Capital Markets Update from Arbutus Financial

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Overview:

- No benchmark for what we are currently experiencing; But it's not the worst environment we've even seen
- Fear and nervousness is reasonable but don't let this turn into panic
- Recession in Canada, US and around the world but 2020 is different from past recessions
- We're likely more than halfway through the bear market
    - Don't think it's the end yet. Can see another modest downturn
- From here, a dollar in the market will have high probability of being positive 12 months out

Why is this environment different?

- Most recessions in the past come about due to excess or a bubble
    - 2008 – US housing bubble
    - 2001 – crash of .com market; overvalued companies, no business plan but overly funded, compounded by 9/11
    - Great depression – combination of excess manufacturing and excess in financial markets

- 2020 Recession was engineered by governments to contain the coronavirus
    - Believe it can easily be turned back on. Economy can resume and pickup again
    - Central governments committed $200B to fiscal spending + other stimuli, including lower interest rates
    - It's a globally coordinated effort

Investment Strategies:

- Being nervous is OK. But fear is not an investment strategy. Don't let fear turn into panic.
    a. Don't recommend going to cash
    b. Stay disciplined and stick to the plan you and your advisor developed together

- Dollar Cost Average into the markets.

- For clients who want to take advantage, we start to see a buying opportunity. At current levels, markets tend to be positive 12 – 24 months out. It's an attractive time to start "dipping a toe" back into markets

<u>Questions:</u>

Bonds typically a safe haven asset but some bonds and fixed income have decreased in value recently. What is going on?

- Good news is, bonds returned to being safe haven status and are now positive in many cases
- Reason bonds were down because of extreme volatility in equites
- Leveraged investors had to sell bonds in order to cover margin calls

- Generally, if equity markets sell off, corporate bonds would weaken but not to the same extent. Usually half of equity downside. Over medium term, investment grade and high yield bonds offer attractive yields. 8 or 9% for High Yield, and 4-5% for investment grade corporate bonds.

Currency, Oil and Gold

- As price of oil has fallen, CAD has fallen. CAD is currently moving in lockstep with oil prices
- OPEC+ Russia agreed to cut production by 9.7M barrels/day but oil demand is down
- Next 12 months, oil prices expected to increase. Nobody is making any money at $22/barrel
- Over next 12 months, oil prices go up, so CAD should move up
- Gold currently at $1,700/ounce. Fair value would suggest $2,000/ounce. Still some upside

Looking beyond covid19. How will the global economy change?

- Companies will have more insight on where they need to go eg:
    - Online platform, no contingency plan for many companies
    - Consumer stocks that can easily transition from bricks and mortar to online
- Healthcare a renewed focus for investors, including vaccines, medicines, medical supplies, etc.
- Companies that depend on global supply chains may need to spread out their supplies.
    - Some redundancies to mitigate risks. Wanting multiple geographic areas of supplies.
- More opportunities for companies that are globally oriented. Can switch from one resource area to another
- Sectors of the economy that have opportunities
    - Telecommunications, technology and industrials can do well
    - Consumer, retail, energy, materials will have a much tougher time

Active vs Passive Investment Styles:

- Volatility is partly due to passive investment techniques. Very easy to sell an ETF. The action of selling is contributing to volatility. Indiscriminate selling of both good and bad companies
- Whereas an active portfolio manager will know when to hold onto a stock with strong fundamentals or purchase ones that have been mispriced.
- Active managers also do their due diligence to find out which companies have a better chance of sustaining their business through various economic cycles.

Lessons from the past:

- Need to be rational. When we hear markets are down 40%, few clients are actually down that much because many are in balanced portfolios. Need to manage our media intake.
- Instead of investors learning from history, we're seeing more investors sell. That is a mistake
    - Investors sold more in 2018 than in 2008 and many did not come back into the markets
    - Such behavior locks in losses permanently and make it difficult to ever make it back
- Understand fear and nervousness. But need to prevent it from becoming panic. Panic is where we make mistakes
- Diversification and asset allocation remain key components of a solid investment strategy