RBC Global Asset Management

RBC Core Bond Pool

Commentary as at December 31, 2022

In January 2022, interest rates were near record lows and monetary stimulus was unprecedented, helping to lift U.S. stocks to record levels as much of the Western world tried to move on from the pandemic. But Russia's invasion of Ukraine in February helped propel rapidly rising inflation to its highest level in four decades. The response to inflation – a rapid rise in global interest rates – led to the worst year for a U.S. balanced portfolio since 1937 and marked the first time since at least 1872 that both U.S. stocks and U.S. bonds had double-digit declines. Meanwhile, Chinese President Xi's appointment to an unprecedented third term made him the country's most powerful political leader since the 1970s, amplifying geopolitical tensions.

Canadian government bonds posted the worst returns since 1980, as central banks in North America and Europe aggressively raised short-term interest rates to fight inflation running at its highest level since the 1980s. In 2022 alone, the Bank of Canada (the "BOC") and the U.S. Federal Reserve (the "Fed") raised short-term interest rates seven times, lifting the BOC's benchmark rate to 4.25% from 0.25% and the Fed's to a range of 4.25% to 4.50% from near zero.

To stem inflation, the central banks ended bond purchases that had helped to hold down longer-term interest rates and started selling bonds. By year-end, economic growth and inflation showed signs of falling, although both central banks indicated that interest rates would keep rising until inflation was clearly weakening. Yields on short-maturity bonds surged more than those on long-maturity securities, reflecting expectations that higher rates would hinder economic growth. Government of Canada bonds outperformed their U.S. counterparts, driven by investors' views that the BOC would end rate hikes earlier.

The Fund's returns were negatively affected by holdings in the RBC Global Corporate Bond Fund, the RBC Global Bond Fund and the RBC Bond Fund.

The portfolio manager expects the 2022 rate hikes to start holding back economic growth significantly in 2023, raising the likelihood that Canada, the U.S. and Europe will fall into recession. A recession marked by rising unemployment would relieve pressure on central bankers to continue hiking interest rates and would indicate, at a minimum, that an end to the tightening cycle is coming. The portfolio manager stands ready to accumulate attractively priced assets in the event of further declines in bond prices.