



2020 Capital market year in review

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A year to remember... and a year to forget

Regional equity indices	2019 Total return	Index level		2020	
		31-Dec-19	31-Dec-20	Price return	Total return
S&P/TSX	22.8%	17,063	17,433	2.2%	5.6%
S&P/TSX Small Cap	15.8%	595	655	10.0%	12.9%
Dow Jones Industrial	25.3%	28,538	30,606	7.2%	9.7%
S&P 500	31.5%	3,231	3,756	16.3%	18.4%
Russell 2000	25.5%	1,668	1,975	18.4%	19.9%
Nasdaq	36.7%	8,973	12,888	43.6%	45.1%
MSCI All Country World	27.3%	565	646	14.3%	16.8%
MSCI Europe	26.8%	140	132	-5.4%	-2.8%
MSCI EAFE	22.8%	2,037	2,148	5.4%	8.4%
MSCI Emerging Markets Index	18.8%	1,115	1,291	15.8%	18.5%

Fixed income indices	2019 Total return	Index level		2020 YTD total return
		31-Dec-19	31-Dec-20	
FTSE Canada Universe Bond	6.9%	1,124	1,221	8.7%
FTSE Canada All Corporate Bond	8.1%	1,285	1,397	8.7%
Bloomberg Canada High Yield	9.5%	147	158	7.2%

Currencies	31-Dec-19	31-Dec-20	% change
CAD/USD	0.77	0.79	2.0%
CAD/EUR	0.69	0.64	-6.4%
EUR/USD	1.12	1.22	8.9%
GBP/USD	1.33	1.37	3.1%
USD/JPY	108.61	103.25	-4.9%

Bond yields	31-Dec-19	31-Dec-20	bps change
10 yr Canada Govt.	1.70%	0.68%	-103
10 yr U.S. Treasury	1.92%	0.91%	-100
10 yr Germany Govt.	(0.19)%	(0.57)%	-38
10 yr Japan Govt.	(0.01)%	0.02%	3
30 yr Canada Govt.	1.76%	1.21%	-55
30 yr U.S. Treasury	2.39%	1.64%	-74

Commodities	31-Dec-19	31-Dec-20	% change
Gold US\$/oz.	1,517.27	1,898.36	25.1%
Oil US\$/bbl.	61.06	48.52	-20.5%

All figures quoted in the text are price only return, local currency, unless otherwise noted
Source: Bloomberg December 31, 2020

2020 was a year that defied expectations in many ways and has unquestionably altered the fabric of our everyday lives. It's hard to believe the year started on a positive note with the US and China ratifying Phase I of the trade deal, leading many equity markets to post fresh all-time highs in February. Then came the COVID-19 pandemic, where the world, and in turn, capital markets were drastically turned upside down. The global economy abruptly ground to a halt and stock markets plummeted, as businesses were forced to close and consumers were placed under strict lockdowns to contain the spread of the virus.

Dramatic change and dramatic policy actions went hand in hand. Central banks around the globe slashed interest rates to near-zero, flooded financial markets with ample liquidity and backstopped risk assets. Meanwhile, world governments provided trillions of dollars in relief to their citizens. The unprecedented coordinated response was enough to provide much-needed stability to capital markets for the rest of the year, ushering in a 'V' shaped recovery for risky assets and allowing most major equity indices to finish in the green. During the worst of the fear and uncertainty, sovereign bond yields tumbled to historic lows and credit spreads widened substantially.

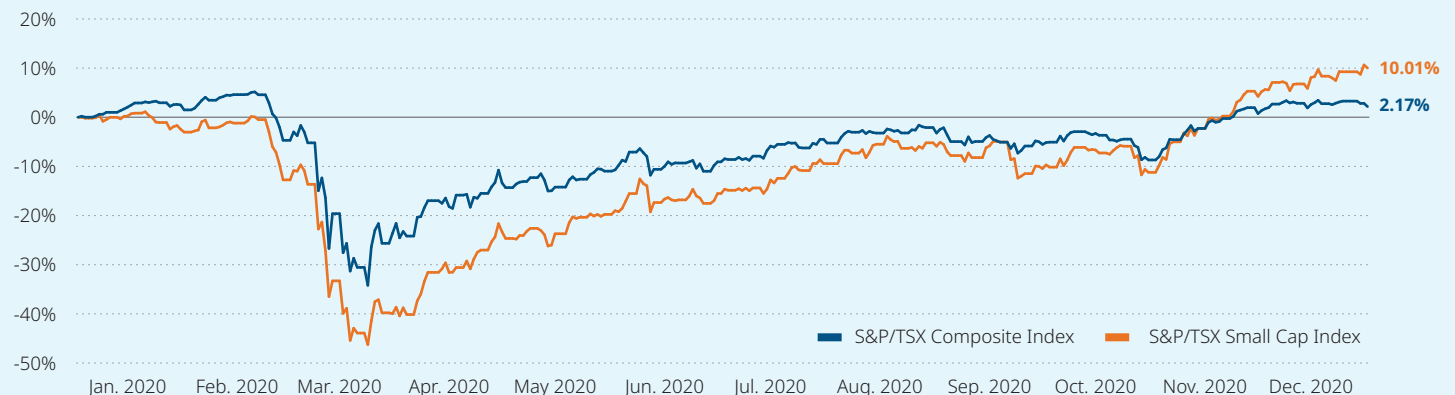
The year closed out with light emerging at the end of a dark tunnel. The launch of the largest vaccination campaign in history brought a hope-inspired belief for the potential of an eventual return to normalcy. This along with expectations for additional fiscal support in the US, and the US election in the rear-view mirror sent equity markets even higher and brought sovereign bond yields off their deepest levels.

A key theme for 2021 is whether the long-awaited rotation into value stocks, which occurred in the latter part of 2020, will continue. The positive vaccine news has triggered investors to begin shifting from richly priced growth stocks into value, with cyclical stocks such as banks, energy and industrials playing catch-up in anticipation of a resumption of economic activity in 2021.

Canadian equity

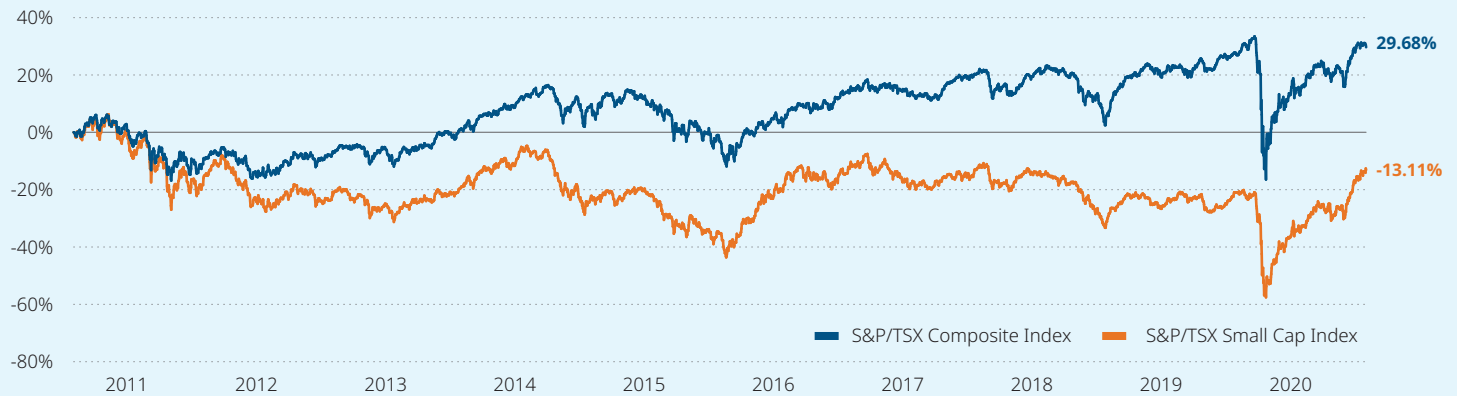
Canadian equities fared worse than their global peers, with the S&P/TSX Composite rising 5.6% (total return) following the 22.8% jump in 2019. Canadian capital markets were aided by monetary and fiscal supports. The Canadian government introduced the Canadian Emergency Response Benefit program which gave \$2,000 a month to Canadians directly affected by COVID-19. The Bank of Canada cut interest rates by 150 basis points in three emergency meetings, taking the overnight rate to 0.25%. The Canadian fiscal response came in at CAD\$354 billion. The Bank of Canada's balance sheet expanded to CAD\$548 billion, up from CAD\$125 billion pre-crisis.

S&P/TSX Composite & S&P/TSX Small Cap – 1 year performance



Source: Bloomberg December 31, 2020

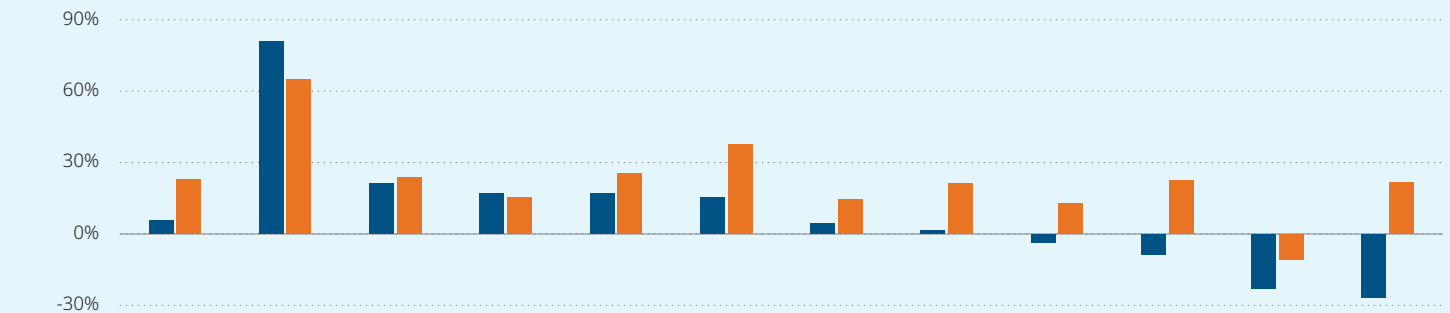
S&P/TSX Composite & S&P/TSX Small Cap – 10 year performance



Source: Bloomberg December 31, 2020

Hefty gains in the information technology (IT) and materials sectors were offset by the slumping energy sector (which began the year at 17% weight of the S&P/TSX Composite only to end the year at 11% weight). IT stocks were the best performers (a third consecutive year in a row), spearheaded by e-commerce enabler, Shopify's blistering 178% surge. The materials sector also contributed significantly, aided by its large exposure to gold. The heavily-weighted financials sector fell during the pandemic with the sudden halt in economic activity, a plunge in global yields and flattening out of the yield curve. Canadian banks were forced to set aside massive amounts of money for loan-loss provisions to absorb anticipated loan defaults. However, they were able to pair losses toward the end of the year, rallying 19% from Oct. 28 to year-end, as credit concerns receded and investors began looking ahead to the possibility of a sharp rebound in economic growth in the new year. The energy sector was the main detractor in the index, nosediving over 30% in the year. An untimely price war between Saudi Arabia and Russia occurring simultaneously with the pandemic-induced cratering of global oil demand sent oil prices tumbling.

S&P/TSX sector total returns (%)



	S&P/TSX Composite Index	IT	Materials	Consumer Disc.	Industrials	Utilities	Consumer Staples	Financials	Telecom Services	Real Estate	Health Care	Energy
FY 2020	5.6%	80.7%	21.2%	17.1%	17.0%	15.3%	4.3%	1.6%	-3.7%	-8.7%	-23.0%	-26.6%
FY 2019	22.8%	64.9%	23.8%	15.3%	25.5%	37.5%	14.4%	21.4%	13.0%	22.6%	-10.9%	21.7%

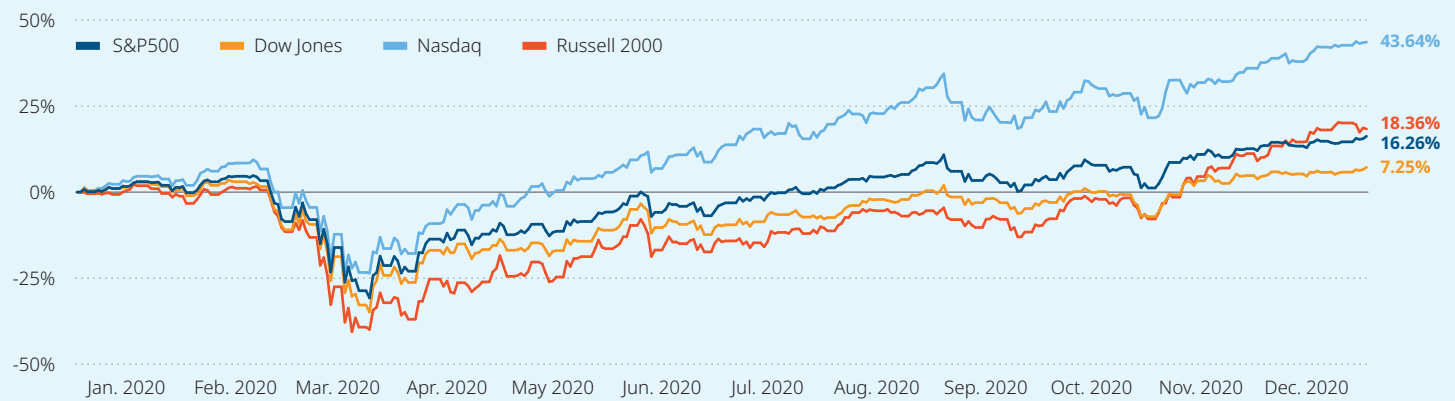
Source: Bloomberg December 31, 2020



US equity

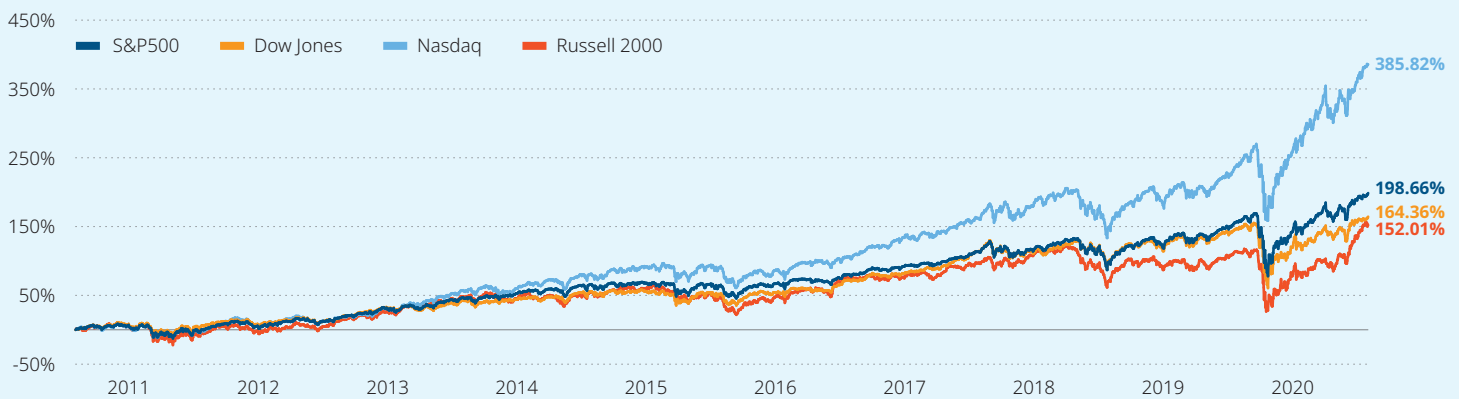
All major large and small cap US equity benchmarks posted new record highs (S&P 500, DOW, NASDAQ and Russell 2000). The S&P 500 rebounded strongly following the sharp COVID-19 drawdown in March, bouncing 18.4% (total return) higher over the year and outperforming its global peers. The pandemic was the catalyst for the largest and most sudden global stock market crash since 1929. With stretched equity valuations already in place to start the year, the S&P 500 plunged 34% in just 23 trading days. Equipped with lessons from the Great Financial Crisis, the US Federal Reserve quickly and aggressively slashed the Federal Funds rate to near zero and launched a massive \$700 billion quantitative easing program. On the fiscal policy side, the US government launched multiple programs, highlighted by the CARES Act, which provided a massive USD\$2.3 trillion of support to individuals and businesses. The extraordinary support led to the sharpest 5-month rally in 80 years for the S&P 500, taking only 126 trading days to climb out of its short-lived bear market (defined as a 20% decline). To put this into perspective, it has historically taken around 1,500 trading sessions or six years to complete this feat.

US equity indices - 1 year performance



Source: Bloomberg December 31, 2020

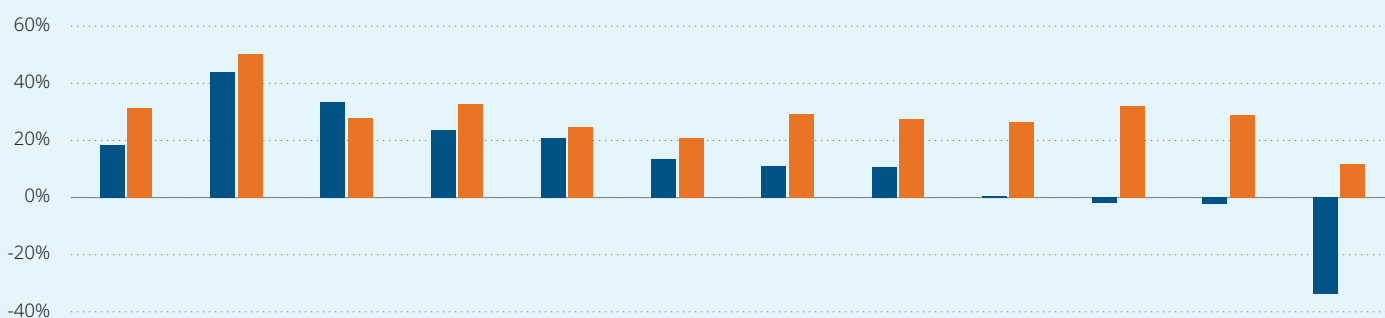
US equity indices - 10 year performance



Source: Bloomberg December 31, 2020

The remarkable rebound in US indices is also attributable to their favourable sector compositions, which was a key theme and driver in equity performance across regions globally. Information technology (IT) stocks were largely unaffected by the pandemic and instead, enjoyed a strong tailwind from the acceleration of existing trends calling for digital transformation in online communication platforms, cloud services and e-commerce. In particular, the mega-cap US tech stocks were the clear winners this year, with the five largest companies in the S&P 500 (Apple, Microsoft, Amazon, Facebook and Google's parent company Alphabet) driving more than half of the 18% gain (total return) for the S&P 500 in 2020, with their combined share of the index rising from 17% in December 2019 to 22% in December of 2020. More broadly, the IT heavy NASDAQ Composite Index (~50% weight) surged almost 45% (total return). US equities also benefitted from a resilient US consumer, less-strict lockdowns and a jump in health care stocks to combat the virus.

S&P 500 sector total returns (%)



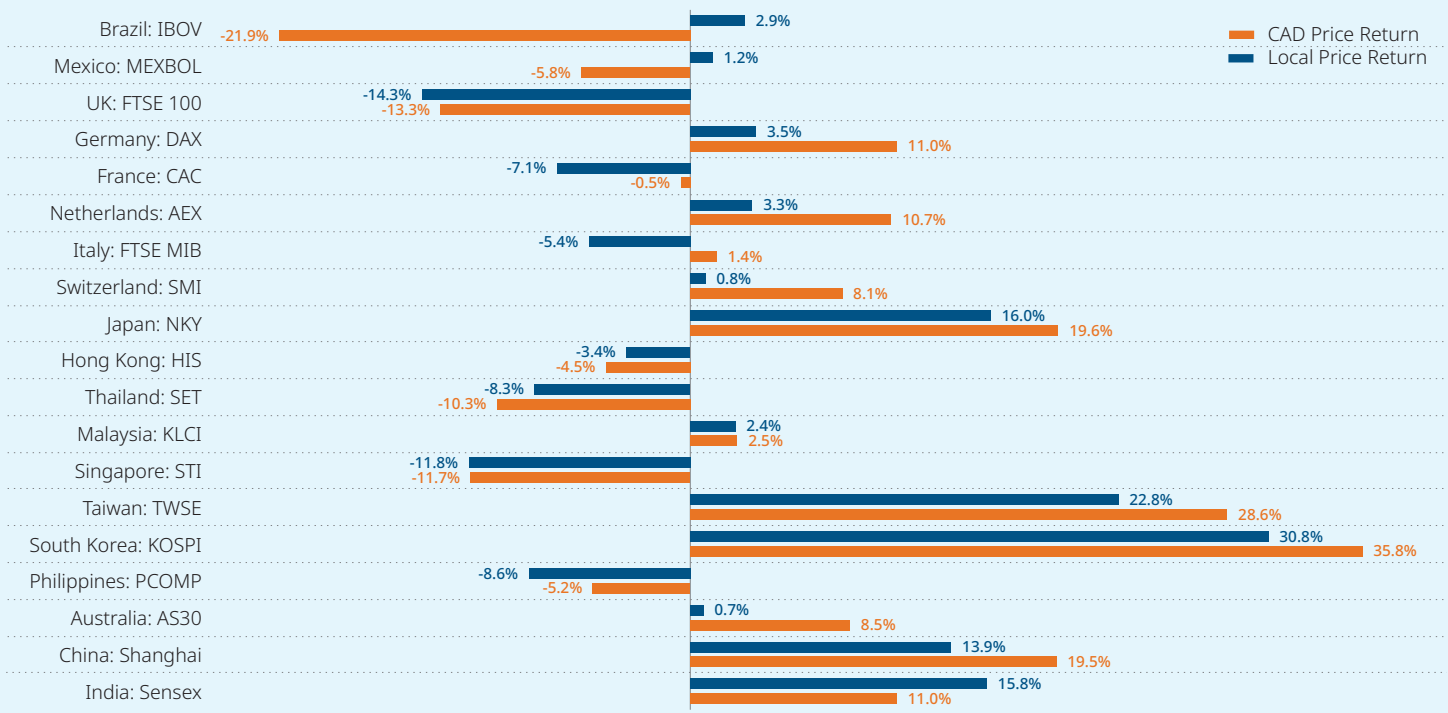
Source: Bloomberg December 31, 2020

International equities

International equities faced similar sector headwinds as Canada, as the value oriented MSCI EAFE Index delivered an 8.4% total return in the year. The devastating impact of the pandemic on Europe weighed on overall EAFE (Europe, Asia, Far East) performance. Despite the strong response from governments and having a firm grasp on the virus through the summer, an autumn second wave of cases forced cities back under strict lockdown measures once again. The more deeply impacted countries such as Italy, France and Spain lost more than 5% in the year, with the latter faring the worst, down 16%. UK equities lagged most of their peers, as the FTSE 100 slid 14% lower. The country not only struggled to contain the virus but was also hurt by rising uncertainty stemming from the UK's departure from the European Union (Brexit). Japanese equities, long underperformers, were surprisingly strong, with the Nikkei 225 Index jumping 16%. Japanese stocks were bolstered by the country's ability to contain the virus (top 5 in Bloomberg's COVID Resilience Rankings) and benefitted from a handful of its largely COVID-winning technology names such as Softbank, Sony, M3 Inc, Keyence and Nintendo.

Emerging market (EM) equities had a strong year, as the MSCI Emerging Market Index kept pace with the S&P 500. Due to two main tailwinds: favourable sector composition; and China, Taiwan and South Korea’s ability to better control the virus that allowed for a strong rebound in economic activity. Contrary to popular belief, emerging market indices have shifted from a reliance on commodities and financials to becoming heavily tilted to the information technology (IT), consumer discretionary and communication services sectors, while still having significant exposure to the materials sector. This evolution allowed EM equities to participate in both the growth rally and the value rotation as these four sectors (that are among the top five weights in the index) all posted between 20% and 55% returns. China, Taiwan and South Korea make up over 65% of the EM index (at 39%, 13% and 13% respectively). These countries demonstrated an ability to contain the virus and recover quicker than their global counterparts, allowing economic activity to resume with fewer economic setbacks than in North America and Europe.

Global equity markets – 1 year performance (price return) in local and Canadian currency



	Canada	US	Europe/Asia/Far East	Emerging Markets	World
	S&P/TSX	S&P 500	MSCI EAFE (USD)	MSCI EM (USD)	MSCI World (USD)
Local currency returns	2.2%	16.3%	5.4%	15.8%	14.1%
Canadian \$ based returns	2.2%	14.4%	3.7%	14.0%	12.2%

Source: Bloomberg December 31, 2020

Canadian fixed income

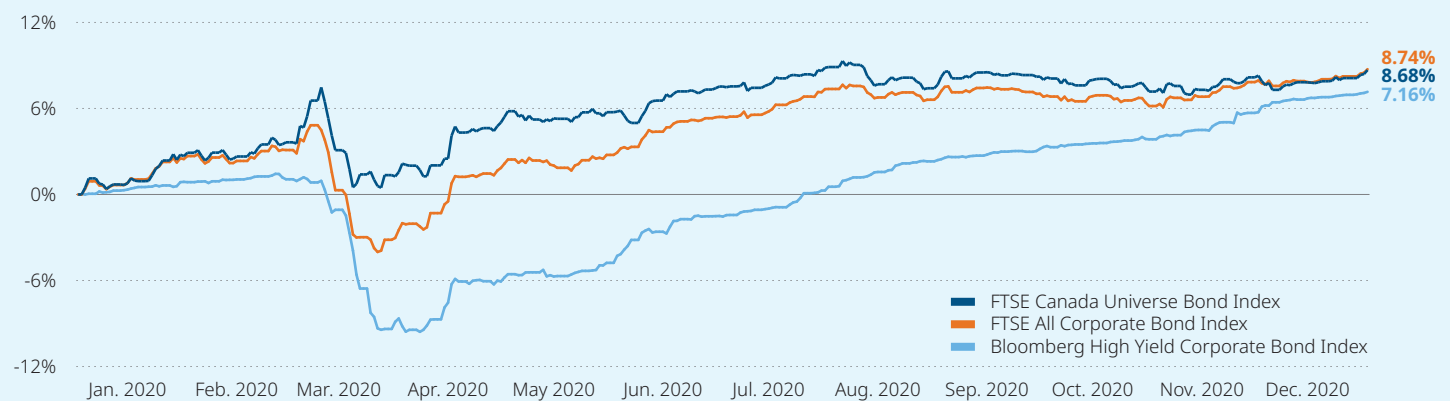
The FTSE Canada Universe Bond Index produced a robust 8.7% total return, exceeding the 6.9% mark set last year. Global yields plummeted to historic lows due to central banks cutting rates to near-zero and launching large-scale quantitative easing programs. However, yield curves steepened (long rates rising with short rates anchored) in the second half of the year on the back of positive vaccine news. All in all, longer-term bonds outperformed relative to their shorter maturity counterparts.

Credit spreads widened out significantly during the worst of the risk-off environment in the spring. This was quickly arrested as central bank intervention extended deep into credit markets. In addition to purchasing sovereign bonds in order to lower the overall yield environment, central banks pledged to buy just about anything and everything credit related, from investment-grade corporate bonds, mortgage-backed securities and in the case of the US Federal Reserve, wading into high yield markets. Buoyed by the notion that central banks “have their backs” investors bought up record debt issuance as they sought both to reach for yield and to gain exposure to bonds of companies in capital intensive and heavy cash-burn industries most beaten down by the pandemic (e.g. airlines, travel, tourism and hospitality).

On a sector level in Canada, investment-grade corporate bonds were able to recover quickly from their small losses earlier in the year and matched the 8.7% return of government bonds amid rapidly narrowing credit spreads. Within the government sector, the municipal and provincial bond indices outpaced the federal index. Within credit, investment-grade bonds edged out high-yield bonds on the year.

The year in fixed income was not without its trials. Market dislocation, unlike any witnessed since the 2008 financial crisis, took hold for a brief period in March. In the 13 trading days between March 9 and 26, the yield on the 10-year Government of Canada bond nearly doubled from 0.54% to 1.04% as the FTSE Canada Universe Bond Index fell -6.5%. Gold, another safe-haven asset, suffered a similar fate as gold prices fell \$200 (-12.5%) in eight trading days. What happened? During the middle of March, at the height of the risk-off environment, both credit and equity markets became dysfunctional. The dysfunction in fixed income materialized with sovereign bond yields spiking and prices falling. For those few weeks in March, a ‘sell what you can’ mentality took root, resulting in a ‘mad dash for cash’. While cash was likely the world’s most unloved asset for much of the past decade, momentarily at least, the mantra ‘cash is king’ was reclaimed! For seasoned market pundits, this felt very reminiscent of the chaotic period following the Lehman Brothers collapse in September 2008.

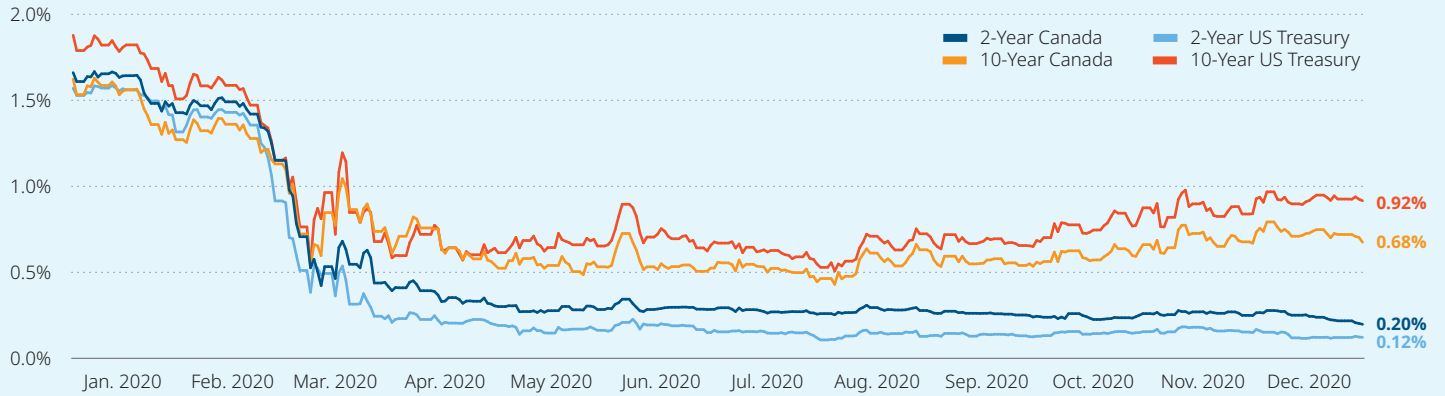
Canadian fixed income indices - 1 year performance



Source: Bloomberg December 31, 2020

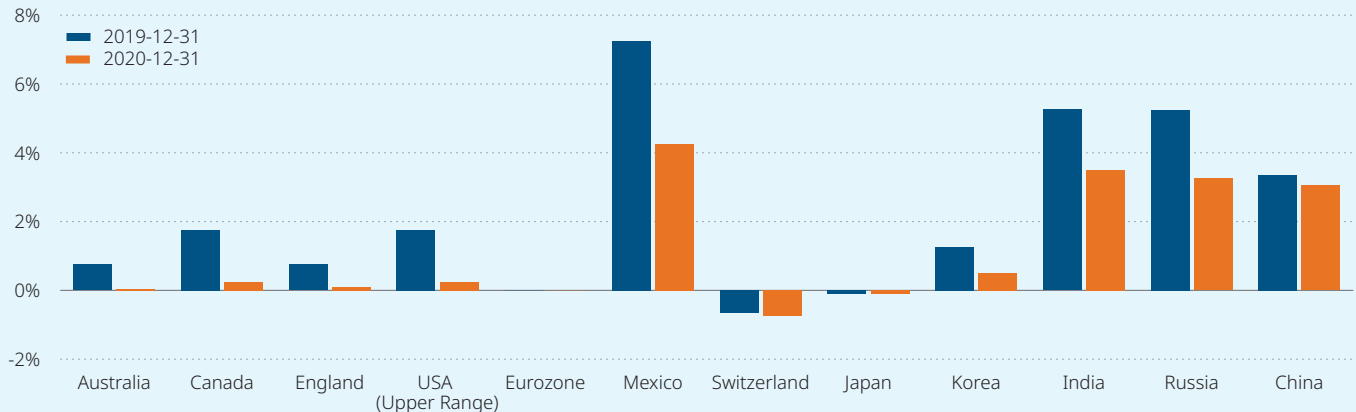


2-Year and 10-Year Government Bond Yields



Source: Bloomberg December 31, 2020

Global Central Bank Rates (%)



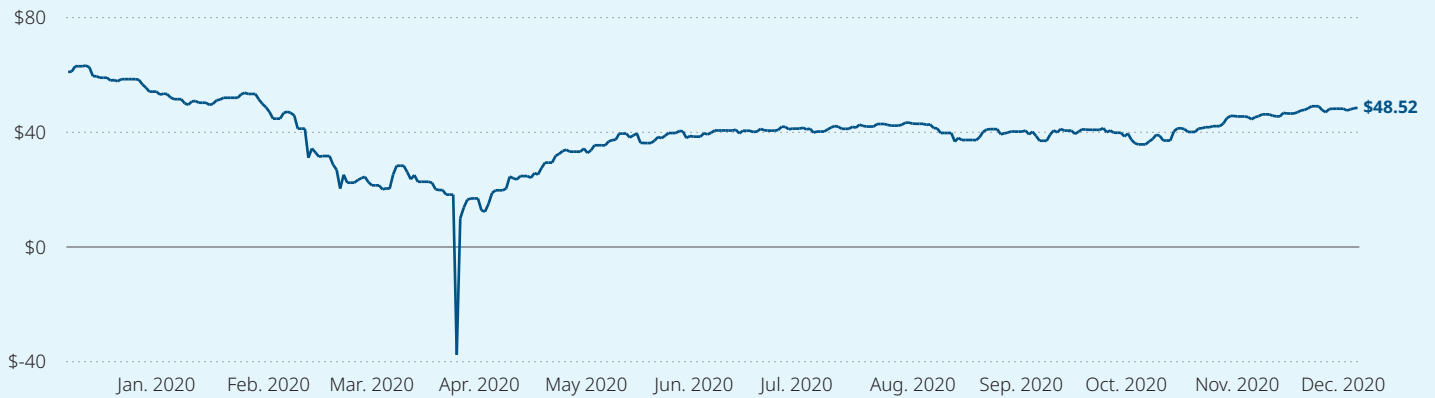
Source: Bloomberg December 31, 2020

Commodities

Oil prices went on a historic and wild ride, with the price of WTI oil ending the year down 20.5%. An untimely price war between Saudi Arabia and Russia occurring simultaneously with the pandemic-induced cratering of global oil demand sent oil prices tumbling. The drop culminated in April when the price of West Texas Intermediate (WTI) took a nosedive. The price for the benchmark front-month contract of WTI oil fell USD\$50/bbl in a mere two hours, momentarily dipping negative and entering the record books as the lowest price quote in 150 years of recorded data (-USD\$40/bbl). Ultimately, prices were able to recover to USD\$49/bbl to close the year as OPEC and Russia (OPEC+) set aside their differences, agreeing to production cuts, in conjunction with improving optimism for a recovery in global oil demand.



WTI crude oil (US\$/bbl)



Source: Bloomberg December 31, 2020

Gold prices extended 2019's 18.3% gain, by notching a solid 2020 yearly gain of 25%. The yellow metal's price spiked 36% into early August, peaking above the USD\$2,000/oz level to set an all-time high as investors piled into safe-haven assets due to the heightened levels of uncertainty. As has so often been the case, the parabolic rise gave way to a second-half correction and consolidation in the USD\$1,900/oz range, as fear and uncertainty retreated.

Gold spot (US\$/oz)



Source: Bloomberg December 31, 2020



Bloomberg Commodity Index

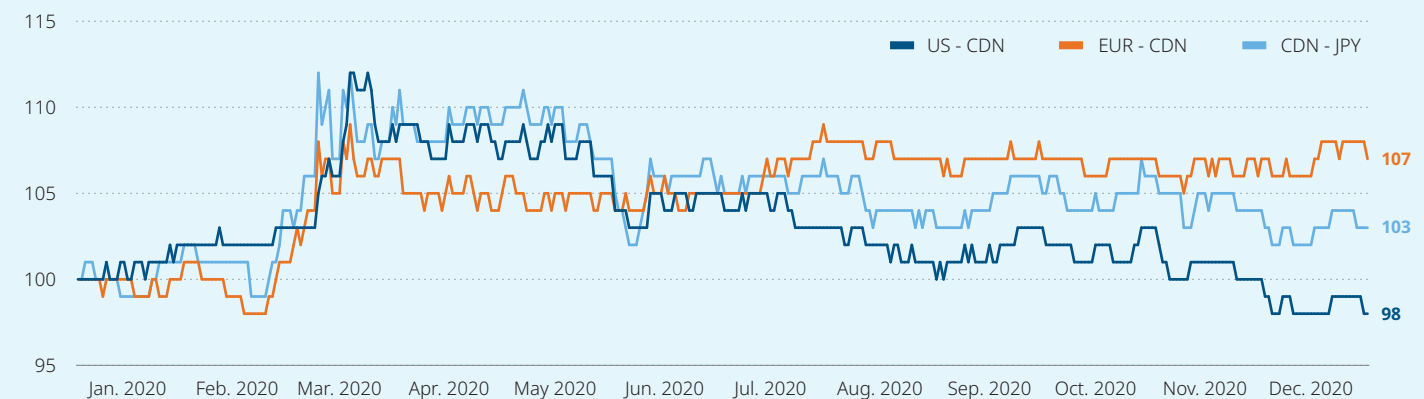


Source: Bloomberg December 31, 2020

Currencies

The Canadian dollar appreciated slightly up 2.0% but not before plumbing a more than four year low of US68.9¢. The Canadian dollar suffered at the hands of the risk-off trade during the worst of the fear and uncertainty touching US68.9¢ on March 19. The global growth and risk-on characteristics of the currency saw it rally sharply off that low to gain 14% through year-end, aided by a general weakening of the US dollar across the globe. The currency was buoyed by favourable short-term interest rate differentials between Canada and the US, the improving 2021 outlook for both the domestic and global economies, general risk-on sentiment, firming oil prices and solid non-oil commodity prices.

CAD performance vs. global currencies (indexed to 100)

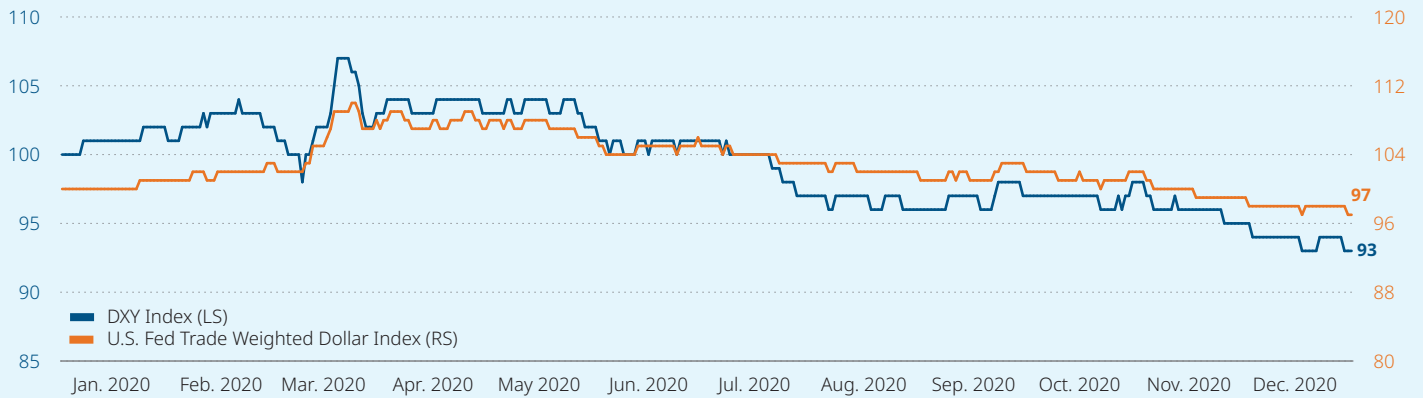


Source: Bloomberg December 31, 2020



The US dollar (DXY Index) put in its worst year since 2017 down 6.7%. But for a brief period of strength during the height of the global capital market dislocation in March, the US Dollar Index extended its downtrend that began in September of 2019. The trend accelerated as the fear-trade unwound over the summer and again post the US election and then the autumn vaccine announcements. Unprecedented liquidity injections by the US Federal Reserve (Fed), including emergency swap lines with other central banks, have the world awash with US dollars. Outright deflation in Europe and the 2020 decline in US bond yields have erased the US' real yield advantage. As a counter-cyclical currency, the expectation of a strong rebound in global growth in 2021 is a headwind for the DXY. Similarly, as a defensive currency, the DXY is weak on abundant risk appetite. Adding to these weaknesses is the US' growing fiscal and trade deficits, which work to drive any currency lower.

US Dollar Index vs. US Fed Weighted Dollar Index



Source: Bloomberg December 31, 2020

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