

Adjusting the [bond] volume

By Warren Lovely

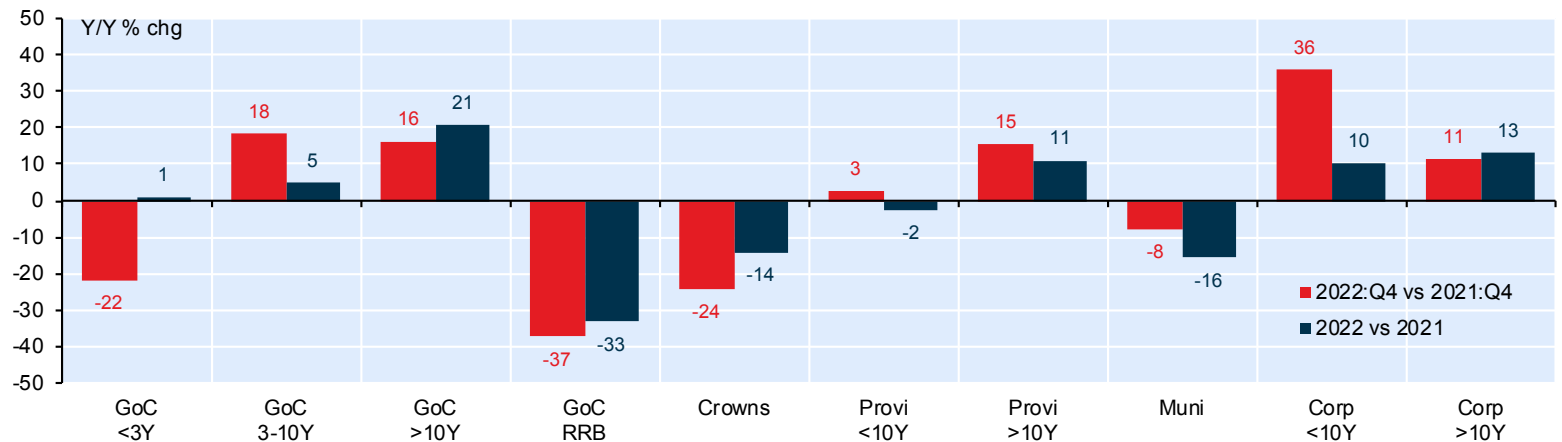
It's still early enough in the year to reflect on what we saw and learned in 2022. After all, when it comes to Canada's secondary market trading volumes, IIROC only recently finalized last year's statistics. At C\$14.3 trillion, total secondary trading in Canada's domestic bond market rose ~3% in 2022, this despite a pronounced step down in primary market activity and the onset of a notionally liquidity-draining Quantitative Tightening program at the Bank of Canada (where 100% passive balance sheet run-off commenced in April 2022).

As always, there's plenty of nuance when dissecting the year that was in terms of Canada's secondary trading. The following charts (a baker's dozen worth) highlight select aspects we found informative, although any number of additional visuals could be conjured from this rich data set. We're reluctant to dwell too much on the past year's data, mindful of an ongoing evolution in rates markets linked to policy rate normalization and a still highly uncertain economic, fiscal, geopolitical outlook. Saying that, we were encouraged by the demonstrated liquidity that was afforded market participants in most key sectors of Canada's fixed income market in 2022. Yes, there were cases where secondary market activity receded, and some segments of the investor base may have turned their positions over less fervently (some non-resident investors come to mind). But 2022 showed a Canadian bond market with enviable depth... a resilient market that nicely accommodated an initial phase of QT... and one that remained well functioning even as liquidity flares shot up in some international bond markets.

As for a brief bit of self-promotion, National Bank Financial was extremely proud to secure the market leading share of total GoC bond trading in 2022, our firm ranking second in overall domestic bond trading last year. We look forward to another eventful year in 2023.

Chart 1: Assessing growth in secondary trading volumes across Canada's domestic bond market

Year-over-year growth in total Canada secondary bond trading by major sector/tenor: 2022 (full-year & latest quarter)

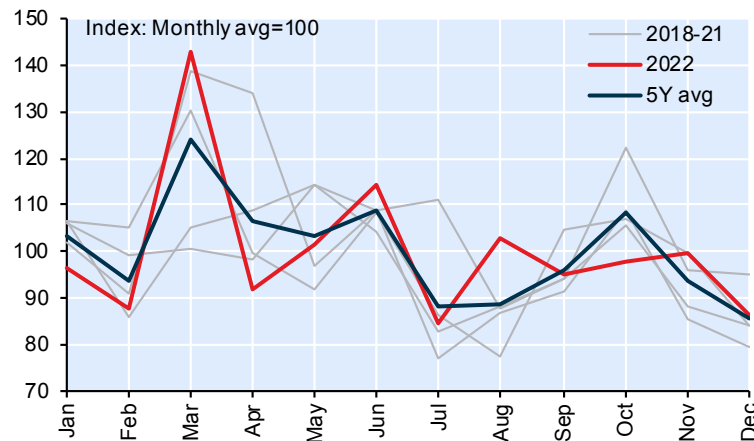


Source: NBF, IIROC | Note: For Charts 1-11, secondary trading volumes based on sum of all counterparties

Over C\$14 trillion traded hands in Canada's domestic bond market in 2022, total secondary volume (all sectors) rising 3% year-on-year. The sovereign (GoC) once again accounted for the lion's share of trade (78%), where some marginal activity migrated out the curve. Provincial volumes held up, despite a major step down in issuance, with longer-dated provincials continuing to demonstrate good depth/liquidity. Corporate bond volumes also defied a slowdown in domestic supply, with total corporate trading rising 8% despite pronounced bouts of risk-aversion as central banks pounded away.

Chart 2: Onset of tightening keyed re-positioning

Monthly pattern of total Canada bond trading: 2022 vs. trend

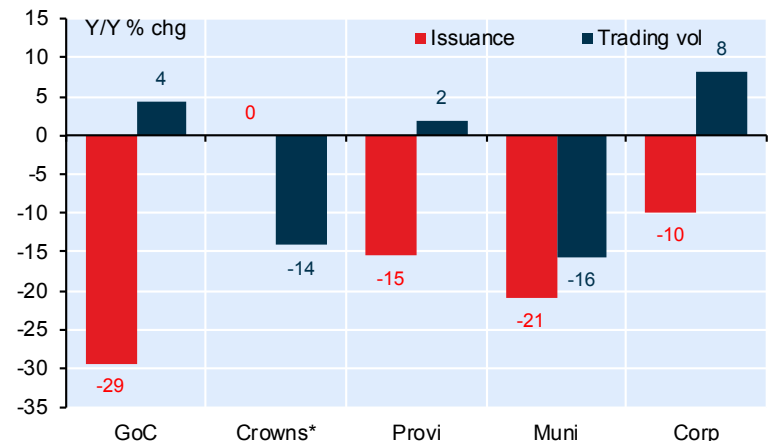


Source: NBF, IIROC | Note: Individual months scaled to average monthly volume

The BoC (and Fed) shook things up in March, initiating tightening cycles. That was followed by a seasonal pick-up in volume in June, activity moderating in the second half with QT taking hold.

Chart 3: In some cases, volume up despite (much) less supply

Growth in Canada bond trading & gross bond issuance: 2022

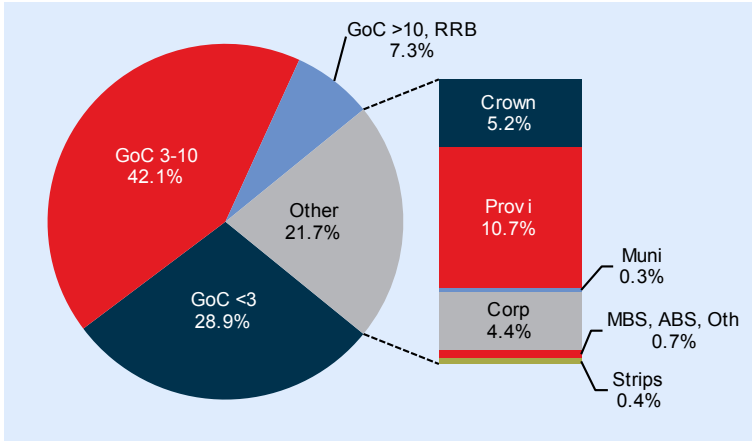


Source: NBF, IIROC, Bloomberg | Note: For Crowns, issuance refers to CHT only

In spite of a primary market pullback, trading volumes rose in key corners of the market like Canadas, provis and corps. For some, a major rate re-think prompted portfolio re-positioning.

Chart 4: GoC home to 78% of 2022's total domestic trading

Share of Canada bond trading by major sector/term: 2022

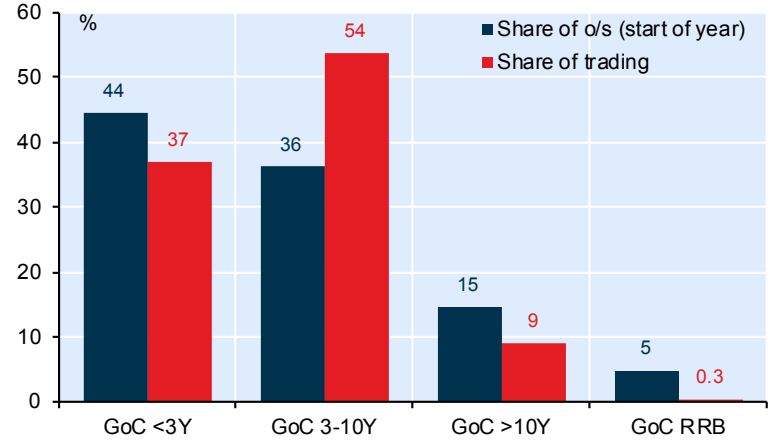


Source: NBF, IIROC | Note: Share of C\$14.3 trillion in total bond trading in 2022

The GoC share of trading may be in line with prior years, but it's hardly status quo. Supply receded as red ink was cleaned up. Meantime, BoC QT is pushing more bonds to end investors.

Chart 5: Where on curve are Canada's trading?

Share of total GoC bond trading vs. share of GoC bonds outstanding: 2022

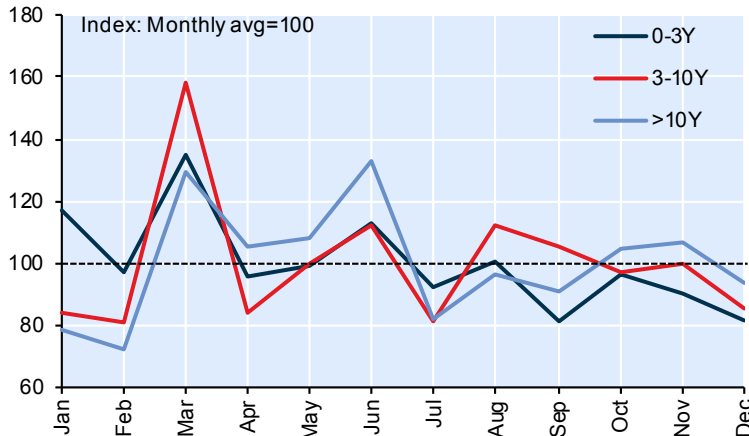


Source: NBF, IIROC, BoC | Note: O/s bonds as at 1-Jan-22; trading share is full year total

There's no shortage of trading (or outstandings) in the front end of the GoC market, but the belly continues to account for a disproportionate share of Canada volume, with active hedging here.

Chart 6: Less activity in second half (not entirely uncommon)

Monthly pattern of GoC bond trading by tenor: 2022

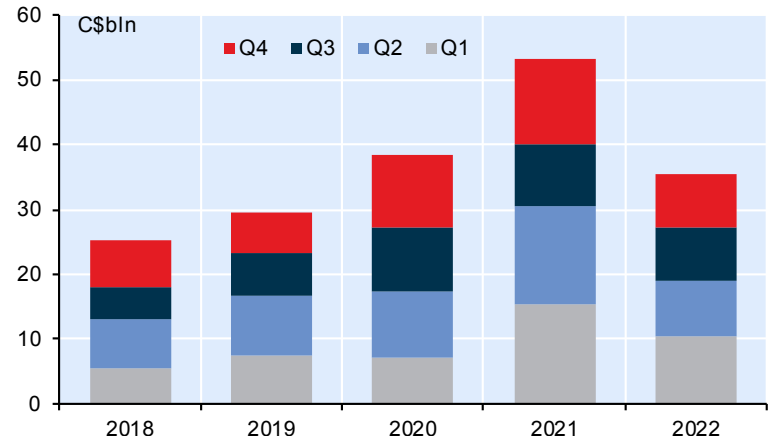


Source: NBF, IIROC | Note: Individual months scaled to average monthly volume

There's a seasonal tendency to GoC bond trading that was partially on display in 2022 (e.g. March, June). Second half GoC volumes were off 12%, with QT poised to pick-up in 2023.

Chart 7: RIP RRBs?

Total GoC RRB bond trading by year/quarter

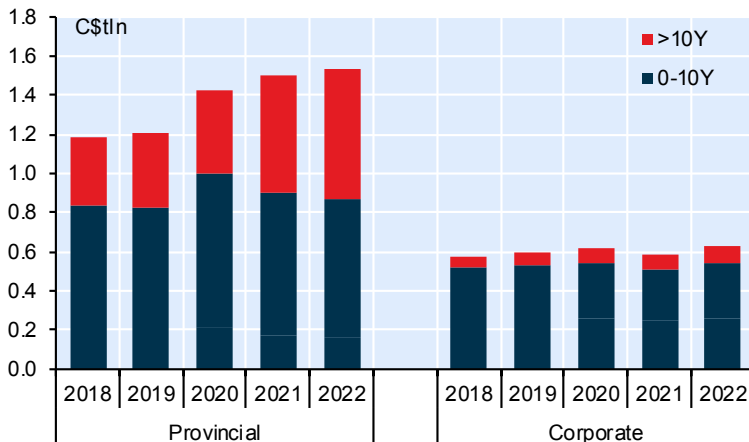


Source: NBF, IIROC

RRBs have long been a special case. After a noted pick-up in 2021, RRB volume retreated last year, Finance Canada's FES sounding the death knell for this product—a decision [we lamented](#).

Chart 8: Plenty of action in long provincials

Total annual provincial & corporate bond trading by term

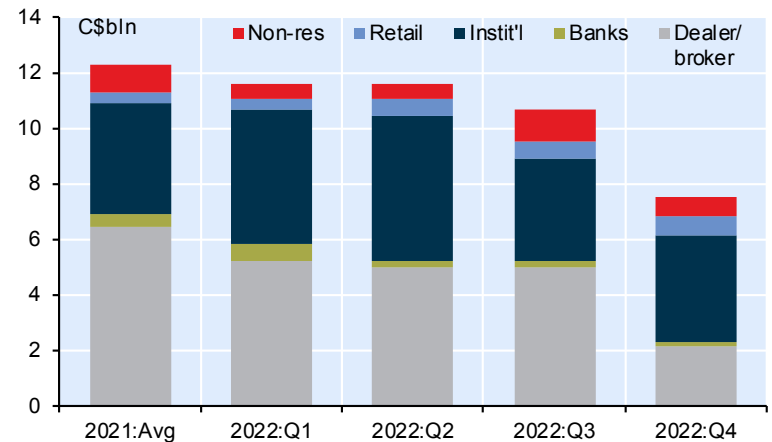


Source: NBF, IIROC | Note: For 2022, total provi vol +2% & total corp vol +8%

Less primary paper, no problem... at least for provis and corps, where volumes edged up. Activity was relatively brisk in long provis, where volume is not that far removed from the GoC.

Chart 9: Muni volumes followed issuance lower

Total quarterly municipal bond trading by counterparty: 2022 vs. 2021 average

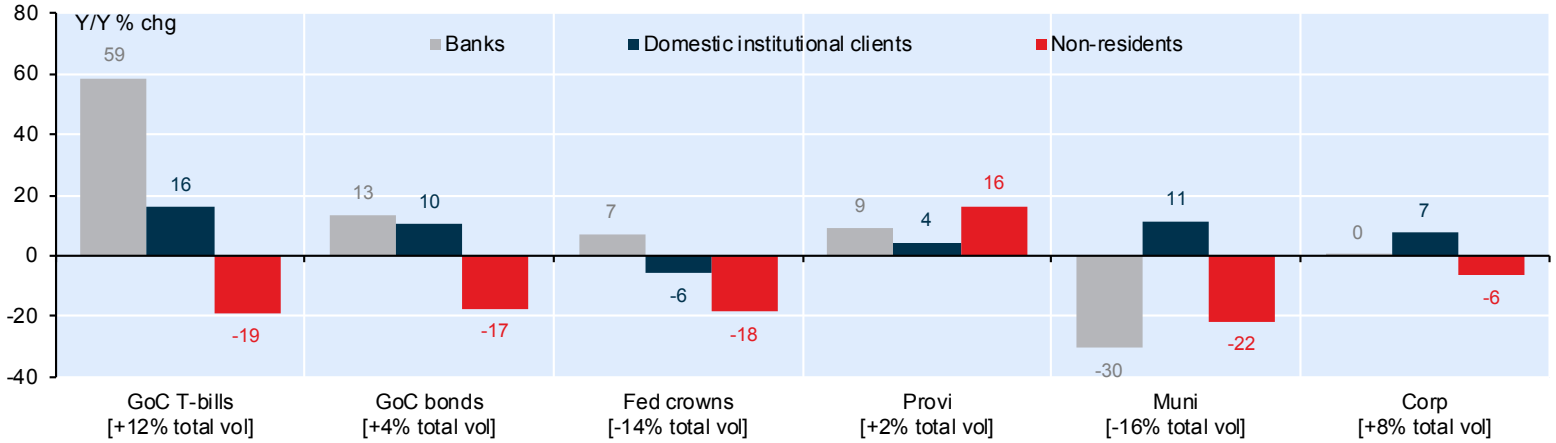


Source: NBF, IIROC | Note: For 2022, total muni vol -16% on full-year basis

Muni bond volume sunk 16% in 2022, activity in the final quarter of the year particularly light. Much of that relates to dealer/broker trade, with institutional investors still reasonably engaged.

Chart 10: A closer look at what some key investor types were trading

Year-over-year growth in Canadian bond & money market trading by select investor type & sector: 2022

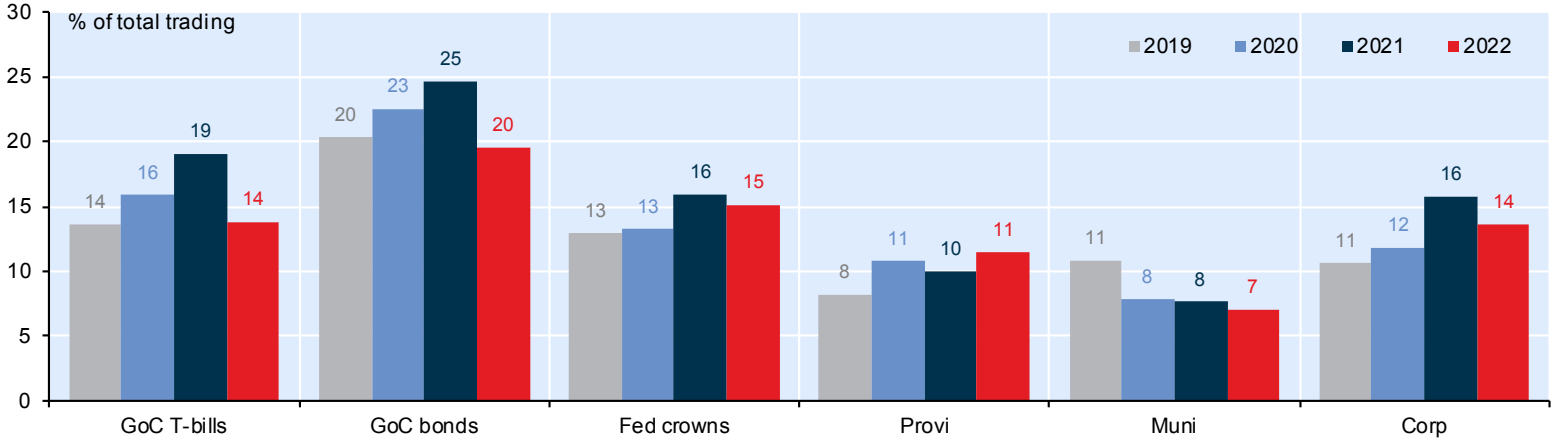


Source: NBF, IIROC | Note: 2022 vs. 2021; figures in [:] under each sector label refer to year-over-year change in secondary trading across all counterparties

With the BoC backing away via QT, more Canadas are being placed with domestic investors (banks and institutional clients). So trading volumes are on the rise here. If anything, Canadian banks were also more active in Crowns and provis. In many cases, non-resident volumes moderated in 2022, despite foreign investors technically adding to the total holdings of domestic paper last year.

Chart 11: Non-resident footprint in domestic market generally lightened up in 2022

Non-resident share of total Canada bond & money market trading by select sector: 2019 to 2022



Source: NBF, IIROC

Non-residents are non-trivial players in Canada's domestic bond market, foreign hedge funds, banks, asset managers and official accounts important sources of secondary market liquidity. Saying that, the non-resident share of domestic trading generally declined in 2022. Non-residents were more active in provincials, BC and Alberta having attracted outsized foreign flow (19-21% of all trade).

Chart 12: NBF #1 in total GoC bond trading...

Individual dealer share of total GoC bond trading (all tenors): 2022



Source: NBF, IIROC

And now a brief self-promotional message: The ~C\$1.7 trillion of Government of Canada bonds National Bank Financial traded in 2022 left us with the market-leading share of total GoC trading in calendar 2022 (having just narrowly missed this honour in 2021.)

Chart 13: ... and #2 in total domestic bond trading in 2022

Individual dealer share of total domestic bond trading (all sectors): 2022



Source: NBF, IIROC

A relatively strong position in total GoC trading (shown at left), combined with solid representation in other segments left NBF in the #2 position in terms of total domestic bond trading in 2022. Thanks to all our counterparties. As always, your bid or offer is welcomed.



Economics and Strategy

Montreal Office

514-879-2529

Stéfane Marion

Chief Economist and Strategist
stefane.marion@nbc.ca

Kyle Dahms

Economist
kyle.dahms@nbc.ca

Alexandra Ducharme

Economist
alexandra.ducharme@nbc.ca

Matthieu Arseneau

Deputy Chief Economist
matthieu.arseneau@nbc.ca

Daren King, CFA

Economist
daren.king@nbc.ca

Angelo Katsoras

Geopolitical Analyst
angelo.katsoras@nbc.ca

Jocelyn Paquet

Economist
jocelyn.paquet@nbc.ca

Toronto Office

416-869-8598

Warren Lovely

Chief Rates and Public Sector Strategist
warren.lovely@nbc.ca

Taylor Schleich

Rates Strategist
taylor.schleich@nbc.ca

General

This Report was prepared by National Bank Financial, Inc. (NBF), (a Canadian investment dealer, member of IIROC), an indirect wholly owned subsidiary of National Bank of Canada. National Bank of Canada is a public company listed on the Toronto Stock Exchange.

The particulars contained herein were obtained from sources which we believe to be reliable but are not guaranteed by us and may be incomplete and may be subject to change without notice. The information is current as of the date of this document. Neither the author nor NBF assumes any obligation to update the information or advise on further developments relating to the topics or securities discussed. The opinions expressed are based upon the author(s) analysis and interpretation of these particulars and are not to be construed as a solicitation or offer to buy or sell the securities mentioned herein, and nothing in this Report constitutes a representation that any investment strategy or recommendation contained herein is suitable or appropriate to a recipient's individual circumstances. In all cases, investors should conduct their own investigation and analysis of such information before taking or omitting to take any action in relation to securities or markets that are analyzed in this Report. The Report alone is not intended to form the basis for an investment decision, or to replace any due diligence or analytical work required by you in making an investment decision.

This Report is for distribution only under such circumstances as may be permitted by applicable law. This Report is not directed at you if NBF or any affiliate distributing this Report is prohibited or restricted by any legislation or regulation in any jurisdiction from making it available to you. You should satisfy yourself before reading it that NBF is permitted to provide this Report to you under relevant legislation and regulations.

National Bank of Canada Financial Markets is a trade name used by National Bank Financial and National Bank of Canada Financial Inc.

Canadian Residents

NBF or its affiliates may engage in any trading strategies described herein for their own account or on a discretionary basis on behalf of certain clients and as market conditions change, may amend or change investment strategy including full and complete divestment. The trading interests of NBF and its affiliates may also be contrary to any opinions expressed in this Report.

NBF or its affiliates often act as financial advisor, agent or underwriter for certain issuers mentioned herein and may receive remuneration for its services. As well, NBF and its affiliates and/or their officers, directors, representatives, associates, may have a position in the securities mentioned herein and may make purchases and/or sales of these securities from time to time in the open market or otherwise. NBF and its affiliates may make a market in securities mentioned in this Report. This Report may not be independent of the proprietary interests of NBF and its affiliates.

This Report is not considered a research product under Canadian law and regulation, and consequently is not governed by Canadian rules applicable to the publication and distribution of research Reports, including relevant restrictions or disclosures required to be included in research Reports.



UK Residents

This Report is a marketing document. This Report has not been prepared in accordance with EU legal requirements designed to promote the independence of investment research and it is not subject to any prohibition on dealing ahead of the dissemination of investment research. In respect of the distribution of this Report to UK residents, NBF has approved the contents (including, where necessary, for the purposes of Section 21(1) of the Financial Services and Markets Act 2000). This Report is for information purposes only and does not constitute a personal recommendation, or investment, legal or tax advice. NBF and/or its parent and/or any companies within or affiliates of the National Bank of Canada group and/or any of their directors, officers and employees may have or may have had interests or long or short positions in, and may at any time make purchases and/or sales as principal or agent, or may act or may have acted as market maker in the relevant investments or related investments discussed in this Report, or may act or have acted as investment and/or commercial banker with respect hereto. The value of investments, and the income derived from them, can go down as well as up and you may not get back the amount invested. Past performance is not a guide to future performance. If an investment is denominated in a foreign currency, rates of exchange may have an adverse effect on the value of the investment. Investments which are illiquid may be difficult to sell or realise; it may also be difficult to obtain reliable information about their value or the extent of the risks to which they are exposed. Certain transactions, including those involving futures, swaps, and other derivatives, give rise to substantial risk and are not suitable for all investors. The investments contained in this Report are not available to retail customers and this Report is not for distribution to retail clients (within the meaning of the rules of the Financial Conduct Authority). Persons who are retail clients should not act or rely upon the information in this Report. This Report does not constitute or form part of any offer for sale or subscription of or solicitation of any offer to buy or subscribe for the securities described herein nor shall it or any part of it form the basis of or be relied on in connection with any contract or commitment whatsoever.

This information is only for distribution to Eligible Counterparties and Professional Clients in the United Kingdom within the meaning of the rules of the Financial Conduct Authority. NBF is authorised and regulated by the Financial Conduct Authority and has its registered office at 70 St. Mary Axe, London, EC3A 8BE.

NBF is not authorised by the Prudential Regulation Authority and the Financial Conduct Authority to accept deposits in the United Kingdom.

US Residents

With respect to the distribution of this report in the United States of America, National Bank of Canada Financial Inc. ("NBCFI") which is regulated by the Financial Industry Regulatory Authority (FINRA) and a member of the Securities Investor Protection Corporation (SIPC), an affiliate of NBF, accepts responsibility for its contents, subject to any terms set out above. To make further inquiry related to this report, or to effect any transaction, United States residents should contact their NBCFI registered representative.

This report is not a research report and is intended for Major US Institutional Investors only.

This report is not subject to US independence and disclosure standards applicable to research reports.

HK Residents

With respect to the distribution of this report in Hong Kong by NBC Financial Markets Asia Limited ("NBCFMA") which is licensed by the Securities and Futures Commission ("SFC") to conduct Type 1 (dealing in securities) and Type 3 (leveraged foreign exchange trading) regulated activities, the contents of this report are solely for informational purposes. It has not been approved by, reviewed by, verified by or filed with any regulator in Hong Kong. Nothing herein is a recommendation, advice, offer or solicitation to buy or sell a product or service, nor an official confirmation of any transaction. None of the products issuers, NBCFMA or its affiliates or other persons or entities named herein are obliged to notify you of changes to any information and none of the foregoing assume any loss suffered by you in reliance of such information.

The content of this report may contain information about investment products which are not authorized by SFC for offering to the public in Hong Kong and such information will only be available to those persons who are Professional Investors (as defined in the Securities and Futures Ordinance of Hong Kong ("SFO")). If you are in any doubt as to your status you should consult a financial adviser or contact us. This material is not meant to be marketing materials and is not intended for public distribution. Please note that neither this material nor the product referred to is authorized for sale by SFC. Please refer to product prospectus for full details.

There may be conflicts of interest relating to NBCFMA or its affiliates' businesses. These activities and interests include potential multiple advisory, transactional and financial and other interests in securities and instruments that may be purchased or sold by NBCFMA or its affiliates, or in other investment vehicles which are managed by NBCFMA or its affiliates that may purchase or sell such securities and instruments.

No other entity within the National Bank of Canada group, including National Bank of Canada and National Bank Financial Inc, is licensed or registered with the SFC. Accordingly, such entities and their employees are not permitted and do not intend to: (i) carry on a business in any regulated activity in Hong Kong; (ii) hold themselves out as carrying on a business in any regulated activity in Hong Kong; or (iii) actively market their services to the Hong Kong public.

Copyright

This Report may not be reproduced in whole or in part, or further distributed or published or referred to in any manner whatsoever, nor may the information, opinions or conclusions contained in it be referred to without in each case the prior express written consent of NBF.