MACKENZIE Investments

Mackenzie Call Series

Calming perspectives in uncertain markets

Oil, coronavirus, rates, and the debt market

On March 10, Mackenzie held a conference call to talk about oil, interest rates, and market volatility. Providing expert insights were **Steve Locke** (Senior Vice President, Portfolio Manager, Head of the Mackenzie Fixed Income Team) and **Benoit Gervais** (Senior Vice President, Portfolio Manager, Head of the Mackenzie Resource Team).

Conference call highlights

- COVID-19 update: As it continues to spread worldwide, it has become a significant headwind to global growth. Containment efforts like quarantines and lockdowns have reduced demand in consumption as people change how they proceed in "everyday life"

Update on fixed income market

- 10-year U.S. Treasury yields are now at historic lows, largely as a result of the recent oil market collapse
- The Fed and Bank of Canada each cut rates by 50bps, but markets were not satisfied as they're still concerned about the ultimate economic impact of COVID-19. More rate cuts may come soon, heading toward but likely not going below the zero-bound level in North America
- Central banks and governments will need to get creative with monetary and fiscal policies to deal with today's volatile markets and the fallout from COVID-19, in order to avoid a recession
- Default rates in the high yield bond and loan markets will likely rise in this risk-off environment, particularly in energy high yield, which may hit a 20% default rate if oil markets continue struggling
- Even before COVID-19, the Mackenzie Fixed Income Team had anticipated lower global trade, policy rates and yields in 2020, so they have been positioning with longer duration in a "flight to quality" scenario and de-risking by reducing corporate credit allocation, increasing quality (moving up the capital structure), seeking greater industry exposures to enhance diversification and tightening high-yield hedges with a put strategy. The team has also assessed what companies/industries may be most impacted by a disrupted supply chain and has cut exposure to be defensive and add protection

Update on resource market

- To balance their budgets (inventories), OPEC+ strives to keep oil prices high enough by limiting production. Russia has recently refused to join Saudi Arabia's strategy. Saudi Arabia with now limited ability to cut production further, changed direction and instead joined Russia's strategy by pledging to increase production to gain market share. This action, along with lower demand amid COVID-19, has caused oil prices to plunge
- Low prices aren't sustainable over the long term. Production cuts and the eventual containment of COVID-19 will support rising prices. Currently, production cuts of almost two million barrels per day in North America are needed to stabilize the market
- Under these challenging conditions, oil companies must decide whether to pay down debt or maintain their dividends. The industry could experience large layoffs and may see capital expenditures cut in half
- Market leaders should get even stronger in a period of industry rationalization, as they have good access to capital, strong processes and solid balance sheets, and may be able to increase dividends when oil prices rebound
- China's production of resources like iron ore and copper has declined as refineries shut down during the COVID-19 outbreak. So far, other countries have continued producing, but circumstances are subject to change
- In uncertain and volatile times like these, gold has been a good diversifier (often as 5% to 10% of a typical portfolio)

Check out the conference call
Listen to our archived conference call on our website here, or dial in to the instant replay number below to learn more about what's going on in the markets.

Toll-free: 1-800-408-3053
Passcode: 7056447

Please note that the dial-in number will only be available for 30 days after the event and will expire on April 10, 2020.