positively to portfolio returns for the quarter as the combination of stimulative fiscal and monetary policies, pent-up demand, and supply bottlenecks lifted inflation expectations. This environment benefited positions in global inflation linked bonds, particularly in the US and Canada, as well as positions in cyclical US high yield sectors. In addition, holdings in non-US sovereign bond markets where inflation trends are more contained or where markets have already price in more aggressive policy responses including China and Canada, proved more resilient. Offsetting these positive contributions were holdings in securitized credit and emerging markets debt that underperformed as markets priced in more aggressive Fed tightening.

Market neutral strategies were negative for the quarter driven by currency positions and in particular underweight exposure in the US Dollar. The US dollar rallied versus most currencies, supported by expectations for a more hawkish path of US monetary and fiscal policy. Tactical strategies also detracted as a 10% allocation to Bank Loans, the strongest performing sector for the quarter, was not enough to offset negative contributions from European credit and duration positions. Within duration strategies positive contributions from short positions in German bunds and long positions in Canadian governments were not enough to offset negative contributions from peripheral European holdings.

As we enter 2022, it is helpful to recap some of the key macro themes of 2021 as they have relevance for the trajectory of the economy and markets.

Following the Democratic sweep of the Georgia Senate elections in early 2021, US real yields rose sharply over the first quarter. The team found this outcome somewhat puzzling as the more obvious impact of the Democratic sweep should have resulted in a rise in inflation expectations given more fiscal spending. A rise in real yields would normally be associated with views of higher future productivity. The market realized this mispricing and US real yields fell substantially throughout the second quarter.

The drop in US real yields initially contributed to a decline in the US dollar and a boon for Emerging Market (EM) assets, which typically perform well when US real yields stay low. However, Fed Chair Powell's press conference in June 2021 indicated a significant shift in policy that set the tone for how assets traded for the remainder of the year. In the conference, Powell pushed back against the idea that the Fed would remain dovish in the face of persistently higher inflation, an assumption the market had made after the Fed's revised policy statement in September 2020.

From then on, inflation surprises meant higher front-end yields and a stronger dollar as the market assigned new credibility to the Fed. This had increased significance as 2021 saw the highest inflation surprise – based on US CPI – since at least 1990. This change in posture had a dramatic effect on smaller developed market (DM) countries and EM countries. Both are too small to run independent monetary policies i.e., if inflation is a problem (largely caused by US fiscal spending/drawdown in US savings) then they have to respond with much more hawkish monetary policy otherwise their currencies will depreciate, exacerbating the inflation problem. The market quickly priced that into the front ends of many EM as well as DM yield curves e.g., New Zealand, Canada, Australia.

The team continues to focus on global assets that they feel still present attractive total return potential in a world of low yields. For example, the Fund has been adding to the Emerging Market Opportunities theme that features a combination of exposures to emerging markets external and local debt.

The Fund continues to focus on assets that should perform well in a period of volatile, but sticky inflation and greater uncertainty. The best protected areas in the teams view include global inflation linked bonds, consumer-linked structured credit, and bank loans. Wellington are least favorable on US corporate sectors as current spread levels do not compensate investors for a risk of rising spread volatility.

Market neutral strategies continue to be an important facet of the Fund as volatility presents relative value opportunities in rates and currency.

The team continues to believe we've entered a new macro era of higher and more volatile nominal growth and higher and more persistent inflation, underpinned by forces that are unique to this new business cycle. The Sun Life Wellington Opportunistic Fixed Income Private Pool is well positioned to take advantage of opportunities in this type of environment.

Fund performance

COMPOUND RETURNS %[1]	Since Inception[2]	5 Year	3 Year	1 Year	Q4
Sun Life Wellington Opportunistic Fixed Income Private Pool - SERIES A	1.2	0.9	4.7	-2.1	-1.0
Sun Life Wellington Opportunistic Fixed Income Private Pool - SERIES F	0.2	-0.1	3.7	-2.9	-1.3
Bloomberg Barclays Global Aggregate Bond Index (C$ Hedged)	2.5	3.0	3.7	-1.4	0.0

[1]Returns for periods longer than one year are annualized. Data as of December 31, 2021.
[2]Partial calendar year. Returns are for the period from the fund's inception date of June 6, 2016 to December 31, 2016.

On May 24, 2019 Sun Life Wellington Opportunistic Fixed Income Fund, previously Sun Life Multi-Strategy Return Fund, changed its name and underwent a change in investment objective to seek exposure to diverse global fixed income strategies; it is structured as an alternative mutual fund. The sub-advisor assumed portfolio management responsibilities at that time. On February 26, 2020 Sun Life Wellington Opportunistic Fixed Income Fund was renamed to Sun Life Wellington Opportunistic Fixed Income Private Pool.

Sun Life Wellington Opportunistic Fixed Income Private Pool

FUND COMMENTARY | Q4 2021

securities does not. Series A securities of the fund are available for purchase to all investors, while Series F securities are only available to investors in an eligible fee-based or wrap program with their registered dealer. Investors in Series F securities may pay a separate fee-based account fee that is negotiated with and payable to their registered dealer.

Sun Life Global Investments is a trade name of SLGI Asset Management Inc., Sun Life Assurance Company of Canada and Sun Life Financial Trust Inc.

SLGI Asset Management Inc. is the investment manager of the Sun Life Mutual Funds, Sun Life Granite Managed Solutions and Sun Life Private Investment Pools.