September 2020
Building your financial future

Investment Strategy

World

After an extraordinary plunge in Q1 and Q2, the global economy has begun climbing back up. Faster than expected, to judge by the Citi Economic Surprise Index. That said, its vigour varies widely from region to region. There are a number of explanations for this variance: seriousness of the pandemic, degree of exposure to the more vulnerable sectors such as tourism, and heft of fiscal and monetary responses by governments and central banks.

Weighing the catastrophic economic effects of the pandemic against the unprecedented response of governments and central banks, we stay with our scenario of a near 4.0% contraction of global GDP in 2020 followed by a rebound of close to 5% in 2021. We are nevertheless cautious about the outlook. Recent weeks have shown that no country has been safe from a resurgence of coronavirus cases.

World: Recovery is stronger than expected
Citi economic surprise index

NBF Economics and Strategy (data via Bloomberg)

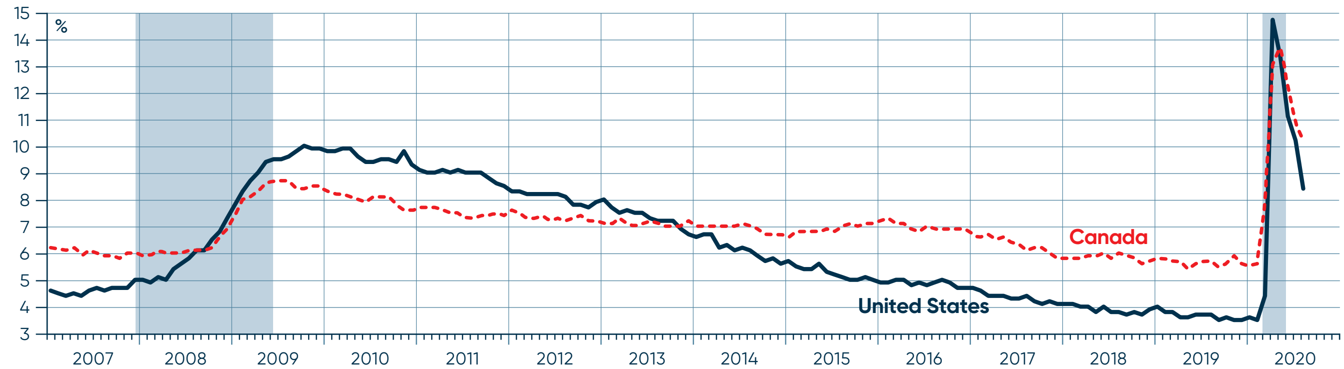
NATIONAL BANK FINANCIAL
WEALTH MANAGEMENT

In this issue

United States

The U.S. economy continues to recover, stimulated by strong latent demand and healthy household balance sheets. That said, it is hard to imagine a lasting recovery without a stronger rebound in services, which will continue to depend on the state of the pandemic. As long as people are fearful—a reality that could last until a vaccine arrives—many activities in which physical distancing is harder to maintain will be slowed despite massive aid from the Federal Reserve. Until then, Washington's fiscal support needs to be extended. Without it, the incomes of many Americans who lost their jobs could drop considerably. We see the U.S. economy expanding more than 3% in 2021. However, that assumes U.S. legislators will reach agreement on an extension of fiscal stimulus.

United States: Jobless rate is coming down
Unemployment rate

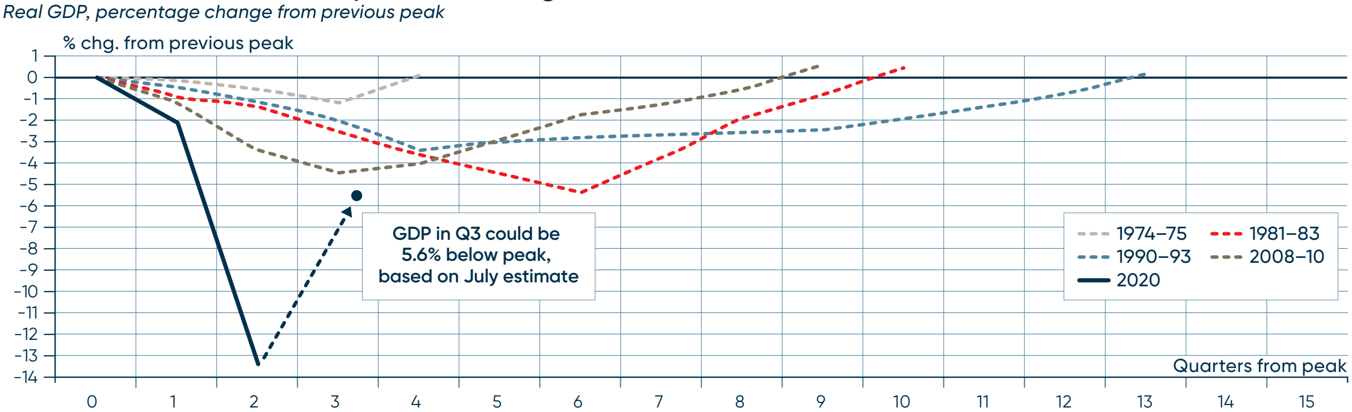


NBF Economics and Strategy (data via Statcan and Refinitiv)

Canada

The second-quarter contraction of the economy was much more pronounced in Canada than in the U.S., but the faster recovery of the Canadian labour market suggests a more vigorous revival in the third quarter. V-shaped recoveries of retail sales and home sales through June signal a faster-than-expected return to normal. But the picture is not all rosy. Households have been able to delay payments on debt, and the government's income-support programs have more than offset losses of employment earnings. One thing is certain: the period of weaning from this extraordinary fiscal stimulus will be a perilous time. We see the Canadian economy contracting about 6% in 2020 and expanding more than 4% in 2021.

Canada: Economic activity is rebounding in Q3
Real GDP, percentage change from previous peak



NBF Economics and Strategy (data via Refinitiv)

Investment Strategy

Despite some turbulence at the end of the quarter, most equity markets managed to post gains without too much difficulty over the summer months. South of the border, the S&P 500 even reached a new all-time high, buoyed in part by the spectacular rise in some of the giants of the technology sector. Meanwhile, central banks' clear intention to keep interest rates low for years to come compelled bond markets to tread water during the period and allowed gold prices to pursue their ascent. If this brief market review seems familiar, it is probably because the last few months have been characterized by a continuation of the trends initiated in the second quarter, to the great benefit of investors.

This positive outcome reflects the fact that six months after the market bottom, several data now allow us to conclude that many of the assumptions that enabled equity markets to initiate a recovery late in March have proved accurate. On the monetary front, emergency measures put in place by major central banks have effectively allowed credit flows to circulate without major complications and for the economy as a whole to avoid a deflationary spiral. In terms of fiscal policy, substantial government support has kept bankruptcies to a minimum, laid the foundations for a strong recovery in employment and ensured that a decent level of consumption was maintained. Regarding the virus, the adoption of best sanitary practices and advances in medical research have so far limited the severity of new waves of contagion, especially in terms of the rate of fatalities, while the possibility of generalized vaccination seems increasingly likely. Nothing can be taken for granted, but if we take a step back, we can only conclude that the overall situation is moving in the right direction, and so much the better.

Against this backdrop, our strategy that advocated a slightly higher allocation to equities and an overweight in the U.S. performed well. We maintain this positioning, but we took advantage of market movements in the third quarter to introduce certain changes to our geographic allocation by favouring emerging markets over Canadian equities. In our view, a possible breakthrough in the fight against the coronavirus and the passage of the presidential election could accelerate the depreciation of the U.S. currency. This, combined with the persistence of highly accommodative monetary policies, could trigger a sustained rotation towards higher-growth assets such as emerging markets.

Naturally, several risks will require close monitoring over the next few months. Important delays in the quest for a vaccine, as well as a potential increase in COVID-19 cases, would weigh on consumer confidence and thus slow the ongoing economic recovery. In addition, the political wrangling over the next round of U.S. tax measures poses a serious risk to the economy, with the Democrats and Republicans unable to reach agreement just weeks before the presidential election. In short, we should not be surprised if the last quarter of the year brings a higher level of volatility than what we experienced over the summer.

Nevertheless, we remain rather optimistic on the outlook for stock market returns for two main reasons. First, all evidence suggests that we are in the early stages of a new business cycle, a time when equity market performance is strongest on average. Second, monetary conditions strongly support equity markets, perhaps even more so than ever before. Therefore, unless one (or both) of these two elements—an early cycle backdrop and accommodative monetary policies—is called into question, risk assets should remain on an uptrend. Under these circumstances, we are maintaining our slightly pro-risk positioning and we stand ready to adjust our views as the situation evolves and opportunities arise.

MODEL PORTFOLIOS

Income Portfolio	Asset Class	Minimum/ Maximum	Benchmark	Recommended Weighting	Change from Previous Quarter
Investor Profile: You want to preserve your capital or establish a source of periodic income to finance ongoing expenses. You do not find the stock market very attractive because of its volatility, but you are not against the idea of investing a small part of your portfolio in stocks, mainly to counteract the effects of inflation. Your tolerance for risk is low.	Cash equivalents	0% to 20%	5.0%	5.0%	0.0%
	Fixed income (duration: 6 years)[1]	60% to 100%	70.0%	67.5%	0.0%
	Canadian equities	0% to 30%	8.0%	9.0%	0.0%
	U.S. equities		8.0%	9.5%	-0.5%
	Foreign equities		4.0%	4.0%	0.5%
	Alternative investments[2]	0% to 20%	5.0%	5.0%	0.0%
Conservative Portfolio					
Investor Profile: On the whole, you want your portfolio invested in fixed-income securities. Although you can tolerate limited volatility to ensure that your assets will grow, you prefer having a portfolio consisting mainly of fixed-income investments for reasons of stability. Your tolerance for risk is low.	Cash equivalents	0% to 20%	5.0%	5.0%	0.0%
	Fixed income (duration: 6 years)[1]	45% to 80%	55.0%	52.5%	-0.5%
	Canadian equities	20% to 45%	14.0%	15.0%	0.0%
	U.S. equities		14.0%	15.5%	-0.5%
	Foreign equities		7.0%	7.0%	1.0%
	Alternative investments[2]	0% to 20%	5.0%	5.0%	0.0%
Balanced Portfolio					
Investor Profile: You give equal importance to achieving growth in your investments and receiving income. You can tolerate moderate changes in market value to ensure growth, but you prefer having a mix of fixed-income investments and equities for reasons of stability.	Cash equivalents	0% to 20%	5.0%	5.0%	0.0%
	Fixed income (duration: 6 years)[1]	30% to 65%	40.0%	37.0%	-0.5%
	Canadian equities	30% to 65%	18.0%	19.0%	0.0%
	U.S. equities		18.0%	20.0%	-0.5%
	Foreign equities		9.0%	9.0%	1.0%
	Alternative investments[2]	0% to 25%	10.0%	10.0%	0.0%
Growth Portfolio					
Investor Profile: Your main goal is capital growth. Although you can tolerate greater volatility in order to increase the value of your assets, you are not prepared to invest your entire portfolio in stocks. Your tolerance for risk is high.	Cash equivalents	0% to 25%	5.0%	5.0%	0.0%
	Fixed income (duration: 6 years)[1]	20% to 45%	30.0%	27.5%	-0.5%
	Canadian equities	40% to 75%	22.0%	23.0%	0.0%
	U.S. equities		22.0%	23.5%	-0.5%
	Foreign equities		11.0%	11.0%	1.0%
	Alternative investments[2]	0% to 25%	10.0%	10.0%	0.0%
Maximum Growth Portfolio					
Investor Profile: You want to maximize the eventual return on your capital by investing all or most of your portfolio in the stock market. In doing so, you accept higher volatility of your investment returns in the hope that these returns will ultimately be higher. Your tolerance for risk is high.	Cash equivalents	0% to 30%	5.0%	5.0%	0.0%
	Fixed income (duration: 6 years)[1]	0% to 30%	15.0%	13.0%	-0.5%
	Canadian equities	55% to 100%	26.0%	27.0%	0.0%
	U.S. equities		26.0%	27.5%	-0.5%
	Foreign equities		13.0%	12.5%	1.0%
	Alternative investments[2]	0% to 30%	15.0%	15.0%	0.0%

1 FTSE TMX Canada Universe Index
2 Includes hedge funds, global infrastructure and gold

FORECAST

			Forecast	
	2018	2019	2020	2021
Gross Domestic Product %				
Canada	2.0	1.7	-5.7	4.1
U.S.	3.0	2.2	-4.0	3.0
Inflation %				
Canada	2.3	1.9	0.7	1.8
U.S.	2.4	1.8	1.1	1.9

	September 2020		December 2020		December 2021	
	Canada	U.S.	Canada	U.S.	Canada	U.S.
Rate %						
Short-term rates (T-bills, 91-day)	0.15	0.10	0.15	0.10	0.20	0.20
10-year bond yields	0.60	0.70	0.65	0.70	0.80	0.95
30-year bond yields	1.10	1.45	1.15	1.50	1.20	1.65
Canadian Dollar	US $0.75		US $0.74		US $0.78	