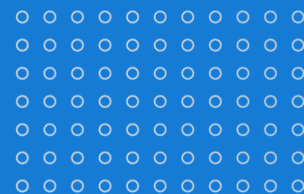
Coronavirus Update

and your Retirement Savings



The end of February 2020 saw a sell-off of equities and other risk assets, while safe-haven assets rallied amid increasing concerns about the novel coronavirus (COVID-19) than initially anticipated. Trading sessions during the latter part of February resulted in global equity markets falling by 6% while gold increased by over 2%. The US 10-year Treasury yield edged closer to 1.3%, which is the lowest level ever recorded. At the time of this writing, the Treasury yield decreased again to a record 0.318% and the S&P500 is 19% below the benchmark's all-time high of February 19, 2020.

As of early March, the number of cases across the globe had increased to over 80,000 cases, according to the World Health Organization (WHO). Meanwhile, WHO has also reported 2,700 deaths from COVID-19. While most of these cases remain within the Hubei province in China where the outbreak originated, there have been over 2,500 cases and 34 deaths reported in 33 countries as of this writing, surpassing the number of deaths from the SARS outbreaks between 2002 and 2004. The number of cases and of deaths is continuing to climb.

ECONOMIC IMPACT

In addition to the health concern for the spread of COVID-19 beyond China, the extent to which economic activity is being disrupted within China appears to be greater than what many economists and market participants had previously thought. This has prompted further downgrades in economic forecasts for the first quarter and for the balance of 2020 across the globe.

Global equity markets experienced sharp selloffs to the end of February, and they resumed into the first week of March as coronavirus fears mounted. While most markets entered correction territory and given the recent example of the 2008 financial crisis, finding the low point in the markets will be illusive for investors.

For the first time since the 2008 financial crisis, the U.S. Federal Reserve implemented an unscheduled rate cut of 0.50% on March 3rd from 1.75% to 1.25% to combat the economic fallout from the coronavirus. Bank of Canada responded on March 4th with a similar cut to 1.25%. Further easing is expected.

Equity markets have also modestly revised their earnings expectations downward, with the MSCI Emerging Markets Index implied earnings per share for the next year falling approximately 2% in February. Although this decline is modest, it comes on the heels of a general contraction in earnings in 2019 as a result of slowing growth and prolonged trade tensions.

Beyond China, there is mounting evidence of COVID-19 causing a significant disruption in economic activity and no industry will be spared. Factories have been forced to reduce capacity along with workers due to goods and services from China not being delivered. Oil is plummeting and Gold is soaring, while safe haven investments offer little or no yield.

HUB

ECONOMIC OUTLOOK

The recent outbreaks of the virus have only added to the economic uncertainty in February. A best-case scenario would be if the downward trend of new cases in China continues, it may loosen restrictions on business in those Chinese provinces deemed less at risk of COVID-19.

Economic data was very weak in February but may stabilize in March before ultimately returning to normal levels in April or May. In this scenario, we expect a v-shaped recovery, but the inflection point may be unknown.

Manufacturing activity that did not take place in February or early March could be made up in subsequent periods, but some Services activity is unlikely to recover. Consequently, economic growth for China will be lower than expected for all of 2020 weighing on corporate earnings.

The outlook for the rest of the world will depend on whether recent outbreaks outside China will eventually be contained. Countries reliant on tourism could see lower growth for 2020 as will businesses serving that market. The many high-profile cases of cruise ships weighing anchor off the coast of Japan and California could put off travelers from planning vacations and business travel until the epidemic has completely receded. In some countries, fiscal easing and additional stimulation from central banks will bring some short-term relief.

Although our analysis is impaired by yet to be seen factors, we do expect modest positive global growth for 2020 with higher downside risk. The global business environment could take a turn for the worse, should COVID-19 become a prolonged global pandemic. For the foreseeable time period ahead, volatility will persist.

IMPACT ON RETIREMENT SAVINGS

The year has begun with palatable anxiety and apprehension for those investors saving for retirement. As economic growth estimates fall, and long-term bond yields drop past the all-time lows set in 2019, investors saving for retirement will be feeling that still familiar uncertainly of the 2008 financial crisis.

YTD MARKET RETURNS at FEBRUARY 28, 2020		
Canadian Equities		
	Information Technology	6.60%
	Utilities	4.90%
	Real Estate	1.20%
	Consumer Staples	-1.80%
	Industrials	-2.10%
	Financials	-3.40%
	Communication Services	-4.10%
	Energy	-9.20%
	Consumer Discretionary	-9.60%
	Materials	-9.80%
	Health Care	-18.70%
	S&P/TSX Composite	-4.30%
	S&P/TSX 60 (Large Cap)	-3.80%
	S&P/TSX (Small Cap)	-12.50%
Foreign Equities		
	S&P500	-5.00%
	MSCI EAFE (CAD)	-7.80%
	MSCI World (CAD)	-5.70%
	MSCI EM (CAD)	-6.50%
Canadian Bonds		
	FTSE Canada Universe	3.60%
	FTSE Canada Long Term	6.00%
	FTSE Canada RRB	5.20%

The advice is the same now as it was then. If you don't have to sell securities in this market, don't. Do not sell or change your asset allocation if you did not rebalance before February 20th. Though it will be a rollercoaster ride for most of 2020, investors have no choice but to ride out the correction for now.

Whether you have a capital accumulation plan or defined benefit plan, the impact is the same. Account balances in capital accumulation plans are lower as of today, and the solvency ratio of defined benefit plans were also impacted quite measurably by the end of February. For DB plans, the impact is two-fold; assets have effectively been reduced almost overnight, while bond yields will increase the value of current liabilities. Overall, long-term risk to DB plans has returned.

However, it is important for investors in retirement savings plans to understand that a typical balanced pension portfolio would have fallen only by 0.5% over the QTD period to the end of February. A diversified portfolio would have softened the decline in assets, while a lack of diversification would result in more measurable losses to the end of February 2020. Here is a summary:

- The S&P/TSX Composite Index returned -4.3%. All sectors posted negative returns except for Information Technology, Utilities and Real Estate.
- Canadian fixed income markets rose amidst lower yields with long-term bonds (6.0%) outperforming universe bonds (3.6%). Real return bonds (5.2%) also rose.
- On a global basis, international equities contracted the most; the MSCI EAFE returned -7.8% in CAD. The US equity market returned -8.3 % in USD terms and -5.0% in CAD. Emerging markets also declined in both local currency (-7.0%) and Canadian dollar terms (-6.5%).

WHAT SHOULD YOU DO?

Investing is a long-term strategy, even for non-professionals. As far as possible, avoid the noise, focus on your financial goals, and invest according to your own personal financial plan and situation. Completing a 'Risk Profile' will help determine the type of investor you are. If you are unsure of the best strategy for you considering today's events, you should seek independent professional advice before making your investment decisions.

Capital markets are unpredictable over short time periods and a well-diversified portfolio will help protect your capital over the long term. Successful long-term investors do not focus on poor performance in any given year – they review their strategy and make sure it is well aligned with their long-term objectives.

Diversification also helps in another way. It reduces the temptation or the need to move money from one type of investment to another in anticipation of what will happen next (market timing). Market timing fails because the markets have unpredictable patterns of return, and their major movements typically occur in short and sporadic bursts. Attempting to predict what the next best performing asset class will be and trying to avoid the worst performing one is counter-productive over the long term.

Investors often react emotionally to short-term market developments (such as a panic sell), despite their long-term investment horizons. Studies of investor behavior have proven this to be a losing strategy. The average investor typically misses out on long-term investment opportunities, as they exhibit more of a short-term focus. Don't be that investor. Stay invested, diversify and trust the process.