INVESTMENT FUNDS

BOND

MONTHLY COMMENTARY

July 31, 2021

Bond yields continued their slide in July. The 10-year Canada bond yield started the month at about 1.40% and finished 20 basis points lower. It is not clear why rates declined like they did recently. Usually, summertime is a period in which the bond market lacks its usual liquidity and that brings periods of higher volatility. Also, most people involved in the bond market try to explain the recent decline by a positioning bias. It is true that people are managing the risk in their portfolios by reducing their exposure to some crowded trades such as curve steepening and short-duration bias but there are also fundamental reasons for the recent dynamic in the bond market.

The recent rates rally followed the Federal Reserve's June 16 meeting, where some members of the FOMC Committee signalled the possibility that overnight rate increases may happen sooner rather than later. That happened at a time when the stock market is near all-time highs and optimism is running high in the markets, potentially triggering some shifts in asset allocation in diversified funds.

There is also growing concern about new variants of COVID-19 (Delta, Lambda). When everybody was hoping for a "normal" summer, the resurgence of cases around the world is leading some countries to return with restrictive measures that, of course, are making headlines in the media.

Outside of our continent, the market is also concerned about the global effects of China's macro-prudential measures to control borrowing and commodity speculation. Interestingly, the People's Bank of China (PBOC) reduced its reserve requirement ratio by 50 basis points last month to free up more liquidity in the financial system. Also, markets are nervously watching Beijing's actions against tech companies and wonder when it is going to stop.

Economic data shows that consumers are spending their money and their confidence is historically high. The media has even reported that some workers now prefer to leave their current jobs rather than physically return to work- they would rather find another job that allows them to work remotely. Such a high "quit rate" is generally associated with a healthy economy. Employment numbers will be scrutinized in the coming months as Federal Reserve Chairman Powell mentioned that he wants to see strong payroll numbers before starting the process of bond purchases tapering. Also, businesses have continued to face bottlenecks with low inventories and high order backlogs. As the economy reopens, this should allow for better growth with an acceleration of industrial production to replenish inventories.

In conclusion, we are maintaining our lower duration bias, as we believe we will see higher rates by the end of 2021 and that strong economic data are not over yet. At the present level, bond yields look expensive to us.

We still see corporate credits as an attractive overweight holding in our portfolios, as they offer good carry considering the low level of bond yield. However, corporate credit spreads tightened strongly last year and in the first quarter of 2021, leaving little to no room for further tightening. We still like this market, but the risks are more balanced than they were. We have a bias to own securities in the short and mid part of the corporate bond curve. We also own some ETFs that provide us with an exposure to corporate securities denominated in U.S. dollars combined with a small interest rate risk.

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ALEXANDRE MORIN, CFA

- 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

iAIM snapshot

- Principal asset manager for iA Financial Group
- 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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