CLIENT MARKET UPDATE · FIXED INCOME

Making Sense of the 2026 Bond Market

Prepared October 28, 2026 · Market data as of October 23, 2026; central bank decisions and 2-year yields as of October 28, 2026

Lindsey Hammond, Senior Wealth Advisor, Senior Portfolio Manager, Manulife Wealth Inc., Mindful Wealth Management

The short version

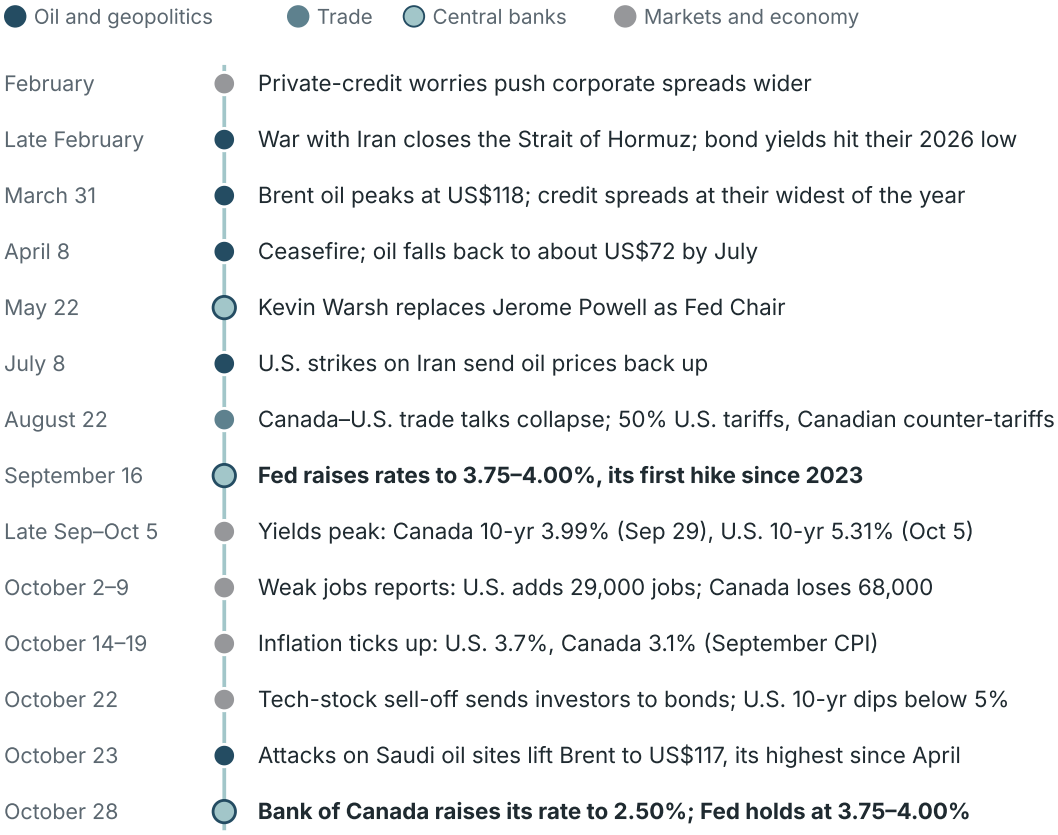
Bonds have had a bumpy 2026 because government interest rates rose, not because companies stopped paying their debts. Rising rates lower bond prices in the short run, but they also raise the income available to bond investors from here.

- **What happened:** an oil shock, new tariffs and stubborn inflation pushed yields up. The 10-year Government of Canada yield rose from 3.42% to 3.83% (Jan 1 to Oct 23), after peaking at 3.99% in late September. The U.S. Federal Reserve raised rates in September and held them steady on October 28. The Bank of Canada raised its rate to 2.50% on October 28, its first increase since 2023.
- **Credit spreads widened, but only modestly.** The extra yield on U.S. high-yield bonds is up about 0.6 percentage points this year. Past credit scares have seen 2 to 7 percentage points.
- **Negative bond years have been uncommon.** The U.S. bond market has had 5 down years in 50. In 4 of those 5 cases the following year was positive, though results have varied and a recovery is never guaranteed.
- **Today's yield has historically been one of the best guides to future returns.** The example funds in this report yield roughly 4.9% to 6.0% before fees. Higher starting yields have historically supported higher income and returns over time, but future results are not guaranteed.
- **Some of the risk is already reflected in prices.** The Bank of Canada's October hike was widely expected, and markets now expect at least one more by early 2027. Bond prices could still fall if rates rise more than expected, credit spreads widen or conditions change. If rates rise less than expected, prices could rise.

What happened in bonds this year

Inflation came back. A war-driven oil spike, new tariffs and heavy government borrowing pushed prices up, and bond markets responded by demanding higher yields.

Oil, tariffs and a Fed rate hike drove 2026

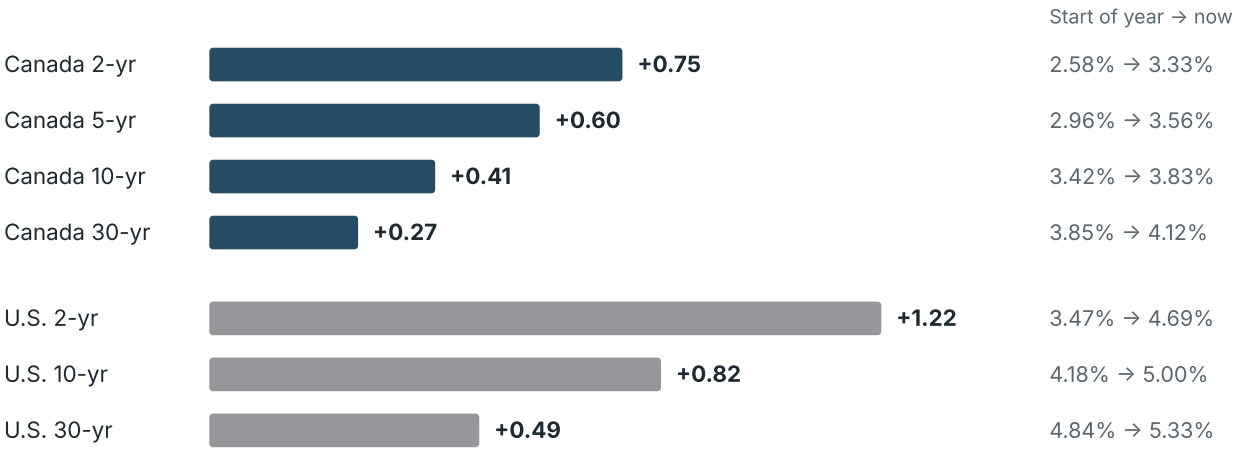


Key events of 2026 · sources listed at the end

When yields rise, the prices of existing bonds fall, because newer bonds pay more. That is the main reason bond funds have struggled lately.

Yields rose across the board in 2026, most at the short end

Rise in government bond yields since Dec 31, 2025, in percentage points (to Oct 23, 2026)



Source: Bank of Canada and U.S. Treasury daily yield data

Short-term yields rose most because they track what investors expect central banks to do next. The Bank of Canada held its rate at 2.25% for most of the year before raising it to 2.50% on October 28

(more on that below). Through September, the broad Canadian bond market (FTSE Canada Universe) was down 0.78% for the year. Shorter-term bonds held up better (+0.52%), while long-term bonds fell 3.12%. Yields have eased somewhat since early October.

Rates vs. spreads: what actually moved

This year's losses came mostly from rising government yields. The extra yield investors demand to lend to companies, called the credit spread, widened only a little.

A corporate bond's yield has two parts; in 2026 the government part moved most



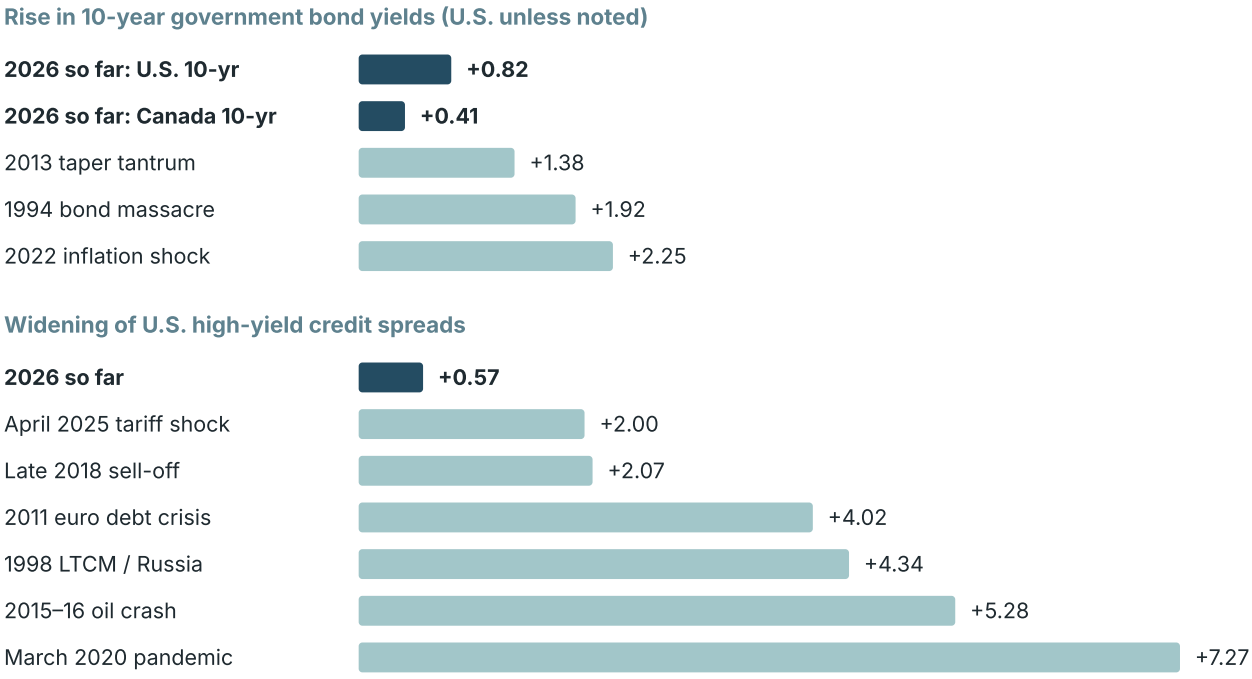
Illustration · 2026 moves from Bank of Canada, U.S. Treasury and ICE BofA data

- **U.S. high-yield spread:** 2.81% at the start of the year, 3.46% at its widest (March 30), 3.38% on October 23.
- **U.S. investment-grade spread:** 0.79% at the start of the year, 0.91% on October 23.
- **Canadian investment-grade spread:** roughly 0.8% to 1.0% through mid-year, based on manager reports (no current official figure).

Put in historical context, this is a mild move.

This year's spread widening is small next to past scares

Size of the move, in percentage points. 2026 shown in dark blue.



Not shown: 2008 financial crisis, when high-yield spreads widened by roughly 19 points.

Source: ICE BofA U.S. High Yield OAS (via FRED and published summaries); U.S. and Canada 10-year yields. Historical widening figures are approximate, measured from pre-episode lows.

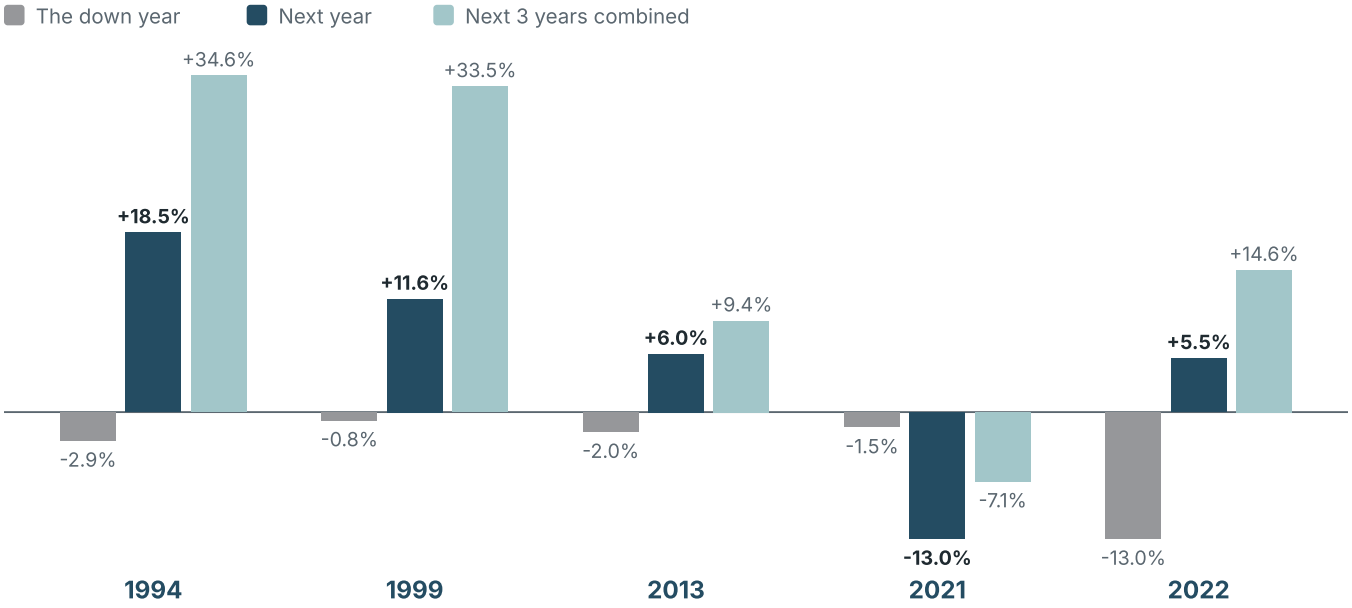
High-yield spreads are still below their long-run norm of about 5%. That suggests markets are not pricing in a recession or a wave of defaults, although spreads can widen quickly if conditions change. Through September, U.S. high-yield bonds were roughly flat for the year (+0.04%) while higher-quality U.S. corporate bonds were down 2.79%. The bonds with more credit risk held up better because their higher income cushioned the rate rise.

What has happened after years like this

Negative bond years have been uncommon. Historically, the years that followed have more often been positive than negative, though results have varied and past patterns do not guarantee future results.

After a down year, bonds were positive the next year in 4 of 5 cases

Every negative calendar year for the Bloomberg U.S. Aggregate Bond Index, 1976–2025, and what followed



Source: Hartford Funds, Bloomberg U.S. Aggregate calendar returns to Dec 31, 2025; multi-year figures compounded from annual returns

The one exception, 2021 into 2022, was the only time the U.S. bond market fell two years in a row. That happened because rates started near zero, leaving almost no income to cushion the fall. Today's starting yields are far higher.

Canada's record looks much the same. The FTSE Canada Universe Bond Index has had five negative years since 1980 (1994, 1999, 2013, 2021, 2022). The year after was +10.2% for 1999, +8.8% for 2013 and +6.7% for 2022. The exception again was 2021, followed by −11.7% in 2022.

Why today's higher yields may support future returns

Historically, a bond portfolio's starting yield has been one of the most reliable indicators of what it went on to earn over the following five years. It is not a guarantee: changes in interest rates, credit spreads and defaults also affect results.

- **For the U.S. bond market since 1976,** the starting yield explains about 91% of the variation in five-year returns (RBC BlueBay).
- **When the Canada 10-year yield has sat between 3% and 3.5%,** the Canadian bond market's return over the next 12 months has averaged 7.4% (Guardian Capital). It is now 3.83%. Past averages may not be repeated.
- **In the 12 months after the Fed's last rate hike** of five past cycles, U.S. bonds returned an average 10.6% (DeMarche). That figure only applies once hikes stop, and no one knows when that will be.

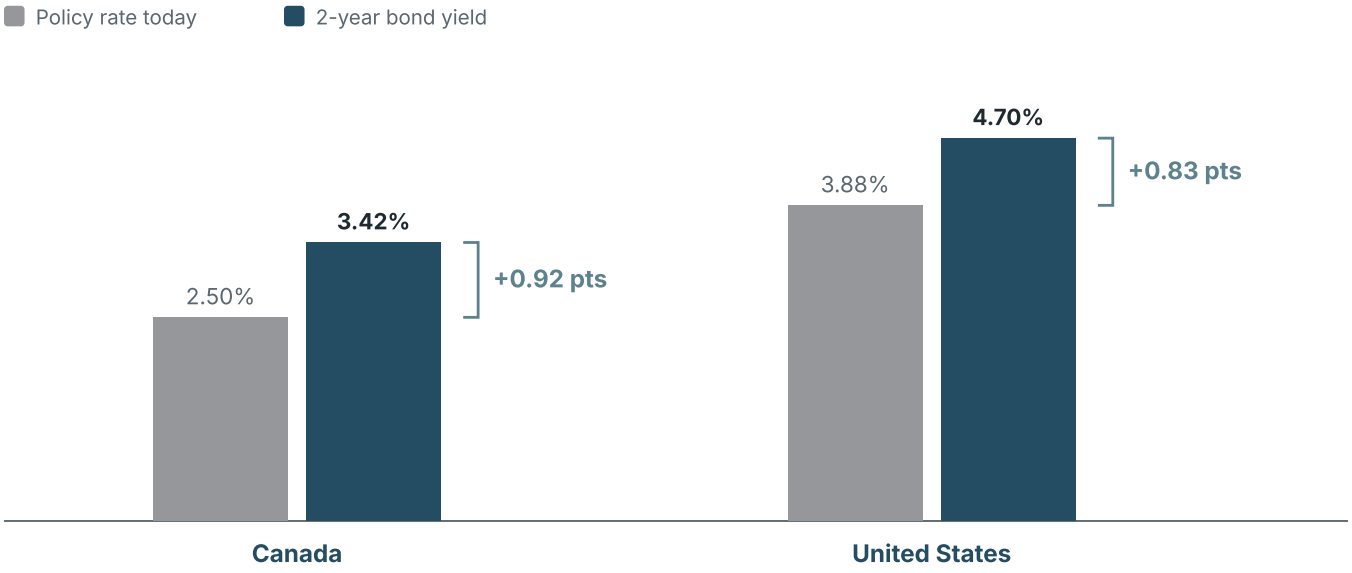
How bond prices “price in” rate hikes

Bond markets move on expectations, not announcements. By the time a central bank raises rates, bond prices have usually already adjusted.

Think of a 2-year bond as an alternative to rolling over a savings deposit for two years. If investors expect deposit rates to rise, they will only buy the 2-year bond if it pays about what they expect to earn on average. So when rate-hike expectations build, 2-year yields rise right away. Traders also track these expectations directly through futures and swap markets, which turn them into probabilities for each meeting.

Two-year yields still sit almost 1 point above policy rates: more hikes are priced in

Central bank policy rate vs. 2-year government bond yield, after the October 28, 2026 decisions, in %



The gap mostly reflects rate hikes investors expect over the next two years, plus a small premium for lending longer.

Source: Bank of Canada, Federal Reserve; 2-year yields near the close on Oct 28, 2026, as reported by Reuters and Investing.com

What is priced in today

- **Bank of Canada (now 2.50%):** on October 28 the Bank raised its rate by 0.25 points, its first hike since July 2023. Markets had put the odds at about 78%. The Bank said inflation is “higher and more persistent” than it expected in July. It now expects inflation to reach about 3.5% by the end of 2026, average about 3% in 2027 and return to about 2% by mid-2028. It said “there could be a need to increase the policy rate further,” but it will proceed carefully. Markets now put the odds of another hike on December 9 at about 45%, with a second hike fully priced by January.
- **Market reaction:** Canada's 2-year yield rose about 0.05 points to roughly 3.42%, its highest since August 2024. That is a small move, because the hike was largely already in prices.
- **U.S. Federal Reserve (3.75–4.00%):** the Fed held rates steady on October 28, as markets expected. Two of the 12 voting members preferred a hike. Markets now put the odds of a hike on December 9 at about 80%.
- **Inflation:** bond prices imply U.S. inflation of about 2.3% a year over the next decade, and about 2.25% in Canada over the long term. That is above the 2% targets, but well below today's headline inflation (3.7% U.S., 3.1% Canada).
- **Extra pay for lending long:** in September, investors demanded the largest premium for holding long-term U.S. bonds since 2011, by one common measure.

Why this matters

Because expected rate hikes are already largely reflected in today's prices, what matters most is how events compare with those expectations. Rates rising more than expected, wider credit spreads or other shocks could push bond prices lower. Rates rising less than expected could push them higher. Either way, bonds continue to pay interest along the way.

If this happens...	Rates	What it could mean for bonds
Hikes arrive about as expected	Little change from today	Returns may be roughly in line with current yields of about 5%, though results will vary
Inflation stays hot; more hikes than expected	Rise further	Short-term price declines, then higher income going forward
Economy slows (tariffs, weak jobs); hikes don't come	Fall	Price gains on top of income

Canadian mutual fund examples

These five Canadian bond mutual funds show how different active managers have handled this market. None is a plain government bond fund, and their approaches range from conservative to flexible.

Fund snapshot

Fund (code)	What it does	Yield to maturity (as of)	Duration, yrs (as of)	MER	Rate-rise cushion[1]
PIMCO Monthly Income Fund (Canada) PMO205	Global, multi-sector bonds; focus on steady monthly income	5.39%[2] Mar 31, 2026	2.7[2] Mar 31, 2026	0.85%	~2.0 pts
Lysander-Canso Corporate Value Bond LYZ801F	Deep-value corporate bonds; currently high quality	5.8% Sep 30, 2026	3.9 Sep 30, 2026	0.89%	~1.5 pts
PICTON Income Fund PIC8501 (formerly Fortified Income)	Mostly Canadian corporate bonds, with hedges to limit losses	6.04% Sep 30, 2026	2.7 Sep 30, 2026	1.13%	~2.3 pts
Canoe Unconstrained Bond Portfolio Class GOC5163	Flexible global bonds; manager shifts quality and duration actively	4.86%[2] Aug 31, 2026	5.8[2] Aug 31, 2026	0.99%	~0.8 pts
CI Corporate Bond Class CIG54043	North American corporate bonds, mostly investment grade with roughly a third in high yield (avg. BBB)	5.60%[2] Aug 31, 2026	4.25[3] date not stated	0.87%	~1.3 pts

Annualized returns to September 30, 2026

Fund	YTD	1 yr	3 yr	5 yr	10 yr	Since inception (start)
PIMCO Monthly Income	−3.30%	−1.16%	5.31%	2.25%	3.22%	6.34% (Jan 2011)
Lysander-Canso Corporate Value	−0.65%	−1.16%	4.50%	2.56%	5.47%	6.02% (Dec 2011)
PICTON Income	−0.61%	−0.04%	5.84%	3.04%	4.28%	4.95% (Nov 2015)
Canoe Unconstrained Bond Class	−3.74%	−3.35%	3.55%	—	—	2.74% (Aug 2023)
CI Corporate Bond Class	0.06%	0.29%	6.36%	2.25%	3.46%	3.57% (Aug 2012)

September was a weak month for bonds, which pulled down year-to-date and 1-year results. Over three years, all five funds are up between 3.5% and 6.4% a year.

Lysander-Canso, PICTON and CI returns are confirmed by the fund companies; PIMCO and Canoe are from Fundata.

Calendar-year returns, 2016 to 2025

Fund	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
PIMCO Monthly Income	7.6%	6.9%	0.6%	7.1%	4.2%	1.6%	−6.6%	7.9%	5.1%	9.2%
Lysander-Canso Corp. Value	8.8%	2.4%	0.6%	5.4%	22.0%	12.7%	−6.4%	8.1%	7.2%	3.6%
PICTON Income	17.4%	9.2%	−1.9%	6.5%	6.8%	3.5%	−5.6%	7.1%	8.6%	6.5%
Canoe Unconstrained Bond	—	—	—	—	—	—	—	—	2.5%	7.7%
CI Corporate Bond Class	5.5%	5.0%	−1.1%	9.7%	6.2%	3.7%	−9.7%	8.3%	9.0%	4.6%

Over the past 10 years these funds lost money only in 2018 and 2022, and every losing year was followed by a gain.

All returns are Series F, after fees.

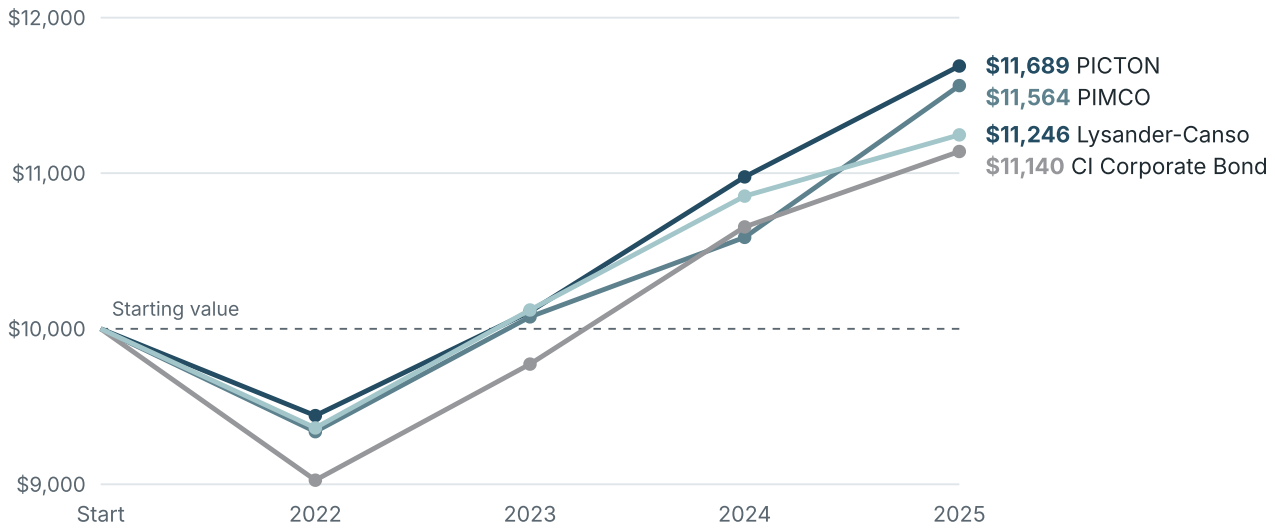
[1] **Rate-rise cushion** = yield ÷ duration. It is a rough guide to how far yields could rise over a year before price losses use up the fund's income. It ignores changes in credit spreads.

[2] From a third-party data provider (YCharts) rather than the fund company. Canoe figures are for the underlying Canoe Unconstrained Bond Fund (GOC5063); Canoe's June 30 report says it reduced duration during 2026, so the current figure may be lower.

[3] CI reports a duration of 4.25 years and a yield of 6.51% on its fund page without an as-of date.

Every fund that lived through 2022 had made back its loss by the end of 2024

Growth of $10,000 invested Jan 1, 2022, after fees, at each year-end



Source: Fundata / Fund Library and CI fund profiles, calendar returns to Dec 31, 2025 · Canoe Unconstrained Bond launched Aug 2023, so is not shown

How the managers are positioned

- **PIMCO** has been cautious on corporate bonds because spreads were tight, favouring high-quality government and mortgage bonds and holding extra cash to buy into weakness.
- **Canso** says there is little room for spreads to narrow further and leans heavily toward high-quality bonds.
- **PICTON** expected spreads to stay near their lows and is using hedges and careful duration management.
- **Canoe's manager (Reams)** cut high yield and shortened duration earlier this year, after strong gains, to keep cash ready for better prices.
- **CI's fixed income team (led by Geof Marshall)** says recent volatility has raised yields in corporate credit, especially shorter-term bonds. It is emphasizing high-quality credit, disciplined high-yield exposure and strong income, while staying cautious on sectors facing higher refinancing costs.

What this means for you

The bond portion of your portfolio is designed to generate income and help reduce overall portfolio volatility. That role has not changed, even in a year of modest returns.

- **Income is higher than it has been in years.** With yields of roughly 5% to 6%, bond funds like these start each year with a larger income cushion against rate rises than they had a few years ago.
- **Some of the expected bad news is already in prices.** Further losses could come from rate hikes beyond what markets expect, wider credit spreads or other market factors. If rates rise less than expected, or fall, bond prices could benefit.
- **Past recoveries have often been relatively quick.** The example funds made back their 2022 losses within one to two years, although past performance does not guarantee future results.
- **Active managers can adapt.** Each of these funds can change its credit quality and interest-rate sensitivity as conditions change.

The Bank of Canada raised rates on October 28, as markets expected, and the Fed held steady. We will be watching the federal budget on November 5 and both central banks' December 9 decisions, and will talk through any changes with you. If rebalancing is warranted, higher bond yields can make adding to bonds more attractive.

Important information

This material is for general information only and is not to be construed as an offer or solicitation, or as personal investment, tax or legal advice. The securities mentioned may not necessarily be considered suitable investments for all clients. Contact your Advisor to discuss your individual investment needs.

Past performance does not guarantee future results; fund values and yields change often. Commissions, trailing commissions, management fees and expenses may apply; please read the fund facts and prospectus before investing. Market data are from the sources below and are believed reliable but not guaranteed. Some figures are preliminary, from third-party data providers or from manager commentary, as noted.

Sources

- Government bond yields: Bank of Canada bond yields; U.S. Treasury daily yield curve
- Central banks: Bank of Canada, Sep 2, 2026 decision; Federal Reserve, Sep 16, 2026 statement; J.P. Morgan on the September FOMC
- Credit spreads: ICE BofA U.S. High Yield OAS (FRED); Canso July 2026 newsletter; Algonquin Capital, April 2026
- Market pricing: TD Economics on the BoC; money.ca on BoC hike odds; U.S. 10-yr breakeven (FRED)
- 2026 events: CNBC, 10-yr Treasury at highest since 2007; Energy Now, oil prices Oct 2; Al Jazeera, Warsh sworn in
- October 2026 update: Statistics Canada, September CPI; BLS, September CPI; Reuters poll on the Bank of Canada; Canadian Press on BoC hike odds; FXStreet on Fed odds; The Hub on Macklem; The Hub, September jobs; GV Wire/Reuters on oil; ICE BofA U.S. IG OAS (FRED)
- October 28 decisions: Bank of Canada press release; BNN Bloomberg on the BoC hike; CP24 on the inflation outlook; Reuters via Kitco on Canadian yields; Investing.com; Fortune on the Fed; Fox Business; FN News on FedWatch odds; AOL on U.S. yields
- Index returns: iShares XBB (FTSE Canada Universe); XSB; XLB; Bloomberg U.S. Aggregate (YCharts)
- History: Hartford Funds, Why Patience Can Pay Off for Bond Investors; Mawer Canadian Bond Strategy; Canso, January 2014; Morgan Stanley IM on 2025 spreads; SEI on 2020 high yield
- Starting yields and returns: RBC BlueBay; DeMarche on hiking cycles; CME FedWatch methodology
- Funds: PIMCO (Fund Library); Lysander-Canso; PICTON Income Fund (Fund Library); PICTON 2026 Fixed Income Outlook; Canoe (Fund Library); CI Corporate Bond Class monthly profile; CI annual management report; Canoe interim report, June 2026; PICTON fund profile; YCharts PMO205, GOC5063