Monthly Fixed Income Update

Hank Cunningham

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Interest Rate Summary	30-Nov-17	30-Dec-16	31-Dec-15	31-Dec-14	31-Dec-13	31-Dec-12
U.S.						
3-Month T-Bill	1.26%	0.50%	0.16%	0.04%	0.07%	0.04%
2-Year Treasury	1.78%	1.19%	1.31%	0.47%	0.38%	0.25%
10-Year Treasury	2.42%	2.44%	2.27%	2.17%	3.03%	1.76%
Canada						
3-Month T-Bill	0.87%	0.45%	0.51%	0.90%	0.92%	0.92%
2-Year Canada	1.43%	0.74%	0.48%	0.99%	1.14%	1.14%
10-Year Canada	1.89%	1.72%	1.39%	1.86%	2.76%	1.80%

Performance

	Nov-2017	Year-to-Date	2016	2015	2014	2013	2012
DEX Universe Bond Index	0.79%	2.94%	3.52%	3.52%	8.79%	-1.19%	2.65%
DEX Federal Bond Index	0.43%	0.76%	3.66%	3.66%	6.91%	-1.52%	2.11%
DEX Provincial Bond Index	1.24%	4.56%	4.14%	4.14%	12.18%	-2.70%	
DEX All Corporate Index	0.68%	3.76%	2.71%	2.71%	7.58%	0.84%	6.22%
DEX "A" Corporate Index	0.78%	4.78%	2.62%	2.62%	9.10%	-0.16%	6.85%
DEX Real Return Bonds	1.37%	0.60%	2.79%	2.79%	13.18%	-13.1%	
DEX High Yield Bonds	0.69%	9.28%					

Comments:

Performance was positive in all sectors of the bond market in November with provincial bonds leading the way. The provincial index has a longer duration than the other indices and thus benefited from the yield curve flattening.

While U.S. yields rose in November, Canadian yields fell for the second straight month and Canadian bonds outperformed their U.S. counterparts. The yield curves in both countries flattened further; this meant that longer-dated bonds outperformed short- and mid-term bonds.

	U.S.	Canada	Net Difference
Three month Treasury Bills	+16 basis points	-2 basis points	-39 basis points
Two-year bond yields	+20 basis points	+3 basis points	-35 basis points
Ten-year bond yields	+4 basis points	-7 basis points	-53 basis points

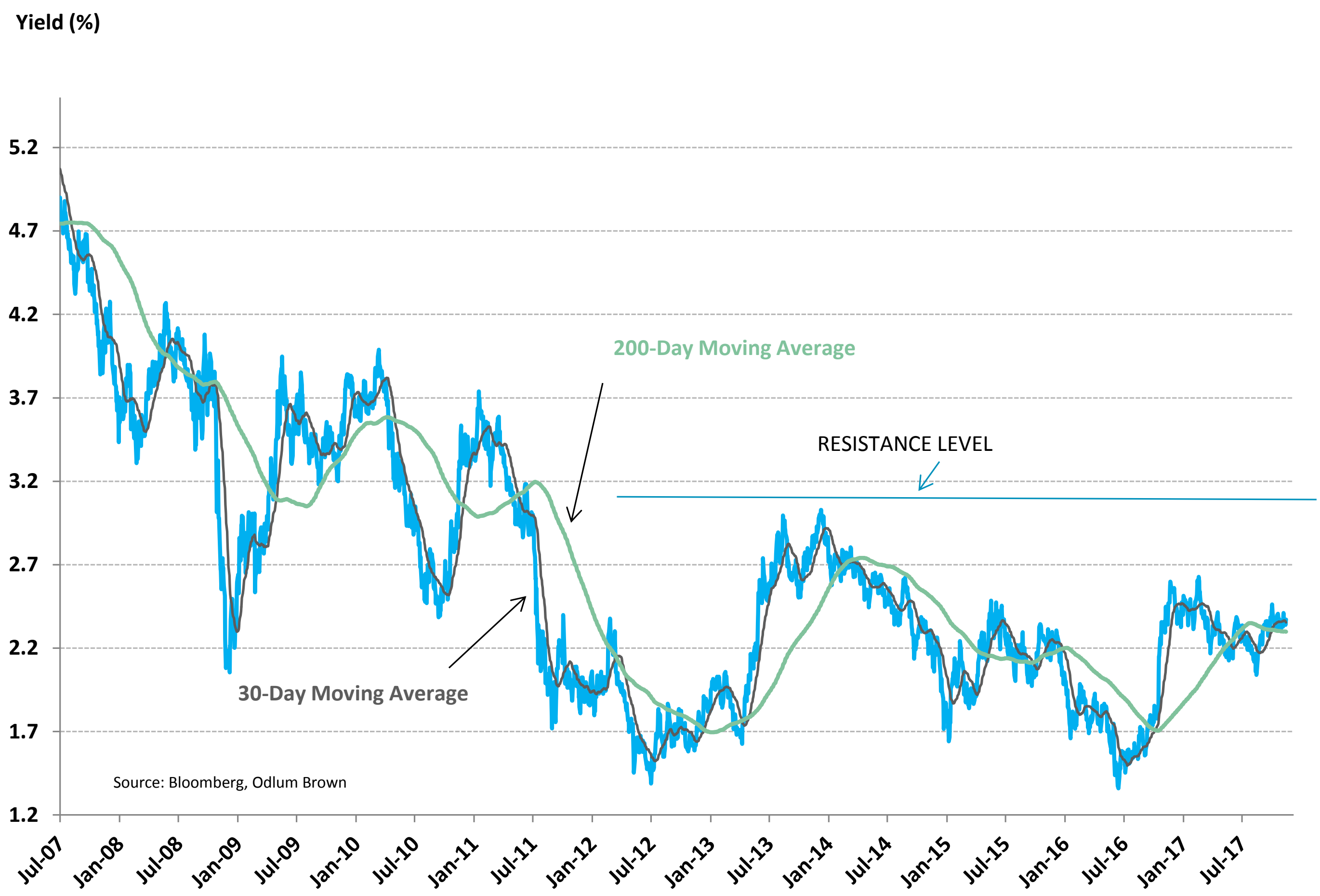
November's bond market action was dominated by the political arena and the constant back and forth on the proposed tax bill and the consequences for the economy, inflation and bond yields. The bellwether U.S. ten-year note rose a net four basis points while trading in a tight range. Two-year yields rose by twenty basis points, flattening the yield curve further.

The global economic picture brightened further with the OECD now forecasting GDP at 3.6% for the next twelve months.

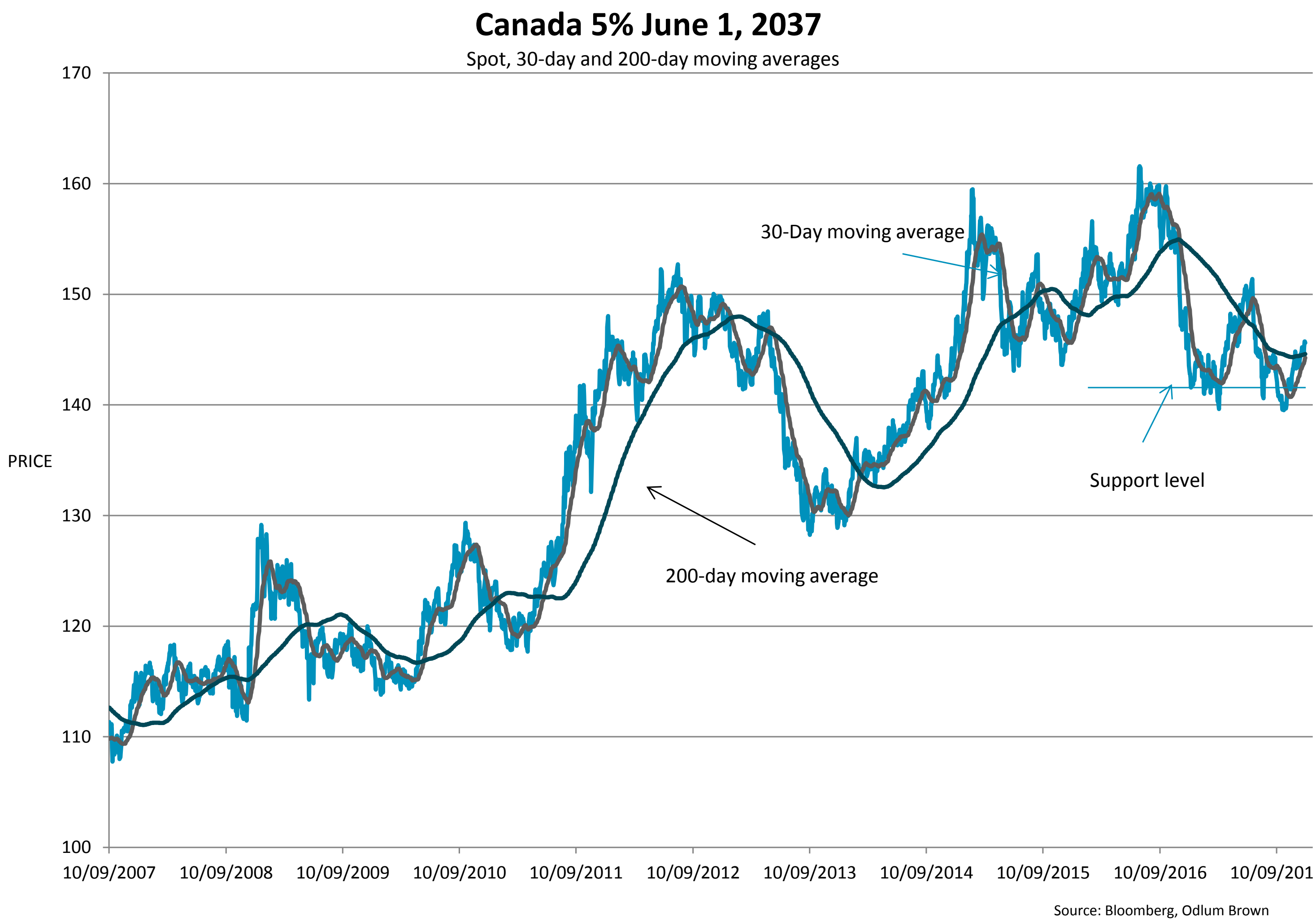
Inflation has begun to creep higher. In the U.S., most economic releases beat estimates consistently, including the important industrial production, housing and retail numbers. The Fed's Beige Book, which reports economic conditions in various regions of the U.S., reported growing price pressures and more passing through of costs. Despite this evidence, bond yields barely moved. The principal reason for this is the ongoing aggressive stimulus by the ECB and the Bank of Japan. Their actions continue to suppress bond yields, making the U.S. bond market relatively attractive.

As for Canada, while third quarter growth slowed as a result of weak retail sales and poor exports, growth remains positive, as witness is the blowout employment report. This was not enough for the Bank of Canada to move its Bank Rate up but the Bank did caution that higher rates were likely next year. The Canadian dollar improved modestly for the month, partly as a result of firmer oil prices.

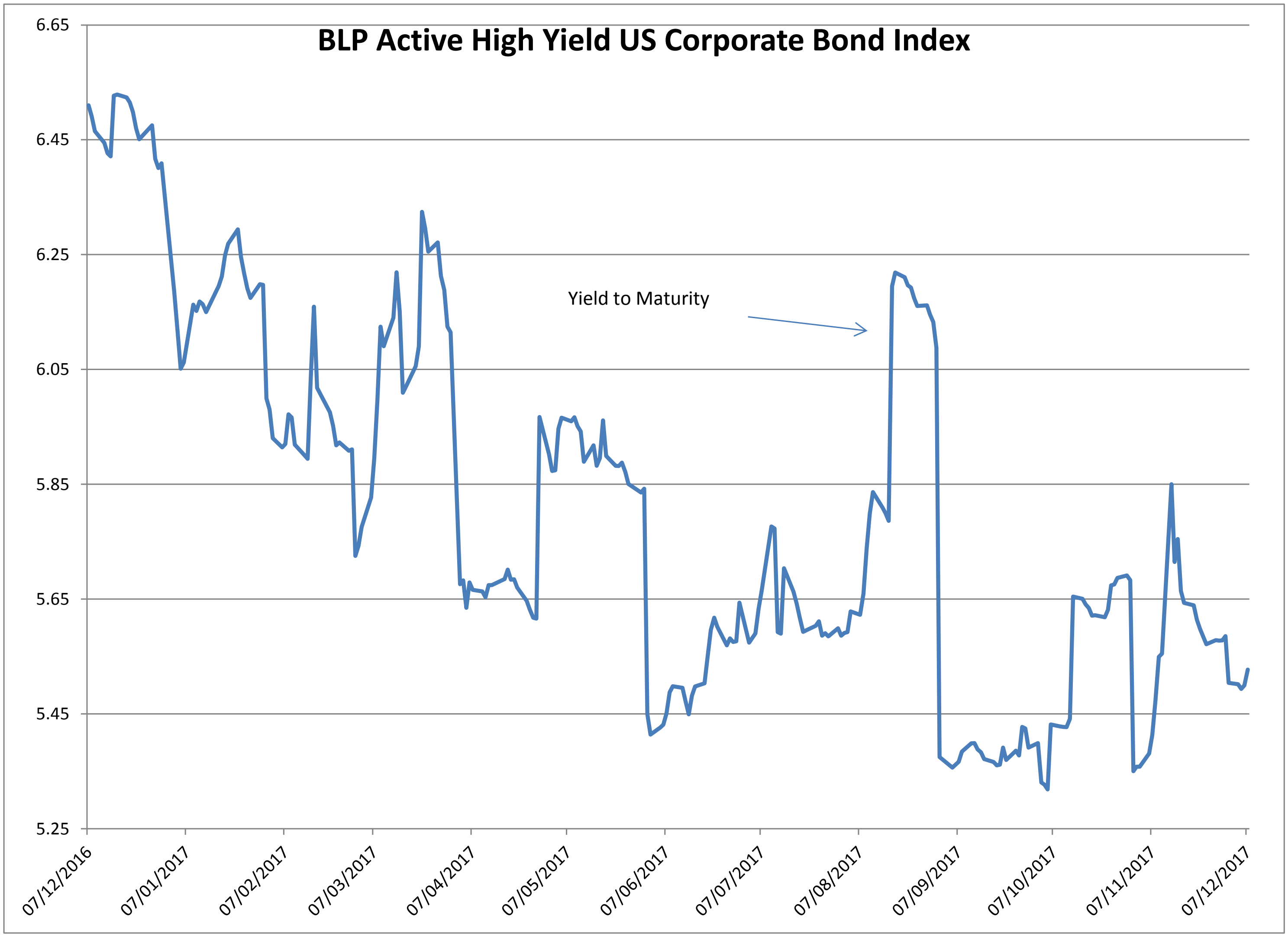
U.S. 10-Year Treasury



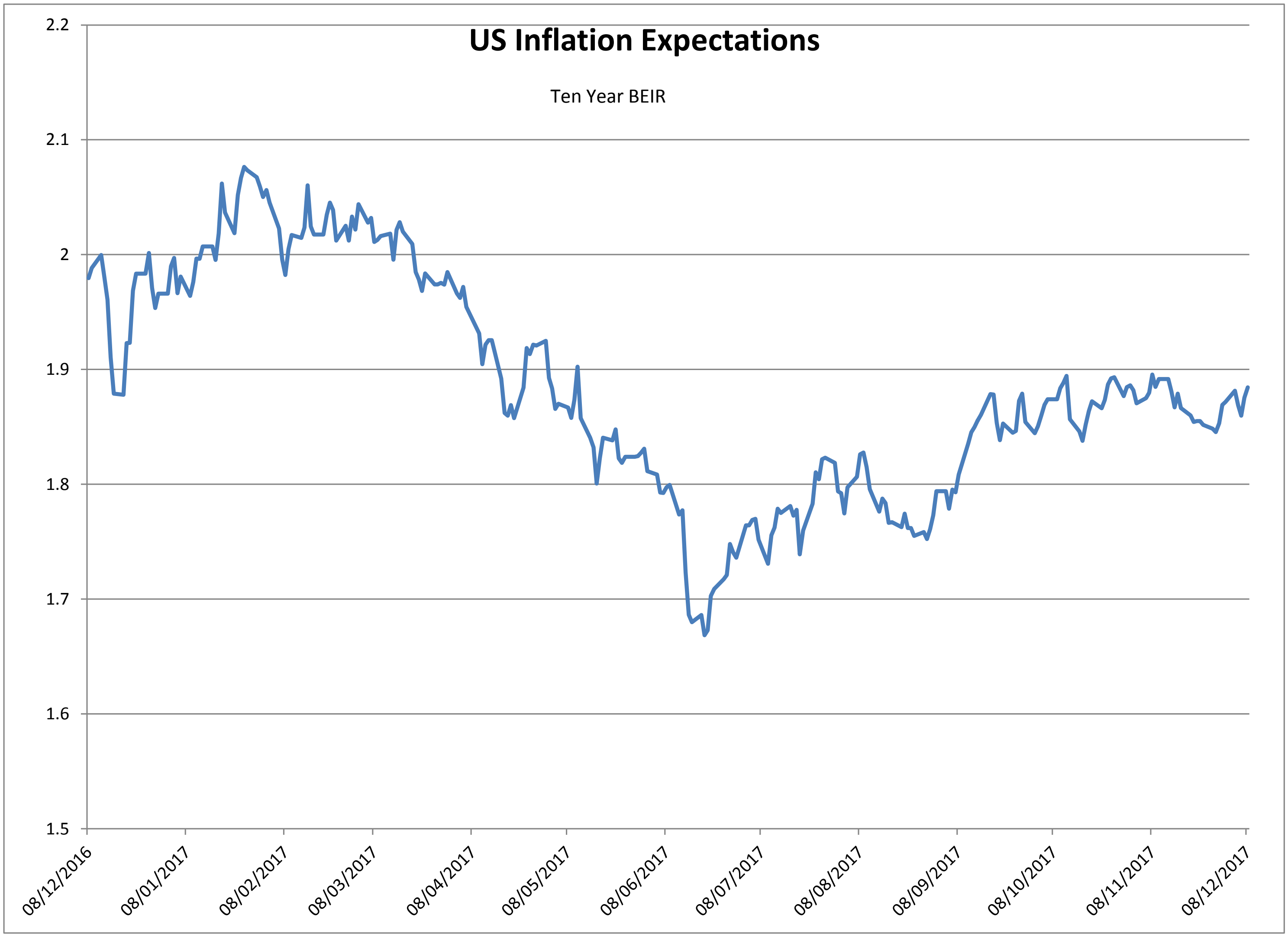
This bond approached, but did not break above 2.50%. It continues to be locked in a narrow trading range with an upward yield bias.



The price of this long-term Canada bond has rallied sharply and has moved above its 200-day moving average.



The high-yield bond market experienced a sharp selloff in early November but has recouped some of its losses.



This chart displays the trend in inflation expectations. As is evident, expectations are rising gradually but are still below where they were a year ago.

Outlook

There is little change in the outlook for debt markets. The Fed will likely raise the Fed Funds Rate next week in Governor Yellen's last FOMC meeting. At this stage, no one expects incoming Governor Powell to rock the boat but he will wish to put his own stamp on Fed policy. U.S. bond yields should continue to grind slowly higher. With the massive gap between Euro and Japanese bond yields, U.S. bonds offer attractive relative yields. With no change likely in the monetary stimulus being carried out by the ECB and the Bank of Japan, it is difficult to forecast anything other than the continuation of the narrow trading range for U.S. bonds. While the ten-year bond is thirty-five basis points higher than its low for the year, it is still ten basis points lower than at year end 2016.

After the Canadian economy cooled during the third quarter, the Bank of Canada struck a more cautious stance and will not likely raise the Bank Rate until late in the first quarter of 2018. Corporate bond spreads will remain tight and, while high yield bonds are also at historically low spreads from government bonds, they remain well bid.

Strategy

There is no reason to alter our stance of maintaining high-quality, laddered corporate portfolios with a short duration. For those investors with the appropriate risk profile, high yield bonds deserve a presence in fixed income portfolios. Continued investment in corporate bonds will result in positive, albeit small, returns.