MACKENZIE Investments

Monthly Market Matters

Summary for February 2021

Brent Joyce, CFA
Investment Strategist

Justin Truong, CFA
Manager, Investment Strategy

Highlights

- Fixed income investors bruised as global bond yields surge amid increasing confidence for a robust economic rebound in the second half of 2021
- US House of Representatives passes President Biden's US$1.9 trillion fiscal stimulus bill; goes to the US Senate for a vote
- Canadian equities deliver strong performance; powered by the cyclical rotation trade and soaring commodity prices
- Bitcoin surpasses US$1 trillion market value as large firms embrace the digital coin

Market Summary

Global bond markets sold off on increased optimism for a sharp rebound in economic growth in the back half of this year. Only the high yield bond index managed a gain. The US 10-year Treasury yield spiked 34 basis points to 1.41% to end the month and has more than doubled (up 90 basis points) from the 0.51% low set in early August. The rise in yields took a bite out of hyper-growth technology stocks and was a catalyst for the ongoing rotation into cyclical stocks. Also supporting the cyclical rotation was an excellent month for commodities. WTI crude oil popped 18%, while copper prices were up 15%, as the reflation trade continues to firm up on the back of plunging global COVID-19 cases and an increase in vaccine distribution.

Canadian equities outpaced most of their global peers for the second month in a row. Rising yields, an acceleration of the growth to value trade and booming energy prices all bode well for the S&P/TSX Composite Index. US and International stocks continued to advance, with the S&P 500 Index up 2.6% and the MSCI EAFE Index marching 2.1% higher. Emerging market equities underperformed, but still managed to eke out a small gain.

Bitcoin surpassed the US$1 trillion market value, as mainstream hype surrounding cryptocurrencies boosted the coin's price to over US$58,000 at one point. Notable firms such as Tesla, Mastercard, and BNY Mellon announced significant investments or some form of adoption in the month.

The US House of Representatives passed President Biden's US$1.9 trillion fiscal stimulus bill, sending the legislation to the 50-50 split US Senate for a vote. Lawmakers are scrambling to get a deal done before jobless benefits expire on March 14. Should the bill pass, capital markets will turn their attention to the impact of a possible US$3 trillion infrastructure package to come later this year.

Canadian Fixed Income	Level	Month	YTD
FTSE Canada Universe Bond Index	1,177	-2.5%	-3.6%
FTSE Canada All Corporate Bond Index	1,362	-2.0%	-2.5%
Bloomberg Canada High Yield Index	161	0.9%	2.1%
Global Equities	**Level**	**Month**	**YTD**
S&P/TSX Composite	18,060	4.2%	3.6%
S&P/TSX Small Cap	719	9.4%	9.7%
S&P 500	3,811	2.6%	1.5%
NASDAQ	13,192	0.9%	2.4%
Russell 2000	2,201	6.1%	11.5%
UK FTSE 100	6,483	1.2%	0.4%
Euro Stoxx 50	3,636	4.5%	2.4%
Nikkei 225	28,966	4.7%	5.5%
MSCI China (USD)	115	-1.0%	6.2%
MSCI EM Index (USD)	1,339	0.7%	3.7%
Currencies and Commodities	**Level**	**Month**	**YTD**
CDN $	$0.785	0.3%	0.0%
US Dollar Index	90.88	0.3%	1.0%
Oil (West Texas)	$61.50	17.8%	26.8%
Natural Gas	$2.77	6.9%	9.2%
Gold	$1,734	-6.1%	-8.7%
Copper	$4.09	15.1%	16.1%
Canadian Interest Rates	**Level**	**Month**	**YTD**
3-month T-bill	0.13	6	7
GOC bonds 2-yr	0.30	14	10
GOC bonds 10-yr	1.35	47	68
GOC bonds 30-yr	1.76	29	55
Canadian Sector Performance		**Month**	**YTD**
Energy		8.5%	11.4%
Materials		-4.5%	-7.9%
Industrials		4.9%	1.8%
Cons. Disc.		8.7%	5.8%
Info Tech		9.9%	9.1%
Health Care		4.6%	41.5%
Financials		6.7%	5.9%
Cons. Staples		-1.1%	-6.4%
Comm. Services		-0.9%	-0.5%
Utilities		-5.7%	-3.2%
Real Estate		4.5%	5.8%

Source: Bloomberg February 28, 2021 – local currency unless noted, equity price only returns, bonds total return

Bond Yields

Global government bonds sold off in the month, jolting bond yields upwards. Yields for the US 10-year and 30-year Treasuries jumped ~34 basis points to 1.41% and 2.15%, respectively, while the shorter end of the curve was mostly unchanged. The situation was similar in Canada and worldwide, leading to a steepening of global yield curves. We have noted bond yields have been steadily climbing from the lows set in August of last year, which has stoked inflation fears. Inflation expectations (proxied by the US 10-Yr Treasury Breakeven Inflation rate) have gradually risen from the ~0.55% low of last March to ~2.15% at the end of February. A quicker than expected rise in inflation, above the consensus 2% target rate for most global central banks, would potentially force them to pull back on ultra-accommodative monetary policies to rein in inflation. This would certainty hurt global markets in ways similar to the 'taper tantrum' in 2013. The focus will be on the US Federal Reserve (Fed) and its tone if bond yields and inflation expectations continue to rise. So far, the Fed has been inconsistent with its peers, largely brushing off any inflation fears, as they reaffirmed their dovish stance with lower for longer interest rates until their inflation and employment mandates are met. They did acknowledge that there will be an inflation spike in the short term due to prior year base effects (when the global economy ground to a halt in the spring 2020 under the most restrictive lockdowns). Ultimately, the Fed believes the jump in inflation will be transitory. However, other major central banks (Europe, Japan and Australia) have raised concerns and have announced they are prepared to increase or alter their bond purchases to combat a further rise in yields.

What catches our attention with the most recent leg up in bond yields is that real yields were accountable for the jump in the nominal figure, with inflation expectations stalling. Falling real yields have been a driving force behind elevated equity market valuations, so a reversal in the trend could be a significant headwind going forward. Equity markets must strike a delicate balance between rising bond yields and inflation being viewed as positives (think financials and cyclicals) and a tipping point whereby inflation and higher yields become too much and turn into a negative. A key caveat is company earnings. If they continue to deliver positive surprises (the recent slate did come in much better than expected) upward momentum can be sustained. However, as earnings expectations rise and stock prices climb higher, so does the hurdle for success.

We believe bond yields are poised to move higher over the medium-term as markets continue to recalibrate, but the ferocity of the recent move suggests some short-term consolidation is likely. All eyes will be on the Fed's next meeting on March 17.

Canadian Equities

The trend whereby Canadian equities are beneficiaries of the ongoing rotation from high-flying growth stocks into cyclicals continued in February. The S&P/TSX Composite Index outpaced most global counterparts, up over 4% in the month. Rising bond yields bolstered financials while soaring commodity prices lifted the energy sector. The price of WTI crude oil was up 18% to US$61.50/bbl, while copper surged 14% amid a very tight supply. Market darling Shopify continued its climb, up 18% in the month, dragging the information technology sector up with it. Industrials were also substantial contributors, strengthened by the reopening trade and led by Air Canada's 25% return in the month.

Bitcoin & Crypto

Bitcoin surpassed the US$1 trillion market value milestone this month, rallying over 50% to US$58,000 at one point before retreating toward US$45,000 to end the month. Several factors are fueling the coin's appreciation. There is increasing confidence that the coin can achieve mainstream adoption. Notable firms such as Tesla, Blackrock, BNY Mellon, and Mastercard have announced significant investments or some form of implementation. Tesla's US$1.5 billion investment shot the coin's value up 23% in a mere two days. There are worries over inflation, and fiat money in general as corners of the market fear the global financial system is deteriorating due to unprecedented fiscal and monetary policies. Bitcoin is also a part of the broader speculative mania that has swept the market (à la Special Purpose Acquisition Companies – SPAC's and highly shorted meme stocks). Volatility remains an issue. The coin tumbled 18% in the last week of the month, exhibiting investors' fickleness toward the currency. A significant hurdle for Bitcoin will be gaining acceptance from global central banks. ECB's Lagarde announced that she does not consider Bitcoin a real currency and that its use as a reserve currency is "out of the question." US Treasury Secretary Janet Yellen cited Bitcoin's past use in money laundering, drug trafficking and terrorism. All suggest the world's most famous crypto-currency has a long way to go before becoming a global reserve currency. (for more, check out Mackenzie's recent report "Bitcoin, more asset than currency").