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We will adapt.**

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STRONG MEDICINE FROM CENTRAL BANKS AS GLOBAL RECESSION HITS QUICKLY

It's almost inconceivable to think of what has occurred in March, both in social and market terms. It was only a few weeks ago that markets were at all-time highs with optimism of future gains heading into the US election. The unprecedented events of the last few weeks have put those dreams on hold and, now, it feels like it was a long time ago.

In a year that central banks were expected to be on the sidelines, we have seen global rates slashed to zero. We've seen a new round of quantitative easing programs more aggressive than those of the global financial crisis. And governments have launched fiscal programs that will spend over \$2-trillion (yes, *trillion*) in an attempt to keep their economies from collapsing.

The world changed on all of us almost overnight. Things as simple as a handshake or face-to-face meeting seem like ancient concepts. They have been replaced with WFH (work from home) protocols, social distancing and video calls. It's now spring and we should be getting ready for the return of baseball season and another Raptors playoff run, but those events have been put on hold. Even the Olympics has been delayed a year. The world we knew ground to a halt and it may never come back in the form we remember. We must adapt. We will adapt.

The global economy has never shut down like this before. It's happening at a time when we have never been more integrated. During the world wars, economic activity and employment increased to meet demand. But this is very different, as everyone has been told to stay home and not travel. As a result, we are witnessing a demand shock unlike any in history.

Air travel has fallen over 90%, restaurants are closed throughout the world and small businesses are facing their biggest threat since the depression. Factory doors shut and commodity demand has collapsed. One economic stat to show the magnitude of these events is US jobless claims, which for the week of March 23 hit 3.3-million. The following week it surged to 6.6-million. The previous high was 650,000. There will be many more shocking stats coming at us before this is over. There is no question that we are in a global recession. The debate is how long it will last.

Markets are often explained as forward-looking. In this case, equities were late to the party as the bond market caught onto these concerns earlier than stocks, with the US 10-year Treasury yield falling from 2% to 0.4%. But there was nowhere to hide outside of cash and long bonds. This bear market left no prisoners.

Globally, most equity markets dropped 25% during a two-week stretch. But even more shocking is that the safe-haven asset of gold dropped in the crash and many defensive equities fell over 50%! Corporate and investment-grade bonds fared little better, falling by 8%. This was a liquidity scare like 2008 and margin selling forced many to ditch whatever they could get a bid on. This resulted in massive dislocations and a rush towards the US dollar and Treasuries.

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By the numbers

as at Mar 31, 2020

S&P/TSX Composite Index	-17.38% ↓
Communication Services (top sector)	-4.21% ↓
Energy (bottom sector)	-30.80% ↓
S&P 500 Index	-12.35% ↓
Health care (top sector)	-3.82% ↓
Energy (bottom sector)	-34.80% ↓
Gold	US\$1596.60
	+1.07% ↑
WTI Oil	US\$20.55
	-54.24% ↓
US 10-Year Treasury Yield	0.70%
	-43bps ↓

Headlines will undoubtedly become worse in North America. The trick for successful investors is to determine what has already been priced into valuations at these levels. Getting too negative at the end of a sell-off can lead to investors missing out on some powerful bear market bounces. And many will remember that markets tend to turn before the news gets better. What is needed is the light at the end of the tunnel – signs that things are getting less worse.

The mass shutdown of entire economies was enough of a negative to derail markets, but there was a second and arguably equal negative March event in the energy sector. OPEC collapsed in a pricing war that resulted in oil falling from \$50/bbl to below \$20/bbl due to increased supply. The timing of this could not have been worse for the battered energy sector. The virus alone was a massive negative to this group. Add in a surge in supply and it's a tragedy.

So, what now? As we saw in the 08/09 global financial crisis, once governments and central banks finally focus on the problem they can and will throw everything at it, often doing previously unthinkable strategies and rewriting the rules. Given the fact it's also a US election year, we would expect these programs to be magnified. The stimulus will be massive and all encompassing. Expect rates to remain close to zero for the foreseeable future. Gold and other precious metals may begin another bull cycle in this environment.

The wildcard here is when the lock downs will end. If things get back to normal by the end of Q2, we could be setting up for a massive rally in the second half of the year. If it drags on until year-end, we should expect more volatility, potentially more downside and will need more stimulus programs to keep economies going. The fact that it's a mandated recession may make it easier to restart, but no one really knows.

Every crisis is different, and this one has many unique aspects. The fact it includes a health scare will affect market participants who are dealing with their own personal situations on top of the market moves is a dimension that should not be overlooked. The work from home aspect many are going through will also have an effect on both sentiment and multiples that is hard to quantify.

We will come through this. Our definition of normal may be different, but economies and markets can adapt. Once the worse is past, this crisis should be looked at as an opportunity. The rise of passive index funds caused many 'good' companies to see their share prices fall as much or more than 'bad' ones. Active stock picking strategies may be looking at the emergence of a new golden area stemming from this crash. Income-producing strategies will become more important with reduced bond yields and this may be the final death knell for the 60/40 portfolio.

We wish everyone all the best in these trying times. We hope everyone is staying safe and staying at home.

All data sourced from Bloomberg unless otherwise noted.

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