April 17th , 2020 Communique
2020 versus 2008

Good afternoon everyone, we hope this Communique finds you and your loved ones safe and healthy.

After having the privilege of being on a couple calls with the likes of CIBC's Deputy Chief Economist, Benjamin Tal, as well as former Chairman of the Federal Reserve, Ben Bernanke, I would like to forward some of their observations and comments as well as the take away we have made at Baker Financial Group. I will attempt to put the current pandemic in economic perspective by contrasting some of the major respective points of difference between the COVID crisis and the financial crisis of 2008/2009. I will report on what Canada and the U.S. have done from both a monetary and a fiscal standpoint. I will then conclude with some of our thoughts on where we are and where we are headed.

In 2008, the primary problem was the financial system itself. Bad mortgages led to panic which led to cutbacks in credit which resulted in financial disfunction ergo economic dysfunction. Saving the economy back then meant saving the big banks and it was easy to be politically opposed to rescue package bailouts. This resulted in wasting precious time. Today there is a common enemy, the virus. A positive result of this has been elevated Congressional cooperation, calls to action are being made swiftly.

This COVID-19 virus is effectively a natural disaster, a pandemic affecting the entire world that is leading to social distancing, shutdowns, lock downs, which all have the effect of bringing down the economy. That is what has caused risk to the financial markets. Financial markets are at the end of the causal arrow this time, not at the outset. This does not preclude the situation from being very scary. However, this has an end game. Once there is a vaccine, presumably the crisis will be over.

Contrary to 2007, the U.S. came into this with a very strong banking system. Canada has always had a strong banking system. Over the last 12 years the U.S. has undergone an overhaul that arguably puts their banks' balance sheets in a comparable, if not even superior position to handle the present crisis. In addition to this strength Congress has approved the FDIC guarantee of bank debt and barring a much worse recession than currently expected, the financial system should ultimately be a source of strength through this recovery as opposed to what transpired in 2008.

Policies are different now than they were in 2008. Back then the problem was the financial market itself. The U.S. had to bring in Troubled Asset Relief Program (TARP) to stabilize the economy and then further administer additional monetary and fiscal stimulus to promote recovery. Contrastingly, the most critical public policy in 2020 is public health. Globally, we need to slow infection to bend the curve, make sure we don't overwhelm health systems and ultimately bring the economy back online. There are lots of steps that can be taken to bolster recovery regardless if they fall short of a cure. This includes social distancing, more extensive testing, different practices in different industries, and the continuing global race toward antiviral medications.

Even just today Gilead reported some 'rapid recovery' in coronavirus patients with the drug remdesivir.

The reason for such quick and large monetary and fiscal policy responses is to support the economy in this period of shut down. It is to help people pay bills and to help businesses avoid bankruptcy so when the all-clear is given people can get back to work.

Federal governments have acted to support liquidity in the capital markets, making sure financial institutions have access to cash and that credit keeps flowing to the real economy. The Current monetary policy of cutting rates close to zero, buying securities and providing forward guidance has calmed the markets and offered relief during the critical period of economic lockdown.

It is worth taking a look at some of the numbers. In the U.S., the size of the Fed`s balance sheet has neared $6TN, the highest it has ever been. The Bank of Canada has been fantastic too, having moved quickly to cut rates dramatically while avoiding negative-rate territory. There is unlimited quantitative easing (QE) with respect to government bonds, designed to put enough liquidity into the system to keep it running. The Canadian Government borrowed a huge amount of money ($200BN), which puts upward pressure on long term interest rates. When this is done with the Bank of Canada simultaneously pushing in the other direction with QE, it effectively puts a lid on the cup. Two opposing forces; proof the two of them are working together very effectively.

Canada saw fiscal policy put forth $250BN in terms of spending. We have never seen this before. Just think back to yester-month when an extra billion or two onto the deficit was a huge deal. Now, it's not even a rounding error. There are also many ways the banks are helping indirectly, such as:

- One can get six months payment deferred on interest and principal
- If you have GIC you can cash it without penalty
- If you have unsecured credit you can skip payments
- Banks entered the MBS market to help price/rate control
- Small businesses can get 6 months deferral interest and principal
- 75% wage subsidy

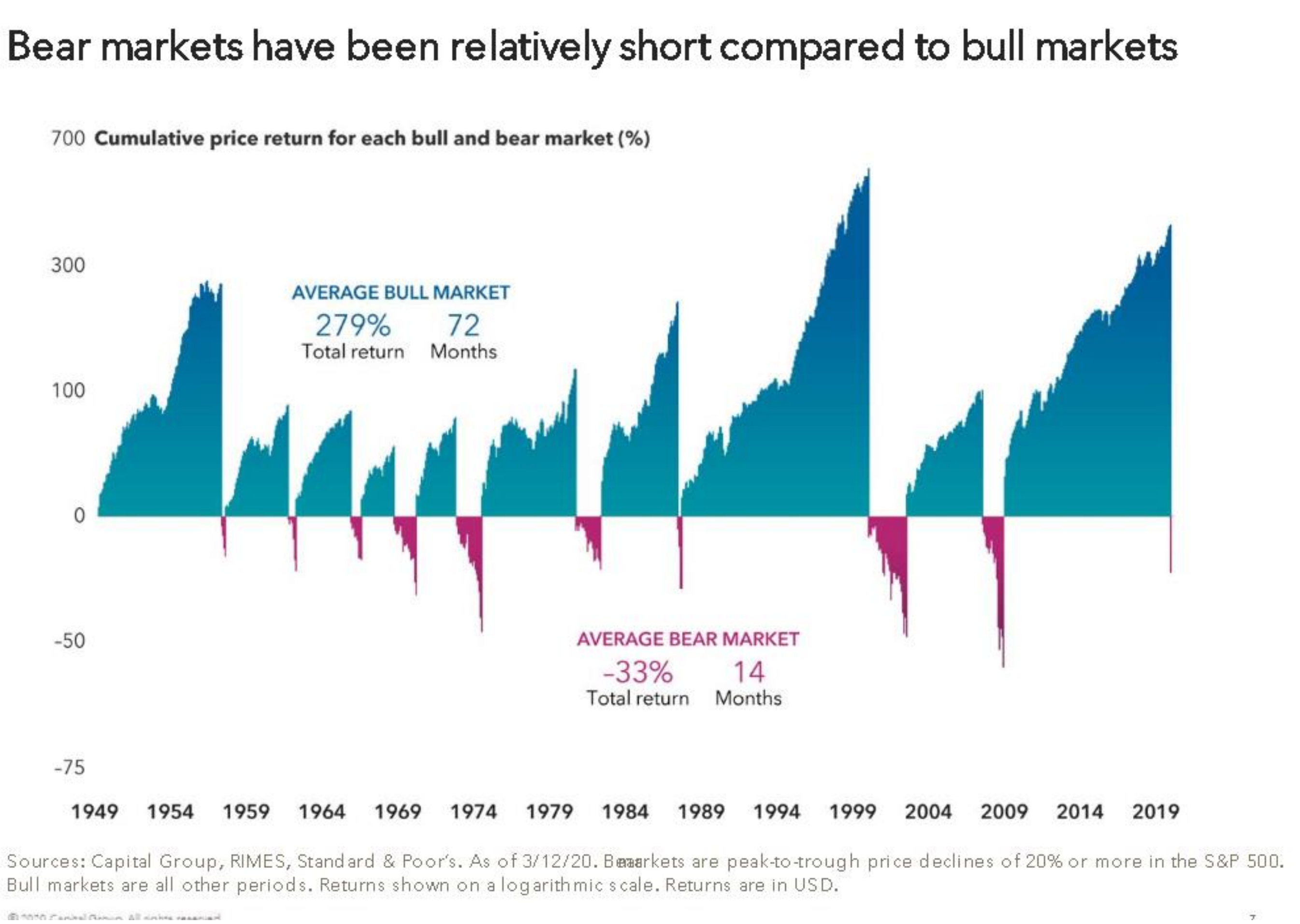
The list goes on and continues to evolve.

The reality remains, however, that recovery both domestically and globally will depend on public health, science, and confidence. It will likely be slow with false starts and it will be different across regions, industries and businesses. While it will be a down year, our best hope is that the economy will open by the later part of the year, especially as the medical situation improves.

At Baker Financial Group our best-case scenario would consist of a deep, but short-lived recession and a U-shaped recovery, although we are cognizant of the potential for a 'W' shape or uneven recovery and of permanent capital impairment in some areas. This is a highly uncertain environment and it is one that warrants extreme caution and care.

We continue to act on lessons learned from past crises as we have been through them and are still here working hard for you every day. It is critical to get through a period that may seem dark from an economic perspective to get to a brighter future. That bridge, from a policy perspective, is liquidity. It is also a bridge for portfolio construction and for portfolio management as we continue to hold the companies best suited to make it though this downturn and come out stronger on the other side. This combined with some geographical, strategic, and asset diversification continues to build safety in your portfolios and helps to participate in recovering asset prices.

Here is a graph from Capital Group that provides some warranted perspective:



Remember bottoming in 2008/2009? If anyone said that we would have had an amazing 10-year bull market… no one would have believed him/her. We are not out of it yet, there is going to be more red added to that graph. However, we are confident that there will be a nice clear blue structure on the other side of it.

Emotions work in a similar pattern, when things are feeling like you want to sell and you cannot get out fast enough and then all of a sudden there is a quick bounce-back and everyone wants back in and then, they get a bad case of FOMO a week later. Have patience. Bryan has been doing this since 1978, he has been through more than a couple of these recessionary downturns. The rest of us writing and or reading this made it through 2008 and we will persevere. This pandemic has an endgame, and that is a vaccine.

There is a recovery in sight. Albeit markets are volatile, and the path is hard and bumpy, but there is a path, nonetheless. This is different from times in the past, like 2008 when there was no path and uncertainty was overwhelming. We are not uncertain. We know where we are headed. We will stick to our process and the facts; we will exercise caution and be very vigilant in execution of uncovered opportunity.

On behalf of Baker Financial Group, CIBC Wood Gundy, we work hard every day to be worthy of your trust.

Most sincerely,

CIBC Wood Gundy
Baker Financial Group

Bryan Baker

Jonathan Baker

Toronto Bay Adelaide Branch | 333 Bay St, 28th Floor, West Tower, Toronto, ON M5H 2R2 | 416-594-7954 | www.bakerfinancialgroup.ca