

RBC \$U.S. Core Bond Pool



Commentary as at December 31, 2023

Economic growth in 2023 was faster than many economists had predicted at the beginning of the year, defying risks that included inflation exceeding central-bank targets, the highest borrowing costs in about 16 years and two wars on Europe's doorstep. By the end of the period, growth and inflation had begun to slow, prompting investors to anticipate that central banks were moving closer to rolling back a portion of the rate hikes that had taken place since early 2022.

The U.S. Federal Reserve (the "Fed") raised short-term benchmark interest rates in smaller increments than it had in 2022 – a total of four to a range of 5.25% to 5.50%. The European Central Bank delivered six rate hikes, putting the policy rate at 4.5% to head off inflation, even as its largest economy, Germany, descended into a recession. Corporate bonds, emerging-market debt and other forms of fixed income perceived to carry higher risks performed particularly well given that the global economy avoided a recession and corporate profitability remained strong.

The Fund's returns were aided by holdings in the BlueBay \$U.S. Global Investment Grade Corporate Bond Fund (Canada), the RBC \$U.S. Global Bond Fund and the RBC \$U.S. High Yield Bond Fund.

Consumer spending, business investment and global trade are starting to feel the pinch of higher interest rates and may deteriorate further. As a result, the portfolio manager expects most major central banks to start easing policy rates in 2024, although by the end of 2023, the Fed was the only major central bank to have hinted at easing. In such an environment, the portfolio manager is favouring assets that would gain if interest rates extend their declines.

The year-end drop in yields suggests we may have seen the peak in interest rates for now. The portfolio manager believes that valuations of riskier corporate bonds may be stretched, making investing in these bonds less attractive in view of the potential for economic weakness over the coming year.

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