

A bond market take on 'supply side' mania

By Warren Lovely, Taylor Schleich & Alpa Atha

Supply chain disruptions, production kinks and goods shortages are seemingly all we can think about these days. In keeping with the prevailing supply side mania, consider (briefly) Canada's international securities transactions data. Foreign investors apparently feasted on Canadian securities in September, gobbling up a net C\$20 billion. Much of that buying happened in debt capital markets, including a record take-down of private corporate bonds. Simultaneously, September delivered an historic offloading of Canadian government securities, including reduced foreign participation in money markets. Digging through the details, you'll see that foreign investors cut their holdings of CAD-denominated bonds by C\$5.5 billion. Despite still-healthy secondary market accumulation, more foreign-held CAD bonds are coming due. We've never seen such a hefty net outflow via CAD retirements in September. And just wait for December, which will key another outsized slug of retirements. (Refer to our [earlier note](#) for detailed analysis of December cash flows.) Sure, BoC uncertainty and impaired front-end liquidity have understandably put some foreign investors on edge. This estrangement bears watching. But before you go thinking there's simply 'no cares' on CAD bonds or Canadian government debt in general, recall the theme here: supply. A rapidly improving fiscal situation means some of Canada's largest bond issues aren't nearly as hungry for cash as they once were. More than anything, it's the resulting drop off in bond supply (less primary and extra-large retirements) that explains the apparent disassociation of foreign investors from Canada's domestic bond market.

Chart 1: Foreign investors feast on corporate bonds, shunning governments & CAD-denominated issues in September

Net foreign purchases of Canadian portfolio securities: By asset class & bond market details by sector, currency of issue, geographic region

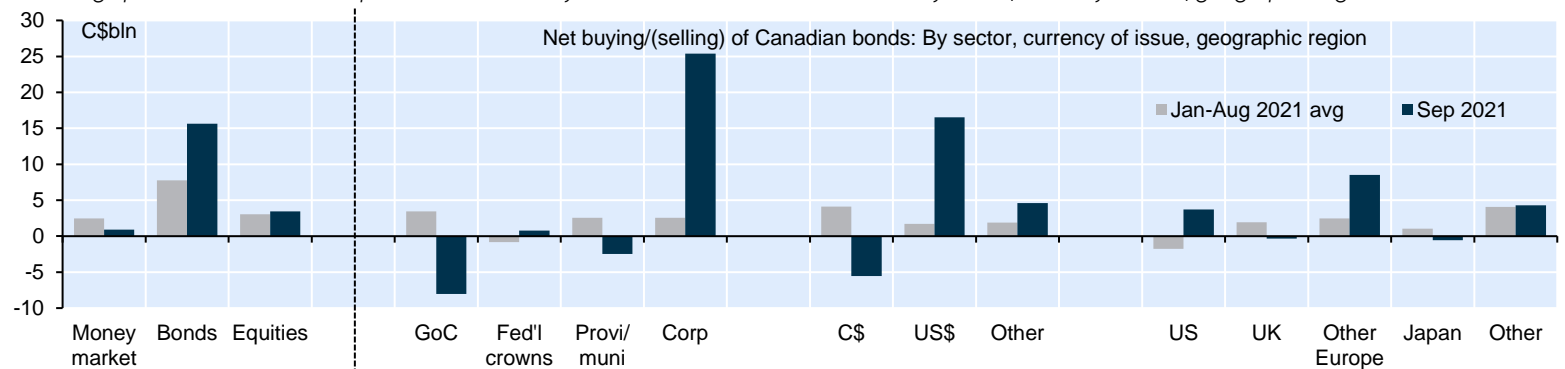


Chart 2: Dissecting CAD bond flows with non-residents

Non-resident flows in CAD bonds by transaction type (9M mov avg)

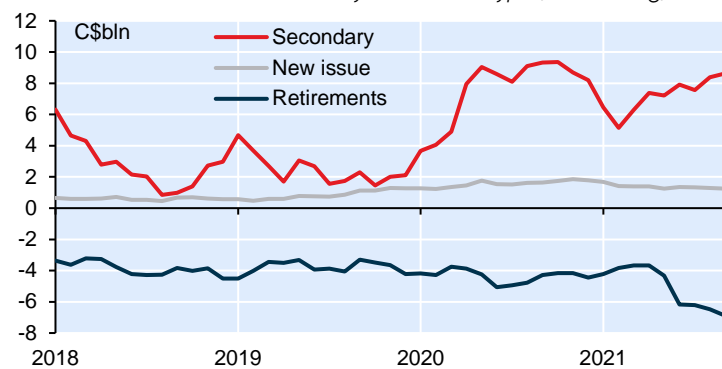


Chart 3: CAD retirements increasingly leave their mark

Retirements of CAD bonds held by non-residents by month: 2021 vs. trend

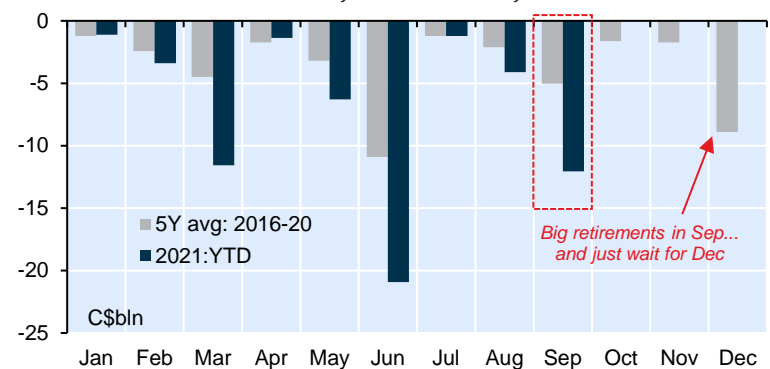


Chart 4: No cares on Canadian government debt?

Distribution of monthly net foreign flows in Cdn government debt since 1988

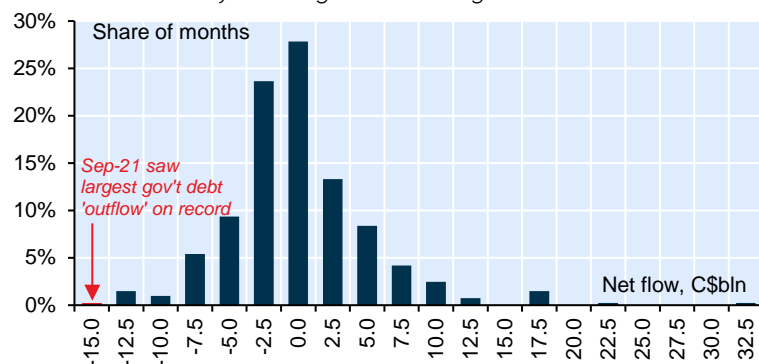
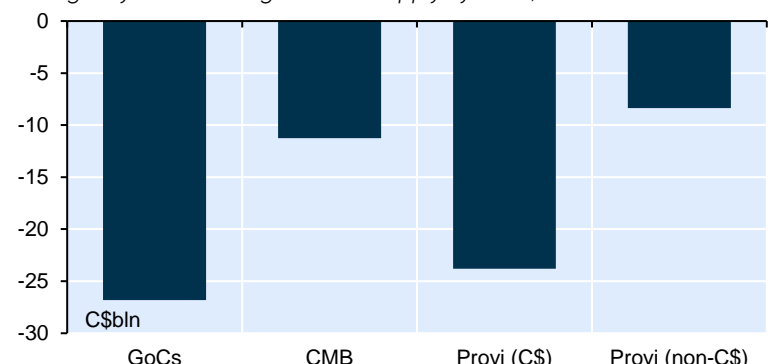


Chart 5: Cdn issuers less hungry for cash (domestic or foreign)

Change in year-to-date gross bond supply by issuer/sector: 2021



Notes: Charts 2-3 refer to CAD-denominated bonds only; Chart 4 refers to non-resident flows in all Canadian government securities (including foreign currency issues); Chart 5 refers to the delta on gross bond issuance on a YTD basis through October (i.e., Jan-Oct 2021 vs. Jan-Oct 2020) | Sources: NBF, StatCan, Bloomberg

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