INVESTMENT
FUNDS

BOND

MONTHLY COMMENTARY

February 28, 2022

Market and Portfolio Update

February extended the pronounced volatility plaguing the markets, which has been the main theme thus far in 2022 as investors grapple with contrasting undercurrents of persistent inflation and accommodative monetary policy reductions versus a flight to safety precipitated by the crisis in Ukraine. Ongoing price swings meant 10-year Canada yields tacked on just over 20 basis points in the first half of February, periodically eclipsing 2.00%, only to see levels slide back in the second half to finish out around where they started near 1.80%. In fact, building concern about the conflict in Ukraine initially shaved off another 10 basis points at the beginning of March, sending the 10-year yield below 1.70% for a spell. The story was similar in the U.S., where 10-year treasuries retraced initial pressure on yields, which temporarily pierced 2.05%, only to end the month just above 1.80%.

Posturing by the central banks on both sides of the border in early February had investors pricing in the chance of a 50-basis-point move to commence their latest respective hiking cycles; but the language from policy makers eventually toned down once the severity of conditions in Ukraine started to grip the global capital markets. Inflation was very much the early story in February, with prints above 7% and 5% in the U.S. and Canada respectively, providing much fodder for growing chatter about the need to act aggressively to tame prices as soon as possible. Strong employment numbers in both countries during the month only added to mounting fears of runaway inflation. Yet, it was not until WTI surpassed US$100 per barrel due to the conflict in Ukraine that the reality of the difficult road ahead for policy makers became all too apparent. With WTI now over US$110 per barrel and prices at the gas pumps screaming to uncomfortably high levels, the need to protect consumers is increasingly at odds with efforts to isolate Russia from the global economy, especially as many companies rush to either shutter production in the country and/or stop selling goods and services there altogether.

The consequences of the shifting tenor in the markets certainly underpinned the aforementioned volatility. From VIX to yields, investors were demonstrating their escalating confusion about what direction the markets should head. Intra-day yield gyrations of 10 basis points or more across all parts of the yield curve in Canada and the U.S. became common place, while the equity markets experienced their own swings. And while yields were on the move, they completely reshaped the curve, with 2s-10s in the U.S. slumping from 60 basis points to 40 basis points during February, dragged down by bouts of both bull and bear flattening. Meanwhile in Canada, 2s-10s shaved off 10 basis points to 40 basis points but slunk down below 30 basis points in the early days of March.

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As was widely expected, the Bank of Canada increased policy rates by 25 basis points to 50 basis points early in March but, as previously mentioned, there was speculation in the first half of February that the move could have been 50 basis points. Regardless, the total return for the FTSE TMX Canada Universe Bond Index suffered another loss in February, with the composite losing 72 basis points and bringing the year to date damage to -4.10%. The bulk of the pain was felt in the long end, which lost -1.66% in February and a stunning -8.41% so far in 2022. Corporates were particularly hard hit in February as a persistent shift towards risk off in credit markets widened spreads by 14 basis points in the month and by 25 basis points year-to-date. Consequently, the total return for All Corporates was the worst monthly performer in the index, losing -1.04% in February and almost 4% thus far in 2022. Provincial credits similarly suffered aversion by investors in February, but nowhere near the extent of corporates, moving out by just 6 basis points, with their total return ringing in at a loss of -0.87%.

We expect volatility in the markets to remain elevated for the foreseeable future as the world digests the ongoing crisis in Ukraine and contemplates the fallout on world commodity prices, and hence inflation. The central banks are definitely in a tough spot, attempting to control rising prices while at the same time having to be wary of the potential negative impact on global growth, which has just become exacerbated by further global supply disruptions in the wake of the geopolitical tensions in Europe.

Our overall view remains biased towards shorter duration given the re-emerging backdrop of higher rates going forward after the initial shock of the Russian invasion of Ukraine was digested by the markets. At present, we believe much of the upward pressure on yields has been priced but expect levels to drift higher once again as the growing specter of inflation percolates. At the same time, we will remain nimble to take advantage of anticipated ongoing volatility as the markets continue to figure out a new narrative while mounting geopolitical risks persists.

We keep our overweight posture towards corporate credits as a softer spread environment presents opportunity to selectively pick away at that asset class.

ALEXANDRE MORIN, CFA

— Principal Portfolio Manager
— Joined iAIM in 2015
— More than 20 years of investment experience
— Bachelor's degree in Business Administration, Université Laval

Main funds managed by the team

✓	Money Market
✓	Short Term Bond
✓	Bond
✓	IA Clarington Bond Fund
✓	IA Clarington Money Market Fund
✓	IA Clarington Real Return Bond Fund

iAIM snapshot

— Principal asset manager for iA Financial Group
— Major player in the asset management industry
— Manages $97 billion in general portfolios and segregated and mutual funds
— A team of 184 people, including 108 investment professionals (including 44 CFA charterholders)
— Composed of experienced managers who emphasize fundamental analysis, identification of value and long-term investing

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