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Weekly Market Compass: Market predictions and investment resolutions for 2021

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Weekly Market Compass: I believe a robust, inclusive economic recovery is in the cards

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Happy New Year! No one wants a year in review for 2020, but here is what I learned from the past year: History may not repeat itself, but it sure does rhyme. What we learned from 2020 is a repeat of the lesson we learned from the global financial crisis (GFC): Central banks are very powerful. They can't cure viruses and they can't create jobs, but they can boost confidence and move markets - a lot. That is the big similarity 2020 had with 2009: Central bank intervention mattered, especially by benefiting risk assets.

When I think of the New Year, I think of predictions and resolutions. And so today, I provide you with a little of both.

My New Year's predictions

1. U.S.-China relations may get warmer. There seem to be two factions emerging among Biden loyalists: “reformists” who want to push China aggressively on key issues and check its power, and “restorationists” who want to restore U.S.-China relations to where they were in the Obama administration. I believe Biden will do what he typically does: land somewhere in the middle.

I don't expect U.S.-China relations to return to what they were pre-Trump. However, I do expect the relationship between the two countries to improve and normalize. In particular, I expect more predictability and less volatility. While Biden may not unwind tariffs immediately, I do expect him to unwind the Trump administration tariffs after a “study” of their impact (which has obviously been negative for parts of the U.S. economy, especially agriculture). The Biden administration will likely be aggressive on specific issues with China and pursue those issues multilaterally - but I expect that to occur within the context of a broader U.S.-Sino relationship that is more cordial because the fortunes of many U.S. businesses are tied to China.

The Chinese economy is on pace to soon overtake that of the U.S., with the timeline expedited due to COVID, which gives China growing leverage. In fact, the Centre for Economics and Business Research recently released its forecast that China will overtake the United States by 2028 as the world's largest economy, which is five years earlier than previously estimated due to the two countries' very different recoveries from the pandemic.¹

In addition, China has already begun to signal that it would like improved relations with the United States. China's Foreign Minister Wang Yi said in a recent interview with the South China Morning Post that both the U.S. and China have been negatively impacted by the deterioration in their relationship over the past several years, and that U.S.-China relations have come to a “new crossroads” with a “new window of hope” opening.²

2. Developed countries may have a better recovery than they did post-GFC. As COVID-19 vaccines are broadly distributed, I expect the economic recovery to be far more robust and inclusive than the economic recovery coming out of the global financial crisis. I believe the services industry will rebound with greater intensity, benefiting many lower income workers. That doesn't mean that there won't be more glitches in distribution - I fully expect there to be. And there will likely be more pandemic-related headwinds, such as the development of worse strains of the virus. However, once a substantial portion of the population is inoculated, I expect the economic recovery to be powerful.

3. Oil may rise. Given my expectation for a strong economic recovery in 2021 as vaccines are distributed, I also expect demand for oil to increase significantly. I believe this will lead to a substantial increase in the price of West Texas Intermediate crude oil - even if we see a ramp up in oil production.

4. Bitcoin may fall. I know there is a lot of excitement over Bitcoin, but it's starting to feel a bit like Tulipmania.³ Bitcoin rose more than 300% in 2020, with much of the gains made in the last few months of the year.⁴ I continue to believe gold is a far better choice for diversification into “hard assets” and as a hedge against geopolitical risk. Bitcoin might continue to run for a while this year, but I expect it to be volatile and to ultimately disappoint, as it has in the past after strong rallies.

5. The S&P 500 Index may have another double-digit return in 2021. With vaccine distribution beginning, a robust economic recovery anticipated in the not-too-distant future, as well as extraordinary accommodation from the U.S. Federal Reserve, I expect a continuation of the stock rally we saw in 2020, albeit with drops and pauses along the way. Better-than-expected corporate earnings should also help.

My New Year's resolutions

1. Stay invested and well diversified. While I feel very confident about risk assets in 2021, that doesn't mean there won't be volatility and sell-offs in the coming year. I believe having adequate exposure to stocks, fixed income, and alternative asset classes is key to building a portfolio that may withstand volatility.

2. Look to Asia's emerging markets. My outlook is especially bright for the emerging markets countries that have managed the pandemic well, such as China and Korea. These economies have a head start on the robust vaccine-fueled economic recovery that I expect in 2021.

3. Don't overlook tech. While the economic rebound may result in strong performance by cyclical stocks in sectors such as energy and consumer discretionary, I don't necessarily expect tech stocks to underperform. I continue to favour adequate exposure to the technology sector, as I believe many tech stocks may continue to benefit from

trends that accelerated during the pandemic.

1 Source: Reuters, "China to leapfrog U.S. as world's biggest economy by 2028: think tank," Dec. 25, 2020

2 Source: South China Morning Post, "China-US relations: Beijing says 'new window of hope' is opening as it offers Biden administration an olive branch," Jan. 2, 2021

3 "Tulipmania" refers to one of the most famous market bubbles in history. In the 1600s, the price of tulip bulbs in Holland rose to extreme highs before crashing.

4 Source: CNBC, "Bitcoin rallies above \$30,000 for first time after advancing over 300% in 2020," Jan. 2, 2021

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