IN FORMED

Coronavirus Infects Markets

North American equity markets seemed unstoppable as the year began, but reversed course quickly this week, as fears of a pandemic spiked on revelations that coronavirus has now spread across Europe, Asia and North America.

At a glance

- While it is still too early to determine how far COVID-19 will spread and how long it will last, there is no question that it will have negative economic consequences.
- It may be too soon to declare that the rate of infections are subsiding, but it is positive to note that China's rate of new infections seem to be moderating to a single digit rate.
- The key drivers underpinning the global economy are still in place: accommodative monetary policy, strong labour markets and accommodative fiscal policy.
- TDAM believes that patient investors will continue to be rewarded.

What is happening?

North American equity markets seemed unstoppable as the year began, hitting record high after record high through two back-to-back crises - the Iran missile attacks and early onset of the coronavirus. But North American equity markets reversed course quickly this week, as fears of a pandemic spiked on revelations that coronavirus - known as COVID-19 - has now spread across Europe, Asia and North America.

While it is still too early to determine how far COVID-19 will spread and how long this flu will last, there is no question that COVID-19 will have negative short-term economic consequences. Things may get a little worse for the economy from here, however at this time we believe COVID-19 may delay economic growth, but not destroy it.

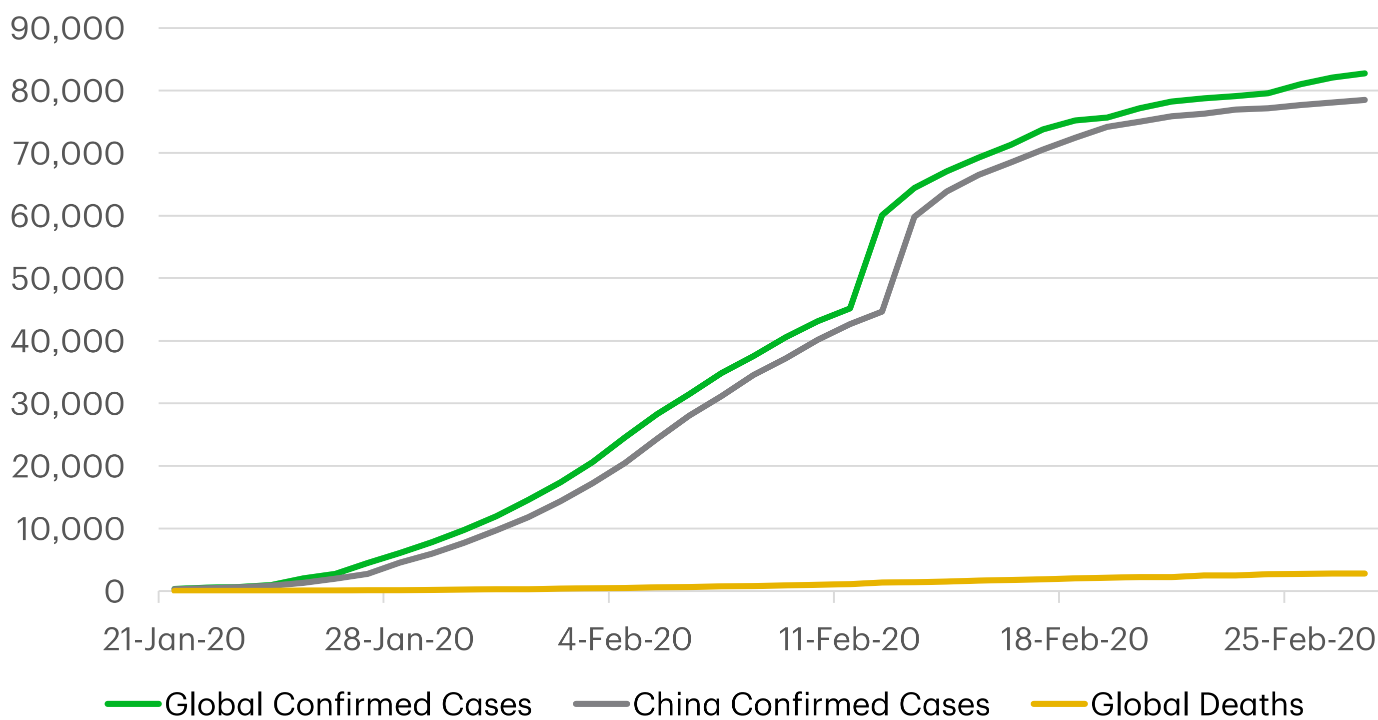
Undoubtedly the temptation to sell everything and move to cash will be high, as many experience motion sickness from the constant market gyrations and barrage of scary headlines. This temptation is normal. But history offers a very clear lesson. Giving into our emotions and selling investments during troubled times can often lead to disappointment. This is because weak markets have historically been followed by rapid recoveries. During times like these, it is important to remember that attempting to determine trends by watching daily market fluctuations and focusing on headlines, is not an accurate way to anticipate of future performance. A better approach is to take a long-term view, because even with the inability to predict where future returns will be year-after-year, the data still supports an investor who stays invested over time. Additionally, significant drawdown periods often present opportunities to acquire stocks in high quality companies at more attractive valuations.

How many cases have been confirmed globally?

According to the World Health Organization, there have been 82,271 confirmed cases and this number is rising as COVID-19 has spread outside of China to other Asian nations, Europe and North America. It is worth noting that while the absolute number of total cases is high and rising, the total number of recovered is also rising as 33,253 people globally have recovered from the virus.

As illustrated in Chart 1, the rate of infection was rising at a double-digit rate during January and early February, but the infection rate has since fallen to a pace in the low single digits. While it is still too early to declare that the rate of infection is subsiding, it is positive to note that China's rate of new infections seems to be moderating to a single digit rate. This may suggest that the dramatic measures (lock downs/travel restrictions) taken to contain the virus may be taking effect – giving hope that the spread can be controlled in the other countries. And fortunately the mortality rate has not appeared to be as high as some of the other coronavirus pandemics (SARS, MERS).

Chart 1: Confirmed Cases



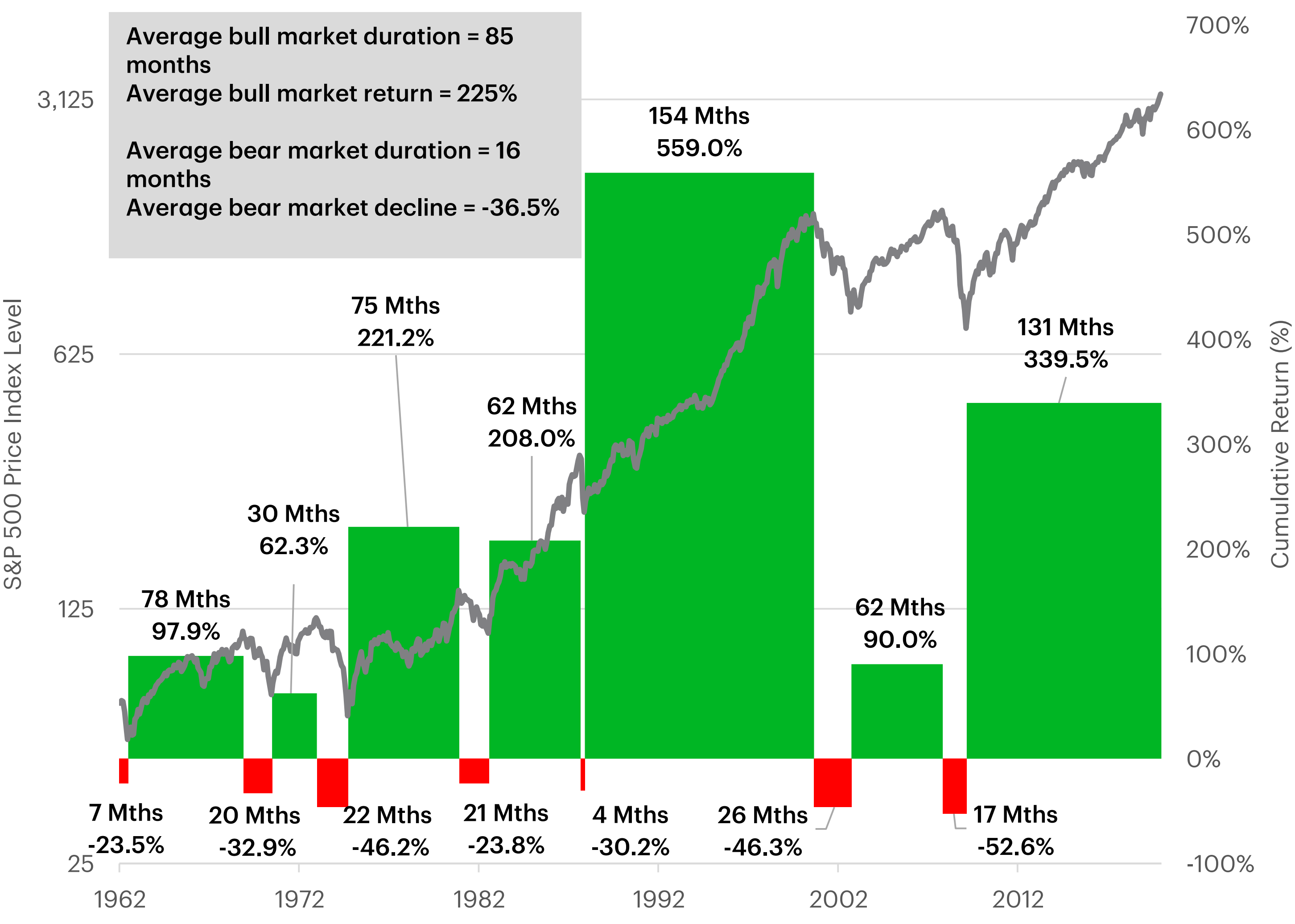
Source: Bloomberg Finance L.P., World Health Organization, TDAM. As of February 27, 2020.

How COVID-19 may impact the global economy and stock markets

It is still too early to know the exact magnitude of the impact of COVID-19, which is not unusual, as the future is always unpredictable. History shows that regardless of the length or depth of a correction, equity markets have recovered and resumed their upward trend through a myriad of crises, turmoil and wars. As shown in the chart 2, 7 bull markets have been interrupted by 7 bear markets in Canada since the 1960s.

Bull markets are much longer in duration than bear markets (defined here as a minimum 20% decline from the peak). Over this period bear markets lasted 16 months on average for an approximate loss of 35%, while bull markets, or rising markets, ran an average 7 years for a typical gain of 225%. In short, equity markets have historically risen far more often than they have come down – regardless of how steep the decline.

Chart 2: Duration of Bull and Bear Markets

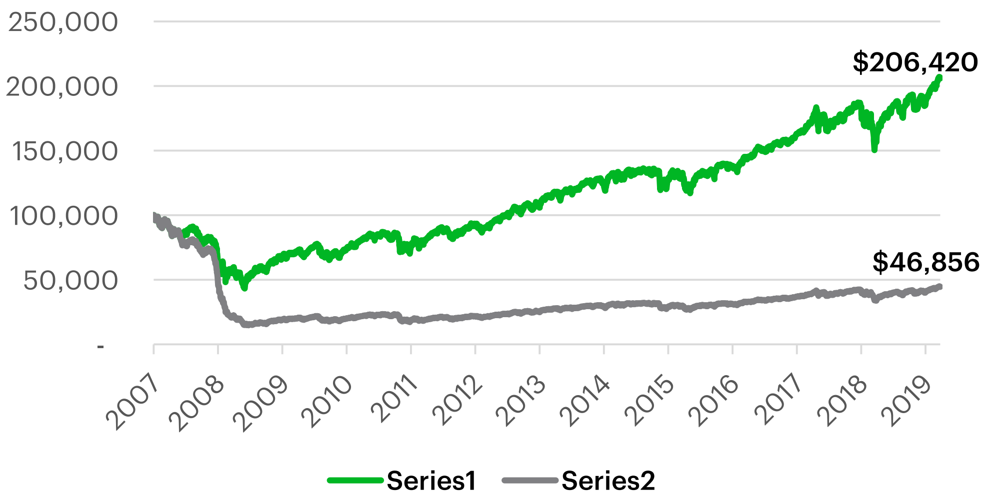


Source: Bloomberg Finance L.P., TDAM. As of December 31, 2019.

Market timing can lead to diminished returns

Moving to cash and waiting for certainty may seem like a prudent strategy, but it is fraught with danger. To illustrate, let's start with Chart 3. A $100,000 investment at the peak of the last bull market on October 10, 2007 would have immediately lost money due to the financial crisis, but would have grown to $206,420 by the end of 2019 had it remained invested. To illustrate how challenging it can be to time the market, consider this: there were 3,079 trading days from October 10, 2007 to December 31, 2019. If you had missed 1% of the best days (approximately 30 days), a $100,000 investment would have returned a mere $46,856.

Chart 3: Growth of $100,000



Series 1 represents the growth of $100,000 in the S&P 500 Price Index (US) from October 10, 2007 to December 31, 2019. Series 2 represents the growth of $100,000 assuming you missed 1% of the best days (30 days) between October 10, 2007 and December 31, 2019.

For illustration purposes only. Source: Bloomberg Finance L.P. as of December 31, 2019

A key consideration is that the best trading days often fall within periods where the worst days also occur. As illustrated below, some of the top 30 days trading actually occurred within days of the top five worst days over the period.

Date	S&P 500 Index Level	Return	Rank Worst Return	Date	S&P Level	Return	Rank Best Return
10/15/2008	907.84	-9.03%	1	10/16/2008	946.43	4.25%	18
				10/20/2008	985.4	4.77%	11
12/1/2008	816.21	-8.93%	2	12/2/2008	848.81	3.99%	24
				12/5/2008	876.07	3.65%	29
				12/8/2008	909.7	3.84%	26
9/29/2008	1106.42	-8.81%	3	9/30/2008	1166.36	5.42%	8
10/9/2008	909.92	-7.62%	4	10/13/2008	1003.35	11.58%	1
11/20/2008	752.44	-6.71%	5	11/21/2008	800.03	6.32%	7
				11/24/2008	851.81	6.47%	5

Source: Bloomberg Finance L.P., as of December 31, 2019.

TDAM's Views

Undoubtedly, things may get a little worse for the economy from here and market volatility may persist for some time yet, but TD Asset Management Inc. (TDAM) remains hopeful that patient investors will continue to be rewarded. The key drivers underpinning the global economy are still in place: accommodative monetary policy, strong labour markets and accommodative fiscal policy. Globally we've seen central banks ready to take decisive action. The Chinese authorities have already provided a liquidity injection of 1.7 trillion Chinese Yuan (US$240 billion) with the expectation that they may also provide further measures in the form of lower interest rates. Fiscal policy of RMB 200 billion (US$29 billion) was also committed to help ease the impact. Other relief measures included rent relief, tax relief, and fee cuts for businesses that were impacted by the outbreak. Interestingly, Chinese stock markets are staging an early recovery and have risen 8.9% since reaching a year-to-date low on February 4, 2020.

TDAM's portfolio management teams are continually monitoring the situation to assess how our investments will be impacted by the outbreak and at this time we believe there is no permanent impairment.