Monthly Fixed Income Update

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December 10, 2019

Interest Rate Summary	Nov-29-19	Dec-31-18	29-Dec-17	30-Dec-16	31-Dec-15	31-Dec-14	31-Dec-13
U.S.							
3-Month T-Bill	1.58%	2.36%	1.38%	0.50%	0.16%	0.04%	0.07%
2-Year Treasury	1.53%	2.49%	1.89%	1.19%	1.31%	0.47%	0.38%
10-Year Treasury	1.78%	2.69%	2.41%	2.44%	2.27%	2.17%	3.03%
Canada							
3-Month T-Bill	1.65%	1.64%	1.05%	0.45%	0.51%	0.90%	0.92%
2-Year Canada	1.58%	1.86%	1.69%	0.74%	0.48%	0.99%	1.14%
10-Year Canada	1.46%	1.97%	2.04%	1.72%	1.39%	1.86%	2.76%

Performance

	2019 YTD	2018	2017	2016	2015	2014	2013
DEX Universe Bond Index	8.16%	1.41%	2.52%	3.52%	3.52%	8.79%	-1.19%
DEX Federal Bond Index	4.85%	2.39%	0.13%	3.66%	3.66%	6.91%	-1.52%
DEX Provincial Bond Index	11.07%	0.66%	4.33%	4.14%	4.14%	12.18%	-2.70%
DEX All Corporate Index	8.64%	1.10%	3.38%	2.71%	2.71%	7.58%	0.84%
DEX "A" Corporate Index	10.67%	0.51%	4. 42%	2.62%	2.62%	9.10%	-0.16%
DEX Real Return Bonds	9.70%	-0.05%	0.72%	2.79%	2.79%	13.18%	-13.1%
DEX High Yield Bonds	8.16%	2.15%	5.20%	13.79%	-5.58%	2.64%	6.87%

All sectors produced positive returns in November. The year-to-date returns are impressive, with double-digit performance in two sectors. High yield bonds merely equalled the Universe returns.

Comments:

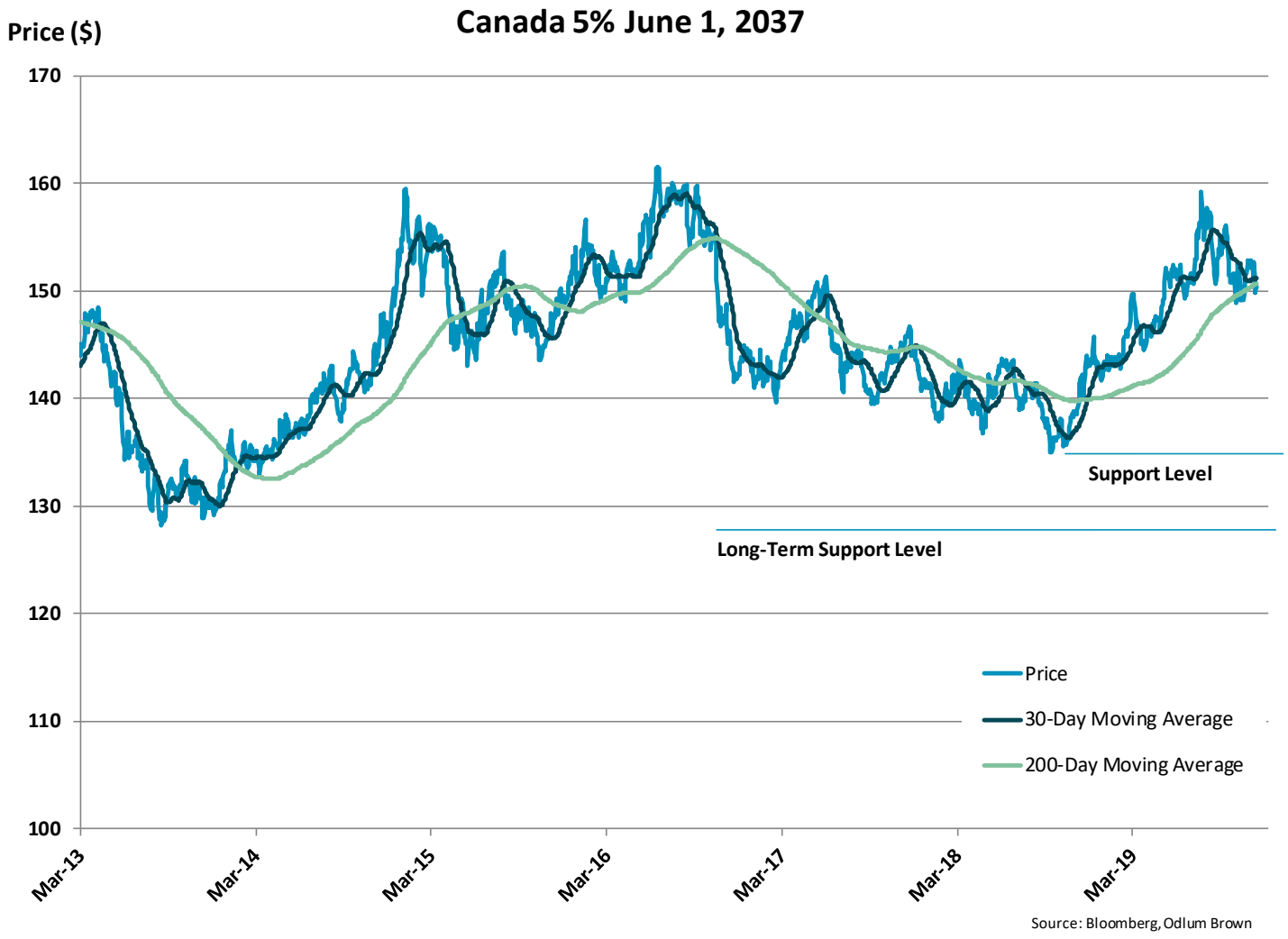
For the second consecutive month, bond yields rose modestly. The nine basis point rise in the yield on the Treasury ten-year note masked the 25 basis point range for this bond during November. Since month-end, yields tacked on a further five basis points. Also, as recession talk fades, the yield curve steepened further, now standing at 23 basis points. This added term premia to longer term bonds. The ongoing trade differences were the leading causes of the whipsaw in bond yields.

The U.S. economy began to grow faster, as witnessed in the upward revision in GDP, a buoyant consumer and strong employment market.

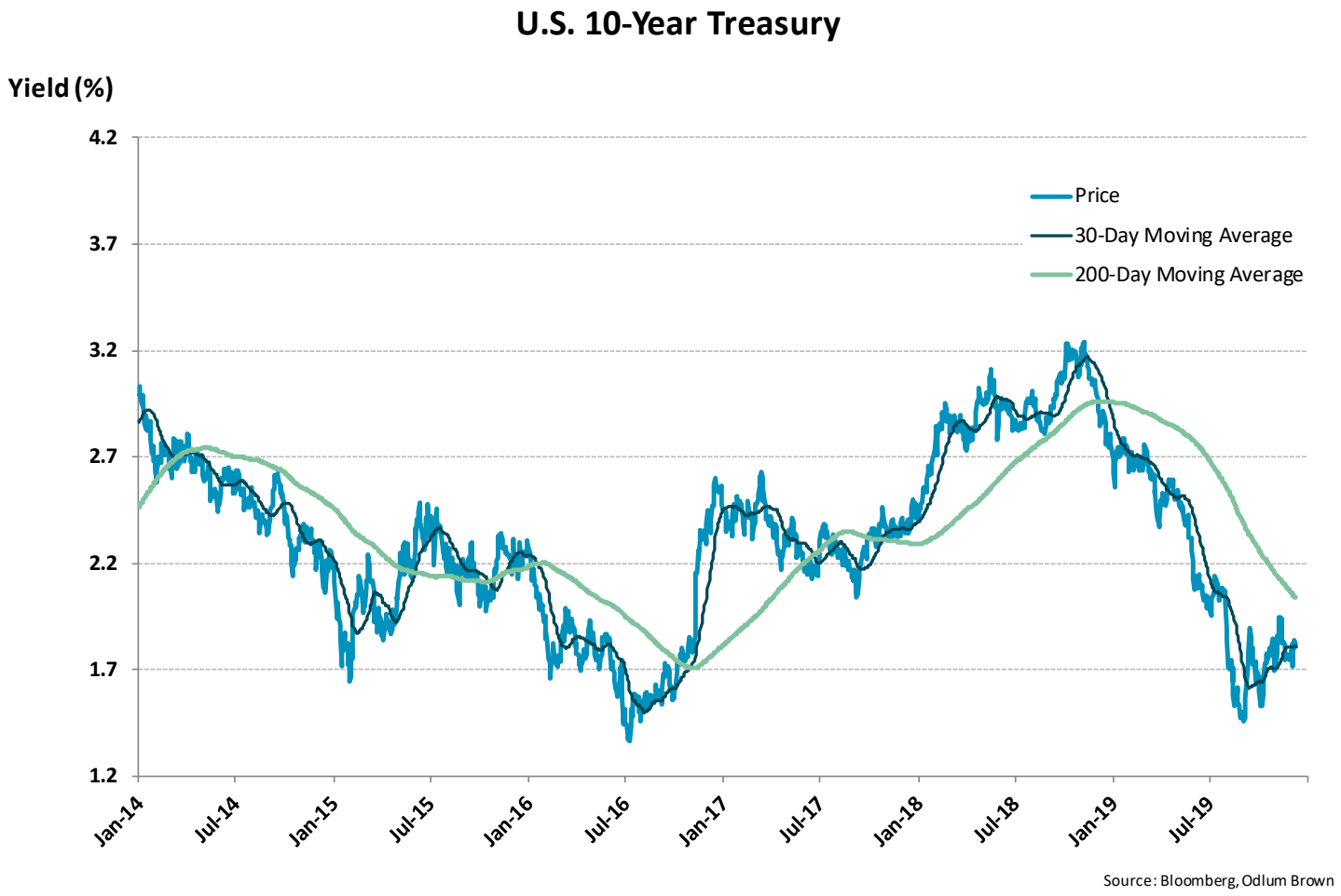
On the fiscal front, Japan announced a $120 billion stimulus package, joining India, China and a few Euro countries. The major holdout, Germany, is still toying with whether to stimulate or not.

Meanwhile, sovereign yields in the Eurozone moved closer to zero, not just in lockstep with the upward move in U.S. government yields, but also as a result of moves by the ECB to push short-term borrowing costs close to zero. The ECB took this action because it came to the conclusion that negative rates were not working. While it is premature to declare the end of the era of negative rates, it is clear that this trend will continue. Further fiscal stimulus would help accelerate this process.

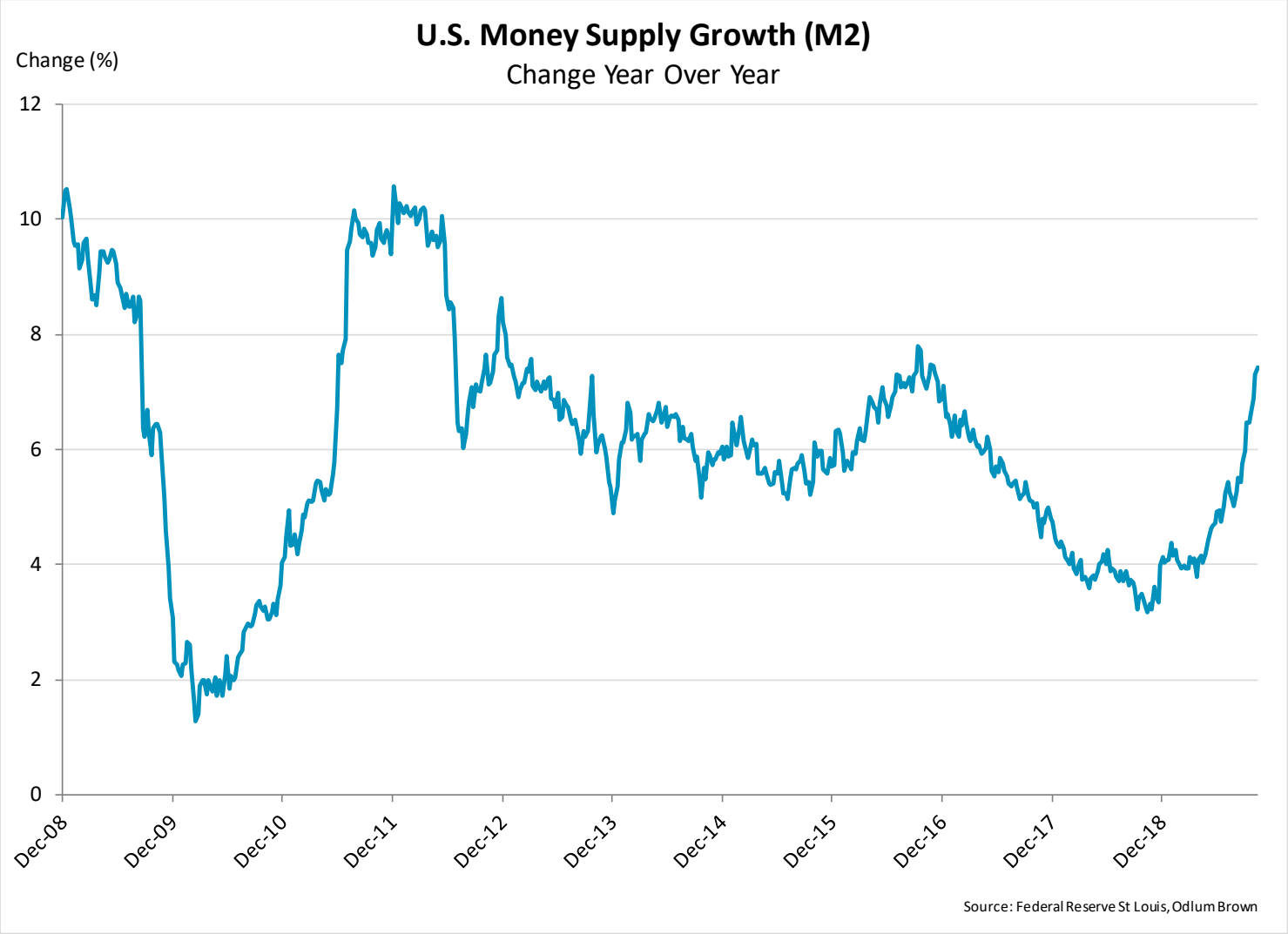
The Bank of Canada (BOC) left the Bank Rate unchanged and issued somewhat hawkish remarks, thus signalling it would not be lowering rates anytime soon. However, the BOC's announcement was followed by a surprisingly weak employment report and other poor data. Despite this, the loonie actually gained versus the U.S. dollar. The positive takeaway from Canada's employment report is that the economy generated some 285,000 jobs thus far in 2019. According to the BOC, the employment market remains tight, which can be seen in wage gains in excess of 4%.



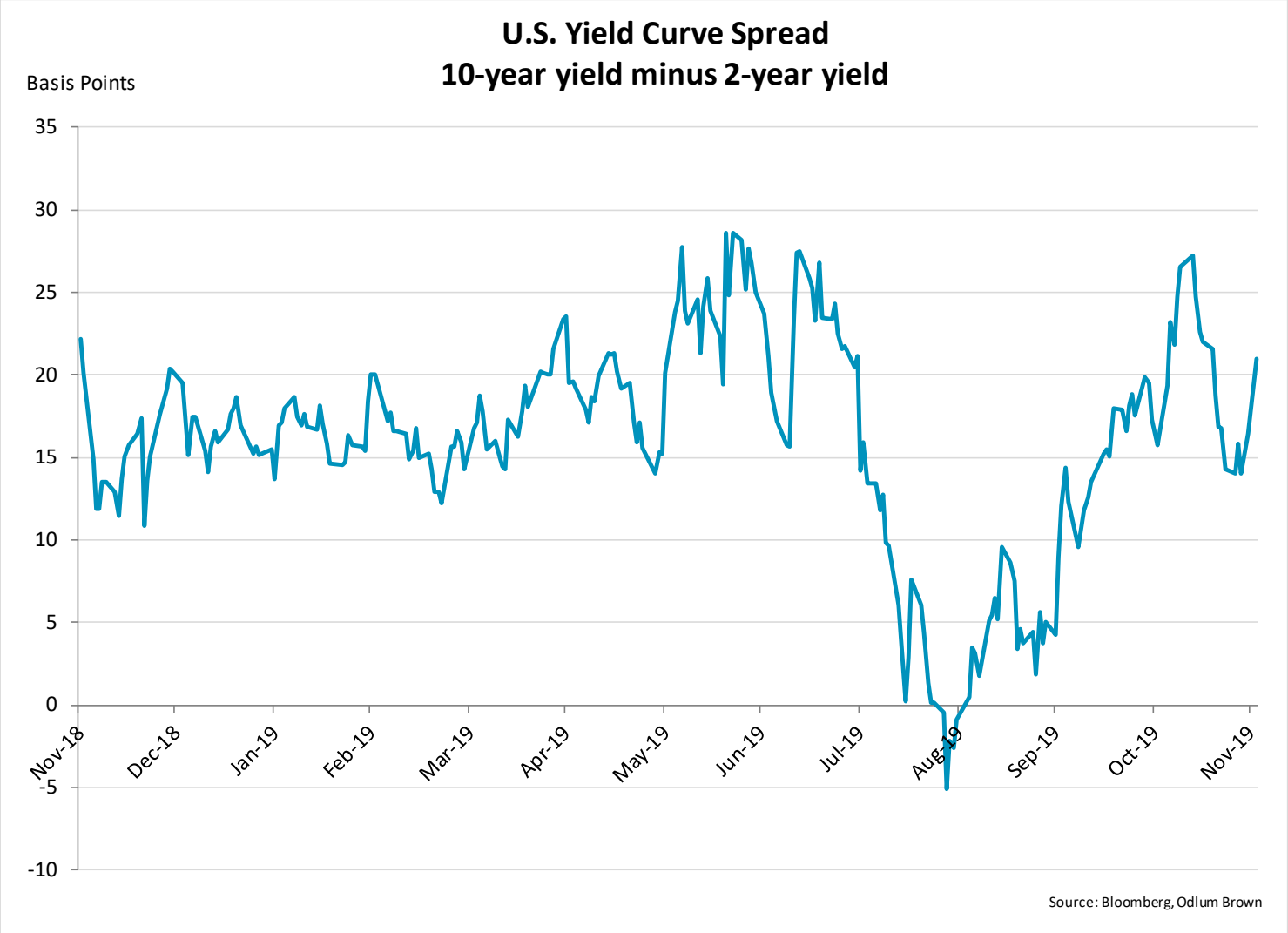
This bond sold off and is below all its moving averages.



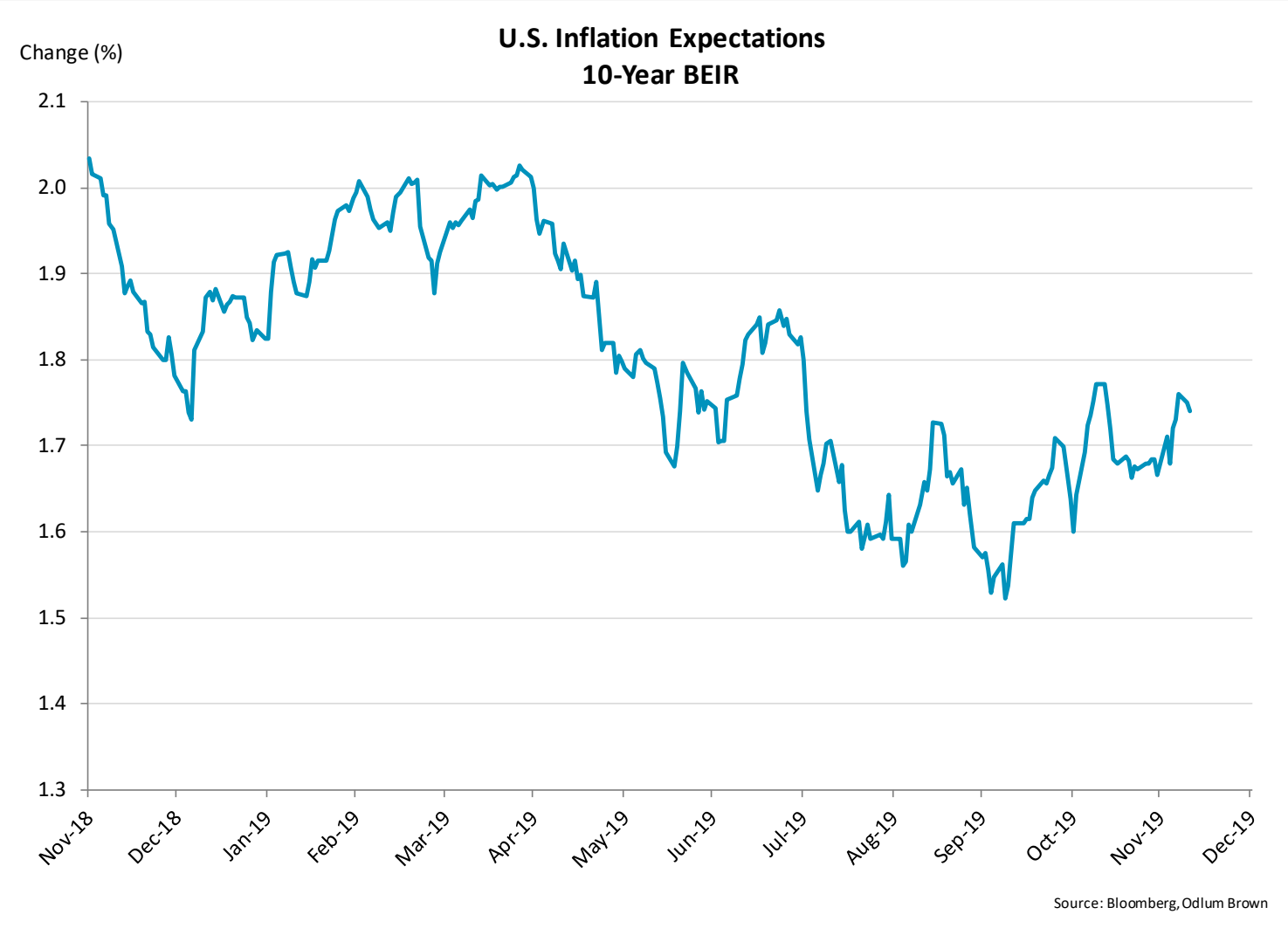
This global bellwether bond's yield moved above its 30-day moving average but remains well below the important 200-day moving average.



This broad measure of money supply continued to accelerate, auguring for a pickup in growth.



The yield curve steepened since being briefly inverted during the summer. It portends positive growth.



Inflation expectations are gradually moving higher.

Outlook

The global economy is rebounding at a modest pace and, with more fiscal stimulus in place, the stage is set for further increases in bond yields. Global growth is forecast to be in the area of 2%. Recently, a blockbuster employment report in the U.S. reinforced the expansion theme and also demonstrated that inflation is beginning to move higher, albeit still at a modest pace.

Significantly, increased fiscal stimulus added to the pickup in growth. Analysts are watching Germany carefully; should it add to the global increase in fiscal stimulus like the $120 billion of new spending announced by Japan, bond yields should rise further. In the Euro zone, sovereign yields moved higher (closer to zero) at a rate faster than that of U.S .yields.

On balance, the U.S. economy appears to be gathering strength. The consumer is in excellent condition with confidence high and debt under control. The employment market is healthy with gains in wages, the housing market is firm and there are signs that the weakness in manufacturing may be bottoming.

In the absence of some adverse news on the trade front, bond yields are poised to move higher with the September lows of 1.43% on the bellwether ten-year looking more and more like an important inflection point. It is possible to see this bond reaching 2% before year-end and perhaps 2.25% in the first quarter of 2020.

Strategy

By most standards, bonds remain overvalued. We continue to counsel a high-quality, short duration approach to bond investments. We have long advocated the laddered approach when constructing a fixed income portfolio. There is no reason to alter this strategy as it removes the guesswork from fixed income investing. Therefore, a ladder composed of high-quality corporate bonds and GICs will continue to produce positive returns while preserving principal.

For further discussion, please speak to your investment advisor.