Tactical Bond Strategy

As of September 30, 2018

Strategy description

Scotia Institutional Tactical Bond Fund invests with an objective to maximize total return by optimizing the risk/reward trade-off in changing market environments.

The Tactical Bond strategy's alpha is derived from core levers such as duration and yield curve positioning, sector allocation and security selection, but also complemented with non-core holdings such as foreign investments and modest currency exposure in order to enhance yield and maximize return in a risk-controlled framework.

The Tactical Bond strategy also integrates the notion of active and tactical management to a higher degree compared to more traditional bond solutions.

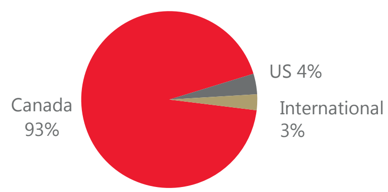
Why invest?

- Active management can produce superior risk adjusted returns for fixed income investors.
- Value added through foreign exposure, discrete currency hedging and tactical positioning.
- Multiple strategies are used to diversify risk.
- Strategies are flexible and responsive to market conditions.

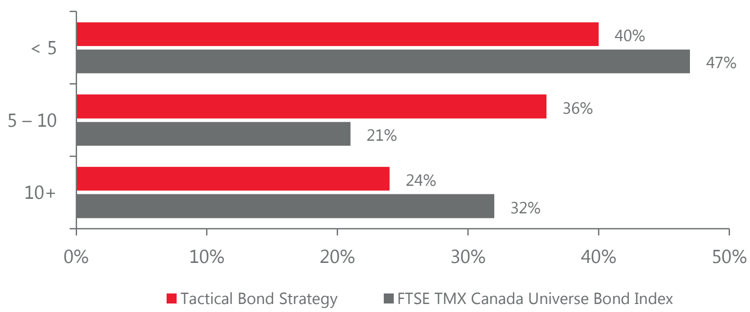
Portfolio characteristics

Top 5 issuers (%)	
Government of Canada	24.4
Province of Ontario	11.6
Province Of Quebec	6.7
Province of Manitoba	4.0
Royal Bank Of Canada	3.5
Total	**50.2**

Geographic allocation



Term distribution (years)



Bond rating (%)	**Tactical Bond Strategy**	**FTSE Canada Universe Bond Index**
AAA	32.6	39.5
AA	19.8	17.9
A	39.3	31.6
BBB	8.3	11.1
Total	**100.0**	**100.0**

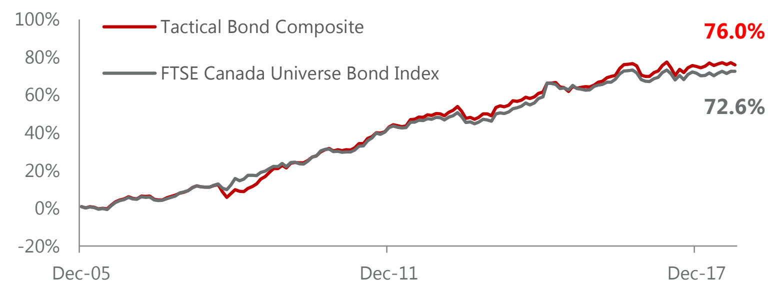
End Weights
Excludes cash

Highlights

Inception	December 1, 2005
Strategy AUM	$584 MM
Liquidity	Segregated: Daily / Pooled: Weekly
Holdings	88
Currency	Discretionary hedging
Benchmark	FTSE Canada Universe Bond Index

Performance

Cumulative returns (%)



Compound returns (%)	**1 mth**	**3 mth**	**6 mth**	**1 yr**	**3 yr**	**5 yr**	**7 yr**	**10 yr**
Composite	-0.69	-0.69	-0.60	2.39	2.35	3.51	3.32	4.92
Benchmark	-0.97	-0.96	-0.45	1.66	1.60	3.26	2.91	4.44
Value add	**0.28**	**0.27**	**-0.15**	**0.72**	**0.76**	**0.25**	**0.41**	**0.48**

Calendar returns (%)	**YTD 2018**	**2017**	**2016**	**2015**	**2014**	**2013**	**2012**	**2011**	**2010**	**2009**
Composite	0.50	3.05	2.86	2.28	8.45	-0.73	4.84	9.16	7.99	10.55
Benchmark	-0.35	2.52	1.66	3.52	8.79	-1.19	3.60	9.67	6.74	5.41
Value add	**+0.86**	**0.53**	**1.20**	**-1.24**	**-0.34**	**0.46**	**1.24**	**-0.51**	**1.24**	**5.14**

Comparative analysis

	Tactical Bond Strategy Guidelines	**Tactical Bond Strategy**	**FTSE Canada Universe Bond Index**
Cash & Floating Rate Notes**	0-30%	8.3%	-
Federal Bonds**	0-100%	24.4%	35.6%
Provincial Bonds**	0-100%	23.3%	34.0%
Corporate Bonds	0-60%	37.6%	28.5%
Real Return Bonds & US TIPs	0-25%	-	-
Canadian Exposure	80-100%	93.0%	100%
Foreign Exposure	0-20%	7.8%	-
Hedges & Derivatives	0-100%	87.5%	-
Yield to Maturity*	-%	2.45%	2.91%
Duration	+/- 2 years	5.55 years	7.40 years
Average Credit Rating	Min BBB-	AA-	AA
Holdings	-	88	1,479

Source: 1832 AM, FTSE Global Debt Capital Markets
*Total yield adjusted for futures
** End weight

Scotia Institutional Asset Management™

Q3 2018 Portfolio commentary (as of September 30, 2018)

Romas Budd, MBA, Vice President & Portfolio Manager, Fixed Income

Fixed income investors generally experienced losses in the third quarter as interest rates in most areas of the globe increased. The FTSE Canada Universe, which represents the broad fixed income market in Canada, fell by 0.97% in the period. Interest rates increased in both Canada and the United States, with the front end of the yield curve rising slightly more than the back end. Both the Bank of Canada and the US Federal Reserve raised rates in the quarter, but the Bank of Canada's hawkish comments after their hike surprised markets given the uncertainty around the future of NAFTA.

Investment grade credit spreads finished the quarter close to where they started, but did spike slightly higher at the beginning of the quarter. Credit spreads have risen over the course of 2018 by approximately 5 bps. Provincial spreads haven't really changed since the beginning of the year and were slightly lower over the course of the quarter. The tightening of provincial spreads can be attributed to a lack of supply as Ontario, one of the major provincial issuers, took a break on issuance while it examined the books of the previous Liberal government. Short dated corporate bonds were the best performing segment of the Canadian market, declining by 0.14% given the lower interest rate sensitivity and higher yields relative to provincial and government bonds. Subsequently, long dated federal government bonds were the worst part of the Canadian bond market as they declined by 2.4%.

The fund was positioned with a short duration view compared to the benchmark index which decreased the portfolio's sensitivity to the upward movement in interest rates. This positioning remained over the course of the quarter as we believe the Bank of Canada will continue to increase overnight rates. The positive duration impact more than offset the unfavorable contribution to relative return by the carry and security selection components of return. Overall the fund outperformed its stated benchmark for the quarter. The fund continued to hold unhedged NZD positions because of the attractive level NZD offers relative to CAD. The defensive positions in corporate credit and provincial bonds were also maintained.

Prospects for significant returns from the fixed income market are expected to be challenging in the near-term given the tightening bias associated with both the Bank of Canada and the Federal Reserve. Additionally, the European Central Bank has hinted at ending its quantitative easing program at the end of 2018 that is expected to also put upward pressure on interest rates.

About Scotia Institutional

Scotia Institutional Asset Management provides progressive and innovative investment solutions to meet the challenges facing institutional clients, including pension funds, non-profits, foundations and corporations.

$127 Billion assets under management*

Fixed Income

The Scotia Institutional Asset Management fixed income team offers a diverse set of fixed income capabilities and solutions, ranging from traditional benchmark-driven to absolute return strategies. We seek to deliver alpha over a full market cycle through the application of a capital preservation philosophy and distinctive investment processes designed to optimize the trade-off between reward and risk.

To complement the skills of our fixed income team, proprietary systems help identify, quantify and manage risks associated with the market. This combination of skills and technologies enables a proactive approach to protecting and growing our clients' capital.

For more information, please contact:

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* As at September 30, 2018. AUM is for 1832 Asset Management L.P., a limited partnership the general partner of which is wholly owned, directly and indirectly, by The Bank of Nova Scotia and is a manager of mutual funds and investment solutions for private clients, institutional clients and managed asset programs.