Quarterly Commentary

North American Equity

The Canadian stock market had a good year as the S&P / TSX index returned 3.2% in the final quarter of the year and posted a strong 22.9% over 2019, a sharp reversal from 2018's 8.9% decline. Performance was broad based with most sectors in positive double digit territory. The leadership baton was passed back and forth between defensive and cyclical stocks and as a result, the TSX tested all-time highs on numerous occasions during 2019 peaking on December 24 at 17,180 points.

Despite the S&P / TSX's strong gain in 2019, performance over the last decade has been far less impressive as some heavyweight sectors like Energy and Materials endured protracted price declines. Canadian equity investors gained less than half of what U.S. equity investors gained over the past ten years and only marginally surpassed a composite government bond benchmark during the same time frame. Nonetheless there is some positive news as the last decade saw the index reach all-time highs by adding more than $700 billion in value. For instance, a few individual bets in Health Care, Consumer Discretionary and Industrials saw stratospheric performance in the thousand percentage range, an indication that Canadian markets are still offering great opportunities for investors.

In the U.S., the Standard & Poor's 500 index skyrocketed 9.1% in U.S. dollar terms over the fourth quarter. In Canadian dollar terms the index was up a healthy 7.0%. For 2019 as a whole the U.S. equity benchmark climbed 31.5% in U.S. dollar terms and was up 26.5% in Canadian dollars. The stellar 2019 performance is partly explained by a relatively low starting point as one year earlier the index lost 13.5% in U.S. dollar terms over the final quarter of 2018. We may be on the cusp of a recovery through the first half of this year thanks to central bank easing, the de-escalation in the trade war and tentative green shoots in global manufacturing. 2019 has seen the largest amount of central bank easing since the 2008 financial crisis and the central bank easing of 2019 may prolong the aged cycle. The main reason for the longevity of this cycle has been the persistence of economic slack. This has allowed the U.S. and other developed economies to grow without generating significant inflation pressure and has deterred central banks from lifting interest rates. The trade war has been a cycle extending global deflationary shock, in that it forced central banks to reverse previous tightening before monetary policy became restrictive.

The strong rebound of Canadian equities and its peers across the globe in 2019 should not overshadow the fact that global GDP growth recorded its slowest pace in a decade and most of the market returns stemmed from PE (Price/Earnings) ratio expansion due to lower rates rather than pure corporate growth. In Canada, the economy has been remarkably resilient in 2019 with record job numbers and unemployment at historical lows shrugging off the USMCA trade dispute as well as the U.S. / China protectionist policies.

The loonie was the best performing major currency, having benefited from a resilient and steady Bank of Canada key rate compared to more dovish rate decisions in other major economies. Job numbers were very strong though they slowed in October and November with back-to-back losses totaling 73,000 jobs. As for Canadian markets, a strong reversal from the previous year's decline and frequent all-time highs should not automatically trigger calls for a market peak or a bearish S&P / TSX outlook. The index is still seen as a 'value proposition" with a PE ratio at around 15 versus 18 for the S&P 500: the largest discount since the last great recession. As historically most markets over time revert to their means, Canadian equities still appear to be low hanging fruit for investors.

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