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Looking Back
A Quarter of Unexpected Moves

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The rally in equity markets that we witnessed for over a decade came to a screeching halt during the first quarter of 2020. After a fairly uneventful grind higher in the first 7 weeks of the quarter, the S&P 500 peaked in mid-February. The answer to the question 'What could bring the long bull market to an end?' soon became clear – a global pandemic.

The last week in February and first three weeks of March were characterized by a massive jump in volatility, back to the levels seen during the great financial crisis, huge daily moves (largely to the downside), and a desire for liquidity as the severity of COVID-19 became clear. The extent to which governments around the world would curtail business activity, implement quarantine and social distancing measures, and provide a massive monetary and fiscal response would have seemed unbelievable a few months ago, but soon became the reality we find ourselves in today.

While all risk assets were significantly impacted during the selloff, equity markets were front and centre with an unprecedented speed of decline. The S&P fell into bear market territory with a drop of more than 20% from its peak in just 16 trading days - the fastest in history. In comparison, during the 2008/2009 financial crisis it took close to a year for markets to experience the same kind of drop. Most major equity markets fell over 30% from their peak in the span of a few weeks before recovering slightly towards the end of the month. For the quarter, the S&P 500 was down 20%, the TSX fell 20.9%, MSCI AC World fell 21.4% and MSCI Emerging Markets fell 23.6%.

From an equity style perspective, in contrast with previous large market selloffs where historically growth stocks have lagged value stocks, the opposite occurred. In the first quarter, the MSCI World Value Index was down 27% in contrast to the MSCI World Growth Index which fell 15.2%. The higher weights in financials, energy and commodity stocks weighed on the performance of value indices, particularly as oil prices collapsed from over $50 USD in late February to around $20 USD by late March.

Further, interest rates collapsed with shocking speed as governments around the world executed a series of rate cuts, asset purchase programs and other stimulus measures. U.S. 10-year yields started the year at close to 2% and dropped to almost 0.5% in March before ending the quarter slightly above that level. In Canada, the drop was not quite as large but fell from 1.7% at the start of the year to just above 0.5% before rebounding slightly to end the quarter. While interest rates fell, credit spreads widened dramatically, leading to a huge dispersion in fixed income returns. High-quality bonds performed well, led by the outperformance of government bonds. The FTSE Canada Universe Bond Index was up 1.6% in the quarter, while the U.S. Barclays Aggregate Index was up 3.2%.

As credit quality continued its decline, high-yield bonds and levered loans both fell around 22% from their peak, while Canadian preferred shares fell over 36% from their peak. As equity markets have rallied recently, these markets have also gained back some of the losses.

When analyzing currencies, the U.S. dollar rallied against most other currencies in a market characterized by flight to safety above all else. The Canadian dollar, which had traded in a pretty tight range of 1.30-1.34 for most of 2019, weakened very rapidly to 1.45 alongside the oil price collapse before recently rebounding to the 1.40 level.

The extreme steps taken by governments around the world to slow down the spread of COVID-19 and enable health care systems to handle the pandemic seem to be taking

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effect, which has been reflected in the recent rebound of risk assets. Governments have thrown everything at their disposal in terms of monetary and fiscal tools in order to ensure that societies are able to get through this period of extreme economic contraction. Markets are looking through this period of shockingly bad economic data for what comes next.

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