November 12, 2020

RBC WEALTH MANAGEMENT

Global Insight Weekly

Just what the doctor ordered?

Frédérique Carrier – London

A vaccine at last—and it appears to be a successful one at that. This helps us look through the COVID-19 valley and focus more confidently on the recovery and post-pandemic world. Do investors need to rethink positioning?

Good news at last

The Pfizer/BioNTech COVID-19 vaccine announcement on November 9 was received by equity markets with enthusiasm, with the S&P 500 rallying 1.2 percent on the day, and the MSCI World Index reaching a new all-time high the day after. The results markedly surpassed general expectations, especially in terms of the vaccine's efficacy in preventing symptoms, and some market participants seemed surprised by the timing of its availability. The vaccine is likely to be the first one to receive regulatory approval in the U.S. and Europe, which could happen within weeks.

The vaccine's efficacy rate of more than 90 percent, far exceeding the U.S. Food and Drug Administration's (FDA) 50 percent hurdle rate, is remarkably high for a first-generation vaccine. This could mean other vaccines using a similar technology are likely to be successful as well.

Some questions remain, including how safe the vaccine is, though this data should also be available within weeks. With time, we will find out how long the vaccine protection lasts and how efficient it is when used on the elderly, as cohorts are added to the trial.

Enthusiasm for the Pfizer/BioNTech vaccine is tempered by logistical challenges. It requires two doses to be administered three weeks apart. It also needs to be stored in dry ice to ensure a temperature of minus 70 degrees Celsius (-94 F) or below—a challenge for governments considering rolling it out, particularly for developing countries and those in temperate regions.

Once safety data is released, emergency use filing can be done in the U.S. and Europe. After receiving the full efficacy data in December, the FDA can approve the drug. Pfizer/BioNTech expects that 50 million doses can be available by year-end and 1.3 billion doses next year (i.e., 750 million vaccinated). For context, the EU has ordered 300 million doses, the U.S. 100 million, and the UK 30 million.

The possibility of vaccines taming the pandemic is becoming more tangible. Data for two other vaccines are due before the end of the year. The vaccine being developed by AstraZeneca and Oxford University is possibly the most eagerly anticipated. Based on a different technology, only one dose is required, and it wouldn't need to be kept below freezing temperatures, suggesting it would be more scalable than Pfizer/BioNTech's. Moreover, it is reportedly already known to be effective for the elderly. We should also know the results of the Moderna vaccine trial by year-end and the results of four others will likely come in sometime in the first half of next year. Should most of these be successful, the global vaccination rollout could make important inroads next year.

Market pulse

Click here for authors' contact information. Priced (in USD) as of 11/12/20 market close, ET (unless otherwise stated). **For important disclosures and required non-U.S. analyst disclosures, see page 6.**
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Good for the economy

To be sure, the manufacturing capacity and the distribution of the vaccine will not be in place to save the winter in the Northern Hemisphere. Social distancing and lockdown measures will likely stay in place for now, capping economic growth in the economically important Q4 2020 and possibly in Q1 2021. But the Pfizer/BioNTech data brings forward the possibility of a better outlook for economic growth in 2021 for several reasons, and as such, it is undeniably good news.

The availability of a vaccine and the success of its technology likely reduces the risk of a potential third wave in autumn 2021. Knowing there is an end to the crisis in sight, some governments could opt to give more generous fiscal relief than would have otherwise been the case. Our national research correspondent thinks a U.S. COVID-19 stimulus package of $1 trillion is more likely than one of $500 billion. A vaccine also helps investors to look through the COVID-19 valley and focus more confidently on the recovery and the post-pandemic world.

The vaccine announcement brought on abrupt risk-on moves in financial markets that day. The S&P 500 closed up 1.2 percent, a performance that came on top of post-election gains which had been the highest in history.

The S&P 500's move camouflages an aggressive rotation in equity markets. Momentum strategies, in which investors buy securities when their prices have been rising and sell those when they have been declining, had their worst performance since 2009. The FAANGs (Facebook, Amazon, Apple, Netflix, and Google parent Alphabet), which have led market gains since March, also retreated abruptly. These technology companies' business models have thrived in the COVID-19 era, with their stocks being widely perceived by market participants as defensive investments in these difficult times. Globally, megacaps underperformed riskier small caps. Struggling Financials and Energy stocks roared upwards. Meanwhile, the oversold FTSE All-Share Index, a broad index of UK stocks, closed up approximately five percent, a rarely seen showing and its second-best performance since the 2016 Brexit referendum.

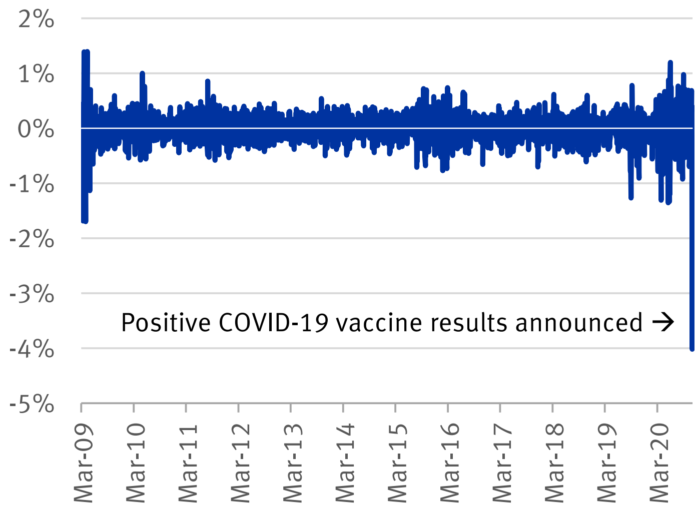
Other traditional growth indicators also pointed to an improvement in the economic outlook: the U.S. yield curve steepened, with the yield on the 10-year Treasury note increasing to 0.95 percent from 0.80 percent prior to the vaccine announcement. Profit-takers brought gold prices down to $1,855/oz, perhaps a sign of a safer environment.

A flash in the pan?

For investors, the question is whether these aggressive one-day moves herald a broader, more sustained rotation towards cyclical positions. To be fair, they were probably also a function of crowded positions, i.e., investors all chasing similar themes and being heavy in certain sectors (such as the FAANG group with their resilient business models for the current environment) while avoiding others (like the Energy sector due to the sharp fall in oil prices and banks due to ultralow interest rates). The aggressive market rotation also facilitated a record valuation differential between growth and value stocks.

Sharpest market reversal since 2009

Daily price change in the Bloomberg US Pure Momentum Portfolio Total Return Index



Source - Bloomberg; daily data through 11/10/20

A general and longer-lasting rotation towards reflationary positioning, or economically-sensitive stocks, would require inflation expectations to continue their ascent and Treasury yields to extend their moves upward.

For now, we believe it's reasonable to expect a period of consolidation for equities following the sharp gains since the U.S. elections and vaccine news. Moreover, the global economy is not out of the woods yet, and investors may start to ponder the logistical challenges of rolling out vaccines globally.

Investors should use this time to consider their portfolios' exposure to cyclicality, or economically-sensitive stocks. The possibility of viable vaccines should enable investors to look through the crisis and assess companies that were most affected by COVID-19 on the basis of normalised earnings. Many of these companies' stocks will appear undervalued, in our view. We recommend adding some exposure to cyclicals and value stocks to take advantage of the likely improvement in economic conditions that COVID-19 vaccines could bring.

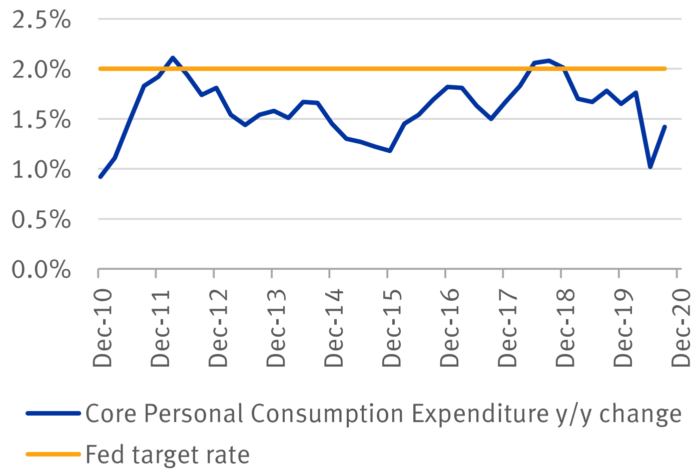
United States

Atul Bhatia, CFA – Minneapolis

- **Investors sold Treasury bonds this past week on a trifecta of headlines**. Nonfarm payroll data showed the U.S. private sector added over 900,000 jobs in October, helping bring the unemployment rate down to 6.9%; the U.S. election—while not resulting in a unified government—has likely opened the doors to at least moderate fiscal stimulus in the early days of the new administration; and the efficacy data for a COVID-19 vaccine raised hopes for a potential return to normal social activity by mid-2021. The combined impact of the news flow was **sufficient to push 10-year government bond yields up to nearly 1%, their highest level since March** of this year, as investors moved into more economically-sensitive assets.
- **While the headlines were positive for potential future economic growth, the impact on Federal Reserve policy is less clear.** The Fed's new average inflation targeting regime should have the central bank on hold until inflation is well-established and has been at least moderately above 2% for sufficient time to compensate for the years of below-target inflation. That combination—plus the need for low policy rates to help the U.S. government fund its debt burden—will likely require the Fed to be on hold for many years.
- **Corporate bonds—particularly those from riskier, lower-rated issuers—have performed particularly well** in November as economic growth and low policy rates are a tremendous boon. The Bloomberg Barclays US Corporate High Yield Bond Index is now priced to yield just under 4.6%, down almost 1.2% in November and below even pre-pandemic levels. The historically low yield on that index, however, is largely attributable to Fed policy and the overall drop in government bond yields; the portion linked to corporate issuer risk—the credit spread—is still above pre-pandemic levels, although it too is down 0.9% since the end of October. **With so few opportunities to generate yield in fixed income, corporate bonds will likely continue to attract investor interest.**

No pressure on the Fed to raise rates

Accumulated sub-target inflation argues for extended monetary accommodation



Source - RBC Wealth Management, Bloomberg

Canada

Richard Tan, CFA & Arete Zafiriou – Toronto

- **The S&P/TSX Composite rallied more than 3% from last Friday's close**, driven by greater clarity regarding the U.S. elections and the announcement of a potential COVID-19 vaccine. News of the latter broke on November 9 and, in our view, ultimately led to a sharp market rotation away from growth- to value-oriented stocks. **Structural pandemic successes** such as video conferencing tools, e-commerce, and gold companies **experienced sizeable pullbacks** as capital rotated into sectors that have been decimated by the socially distanced environment. Examples include Real Estate and Energy, which have been among the worst-performing sectors through the majority of 2020 due to lower retail foot traffic, work-from-home trends, and reduced energy consumption levels. The idea that the economy could return to some degree of normalcy caused these sectors to re-rate but, generally speaking, most stocks within them are experiencing significant year-to-date losses. Overall, we believe **momentum is in the value camp** but we note that tax-loss selling season is also around the corner and many of these value stocks could be likely candidates from our perspective.
- **The Canadian labor market added 84,000 new jobs in October.** Employment grew 0.5% m/m, according to Statistics Canada, a slower pace than the average of 2.7% since May, as a number of provinces tightened COVID-19 containment measures in response to an increase in infections. Notably, the accommodation and food services sector lost 48,000 jobs in October after five months of job gains. Over 85% of the losses occurred in Quebec, one of the earliest provinces to put renewed restrictions on indoor dining and bars. The labor market has yet to recover to pre-shock levels, with more than 600,000 fewer people working than in February. The **unemployment rate has dropped from its 13.7% peak in May to 8.9% in October**, but remains above the 2008–09 financial crisis peak of 8.7%.

Europe

Frédérique Carrier & Thomas McGarrity, CFA – London

- **Spurred by encouraging vaccine news, UK and European markets rallied** during the week. The FTSE All-Share Index gained nearly 7% and the STOXX Europe 600 ex UK nearly 4% in the three days after the announcement of positive results from the Pfizer/BioNTech COVID-19 vaccine trial. The FTSE's gains were helped by its heavy tilt towards **Energy and Financials**; these two sectors had sold off strongly due to the economic impact of the pandemic, and **both stand to benefit from a potential vaccine-driven improvement in economic prospects**. The FTSE's UK oil and gas subindex gained 19%, and the financial stocks close to 10% with life insurers in particular registering strong gains. In Europe, banks and the oil and gas subsectors led the gains and were up 16% and 13%, respectively.
- **In the UK, Q3 GDP expanded by 15.5% quarter over quarter**, a strong bounce after a nearly 20% q/q contraction in the preceding quarter. The expansion brought the UK economy to 92% of its pre-pandemic level at the end of September. With the reintroduction of lockdown measures, we believe the gap will not close before year's end, even if the hit to activity is not as severe as it was in the spring given restrictions are not as drastic. **RBC Capital Markets expects Q4 GDP to contract by 3.4% compared to Q3**, leaving full-year 2020 GDP decline in the 11.5% region.
- **Europe's overall industrial production declined in September, but this was due to a drop in Italy** following an exceptionally strong production number in August; all other countries reported a small expansion. This suggests **the European industrial sector's recovery remained healthy** in September despite additional lockdown measures imposed in several countries. This trend may weaken somewhat going forward the longer the measures remain in place.

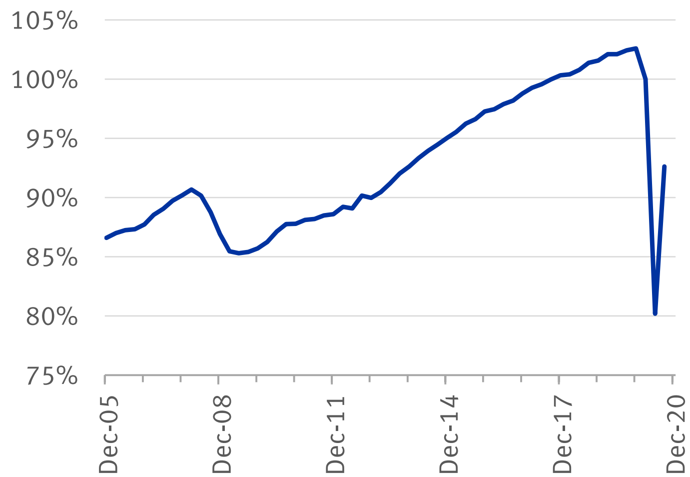
Asia Pacific

Jasmine Duan – Hong Kong & Nicholas Gwee, CFA – Singapore

- Following the Pfizer vaccine results news, a rotation from growth to value stocks occurred globally, including in **China and Hong Kong equities. China banking, China property, and energy stocks led the market, while tech stocks sold off**.

Strong September bounce, but UK GDP still at 2014 levels

UK GDP as percentage of 3/31/20 level



Source - RBC Wealth Management, Bloomberg

- The Asia tech decline gained momentum after **China released a consultation paper** on guidelines for anti-trust activities regarding internet platforms on Nov. 10. The regulation aims to promote fair competition, protect consumers' rights, and ensure sustainable, healthy development of the platform-based economy. The news **triggered further profit-taking of tech stocks**, particularly for Alibaba (9988 HK) and Meituan (3690 HK), as investors worry that the business of platform leaders will be affected more. The Hang Seng TECH Index slumped 11.4% on Tuesday and Wednesday. Feedback on the guidelines will be accepted until Nov. 30. Due to the ambiguity of the enforcement and lack of clarity on the effective date, the introduction of guidelines may be a short-term overhang for tech stocks.
- **Despite recent regulatory headwinds, Alibaba reported strong Singles' Day (Nov. 11) sales** with total sales for the Singles' Day Festival of RMB 498.2 billion representing 26% y/y growth. The strong growth was **boosted by the introduction of an additional sales window** Nov. 1–3.
- **DBS (DBS SP) Q3 2020 results came in ahead of expectations** with profit before allowances down 9% q/q (-8% y/y) and net profit up 4% q/q (-20% y/y). Quarter-over-quarter net profit improved as business momentum recovered with fee income rebounding 17% to pre-COVID-19 levels, softening the impact of lower interest rates as well as a decline in trading income from a high base. **A SG$0.18 dividend was declared**, in line with Monetary Authority of Singapore guidance.

MARKET SCORECARD

Data as of November 12, 2020

Equities (local currency)	Level	MTD	YTD	1 yr	2 yr
S&P 500	3,537.01	8.2%	9.5%	14.4%	29.7%
Dow Industrials (DJIA)	29,080.17	9.7%	1.9%	5.0%	14.5%
Nasdaq	11,709.59	7.3%	30.5%	38.0%	62.6%
Russell 2000	1,708.47	11.0%	2.4%	7.1%	12.5%
S&P/TSX Comp	16,582.18	6.4%	-2.8%	-1.9%	9.4%
FTSE All-Share	3,569.99	13.3%	-14.9%	-12.1%	-7.7%
STOXX Europe 600	385.16	12.5%	-7.4%	-5.3%	6.4%
EURO STOXX 50	3,428.20	15.9%	-8.5%	-7.7%	7.3%
Hang Seng	26,169.38	8.6%	-7.2%	-3.3%	2.1%
Shanghai Comp	3,338.68	3.5%	9.5%	14.5%	26.9%
Nikkei 225	25,520.88	11.1%	7.9%	8.5%	14.6%
India Sensex	43,357.19	9.4%	5.1%	7.5%	24.5%
Singapore Straits Times	2,711.90	11.9%	-15.9%	-17.0%	-11.6%
Brazil Ibovespa	102,507.00	9.1%	-11.4%	-4.0%	19.9%
Mexican Bolsa IPC	40,335.95	9.1%	-7.4%	-6.4%	-6.9%

Commodities (USD)	Price	MTD	YTD	1 yr	2 yr
Gold (spot $/oz)	1,876.60	-0.1%	23.7%	28.9%	56.3%
Silver (spot $/oz)	24.27	2.6%	35.9%	44.7%	73.4%
Copper ($/metric ton)	6,866.00	2.4%	11.7%	17.5%	13.0%
Oil (WTI spot/bbl)	41.12	14.9%	-32.7%	-27.6%	-31.4%
Oil (Brent spot/bbl)	43.44	16.0%	-34.2%	-30.0%	-38.0%
Natural Gas ($/mmBtu)	2.95	-12.0%	34.8%	12.6%	-22.1%

Govt bonds (bps chg)	Yield	MTD	YTD	1 yr	2 yr
U.S. 10-Yr Tsy	0.880%	0.6	-103.8	-105.5	-230.2
Canada 10-Yr	0.720%	5.7	-98.2	-88.3	-178.5
U.K. 10-Yr	0.348%	8.6	-47.4	-45.8	-110.4
Germany 10-Yr	-0.536%	9.1	-35.1	-28.4	-93.4

Fixed Income (returns)	Yield	MTD	YTD	1 yr	2 yr
U.S. Aggregate	1.28%	-0.1%	6.2%	7.0%	18.5%
U.S. Invest Grade Corp	1.98%	0.7%	7.2%	8.9%	23.9%
U.S. High Yield Corp	4.73%	3.0%	4.2%	6.4%	14.2%

Currencies	Rate	MTD	YTD	1 yr	2 yr
U.S. Dollar Index	92.9700	-1.1%	-3.5%	-5.4%	-4.7%
CAD/USD	0.7609	1.3%	-1.2%	0.7%	0.8%
USD/CAD	1.3142	-1.3%	1.2%	-0.7%	-0.8%
EUR/USD	1.1808	1.4%	5.3%	7.3%	5.3%
GBP/USD	1.3118	1.3%	-1.0%	2.1%	2.1%
AUD/USD	0.7231	2.9%	3.0%	5.7%	0.8%
USD/JPY	105.1200	0.4%	-3.2%	-3.6%	-7.7%
EUR/JPY	124.1200	1.8%	1.9%	3.4%	-2.8%
EUR/GBP	0.9002	0.1%	6.4%	5.0%	3.1%
EUR/CHF	1.0807	1.2%	-0.4%	-1.1%	-4.7%
USD/SGD	1.3497	-1.2%	0.3%	-0.9%	-2.5%
USD/CNY	6.6130	-1.2%	-5.0%	-5.6%	-5.0%
USD/MXN	20.6385	-2.5%	9.0%	6.8%	1.4%
USD/BRL	5.4575	-5.0%	35.4%	44.4%	45.0%

Source - Bloomberg. Note: Equity returns do not include dividends, except for the Brazilian Ibovespa. Bond yields in local currencies. Copper Index data and U.S. fixed income returns as of Wednesday's close. Dollar Index measures USD vs. six major currencies. Currency rates reflect market convention (CAD/USD is the exception). Currency returns quoted in terms of the first currency in each pairing. Data as of 8:35 pm GMT 11/12/20.

Examples of how to interpret currency data: CAD/USD 0.76 means 1 Canadian dollar will buy 0.76 U.S. dollar. CAD/USD -1.2% return means the Canadian dollar fell 1.2% vs. the U.S. dollar year to date. USD/JPY 105.12 means 1 U.S. dollar will buy 105.12 yen. USD/JPY -3.2% return means the U.S. dollar fell 3.2% vs. the yen year to date.

Authors

Frédérique Carrier – London, United Kingdom
frederique.carrier@rbc.com; RBC Europe Limited

Atul Bhatia, CFA – Minneapolis, United States
atul.bhatia@rbc.com; RBC Capital Markets, LLC

Richard Tan, CFA – Toronto, Canada
richard.tan@rbc.com; RBC Dominion Securities Inc.

Arete Zafiriou – Toronto, Canada
arete.zafiriou@rbc.com; RBC Dominion Securities Inc.

Thomas McGarrity, CFA – London, United Kingdom
thomas.mcgarrity@rbccm.com; RBC Europe Limited

Jasmine Duan – Hong Kong, China
jasmine.duan@rbc.com; RBC Investment Services (Asia) Limited

Nicholas Gwee, CFA – Singapore
nicholas.gwee@rbc.com; Royal Bank of Canada, Singapore Branch

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As of September 30, 2020

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Buy [Outperform]	788	52.96	248	31.47
Hold [Sector Perform]	619	41.60	135	21.81
Sell [Underperform]	81	5.44	11	13.58

Ratings:

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