

# 2018

## INTERIM MANAGEMENT REPORT OF FUND PERFORMANCE

For the period ended June 30, 2018

Offered by Educators Financial Group  
Portfolio Manager: HSBC Global Asset Management (Canada) Limited, Toronto, Ontario

### Educators Mortgage & Income Fund



This interim management report of fund performance contains financial highlights but does not contain either the interim financial report or annual financial statements of the investment fund. You can get a copy of the interim financial report or annual financial statements at your request, and at no cost, by calling 1.800.263.9541, by writing to us at Educators Financial Group, 2225 Sheppard Ave. East, Suite 1105, Toronto, Ontario, M2J 5C2, or by visiting our website at [www.educatorsfinancialgroup.ca](http://www.educatorsfinancialgroup.ca) or SEDAR at [www.sedar.com](http://www.sedar.com).

Securityholders may also contact us using one of these methods to request a copy of the investment fund's proxy voting policies and procedures, proxy voting disclosure record, or quarterly portfolio disclosure.

## MANAGEMENT DISCUSSION OF FUND PERFORMANCE

### Results of Operations

The Fund's net assets decreased by 13.9% to \$161.9 million at the end of June 2018, down from \$188.0 million at the end of December 2017.

#### Investment Performance

For the six-month period ending June 30, 2018 (the 'period'), the Educators Mortgage & Income Fund – Class A Series provided a return of 0.14%, versus the FTSE TMX Canada Short Term Bond Index (the 'Benchmark') return of 0.53%. Investors cannot invest in the Benchmark without incurring fees, expenses and commissions which are not reflected in index returns.

While a number of risks and uncertainties remain, the second quarter saw a rebound in risk assets in most developed markets following the weakness in the first quarter. Despite inflation concerns, ongoing trade disputes and a softening of economic data, U.S. and European equity markets had positive returns in the second quarter, while the Canadian equity market enjoyed its strongest quarter since 2013. The same cannot be said for emerging markets which struggled under the weight of continued U.S. dollar strength and worries over a potential global trade war.

The global growth trend appears to be strong, corporate earnings are solid and inflation, while shorter term upward pressure has been seen, longer term structural inflation remains low. Despite the better market tone however, uncertainty and uneasiness amongst investors can quickly shift towards greater risk aversion and prove challenging for assets such as equities and corporate bonds.

Since 2017, an improving fundamental backdrop has prompted many key central banks to signal that global policy rates would likely to be moving higher in unison following years of aggressive, coordinated monetary stimulus. This shift in policy direction was also witnessed here in Canada, with the Bank of Canada (BoC) raising policy rates three times since July of last year, including once in January. Further rate hikes are expected in the second half of 2018.

Overall, the increasing evidence of a more universal global expansion continues to provide a positive backdrop for equity markets – challenging the outlook for fixed income assets going forward. For global fixed income markets, mixed returns have been seen across

different sectors and terms. The 5-year Government of Canada bond yield, commonly looked at as a proxy for the broad short-term market, rose by 10 basis points (bps) to 2.07% in the second quarter, having ended the first quarter at 1.97% and 2017 at 1.87%.

The yield curve flattened further in the first half of the year, with the difference between 2-year and 10-year Government of Canada bond yields falling 7 bps to 25 bps in the second quarter, after starting 2018 at 37 bps. Overall, short-term Government bond yields increased in the first six months of 2018, rising 16 bps in the second quarter to 2.34% from 2.18% in the first quarter and 2.05% at the end of 2017. This resulted in a return for the overall short-term bond market of 0.53% in the first half of 2018. There were only marginal differences in performance across the various sector of the short-term bond market; with Government of Canada (0.51%), Provincial (0.52%), and Corporate bonds (0.59%) all generating modest positive returns.

Broad posted mortgage rates were higher in the quarter, with the yield on the FTSE/TMX Residential Mortgage Index rising to 4.04% from 3.94% in Q1 and 3.74% at the end of 2017. The yield differential between 5-year fixed mortgage rates and the 5-year Government of Canada bond widened to 327 bps from 317 bps in the first quarter and 312 bps at the end of 2017. Overall, mortgages slightly outperformed short-term government bonds in the first quarter as their higher-running yield offset wider mortgage yield spreads. We believe that mortgage rates still represent an attractive value at current levels. While the yield spread is now slightly tighter than its long-term historical average, the incremental yield advantage is still considerable – given the historically low interest rate environment.

Asset quality in the Canadian residential mortgage market remains very strong. The current average delinquency rate across the country is ~0.25%, essentially unchanged year-to-date and close to the lower end of its long-term range.

The high-running yield of the Fund, compared to the broader market continues to be positive for returns and will help offset some of the negative impacts if bond yields and mortgage rates move higher. The Fund's lower duration, or interest rate risk, had a small positive impact on relative performance, as did the Fund's yield curve positioning. Security selection within corporate bonds was a small contributor to

relative returns, with high-yield and emerging-market debt exposures detracting value.

### Recent Developments

The global growth environment appears to be starting to shift from “synchronized growth” towards greater economic divergence. U.S. growth has outperformed most other developed markets as of late, and has also shown more resilience than growth in emerging markets in recent months. That said, overall global growth appears to be solid, albeit having lost a little momentum in the first half of the year. Despite this softening of cyclical growth, recession risk is low and corporate fundamentals are strong. So for now, we believe the current environment remains constructive for investment returns. However, we remain mindful that the “Goldilocks” scenario of solid growth and low inflation, which markets have enjoyed over the last 2 years, cannot last forever.

In Canada, while the labour market continues to be healthy, uncertainty over U.S. trade policy and the impact of higher borrowing costs on consumers have created some headwinds to growth in the first half of the year. Growth is expected to firm in the second half of 2018 and should remain at, or slightly above, potential (~1.5-2%) next year. The BoC began 2018 with its third rate hike in January and is expected to further tighten monetary policy in the second half of the year.

At this point, with longer-term yields expected to rise modestly over the next year, the objective will be to maintain the Fund’s interest rate exposure at, or slightly below, the benchmark in the near term.

We feel that the corporate sector remains fundamentally sound with stable-to-improving earnings growth and defensively positioned balance sheets. Sector valuations in credit markets improved slightly in the second quarter, but have deteriorated over the previous few quarters. That said, we continue to prefer provincial and corporate bonds to Government of Canada bonds, and will look to remain overweight in these sectors.

Potential risks to our central outlook include disappointing global growth, escalation of global trade disputes, renewed weakness in commodity prices, and heightened geopolitical concerns in the Eurozone.

### Related Party Transactions

Pursuant to the Fund’s investment strategies included in the Fund’s Simplified Prospectus, the Fund may invest in other mutual funds and for the period has invested in HSBC Emerging Markets Debt Fund, Institutional Series; and HSBC Mortgage Fund, Institution Series which are funds managed by the Fund’s Portfolio Manager.

In the first six months of 2018 Educators Financial Group did not refer any conflict of interest matters to the Fund’s Independent Review Committee (IRC) and accordingly did not rely upon any recommendation of the IRC in respect of any related party transactions.

Educators Financial Group is the Manager and Trustee of the Fund. Educators Financial Group is a wholly-owned subsidiary of the Ontario Secondary School Teachers’ Federation (“OSSTF”). OSSTF may from time to time invest in units of the Fund.

### FINANCIAL HIGHLIGHTS

The following tables show selected key financial information about the Fund and are intended to help you understand the Fund’s financial performance for the six-month period and for the past five years. Currently Class I units of the Fund are not being offered to purchase.

#### Educators Mortgage & Income Fund – Class A Series – Net Assets per Unit <sup>(1)</sup>

	Six months ended June 30		Year ended December 31			
	2018	2017	2016	2015	2014	2013
Net Assets, beginning of period	\$11.22	\$11.35	\$11.38	\$11.44	\$11.38	\$11.50
<b>Increase (decrease) from operations:</b>						
Total revenue	\$0.16	\$0.32	\$0.35	\$0.37	\$0.38	\$0.39
Total expenses, including transaction costs [excluding distributions]	(\$0.07)	\$(0.14)	\$(0.14)	\$(0.14)	\$(0.14)	\$(0.14)
Realized gains (losses) for the period	(\$0.08)	\$(0.05)	\$0.04	\$0.00	\$0.03	\$(0.03)
Unrealized gains (losses) for the period	\$0.00	(\$0.10)	(\$0.07)	\$(0.06)	\$0.05	\$(0.09)
<b>Total increase (decrease) from operations <sup>(2)</sup></b>	\$0.01	\$0.03	\$0.18	\$0.17	\$0.32	\$0.13
<b>Distributions:</b>						
From net investment income (excluding dividends)	\$0.10	\$0.17	\$0.21	\$0.23	\$0.25	\$0.25
From dividends	\$--	\$--	\$--	\$--	\$--	\$--
From capital gains	\$--	\$--	\$--	\$--	\$--	\$--
Return of capital	\$--	\$--	\$--	\$--	\$--	\$--
<b>Total Annual Distributions <sup>(3)</sup></b>	\$0.10	\$0.17	\$0.21	\$0.23	\$0.25	\$0.25
<b>Net Assets, end of period</b>	\$11.13	\$11.22	\$11.35	\$11.38	\$11.44	\$11.38

#### Ratios and Supplemental Data (based on Net Asset Value)

	Six months ended June 30		Year ended December 31			
	2018	2017	2016	2015	2014	2013
Total Net Asset Value (000's) <sup>(4)</sup>	\$161,865	\$188,011	\$199,421	\$204,316	\$205,273	\$206,956
Number of units outstanding <sup>(4)</sup>	14,544,154	16,764,263	17,566,363	17,955,859	17,939,038	18,192,370
Management expense ratio <sup>(5)</sup>	1.19%	1.19%	1.19%	1.19%	1.19%	1.20%
Management expense ratio before waivers or absorptions <sup>(6)</sup>	1.24%	1.25%	1.25%	1.25%	1.25%	1.25%
Trading expense ratio <sup>(7)</sup>	--	--	--	--	--	--
Portfolio turnover rate <sup>(8)</sup>	22.42%	37.56%	59.84%	28.07%	27.89%	40.50%
Net Asset Value per unit	\$11.13	\$11.22	\$11.35	\$11.38	\$11.44	\$11.38

- (1) This information is derived from the Fund's interim financial report and audited annual financial statements.  
For the financial year beginning after January 1, 2014, the financial highlights were derived from the Fund's financial statements prepared in accordance with International Financial Reporting Standards ("IFRS").  
For the financial year ended December 31, 2013, the financial highlights numbers were restated to comply with IFRS reporting.  
For financial years beginning before January 1, 2013, the financial highlights were derived from the Fund's financial statements prepared in accordance with Canadian GAAP.  
For financial years beginning after January 1, 2013, all references to "Net Assets" or "Net Assets per Unit" in these financial highlights are references to net assets attributable to holders of redeemable units determined in accordance with IFRS as presented in the financial statements of the Fund.
- (2) Net assets and distributions are based on the actual number of units outstanding at the relevant time. The increase/decrease from operations is based on the weighted average number of units outstanding over the financial period. This table is not intended to be a reconciliation of beginning to ending net assets per unit.
- (3) Distributions were either paid in cash or reinvested in additional units of the Fund.
- (4) This information is provided as at June 30 or December 31 of the year shown.
- (5) Management expense ratio is based on total expenses (excluding [distributions], commissions and other portfolio transaction costs) for the stated period and is expressed as an annualized percentage of daily average net asset value during the period.
- (6) The management expense ratio before waivers or absorptions shows what the management expense ratio of the Fund would have been if Educators Financial Group had not charged a lesser amount for its management fee.
- (7) The trading expense ratio represents total commissions and other portfolio transaction costs expressed as an annualized percentage of daily average net asset value during the period.
- (8) The Fund's portfolio turnover rate indicates how actively the Fund's portfolio manager manages its portfolio investments. A portfolio turnover rate of 100% is equivalent to the Fund buying and selling all of the securities in its portfolio once in the course of the year. The higher a fund's portfolio turnover rates in a year, the greater the trading costs payable by the fund in the year, and the greater the chance of an investor receiving taxable capital gains in the year. There is not necessarily a relationship between a high turnover rate and the performance of a fund.

### Management Fees

Educators Financial Group is the Manager-Trustee, promoter and principal distributor of the Fund, and is responsible for the day-to-day management and administration of the Fund.

The Manager-Trustee monitors and evaluates the performance of the Fund, and pays for the investment management services of the portfolio manager, as well as all administrative services required by the Fund. As compensation for these services, Educators Financial Group is entitled to receive a fee, payable monthly and calculated daily, based on the Net Asset Value of the Fund, at the annual rate of 1.10% for the Class A Series. The Class I Series is identical in all respects to the Class A Series, except that there is no management fee payable by the Fund in respect of the Class I units.

The Fund is responsible for paying any applicable tax owing on its management fee.

Approximately 11.1% of the total management fees collected were used to pay for portfolio management services, with the remainder of the fees allocated to custodial services, marketing, technology and Manager-Trustee operating expenses.

## PAST PERFORMANCE

### General

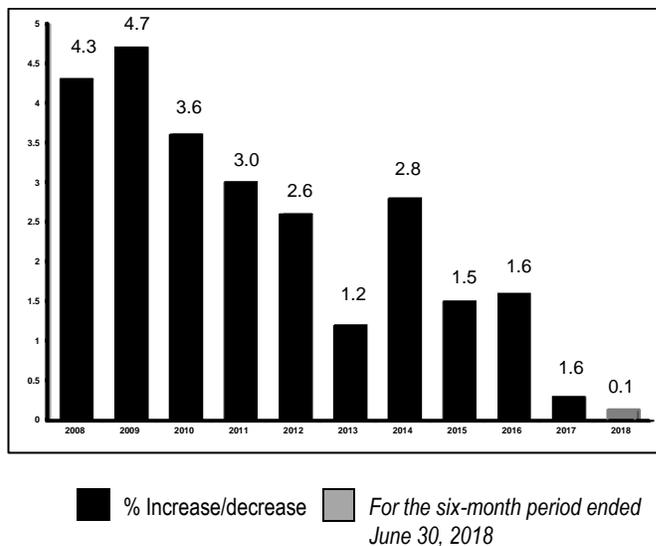
The Fund's performance information shown assumes that all distributions made by the Fund in the periods shown were reinvested in additional units of the Fund.

The performance information does not take into account sales, redemption, distribution or other optional charges that would have reduced returns or performance. The performance of different fund series may vary for a number of reasons, including differences in management fees and expenses. Please remember that how the Fund has performed in the past does not necessarily indicate how it will perform in the future.

### Year-by-Year Returns

The bar chart shows the Fund's performance for each of its past 10 financial years and illustrates how the Fund's performance has changed for the 6-month period ended June 30, 2018 and for each 12-month period ending December 31. The chart shows, in percentage terms, how much an investment made on the first day of each financial period would have grown or decreased by the last day of each financial period.

Annual Returns – Class A Series



Annual Returns – Class I Series

Currently Class I units of the Fund are not being offered to purchase.

**SUMMARY OF INVESTMENT PORTFOLIO**  
**(Based on Net Asset Value)**

As at June 30, 2018

Sector Mix	Percentage of Net Asset Value
Canadian Mutual Funds	51.95%
Corporate Bonds	34.22%
Government Bonds	7.07%
Asset-Backed Securities	6.13%
Cash and Cash Equivalents	0.55%
Net Other Assets	0.08%

**Top 25 Holdings**

Security Name	Percentage of Net Asset Value
HSBC Mortgage Fund, Institutional Series	49.84%
Canada Housing Trust No. 1, 2.35%, June 15, 2027	3.63%
Canadian Government Real Return Bond, 6.82%, December 1, 2021	2.25%
HSBC Emerging Markets Debt Fund, Institutional Series	2.11%
Aviva PLC, 4.50%, May 10, 2021	1.36%
TMX Group Ltd., 4.46%, October 3, 2023	1.29%
Citigroup Inc., 3.39%, November 18, 2021	1.26%
Bank of Nova Scotia, 2.29%, June 28, 2024	1.19%
Real Estate Asset Liquidity Trust, 2.56%, October 12, 2049	1.15%
Saputo Inc., 2.83%, November 21, 2023	1.10%
Royal Bank of Canada, 3.31%, January 20, 2026	1.08%
Goldman Sachs Group Inc., 2.43%, April 26, 2023	1.05%
Suncor Energy Inc., 3.10%, November 26, 2021	1.00%
Institutional Mortgage Securities Canada Inc., 1.94%, Sept. 12, 2024	1.00%
Canadian Imperial Bank of Commerce, 1.64%, July 12, 2021	0.99%
BP Capital Markets PLC, 3.50%, November 9, 2020	0.95%
Bank of Montreal, 2.70%, September 11, 2024	0.93%
Anheuser-Busch InBev Finance Inc., 2.60%, May 15, 2024	0.91%
Canadian Natural Resources Ltd., 3.31%, February 11, 2022	0.87%
Canadian Western Bank, 2.74%, June 16, 2022	0.83%
Alimentation Couche-Tard Inc., 3.90%, November 1, 2022	0.83%
AT&T Inc., 3.83%, November 25, 2020	0.82%
Granite REIT Holdings LP, 3.87%, November 30, 2023	0.82%
Intact Financial Corp., 4.70%, August 18, 2021	0.82%
MCAP RMBS Issuer Corp., 2.17%, April 15, 2019	0.76%
<b>Total Net Assets (000's)</b>	<b>\$161,865</b>

The top 25 holdings represent approximately 78.84% of the total net assets of the Fund.

The summary of investment portfolio of the Fund is as at June 30, 2018 and may change due to the Fund's ongoing portfolio transactions. Updates are available quarterly. Information about the holdings of the HSBC Funds owned by the Fund is contained in their simplified prospectus, annual information form and fund facts documents available on SEDAR at [www.sedar.com](http://www.sedar.com).

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