# Expert Access - Fixed income - Seizing opportunity in an outlier period

[Energetic music]

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[Expert Access
Fixed income
Seizing opportunity in an outlier period]

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To look at the current trends in the fixed income market, you really have to go back to what we experienced over the last five, six years. And it's really been an experience of extremes.

[Bond yields over time (2009-2024)

A chart shows the change in bond yield maturity percentage; in 2009 it was just below 4%, then dropped to just under 1% in 2020, at which point it began rising again to over 4% around 2024.

Source: Bloomberg®. As at Dec. 31, 2023. Based on Bloomberg Global Aggregate Bond Index.]

Going into the COVID 19 pandemic, we saw easing monetary policy in full force. Rates near zero and that really made fixed income a relatively unattractive asset class.

Coming out of the pandemic and the easing monetary policy central banks have now gone the other way.

[BOC hiking cycles and Fed hiking cycles. Two twin charts measure “% increase from first hike” on the y-axis and “# of months from first hike” on the x-axis. In both charts, rate increases in 2022 rose significantly sharper than any previous rate increases dating back to 1988.

Source: Bloomberg®. As at Dec. 31, 2023. Based on Fed Funds Rate (Upper Bound) and Bank of Canada (”BoC”) policy rate.]

This is the most aggressive, fastest rate-hiking cycle we have seen in quite a long time.

In fact, you'd have to go back to the 1980s in both Canada and the US to see a similar move. And so really, the trend we're seeing now, to be fair, is: 'income' is back in fixed income. Yields are at levels we haven't seen since the great financial crisis in '07/'08. This is really an opportunity where you can capture yield that hasn't been in the market for quite some time.

[A graphic of a stock market chart.]

The other side of it, I would mention, is volatility: geopolitical risks, inflation's not just one way coming down.

[Several flagpoles hanging flags from a variety of nations. A woman outside a grocery store looking at her receipt.]

It's actually a great opportunity for us to add value, find areas where the markets got it wrong and capture those returns for our clients.

[Interest rate outlook]

Generally speaking, market participants are expecting inflation to continue to come down and therefore the need for central banks to keep interest rates where they are to alleviate over time.

We're of the view that cuts are coming in 2024.

[The Bank of Canada building. The US Federal Reserve building.]

We're thinking 2 to 3 cuts is probably likely as our base case. But again, recognizing there's a lot of unknowns there. It could be as small as one cut, or we could see zero if inflation really takes off again. Positioning around those possibilities is really the key.

[How is this creating opportunity for investors?]

With the back up in yields, right now we can actually construct a really attractive income portfolio without taking very much risk.

And the perfect example is the short end of the yield curve.

[Canada & US yield curves

A chart shows the yield percentage of US Treasury and Canada Government bonds with durations from 3 months to 30 years. From 30 years to about 5 years, yield of US bonds are around 4% and Canada bonds are around 3%. The rates increase sharply from 5 years to 3 months, with a three-month US bond reaching 5.5% and a three-month Canada bond reaching 5.0%. The 5 year to 3 month periods are supplemented with text graphics that read “5-year ladder: 5.0%” for US Treasury and “5-year ladder: 4.5%” for Canada Government.

Source: Bloomberg®. Curves as at Dec. 31, 2023.]

So call it five years and in. We can generate a yield north of 4% without taking hardly any credit risk if any credit risk at all in government bonds. That’s an opportunity we have not had for quite a long time. That’s the kind of base line that we’re building portfolios around and that’s exciting for us.

The other element that we're really excited about is duration.

[Timelapse of a busy downtown city street. Timelapse of downtown Ottawa including the Canada Parliament building.]

If you believe we're closer to the point of rate cuts this is where fixed income markets really show their upside and as we see a reversal in interest rates, fixed income markets, bonds and hopefully our portfolios as well should be able to generate returns that look almost equity-like in nature. We're talking closer to 10%.

[Fixed income funds positioned to capture upside (Hypothetical scenario)

A chart shows estimated total return percentage for three fixed income funds: Conservative, Core, and Core Plus. Three scenarios are presented for each fund: rate increase by 50 bps (Conservative returns 3.1%, Core returns 3.1% and Core Plus returns 2.9%), no change in rates (Conservative returns 4.9%, Core returns 5.1% and Core Plus returns 5.2%), and rate fall by 50 bps (Conservative returns 6.6%, Core returns 7.1% and Core Plus returns 7.5%).

Source: CIBC Asset Management Inc. Based on respective portfolio characteristics as at December 31, 2023 Probability weighted average assumes 25%. Probability of rates increasing by 50 bps, 10% chance of no change in rates and 65% chance of rates falling by 50 bps. This hypothetical scenario is shown for illustrative purposes only and is not indicative of future results. Please refer to the disclaimer for further information. As at December 31, 2023]

That really gets us excited, the combination of kind of the baseline yield, we can generate if nothing happens, and then the upside that comes with when central banks decide to pivot and start cutting rates.

The other element really is as I mentioned earlier, the volatility;

[Charts on several computer screens. A business person talking on the phone. A business meeting with several people in an office. A larger business meeting in an office conference room. A business meeting in an office conference room. Close-ups of business people at a table talking. Hands typing on a keyboard.]

the idea that our active management capabilities, our ability to move portfolios around, whether it be in government bonds in Canada, US Treasuries, corporate bonds in Canada.

[A US bond. A building with the title ‘THE TREASURY DEPARTMENT’ etched into stone. Two skyscrapers with a row of Canada flags at the base.]

There's lots of added value to be had there. We’re finding lots of opportunities where securities are mispriced and we can utilize our skill as long-term active managers, our dedicated credit research team, to find the value in the fixed income market and add extra value above and beyond what you would get in say a passive fixed income portfolio.

[The role of fixed income in CIBC Asset Management funds]

This opportunity set is embedded in all of the portfolios that we manage.

[Donut charts for CIBC Conservative Fixed Income Pool, CIBC Core Fixed Income Pool, and CIBC Core Plus Fixed Income Pool. A legend shows the pools are comprised, in differing amounts, of short-term bonds, core bonds, plus bonds, private credit, EMD, currency and cash.]

This is an opportunity across the market. I would argue if you're someone who's allocating to a balanced fund that includes equities and bonds, you can rest assured that the bond section of this portfolio has that upside and that potential embedded in it.

[A financial analyst looks at data on a computer screen. A closeup of eyes looking at data on a screen. A stylus swiping through data on a screen.]

That's really for us an exciting opportunity to talk to clients about almost a bit of a new role that fixed income plays in the total portfolio solution because you could see fixed income doing a lot of the heavy lifting over the next 1 to 2 years versus riskier asset classes like equities and alternatives.

[The CIBC logo mounted on a wall. A financial advisor meeting with clients in an office. A financial advisor meeting with clients at a home.]

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