RBC Monthly Income Fund

Commentary as at December 31, 2022

Canadian and U.S. stocks tumbled in 2022, fueled by the highest inflation in decades and the concurrent rise in interest rates. Stocks came under pressure after the U.S. Federal Reserve (the "Fed") and the Bank of Canada (the "BOC") responded to inflation – the fastest in 40 years – with a vow to stamp it out with successive interest-rate hikes. Interest-rate-sensitive stocks were hurt most, resulting in a sell-off in the Information Technology sector in both markets. Meanwhile, a surge in energy prices helped cushion market returns in Canada, which outperformed most other major markets during the year.

Canadian government bonds posted the worst returns since 1980, as central banks in North America and Europe aggressively raised short-term interest rates. In 2022 alone, the BOC and 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.

In the equity portion of the Fund, relative exposure to Brookfield Asset Management, PrairieSky Royalty and Algonquin Power & Utilities had the most positive impact on the Fund's returns, while exposure to Brookfield Corp., Cenovus Energy and Onex was negative for performance.

The sectors that had the most positive impact on the Fund's returns were Energy, Materials and Consumer Discretionary, while exposure to Financials, Real Estate and Industrials had a negative impact.

In the fixed-income segment of the Fund, overweight positions in longer-term provincial bonds and non-government debt negatively affected relative returns. However, this weakness gave the portfolio manager the opportunity to add corporate and emerging-market fixed-income securities at more attractive yields.

Uncertainty is elevated and there is a wide range of potential outcomes for the economy and financial markets. The good news for investors is that stocks are now much more reasonably priced than they were at the start of the year.

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.

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