

RBC Canadian Bond Index Fund



Commentary as at December 31, 2020

Government bonds in major developed markets recorded above-average returns in 2020, as fears of a pandemic-driven global economic recession prompted major central banks to support financial markets via drastic rate cuts and unprecedented monetary stimulus. Stocks and corporate-bond prices had plummeted in March and government-bond yields touched historic lows. Only the extraordinary stimulus measures, both monetary and fiscal, led to a rebound in riskier assets and reversed some of the first-quarter gains for government bonds.

By the end of the year, the Bank of Canada (the “BOC”) had shelved many of its market-calming measures as macroeconomic stability continued to improve, and bond purchases were scaled back. The U.S. Federal Reserve followed a similarly generous monetary policy of asset purchases and promises to keep interest rates low until the economy was back on track. While approvals of COVID-19 vaccines late in the period and specter of additional fiscal stimulus lifted bond yields slightly, major central banks will likely be successful at keeping them from rising too much for some time. The BOC, for example, said it did not anticipate raising its short-term benchmark rate before 2023, based on the bank’s current economic forecast.

The portfolio manager expects that major central banks will hold interest rates steady for at least the next 12 months on concern that the recovery in labour markets will likely stretch over several years and involve only a gradual removal of monetary stimulus. In the near term, the rise in COVID-19 cases and related business restrictions are slowing the economic recovery and holding down bond yields. Over the next year, the portfolio manager anticipates that the economic recovery will likely lead to only modestly higher bond yields.

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