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Global Economic & Market Review
Fourth Quarter 2020

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Summary:

The coronavirus pandemic remained a major global issue throughout the fourth quarter. While most major countries reported that their economies had recovered in the third quarter, economic data for Q4/20 showed that additional efforts to contain new coronavirus infections had dampened economic activity in many countries. Policymakers around the globe continued to support their economies in the hopes of curtailing the damage. On the other hand, following a slow start in October, major equity markets continued higher in the final months of the year, ignoring surges in cases and the resulting economic slowdown. Instead, investors focused on vaccine developments and the eventual approval of some COVID-19 vaccines by major countries near the end of the quarter. Once again, the International Monetary Fund (IMF) improved its forecast for global growth, projecting that the global economy would shrink by -3.5% in 2020 up from its previous forecast of a -4.4% contraction.

CFAL Global Economic & Market Review Q4 -2020

United States

In the final quarter of 2020, US equity markets bested their gains from the previous quarter as vaccine optimism resulted in improved investor confidence. The US Presidential elections in November also helped to boost markets, as former Vice President Joe Biden triumphed over the incumbent Donald Trump, who agreed to a transition of power after weeks of delay. While the September market sell off continued in October, all three major indices rallied in the last two months of the year and ended the quarter with double digit returns. Once again, the Nasdaq Composite was the best performer, adding +15.41% during the quarter to end the year with a remarkable return of +43.64%. The S&P 500 followed suit with a quarterly return of +11.69% while the Dow Jones Industrial Average continued its rebound returning +10.17% in Q4. In late November, the blue chip index closed above 30,000 for the first time. Year to date, both indices were up +16.26% and +7.25% respectively. In the bond market, US Treasuries 1-10 years saw lackluster returns, and were down -0.23% for the quarter. On the other hand, USD corporate (+2.99%) and high yield (+6.48%) issues improved on their Q3 returns. In mid-December, the US Federal Reserve indicated that they would continue to buy $120 billion of bonds per month until “substantial further progress” was made in the economic recovery. The Fed maintained its forecast that rates would remain near zero at least through 2023 and kept its benchmark interest rate unchanged at a target range of 0% - 0.25%.

As projected, the US economy saw a sharp rebound in the third quarter primarily due to the reopening of businesses and a surge in consumer spending. The Commerce Department reported that US GDP growth came in at an annualized rate of 33.4% in Q3/20. This follows a significant contraction of 31.4% in the second quarter when economic activity came to a halt due to the pandemic. However, a surge in cases in the last quarter of the year led to new measures to control the spread of the virus which likely dampened fourth quarter economic activity. This was reflected by a sharp drop in job gains in November where the economy added 245,000 jobs compared to the 610,000 jobs added in the previous month. The unemployment rate slightly improved to 6.7% from 6.9%. To counteract the effects of the slowing economy, US lawmakers negotiated another stimulus package aimed at providing relief to millions of Americans. The $900 billion relief bill was signed into law by President Trump during the last few days of December and included payments of $600 to individuals, improved jobless benefits and $285 billion earmarked for loans to small businesses. It was the second largest stimulus package after the $2 trillion package approved in March.

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Europe

European equities fared well during the fourth quarter even as coronavirus related restrictions continued to suppress the economy. The DJ Euro Stoxx 50 index added +11.24 in Q4/20 to close the year out with a return of -5.14%. The euro area reported double digit growth of 12.5% in the third quarter, after contracting by an historic -11.8% in the preceding three months. Countries including France (18.7%), Spain (16.7%) and Italy (15.9%) all posted sharp rebounds in the third quarter after reporting large declines in Q2/20. No country reported an economic contraction, with Greece (2.3%) growing at the slowest rate. However, the outlook for growth in the fourth quarter was bleak as new stay-at-home orders restrained economic activity. Member countries including Germany grappled with an increase in cases and deaths forcing the government to introduce additional lockdowns. Economists project that the decline in activity in the region's largest economy would lead the EU into a double dip recession. In December, the European Central Bank (ECB) launched a new round of stimulus to help the economy deal with the fallout from the pandemic. The central bank promised to purchase an additional €500 billion in bonds, increasing its pandemic emergency purchase program (PEPP) from €1.35 trillion to €1.85 trillion. The PEPP was also extended from June 2021 to March 2022. ECB President Christine Lagarde indicated that if the EU economy recovered quickly enough, it would not be necessary to use the entire amount earmarked for the PEPP. The ECB also projected that the eurozone economy would contract by -2.2% in the fourth quarter, with the downturn continuing into the first quarter of 2021.

After nearly a year of difficult negotiations and just one week before the December 31 deadline, the UK and the EU finally reached a Brexit trade agreement on Christmas Eve. The landmark deal came more than four years after the UK voted to leave the EU and is a key element in governing relations between the two sides going forward. The deal grants both sides preferential access to each other's markets, meaning there would be no tariffs or quotas applied. However, as of January 1, 2021, the UK would be subject to a hard customs border where goods would require checks potentially leading to more paperwork and delays. Meanwhile, the UK continued to struggle with the coronavirus pandemic and lockdowns throughout the quarter which stifled economic activity. The economy was estimated to have grown by 16.0% in Q3/20, however a full four-week lockdown in November and another in December after the discovery of a fast spreading variant of the coronavirus is projected to have driven the economy back into negative territory that could persist throughout the first quarter of 2021. However, in a positive sign for the economy, the UK became the first country in the world to approve and administer the Pfizer COVID-19 vaccine. By the end of the quarter, the country had approved a second vaccine developed by Oxford and AstraZeneca. Investors reacted well to the Brexit trade deal and vaccine approvals; the FTSE 100 was up +10.13% for the quarter. Year to date the index was down -14.34%.

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Asia Pacific

Asian equities experienced another positive quarter as economies in the region experienced sharp rebounds in GDP growth. The Shanghai Composite Index increased by +7.92% for the quarter for a year-to-date return of +13.87%. China's successful containment strategies and fiscal stimulus proved to be beneficial as the country neared pre-COVID growth levels. Despite the deep downturn experienced in Q1/20, China is the only major economy on track to experience positive GDP growth for the year. Following growth of 3.2% in the second quarter, China's economy expanded by 4.9% in Q3/20, and unemployment remained relatively low standing at 5.2% as of November. Economists forecast that the world's second largest economy will end 2020 with growth around 2.0%. The reopening of the global economy led to increased demand for Chinese goods in November with exports growing 21.0% from a year earlier. As a result, the country's trade surplus hit a new monthly high of $75.42 billion. Geopolitical tensions between the US and China remained high, even after the US presidential election, as President Donald Trump prohibited US investments in Chinese companies perceived to be owned or controlled by Chinese military. Effective January 11, 2021, US investment firms, pension funds and other entities are banned from investing in a list of 31 Chinese companies. Some of these companies include Huawei, China Telecom, China Mobile, and Hikvision Digital Technology. By the end of the quarter, there was little indication on how President-elect Joe Biden would handle the US/China relationship as he had yet to formally review the measures put in place by the Trump administration.

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Elsewhere in Asia, Japanese Prime Minister Yoshihide Suga approved a third stimulus package worth US$708 billion in an effort to assist the country's recovery from the COVID-19 pandemic and improve Japan's long-term growth potential. This would bring the country's combined value of coronavirus-related stimulus to approximately $3 trillion. The package is expected to boost GDP growth by 2.5% in FY2021, and 0.6% in FY2022. Japan's economy grew 5.3% in Q3/20 compared to the previous quarter's decline of -8.2%. Japanese shares were up as a result, the Nikkei 225 posted double digit gains of +18.37% for the quarter to end the year up +16.01%. In the South Pacific, Australia's economy rebounded by 3.3% in Q3/20 after a contraction of -7.0% in the second quarter. This ended the country's first technical recession in three decades. The main driver of growth was household consumption which grew 7.9%, the highest in 60 years, primarily due to government stimulus and interest rate cuts. Growth for Q4/20 is expected to be even stronger as the country has near-zero new COVID-19 cases.

Emerging Markets

Emerging market equities exhibited the strongest performance in over a decade as the MSCI Emerging Market Index jumped +19.34%, outperforming the MSCI World Index by 5.71 percentage points. Year to date, the index was up +15.84%. Vaccine developments contributed to the equity gains; however, it is expected that vaccine distribution may take longer than expected in some emerging market countries due to transport infrastructure and healthcare limitations. In Latin America, the recovery is expected to be especially slow due to the region being particularly hard hit by the virus and having widespread economic weaknesses prior to the pandemic. Brazil emerged from a recession in Q3/20 with GDP growth of 7.7%, the largest quarterly growth since 1996. Growth was driven by heavy stimulus spending with the Brazilian government providing emergency assistance to over 60 million people to mitigate the impact of the COVID-19 pandemic. Latin America's largest economy is expected to contract by -4.8% for the year. Meanwhile, Mexico experienced a sharp rebound in Q3/20 after five consecutive quarters of contraction. The country reported GDP growth of 12.0% from the previous quarter, as massive stimulus spending in the United States led to an increase in exports and remittances. However, the country is forecast to shrink by 10.0% in 2020, the

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largest decline since the Great Depression.

Elsewhere in Latin America, Peru's President Martin Vizcarra was impeached in November over corruption allegations and his handling of the pandemic. Following this, two additional presidents took office in the span of a week due to the resignation of Vizcarra's successor. In the midst of this political crisis, the Peruvian government issued $4 billion worth of debt in November including a $1 billion 100-year bond to combat the fallout from the pandemic. The 100-year bonds were priced with a spread of 170 basis points above US Treasuries, the lowest yielding century bonds ever sold by an emerging market government. Despite implementing one of the earliest and strictest lockdowns in Latin America, Peru has one of the world's highest coronavirus death rates. In South Africa, COVID-19 containment issues continued over the quarter as the country experienced a surge in cases due to a new, more contagious variant of the virus. The country has the highest number of cases in Africa, placing a large strain on the healthcare system. GDP fell -6.0% in the Q3/20 compared to -17.6% in Q2/20. The IMF projects that South Africa will contract by -8.0% in 2020 and will not return to pre-crisis levels until 2023 or 2024. India's economy also experienced another quarterly decline in GDP and entered a technical recession in the quarter ending September 2020. The economy shrank by -7.5% following a drastic decline of -23.9% in the second quarter. India's Q4/20 GDP numbers are expected to be stronger following the easing of lockdowns. As a result, the IMF revised the country's 2021 growth numbers upwards from 9.4% to 11.5%.

Commodities

In the commodities market, gold (+0.66%) cooled off during the fourth quarter as equity markets roared higher while silver's industrial features led to a +13.63% gain and a continued outperformance of gold. Despite the weakness during the second half of the year, both metals had a great 2020, rising 25.3% and 47.3% respectively. Overall, investors became less cautious with equity markets rising as vaccine distribution began in December. Both metals are expected to continue to do well as governments and central banks carry on with efforts to stimulate the economy through expansive monetary and fiscal policies. In the oil market, U.S. WTI crude oil prices (+17.97%) also jumped significantly in Q4/20 but were down (-12.97%) for the full year as demand remained below pre-pandemic levels. However, optimism surrounding the vaccine led to an increase in consumption as the supply and demand equilibrium drew closer. Elsewhere in the commodities market, copper prices (+15.79%) posted a noteworthy gain as investors bet on an increase in economic activity. This took 2020 gains to +24.32% for the commodity most commonly used to determine the health of the global economy.

"Overall, investors became less cautious with equity markets rising as vaccine distribution began in December."

Conclusion

The year 2020 was certainly an unexpected and unforgettable one. At the beginning of the year, no one could have predicted that the world would experience the worst pandemic in modern history that would bring the global economy to its knees. Governments around the world were caught off guard but many eventually sprang into action to protect their economies from the repercussions and continued to do so throughout the remainder of the year. The world economy saw a drastic plunge in activity in the second quarter, however many countries recovered in the third quarter as economies slowly reopened. Unfortunately, the pandemic was still a major determinant of global economic growth in the fourth quarter as increases in cases and newly discovered variants in certain parts of the world resulted in the reinstatement of measures to combat the spread of the virus. On a brighter note, developments in COVID-19 vaccines became a sign of hope for global economy in Q4/20 and vaccine rollouts are expected to accelerate during the first quarter of 2021. However, widespread immunity is not expected until the latter part of the year. Until then the outlook for global growth, while encouraging, remains uncertain and the global economy will continue to face challenges. #

Market Returns Q4-2020

	As at 31 December 2020			
	MTD	**QTD**	**YTD**	**1 year**
Equity Indices *(% local currency)*				
S & P 500	3.71	11.69	16.26	16.26
Dow Jones Industrial Average	3.27	10.17	7.25	7.25
NASDAQ	5.65	15.41	43.64	43.64
S & P TSX	1.41	8.14	2.17	2.17
FTSE 100	3.10	10.13	-14.34	-14.34
DJ Euro Stoxx 50	1.72	11.24	-5.14	-5.14
Shanghai SE Composite	2.40	7.92	13.87	14.24
Nikkei 225	3.82	18.37	16.01	16.01
Ibovespa Brasil	9.30	25.81	2.92	2.92
MSCI Emerging Markets	7.15	19.34	15.84	15.84
MSCI World	4.14	13.63	14.06	14.06
ICE BofA Bond Indices *(% local currency)*				
US Treasuries 0-3 months	0.01	0.03	0.54	0.54
US Treasuries 3-5 years	0.11	-0.03	6.06	6.06
US Treasuries 1-10 years	0.03	-0.23	5.65	5.65
US Corporates	0.49	2.99	9.81	9.81
US High Yield	1.91	6.48	6.17	6.17
UK Gilts 1-10 yrs	0.54	0.17	3.16	3.16
Canada Government 1-10 yrs	0.13	-0.09	5.36	5.36
Euro Government	0.12	1.22	4.94	4.94
Global High Yield & Emerging Markets	2.50	7.81	6.89	6.89
Global Broad Market Index	1.17	2.68	8.94	8.94
Currencies vs. USD				
British Pound	2.60	5.80	3.12	3.12
Euro	2.42	4.22	8.94	8.94
Canadian Dollar	-2.12	-4.46	-2.04	-2.04
Japanese Yen	-1.02	-2.11	-4.94	-4.94
Australian Dollar	4.77	7.43	9.59	9.59
Swiss Franc	-2.61	-3.88	-8.42	-8.42
Commodities *(% USD)*				
Gold	6.83	0.66	25.12	25.12
Silver	16.60	13.63	47.89	47.89
Copper	2.36	15.79	24.32	24.32
WTI Crude Oil	6.61	17.97	-12.83	-12.83
Alternatives *(% USD)*				
HFRX Global Hedge Fund	2.45	5.11	6.81	6.81