INVESTMENT FUNDS

BOND

MONTHLY COMMENTARY

April 2022

After a brief respite in March, the tone in the capital markets resumed its dour posture during April as investors were buffeted by a growing array of concerns, ranging from inflation, to recession, geopolitics, stagflation, supply chain disruptions and all points in between. At a broader level, the principal focus seemed bookended by trepidation central bankers had not acted fast enough to tame inflation and that they will do too much and mistakenly engineer a recession. And while risk assets sold off sharply in April as a result, bond yields continued their march ever higher as 10-year Canada bonds tacked on another 45 basis points or so to exit April just above 2.85%. In the US, the damage suffered by bonds was a little more acute, with 10-year Treasuries adding on nearly 60 basis points to reach 2.93% by the time April was over, punctuating what has been one of the worst starts to a year for bonds in over a generation or two. Notwithstanding the overall escalation in yields during April, the curve did recover modestly after plunging in March to flat or inversion in many segments, which prompted considerable fears that a recession was in the offing. In Canada, the 2s-30s curve elevated from 9 basis points at the start of April to end at around 17 basis points. By comparison, the US saw its 2s-30s curve begin the month flat only to see it increase by almost 30 basis points.

Underscoring the weakness in bonds was ongoing volatility in the capital markets overall, particularly as April wore on and the reception for risk sentiment abated. As has been characteristic for much of 2022, daily moves of 10 basis points or more in all areas of the yield curve remained commonplace, leaving traders and investors alike reluctant to leave positions open overnight for fear they would awaken to an entirely different market ethos that would render stop losses as a mere recipe for crystallizing losses. In essence, investors have seemingly become anesthetized to rampant volatility percolating in the markets, essentially accepting it as part and parcel of figuring out a new direction forward, regardless of its fundamental contribution to catalyzing material year-to-date losses for most asset classes.

Not helping matters for bonds in April were musings from central bank officials south of the border about possible 75 basis point rate hikes in order to get a handle on inflation, as well as a potentially accelerated timeframe for quantitative tightening. And, of course, feeding into the posturing around more aggressive actions by central banks on both sides of the border were eyepopping March inflation reads of 8.5% in the US (the highest since 1981) and 6.7% in Canada (the highest since 1991). Ostensibly these throwback inflation numbers had sell-side analysts pulling out their Sony Walkmans and Atari 2600s, calling for policy prescriptions and market forecasts from a bygone era, trying to outdo each other with more and more outlandish predictions for everything from terminal rates, to inflation, to the size of policy rate increases. Yet, when the BoC did raise rates in the middle of April, they moved by 50 basis points and reaffirmed policy rates were its main communicative mechanism for the markets, with quantitative tightening to be used as a complement, not a driver. The US Fed similarly chose to increase rates by 50 basis points at the beginning of May, with quantitative tightening also seen to be a complementary feature. Both moves, while indicating a measured approach by central banks on both sides of the border, failed to fully rein in market fears about how aggressive policy-makers will have to become as investors await meaningful signs that inflation has started to ebb. And even at that, there is much debate over how persistent higher inflation will be even if it has peaked.

With worries about inflation, rates and a possible recession taking centre stage in April, the total returns for bonds once again suffered a dismal performance. The FTSE Canada Universe Bond Index lost-3.49% during April 2022, bringing the year-to-date loss to a staggering-10.22%. The Federal component of the index lost-2.52% (-7.93% YTD), while Broad All Corporates were down-3.20% (-9.44% YTD) as spreads widened by 16 basis points. As has been the case all year, we expect volatility in the global capital markets to persist for the foreseeable, with bonds to be no exception. Investors remain focused on inflation and recession worries, with elevated geopolitical turmoil and its attendant impact on commodity prices poised to take centre stage at any moment. We continue to believe central bankers remain in a tough spot, endeavouring to tackle inflation without being able to directly address some of its root causes, like geopolitical conflict and ongoing supply chain issues.

Our overall view is now biased towards being closer to home in our duration management given the historic pace at which bond yields increased since the beginning of the year. We think bond yields will not continue to increase at that brisk pace much longer since game plans from the FED and the BoC (O/N rate and reduction in bond holdings) are known now. At the same time, we will remain nimble to take advantage of anticipated ongoing volatility as the markets continue to figure out which yield levels will be enough to bring back buyers. We are more cautious towards corporates in the current environment as ongoing inflation and likely slowing economic activity begin to eat away at profits and start to adversely impact credit profiles.

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— 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

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— 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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