Winter 2020

Following a summer of market malaise, equity markets broadly broke out of their summer ranges and traded higher in the fourth quarter. As we moved towards the end of 2019, the on again off again trade concerns were alleviated with the agreement of U.S.-China Phase One trade deal and long-awaited progress towards ratification of the United States-Mexico-Canada Agreement (USMCA). While the net new growth that will come from these deals can be debated, their completion was reflective of a de-escalation of trade rhetoric that had been weighing on general market sentiment and allowed for most markets to close at or near their 2019 highs: S&P/TSX Composite Index 22.88%, S&P 500 25.18%, U.K. London FTSE 16.04%, German DAX 17.09%, MSCI Japan 14.32%, China Shanghai Comp 14.41%, MSCI EAFE 16.78%, MSCI Emerging Markets 13.20%, and MSCI World Index ex-USA 17.26%. These returns reflect a Canadian dollar that strengthened relative to most other currencies, including 5.03% and 6.86% relative to the U.S dollar and Euro, respectively. Though the currency appreciation wasn't enough to close the U.S. to Canadian equity performance gap, it did help in Canada outperforming most of the rest of the world's equity markets on a currency adjusted basis. The 2019 equity gains displayed strong sector breadth, with all but the particularly focused Canadian healthcare sector experiencing double digit gains. Information technology was the leading sector in both Canada and the U.S., though several other sectors, including industrials, materials, and financials, were also able to post 20+% returns.

After three 2019 rate cuts brought the U.S. Federal Reserve (Fed) Funds Rate target range to 1.50-1.75%, the Fed's Federal Open Market Committee (FOMC) appears to be entering an extended holding pattern. Their recent commentary has focused on maintaining the current relatively easy policy levels that they deem to be "appropriate." While they have been supportive of the repo market via asset purchases, we believe their preference is to be relatively inactive in 2020 so as not to be dragged in to what is expected to be a hotly contested and contentious U.S. election. What remains to be seen is whether the data on which their policies will be "dependent" will allow them to do so. Current market discounting shows that the market isn't currently expecting much activity from the FOMC in 2020.

The Fed's Canadian colleagues are in a similar 'wait and see' period at the Bank of Canada. Their first meeting of 2020 came and went without a change to their 1.75% overnight rate. If anything, they tilted the meeting's accompanying statement towards a more accommodative stance after a downgrade in 2019's fourth quarter economic activity projection. Should the Bank of Canada's 2020 GDP projection of 1.60% be realized or even deteriorate amid recent coronavirus concerns, the Bank would have room to cut given their benchmark rate remains higher than much of the rest of the world's developed markets. That appears to be what the bond markets are increasingly expecting with short and mid-term rates recently moving below the aforementioned overnight rate.

One of the by-products of the U.S. Federal Reserve's activity in the very short-term repo market, was a steepening of the yield curve in late 2019. While this affects the U.S. curve in a more meaningful way, the Canadian Treasury curve experienced a similar move though it would be better described as a narrowing of its inversion. The move however has turned out to be temporary, as the late-2019 upward move in rates has been given right back following concerns around the difficult to discount coronavirus concerns. With the Bank of Canada and the FOMC in a holding pattern and much of the rest of world's interest rates at lower levels, we expect rates to be range-bound between their early 2020 highs and mid 2019 lows (roughly plus/minus 0.30% from their current levels).

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While Canadian GDP growth lagged the U.S., there was a meaningful narrowing of the relative interest rate gap; from a 5-year Treasury difference of 66 basis points (bps) to a single basis point by the end of 2019. This move offset the economic growth differential, helping the Canadian dollar (CAD) gain 5.03% relative to the U.S. dollar. As the gap narrowed while the year progressed, the Canadian dollar followed a similar pattern and finished 2019 at its lowest point of the year. This is another trade that has reversed in early 2020 with the Loonie taking a cue from the Bank of Canada's recent downgrade to Q4's expected GDP in moving back towards the middle of its range of the last six months. We expect the recent move will continue with the Canadian dollar per U.S. dollar extending towards the upper end of that range around 1.334.

On the equity front, the late 2019 momentum has continued into early 2020 with markets broadly adding to their historic or multi-year highs. The only hiccup to trading experienced thus far has been driven by coronavirus concerns. The market impact thus far has been concentrated in Asia while North American markets remain within a few percentage points of their recent highs. With last year's gains being primarily multiple based, 2020 will require earnings growth to carry the markets forward. Beyond better than 2019 earnings growth expectations, the U.S. election cycle and its related themes will garner increased attention as the year progresses. Historically, U.S. election years tend to experience weaker, though still positive, returns compared to the other three years of the election cycle. Our expectations is that 2020 will follow a very strong 2019 with more modest returns along with additional volatility provided by the uncertainty that comes with contentious political campaigns.

Registered Account & Tax Reporting Information

As per the Ottawa Wealth Advisory Group tax card, note that the 2020 Tax Free Savings Account (TFSA) contribution limit is $6,000 and 2019 and 2020 Retirement Savings Plan (RSP) contribution limits are $26,500 and $27,230, respectively.

Please note that we are expecting the 2019 TD Wealth Tax Packages to be delivered in mid-March. Third-party slips will be delivered separately and have the following mandatory mailing dates, to the degree that they apply:

T5 February 29, 2020
T-5008 February 29, 2020
T3 April 1, 2020

Sources:
Bloomberg Finance L.P. as at December 31, 2019. Total Index returns. Index returns calculated in C$.
bankofcanada.ca/rates/exchange/currency-converter/
Thomson ONE

Interest Rates as of February 3, 2020

Fixed Income Securities	1 year	2 years	3 years	5 years	10 years	20 Years	30 Years
GICs**	2.00%	2.06%	2.11%	2.26%			
Canadian Treasury Bonds*	1.58%	1.46%	1.44%	1.33%	1.32%	1.44%	1.47%
U.S. Treasury Bonds*	1.46%	1.36%	1.38%	1.40%	1.58%	1.93%	2.06%

* Rates provided by TD Securities
** Rates provided by TD Wealth

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