Global Asset Management

Exploring a new

WORLD OF BONDS

Why global bonds should be part of your portfolio

With bond yields near or at historic lows, many investors are anticipating that interest rates will eventually rise, which can be seen as a risk for bonds. However, bonds, particularly global bonds, can occupy an important place in a well-diversified portfolio by helping to reduce volatility. In fact, this long-term investment strategy is one that RBC Global Asset Management has incorporated across our actively managed multi-asset portfolios for some time.

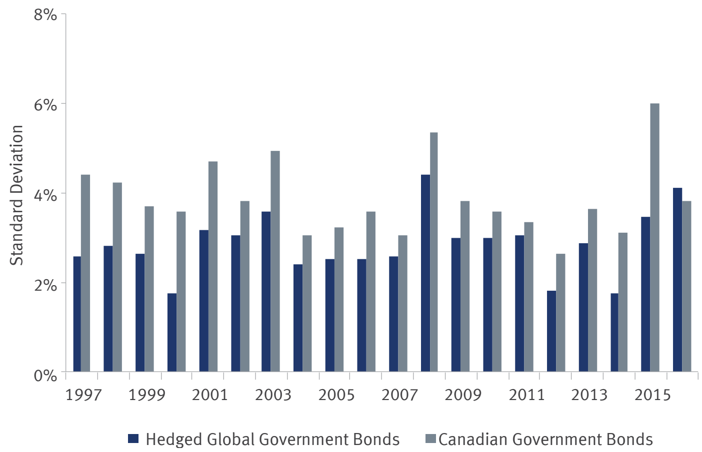
They may be less volatile than Canadian bonds

Contrary to popular perception, a global bond portfolio is typically less risky than a Canadian bond portfolio – provided the currency exposure is hedged. Chart 1 illustrates that in almost every year since 1997, a portfolio of Canadian dollar-hedged global government bonds had lower volatility than a portfolio of Canadian government bonds.

The currency hedging aspect of this example is important because a currency-hedged portfolio significantly reduces volatility over time.

Chart 2 illustrates this significance on a long-term basis. Over the past 20 years, an unhedged global government bond portfolio had an annualized volatility of 9.5%, while on a fully hedged basis, it had less than one-third of the volatility, at 2.9%. For local context, a Canadian government bond portfolio had a long-term annualized volatility of approximately 3.9%.*

Chart 1: Global bonds have generally been less volatile



Hedged Global Government Bonds are represented by the Citi World Government Bond Index. Canadian Government Bonds represented by FTSE TMX Canada All Government Bond Index.

Source: Morningstar Direct, December 2016

Chart 2: Managing currency risk can help mitigate volatility

Jan. 1997 – Dec. 2016	Global government bonds (C$ Unhedged)	Global government bonds (C$ Hedged)
Average Annual Return	4.0%	5.3%
Worst 12-Month Return	-14.3%	-1.1%
Standard Deviation (Volatility)	9.5%	2.9%

Global government bonds are represented by the Citi World Government Bond Index. All returns are annualized.
Source: Morningstar Direct.

*Annualized volatility of the Canadian government bond portfolio is represented by the FTSE TMX Canada All Government Bond Index for 20 years ending December 31, 2016.

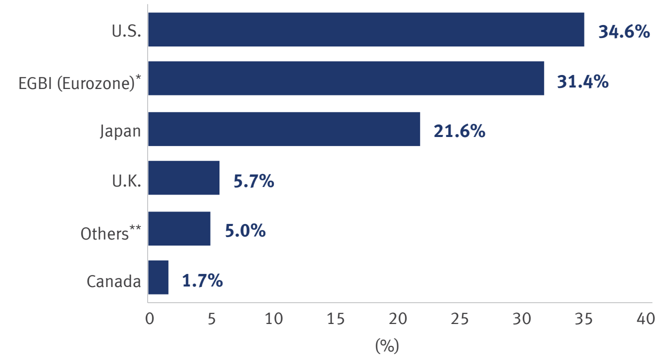
They offer more diversification opportunities

The Citi World Government Bond Index, which represents the world's government bond market, is enormous. It holds 1,008 bonds for a total market value of nearly US$20 trillion. As shown in Chart 3, Canada represents only 1.7% of this overall global bond universe, while the U.S. and qualifying countries from the eurozone represent the largest components, each over 31%. Exposure to the vast market available outside of Canada provides greater diversification opportunities.

They provide greater return potential

Although yields are low in most global economies, the risk and return potential can vary significantly from region to region. Chart 4 shows how wide the range of outcomes has been and that Canadian government bonds seldom lead the way. This demonstrates that a diversified, global approach to bonds can help provide greater return opportunities.

Chart 3: Canada is only a small share of the global bond market



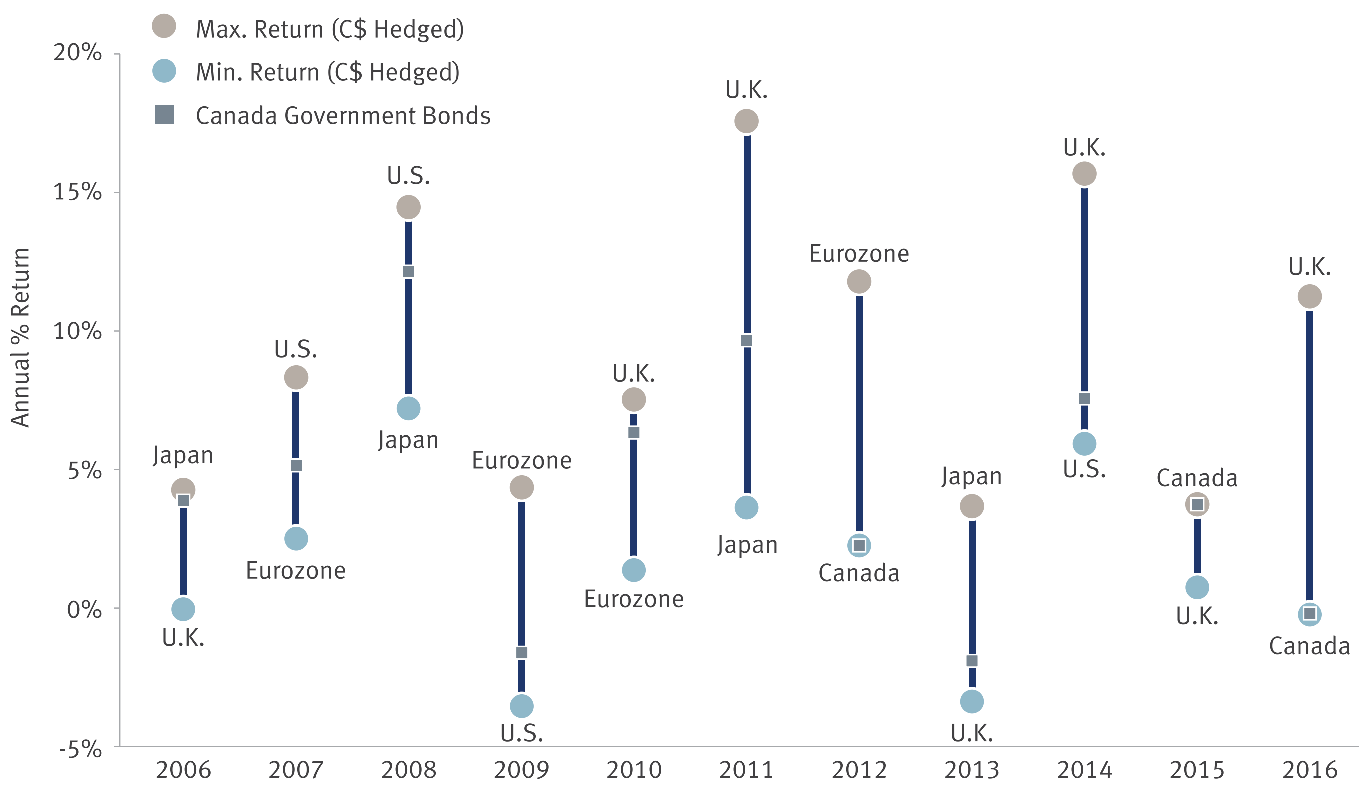
*The Citi EMU Government Bond Index (EGBI) consists of EMU-participating countries that meet the WGBI criteria for market inclusion: Austria, Belgium, Finland, France, Germany, Ireland, Italy, Netherlands and Spain.

**Others include the following countries: Australia, Denmark, Malaysia, Mexico, Norway, Poland, Singapore, South Africa, Sweden and Switzerland.

Source: Citigroup, as of December 31, 2016.

Chart 4: Global bonds offer more diversified return potential

The wide dispersion of returns from global government bonds can offer greater opportunities



Source: Citigroup, RBC Global Asset Management, as of December 31, 2016. Universe consists of Citi WGBI EGBI (Eurozone), Citi WGBI Canada, Citi WGI US, Citi WGBI UK, and Citi WGBI Japan denominated in local currency.

They exploit diverging central bank policies

Uneven economic growth and inflation across countries and regions present opportunities for global bond investors. Working in a global bond universe and understanding the global monetary policy landscape both enable active bond managers to take advantage of investment opportunities that can provide downside protection with the potential for some capital appreciation.

Chart 5 illustrates this opportunity by depicting the current monetary policy landscape of major economies around the world (tightening/loosening). As central bank policies in different regions diverge across the tightening-loosening spectrum, a wider range of investment opportunities is presented to global fixed income investors.

Chart 5: Monetary policy diverging around the world

Loosening (lowering rates)	Neutral	Tightening (raising rates)
	Canada	
Japan	United Kingdom	United States
	Eurozone	

Information as of November 30, 2016. For illustrative purposes only.
Source: RBC Global Asset Management.

Going global with your bond portfolio

Diversifying your bond portfolio by taking advantage of global bond markets can be a winning strategy that helps reduce risk and enhance return potential. Global bonds not only provide diversification opportunities, but can also offer a wider range of potential returns than Canadian bonds, helping you meet your long-term investment goals.

Talk to your advisor about how global bonds may be able to enhance your portfolio.

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