The Right Combination for Fixed Income

By Kevin B. McLachlan

Since the US election last November, bond yields in Canada and the United States have been volatile. Despite this environment, Fiduciary Trust Canada's fixed income portfolios have performed well. For example, the FTC Core Canadian Bond Model Portfolio rose 2.8% over one year (as of March 31, 2017), outperforming the FTSE TMX Canada Universe Bond Index by 1.3%.

The tables below help illustrate our approach for the FTC Core Canadian Bond Model Portfolio and its positive influence on results. The first one highlights our overweight position in investment grade Canadian corporate bonds, with a lesser emphasis on federal and provincial bonds.

The second one, which shows the portfolio's term structure as compared to the Index, highlights our heavier weighting in mid-term bonds (six- to 10-year maturities).

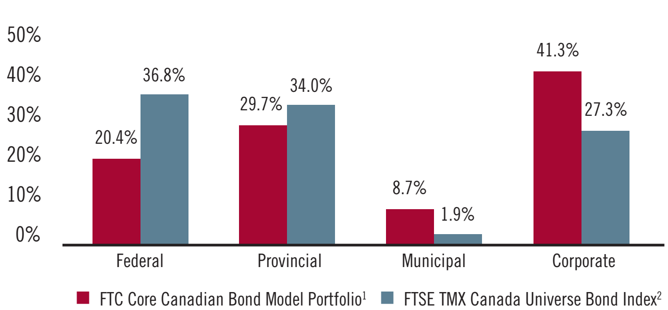
This combination of portfolio composition and term structure means the FTC Core Canadian Bond Model Portfolio has a shorter average maturity and a lower duration as compared to the Index. Here are a few ways this approach is working to benefit investors:

- Duration is a measure of how sensitive bond prices are to interest rate changes. While we do not anticipate a significant further rise in bond yields in the near term, lower duration means the prices of bonds in this portfolio will decline by less than the benchmark should interest rates suddenly and unexpectedly rise. Consider it an embedded defensive measure.
- The portfolio has a higher yield to maturity than the Index, while maintaining investment grade corporate bonds.
- Being underweight government bonds and overweight corporate bonds combined with lower duration, as compared to the Index, has been a key performance driver.

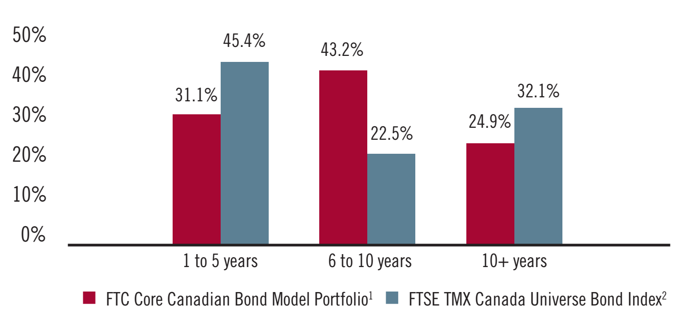
LOOKING AHEAD

We expect investment grade corporate and provincial bonds to continue offering relative value, finding further support in light of investors' ongoing search for yield and reasonably healthy conditions in corporate Canada. The US inflation and growth outlook are likely to be key to Canadian bonds for the balance of 2017. We anticipate that yields will move somewhat higher in coming months on the back of rising US Treasury yields. With that in mind, we plan to maintain our current overweight in investment grade corporate bonds and lower duration as compared to the Index.

FTC Core Canadian Bond Model Portfolio
Composition as of March 31, 2017



FTC Core Canadian Bond Model Portfolio
Term Structure as of March 31, 2017



1. Fiduciary Trust Canada proprietary data.
2. Debt Market Indices, FTSE TMX Global Debt Capital Markets.