MARKET UPDATE FROM THE GLOBAL CIO OFFICE

MARCH 2020

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Investor anxiety morphed into panic in February. Financial markets were rattled by the latest headlines around the novel coronavirus, with investors attempting to gauge the severity of the widening epidemic and the implications for global growth. While the outbreak has slowly been abating in China and businesses have gradually resumed operations, news that the deadly virus has spread outside of China (to Korea, Japan, Iran and Italy) has stoked fears of a wider pandemic and a more pronounced global economic slowdown. Risk appetite dwindled in response, with the gloomy mood manifesting itself and sending shockwaves through the global marketplace.

FINANCIAL MARKET DASHBOARD

	FEB. 28, 2020	FEB.	YTD	1 YEAR
EQUITY MARKETS		% PRICE CHANGE (LC)		
S&P 500	2954	-8.41%	-8.56%	6.10%
S&P/TSX	16263	-6.09%	-4.69%	1.65%
MSCI EAFE	1810	-9.23%	-11.16%	-3.42%
MSCI EM	1006	-5.35%	-9.79%	-4.32%
FIXED INCOME (%)		BASIS POINT CHANGE		
US 10 Year Bond Yield	1.15	-35.8	-76.9	-156.6
US 2 Year Bond Yield	0.91	-40.0	-65.6	-160.1
US Corp BBB Spread	1.45	13.0	20.0	-18.0
US Corp High Yield Spread	5.08	107.0	181.0	126.0
CURRENCIES		% PRICE CHANGE		
CAD/USD	0.75	-1.15%	-3.00%	-1.61%
EUR/USD	1.10	-0.60%	-1.67%	-3.03%
USD/JPY	107.89	-0.42%	-0.66%	-3.14%
COMMODITIES		% PRICE CHANGE		
WTI Oil (USD/bbl)	44.76	-13.19%	-26.70%	-21.78%
Copper (USD/pound)	2.55	1.15%	-8.97%	-13.69%
Gold (USD/oz)	1566.70	-1.02%	2.86%	19.04%

After breaching all-time highs, global equity markets abruptly reversed course and entered full-blown correction-mode in February. The MSCI All Country World tumbled lower, while the S&P 500 dropped over 15% from its mid-February record high. The S&P/TSX also got caught up in the wave of selling, while MSCI's gauge of emerging market stocks outperformed their developed market peers and fell more modestly as investors embraced pledges from Chinese policymakers to revive the economy.

Mounting fears about the global impacts of the fast-spreading coronavirus saw traders seek a refuge in government bonds and drove yields to unprecedented lows, while expectations for weaker global growth, declining inflation expectations, and increased bets for central bank easing also added to the downward move. While both the 10- and 30-year treasury yields breached new lows, the 2-year treasury yield sunk even further as investors ramped-up their wagers for Federal Reserve easing and are now pricing close to four fed fund rate cuts by year-end. In the end, the Federal Reserve validated the market's dovish expectations and announced an emergency 50 basis point rate cut in early-March to shield the economy in the face of evolving virus-related risks.

The greenback thrived in February as investors bid-up the haven currency in what was an erratic month, underscoring the dollar's reserve status and the US economy's relative resilience. The dollar gained against most of its peers, with the exception of the Japanese yen that was also buoyed by haven flows. In contrast, the pound faltered after PM Johnson threatened to walk away from trade talks with the EU if its not clear a comprehensive trading agreement will be reached by June, while the Canadian dollar slid to an eight-month low alongside the severe pullback in crude prices.

Finally, the shock from the viral outbreak saw commodity prices plunge lower as the fast-spreading epidemic sparked fears about global growth prospects and accordingly, commodity demand. Oil assumed the brunt of the weakness and slipped below $45/barrel ahead of a crucial OPEC+ meeting about whether to extend the current production curbs in an effort to stabilize prices. Even gold (a traditional safe haven) wasn't immune as investors were forced to take profits to cover their equity losses and margin calls. Interestingly, copper edged marginally higher in February as the profound policy response from Chinese policymakers saw the red metal regain some stability after the steep sell-off in 2020.

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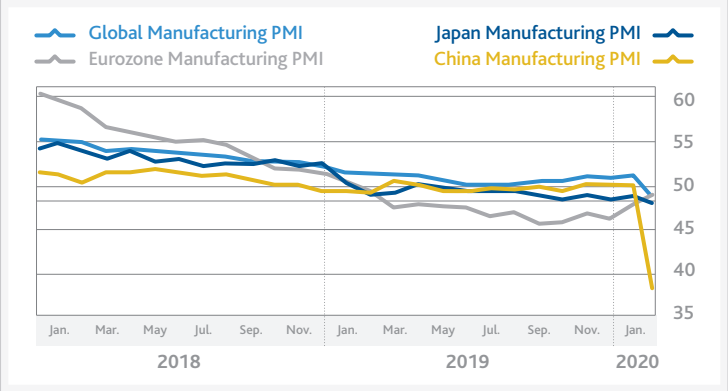
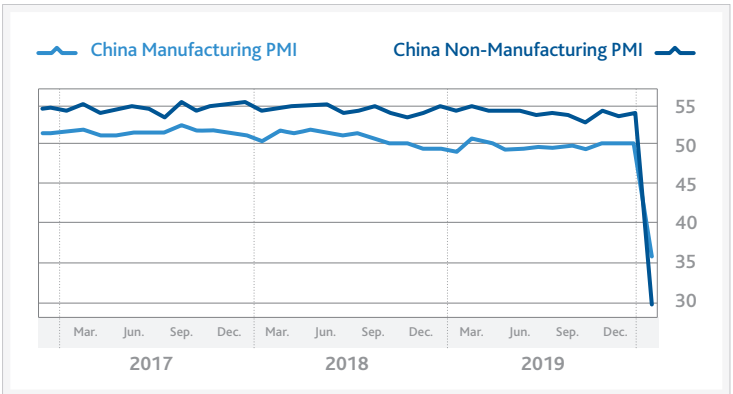
The ISM factory gauge retreated to near-stagnation in February as concerns mounted that the world's largest economy won't be able to dodge the hit from the coronavirus. Encouragingly, the services side of the economy demonstrated some notable momentum and posted its fastest growth in a year – though weakness is likely to emerge in March as reduced tourism weighs on travel and hospitality.



The Global Manufacturing PMI snapped a three-month streak of expansionary readings and was pummelled back into contraction terrain in February as businesses braced for the fast-spreading coronavirus to weigh on activity – with both production and export orders deteriorating substantially during the month. While several regions registered contraction, the decline was driven by record weakness in the Chinese factory sector.



Activity in China's manufacturing sector contracted sharply in February, with the official gauge plunging to the lowest level on record (35.7) amid factory closures and supply chain disruptions. Similarly, the non-manufacturing gauge fell to an all-time low of 29.6 as the Chinese services sector was hard-hit by quarantines that sharply reduced consumer spending and tourism.

CANADA

While the Canadian economy came to a virtual standstill at the end of 2019, December's robust results provided a strong handoff into 2020. Together with simmering trade tensions and the reversal of several temporary factors that weighed on growth late last year, the economy was on the path to recovery early-on in 2020. Regrettably, the COVID-19 outbreak has fuelled a profound collapse in commodity prices and supply-chain disruptions in the manufacturing space that have dampened hopes for a swift rebound, while transportation blockages on the rail network are certain to weigh on growth in the near-term. That said, pledges for government fiscal stimulus and an easier monetary policy stance from the Bank of Canada suggest that any growth slowdown will be transitory in nature and should provide some relief for the economy later this year.

USA

The US economy was on solid ground leading up to the coronavirus crisis. While business optimism was buoyed by reduced policy (trade) risks following the US-Sino and USMCA trade deals late last year, the consumer remained resilient amid solid employment and wage gains that bolstered confidence and spending. However, the economy will not be immune to virus-related risks amid impaired supply chains, weaker production, slower global demand, and lost business revenues. And while the extent of the outbreak in the US remains unknown, fear is likely to grip consumers and weigh on spending and hiring in the near-term. After conveying a degree of complacency and reaffirming that its comfortable with its current policy stance, the Federal Reserve abruptly switched gears in early-March and announced an emergency half point rate cut to limit the fallout and extend the record-long expansion in the US.

INTERNATIONAL

The near-term impacts of the fast-spreading coronavirus are being felt on the global scale. After spending three straight months in expansion terrain, global factory activity contracted by the most since 2009 in February as the outbreak severely disrupted demand, trade, and supply chains. Not surprisingly, the slump largely reflects weakness in China. Outside of China, weakness was more limited - though the full effects have yet to be felt and will indeed spillover more broadly in the next month. Indeed, already-fragile German and Japanese economies are particularly vulnerable due to their export-oriented nature and their supply chain linkages to China. However, similar to previous epidemics, weakness should largely prove transitory in nature and result in a V-shaped recovery later this year, while the flood of fiscal and monetary stimulus from policymakers worldwide should also lend support.

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