January 2020 Financial Markets Update

A Complete Wrap-Up Across FX, Interest Rates, and Energy Commodities

ATB listens

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Highlights

- *Mark Johnson on the balancing act being pursued by the BoC and the Fed*
- *Janek Guminski and Mark Engelking walk us through the currency markets, while CJ Hilling and JP Doré take a look at Natural Gas and Crude Oil*
- *In the Chartpack we illustrate the delicate dance between equity valuation and the Fed's balance sheet; introduce our country 'snapshots'; and review crude oil, yields, FX, and volatility indices*

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Central Bank Overview

Mark Johnson MBA, Director Interest Rates

In November's month end update we wrote that we thought that 2020 might be the year in which we question the benefits of uber-easy policy. We suggested that perhaps the financial instability that low rates can bring - coupled with the inherent lift that it gives to wealth inequality by inflating asset values - might call into question such policy accommodation. Just goes to show what we know. We are barely in February and that (admittedly qualified) prediction looks deluded.

In fairness, we did suggest that we may see more easy policy across the planet in 2020 - possibly in Canada and the US and certainly in China, for example. That certainly appears a distinct possibility. But we also speculated that this might be viewed as the final card laid and the narrative might turn (in the developed world) towards fiscal support for those economies being more needed than monetary.

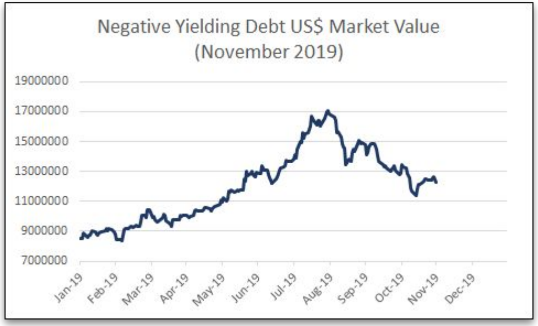
Currently, this looks to be some way in the distance - if indeed it is to happen at all. Despite 68 rate cuts by 46 central banks global in the second half of last year, 2020 opens on the same theme. Central banks on the whole did not turn over into the New Year and resolve to think differently, it would appear. The Federal Reserve, the alpha male in the central bank pack, is leading the way in staying the intellectual course. Despite leaving rates on hold at 1.50% (as expected), Chair Jerome Powell had this to say when questioned on the Fed's (dovish) attitude to inflation;

"Policy makers are not comfortable with inflation running persistently below our 2% objective."

Certainly, the market does not think we are about to see a shift away from central bank super heroes saving us all in 2020

Look at the charts below. Yields are tipping further into negative territory globally again after a respite in H2 2019.

<u>Negative Yielding Debt as of Nov '19 (top) and Jan '20 (bottom)</u>



Source: Bloomberg, ATB Financial Markets

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The Fed will be as cautious and patient as it sees fit, but will do whatever it has to do to prevent benign inflation influencing activity through reduced inflation expectations (ie not become Europe -becoming "European" is a bad look in today's America on so many levels.....)

As Powell said back in December:

"We would need to see a really significant move up in inflation that's persistent before we would consider raising rates to address inflation concerns."

"We of course have watched the situation in Japan, and now the situation in Europe. We note that there are significant disinflationary pressures around the world, and we don't think we're exempt from those."

At present, there are currently two Fed cuts priced into the curve for 2020. And right now, in the absence of more data, and leaving the threat the Coronavirus poses to the global economy aside for a moment, it is hard to argue with that assessment.

What of Canada, I hear you ask? Well, when I said that there was no new thinking in this space in 2020 as of yet, I did the Bank of Canada a huge disservice.

You see, they appear to be considering the adoption of this new European and American hip paradigm in monetary policy - *Let The Horses Run and Inflation Be Darned*. The BoC followed the Fed in their old school inflation-preempting hikes of 2018, but sat still as the Fed reversed these moves and adopted a more relaxed attitude to letting their economy run hot (in fairness, in the absence of inflation in the US) in the second half of 2019. But you may recall this chart from November's update:

The gist of the message conveyed here was one echoed by the BoC in late 2018 - being that a decade of low rates in a fundamentally sound domestic economy has created high levels of indebtedness in the Canadian household. It appeared to be different up North, as it were.

Deputy Governor Wilkins touched on this in October;

"And while Canada's economy is performing well overall and financial vulnerabilities have stabilized on the back of more stringent regulations, the nation's debt levels remain elevated - a situation unlikely to change if global interest rates remain low."

"With vulnerabilities high and inflation close to target for more than a year, we said at our most recent interest rate decision that taking out insurance wasn't worth the cost at that time."

Central Bank Overview

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In other words, we will sit tight as the Fed ease - we do not have their problems (falling inflation), and we have plenty of our own that make rate cuts tricky at best and inappropriate at worst.

But that was then. Let us focus on what is now. This to what Governor Poloz said just over a week ago (Jan. 22nd);

"In forming this view, we weighed the risk that inflation could fall short of target against the risk that a lower interest rate path would lead to higher financial vulnerabilities. There are emerging downside risks to the outlook for inflation."

So is a shift in the thinking on inflation happening? and what could that mean for rates?

Poloz went further;

"Household financial vulnerabilities remain elevated, although we will be analyzing the positive implications of a higher household savings rate for those vulnerabilities. All things considered, then, it was Governing Council's view that the balance of risks does not warrant lower interest rates at this time. "

"A crystallization of some domestic downside risks….suggested that overall excess capacity in the Canadian economy has increased, which will bring a degree of downward pressure on inflation over the projection horizon. "

Now that's a lot of economics and central bank-speak, but the message is pretty clear.

Having marked down growth projections for Q4 2019 and Q1 2020, the BoC see the possibility that *relatively* deficient demand in our economy may start to push inflation down -much as it appears to be doing in the US.

They also see the possibility - given the slowdown that they are seeing is largely on the back of a hibernating consumer - that the additional after-tax earnings that workers are experiencing (wage growth at 4% is double the rate of inflation, which means extra money in your jeans) may be getting used to pay down debt instead of being spent at the store.

What to make of all of this technical talk?

Central Bank Overview

Mark Johnson MBA, Director Interest Rates

In other words, the two barriers to cutting in 2019 may be disappearing as we enter 2020. Perhaps they can ease and get Canadian rates down to where US rates currently are. As if to make his point crystal clear, Governor Poloz finished;

"I'm not saying that the door is not open to an interest rate cut. Obviously it is. It is open."

That was for all those that were not paying attention and the headline writers (which may be the same people). We can be in no doubt that there is an excellent chance that the BoC will deliver a rate cut in H1 2020 (and the Coronavirus only increases that possibility). The market, never requiring a second request, has fully priced in that cut.

How to summarize this? Well, we had previously described the BoC's thoughts on rate direction as a "Reluctant Easing Bias."

For now it is fair to say that they are reluctant no more. They appear to be coming around to the idea that they can ease rates and deal with inflation when, and indeed if, it shows up - all while not risking an avalanche on a mountain of debt to boot.

For the observer, the next steps should be to pay close attention to the Canadian data over the next couple of months.

- ***Will Q4 2019 GDP and Q1 2020 GDP print at a worrying 0.3 and 1.3% respectively, as the BoC suggests?***
- ***Will inflation start to drift under 2% regularly as the BoC fears?***
- ***Will the consumer continue to pay down debt?***

Answer "yes" to either 1 or 2, plus 3 and you can bank on a rate cut in Canada in H1 2020.

It appears that we underestimated the concern that central banks globally have with regards to seemingly unboostable inflation. The new paradigm in policy towards historically unmatched loose rate settings is clearly compelling. We suspected the Fed would not be able to resist. We are surprised that this might also be the case for the Bank of Canada.

All that said, should the data disappoint and the market push on in its rally - pricing in further cuts - we feel that their may be opportunity. After all, the BoC take their responsibility for the long term financial health of Canadians very seriously and while the trend towards savings is helpful, it hardly changes the overall picture.

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Central Bank Overview

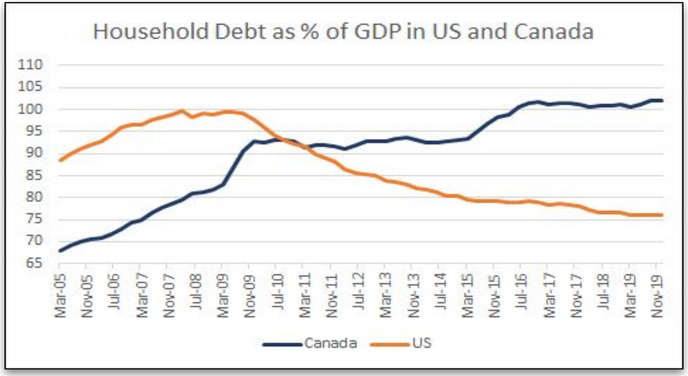
Mark Johnson MBA, Director Interest Rates

In the US, Corporate debt is the issue, not household. Firms have leveraged themselves over the last decade on the back of easy policy. While this will keep the Fed concerned, it is not the headache of household debt. Those ratios have moderated since the financial crisis (getting financially ruined will clip your wings and encourage prudent behaviours). So the Fed can let the US economy run hot without fearing tipping the average american over the edge.

In Canada, as we have discussed previously ad nauseum, the picture is still very different. I think the chart here paints that picture for us as clear as can be. The US has de-levered; Canada has not.

The Bank of Canada will take heart on the increased trend in savings in Q4 2019. They will likely use it pragmatically to get Canadian rates at parity with those in the US (one cut.) But I refuse to believe that they will ignore the differences in our two economies and throw caution to the wind on policy setting.

Debt Levels in Canada and the US



Source: Bloomberg, ATB Financial Markets

Right now they are throwing open the possibility that they may be moving their thinking on the relationships between growth, inflation and rates. They may be trying to get a little more hip to match some of their central bank peers around the globe. Certainly they are giving us the heads up that their thoughts are turning in that direction. The data will have to comply if they are to follow through.

When push comes to shove, all the BoC may have achieved - and it is not insignificant to be fair to them - is the creation of the opportunity to cut that 25 bps to get our rates at par with the US again.

The bar to more activity on the rates than that is higher than the market believes. That may create some opportunity should the market rally further.

The next few months will be fascinating as we discover just how "thoroughly modern" and hip the BoC wants to be in 2020.

Canadian Dollar

Janek Guminski CFA, Sr. Director FX Sales

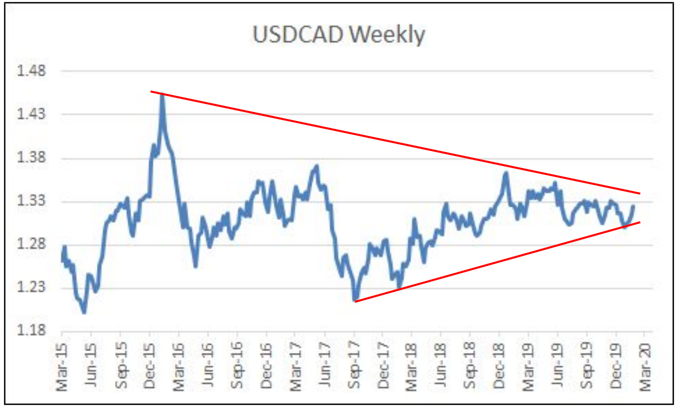
In January, both the Bank of Canada as well as the FOMC gave indications that further rate cuts are being considered. The market has a cut priced in for both countries by July and an additional 50% chance of a cut for the end of 2020. Next meetings are March 4th for Canada and March 18th for the Fed.

The Canadian dollar remains range bound despite having shown a little bit of strength to finish off 2019. A move below the 1.3000 level in late December proved to be far less interesting than we had hoped. In January, we saw a one-way move from 1.2975 to 1.3225, which is basically the mid-point of the 1.2952 - 1.3565 range that the currency has traded in over the last twelve months.

The pennant pattern that has formed on the USDCAD chart appeared to have been broken in late December but CAD could not follow through and spent most of January giving up its gains.

As you can see from the chart, USDCAD has made its way back into the point of the pennant. It is just a matter of time until we see a break higher, or a break lower. Currently it seems more likely that breakout will be higher (stronger USD) but as we know, and have all likely lived through, that can change very quickly. The longer the pennant takes to form (and seven years is a significant amount of time) the greater the move once it is broken.

USDCAD Pennant - could break either way

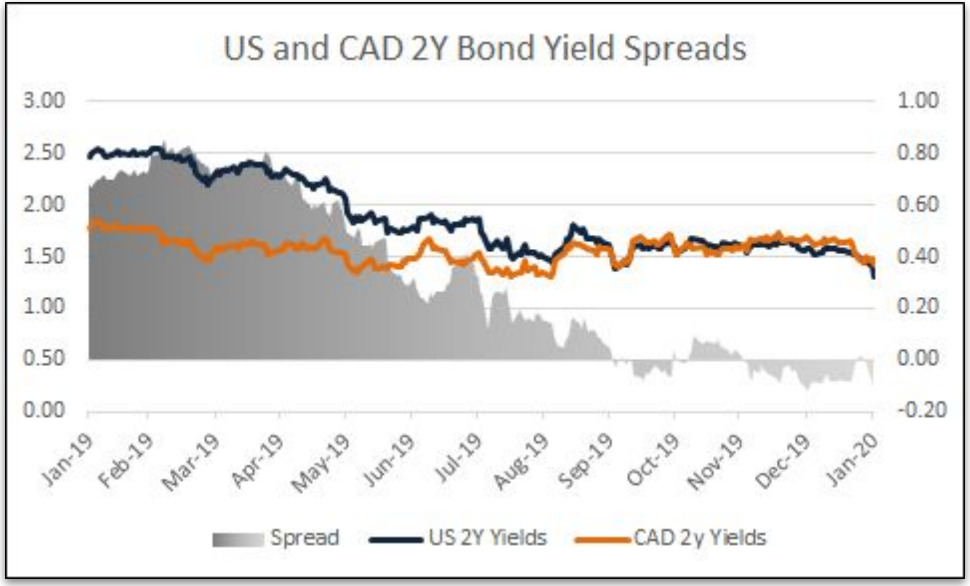


I suspect once this move happens, and it will, many participants will be caught flat-footed. Because of the narrow range in 2019, many clients have become complacent about hedging and that makes me very uncomfortable. I strongly suggest hedging using a strategy that provides full protection (in case the breakout move works against you) with some participation (in case the breakout move works in your favour). **The exact details can be tailored to your particular needs...reach out to your ATB foreign exchange specialist for further discussion on this.**

Canadian Dollar

Janek Guminski CFA, Sr. Director FX Sales

- The advantage that US yields once held over CAD yields has all but disappeared
- The Fed has been rather dovish, driving yields lower, and the BoC has finally taken a slightly more dovish tilt as well
- With the shift from the BoC putting downward pressure on the CAD curve, coupled with the risk-off tone across markets, it will be difficult for the Loonie to strengthen materially in the near term
- The synchronicity of Global Central Banks has created the perfect landscape for currency pairs to exhibit incredibly low levels of volatility by historical standards...

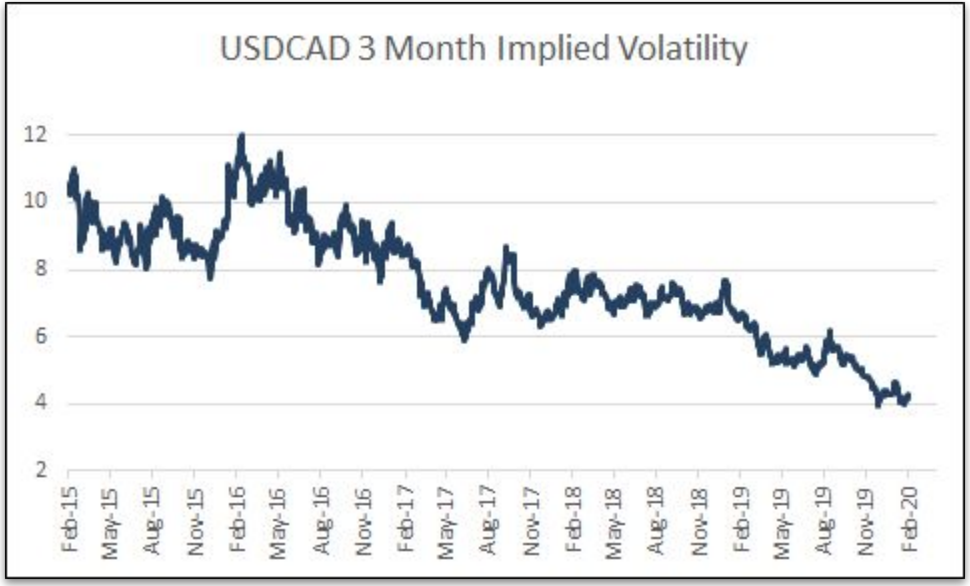


Source: Bloomberg, ATB Financial Markets

Canadian Dollar

Janek Guminski CFA, Sr. Director FX Sales

- The Canadian Dollar, along with pretty much the whole G10 FX complex, has exhibited exceedingly low levels of volatility over the past few years
- The chart here is of 3 month implied volatility for the Loonie, quoted as an annualized percentage
- Essentially this means that over the next three months, we would expect to see USDCAD trade in a 4% range
- You can see how that compares to Feb 2016 when volatility was quoted at 16%
- While volatility does exhibit mean reversion, it is also true that low volatility tends to beget more low volatility - so don't expect things to change anytime soon…
- From a hedging perspective, low volatility readings make Vanilla option strategies more attractive



Source: Bloomberg, ATB Financial Markets

USD Index and G10 FX

Mark Engelking CFA, Director FX Trading

Welcome back! I hope everyone had a nice holiday break. For those that do New Year's resolutions I hope you are off to a good start. If the USD made a resolution to be stronger in 2020 it is certainly off to a flying start. The greenback is the best performing currency in the month of January for one reason. It is not the Fed, it is not the economy, and it is not Trump. It is the first time the phrase 'having a Corona' is not associated with a positive outcome, unless of course you are more of a Pacifico fan.

The coronavirus has sent shockwaves through markets in January and in the G10 that means a flight to safety. The USD along with the other "safe" currencies like the Japanese Yen and Swiss Franc were the front runners. Meanwhile the higher risk currencies like the Scandies and the Antipodeans have struggled along with the Norwegian Krone.

As we speak, the WHO declared the virus and International Emergency and where we go in the month of February will depend an awful lot on what the virus does from here.

G10 FX Returns Against the USD

Monthly FX Spot Returns % Against USD	
Japanese Yen	0.38%
Swiss Franc	0.37%
British Pound	-0.36%
Euro	-1.06%
Danish Krone	-1.09%
Canadian Dollar	-1.89%
Swedish Krona	-2.70%
New Zealand Dollar	-3.87%
Norwegian Krone	-4.57%
Australian Dollar	-4.63%

Source: Bloomberg, ATB Financial Markets

The DXY Index has broken above the 200-day moving average and is rapidly approaching resistance around 98.40. Momentum indicators point to the big dollar being overbought but fears of contagion may inspire more buying in the short term as we come up against support on a short term trendline higher.

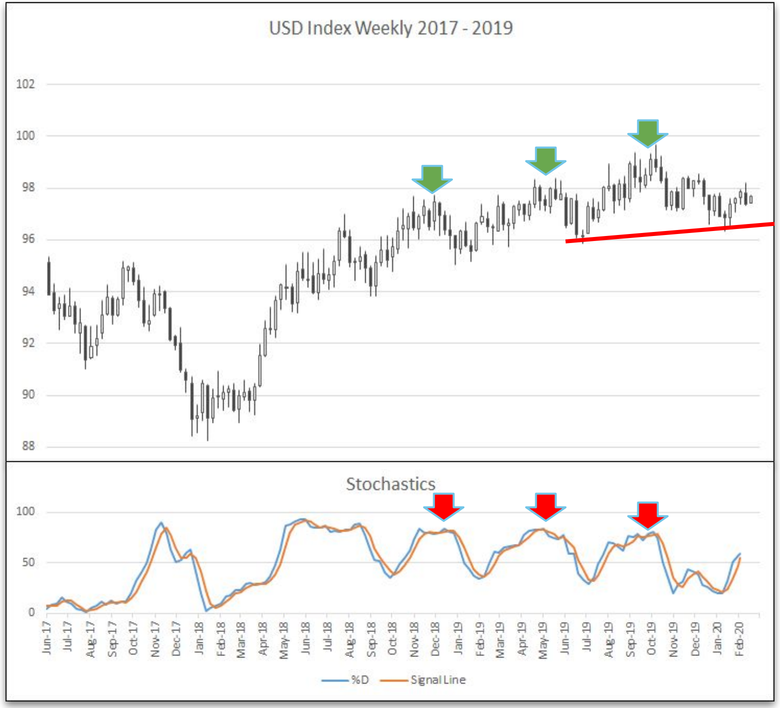
The University of Hong Kong estimates that the outbreak may peak between April and early May.

With a bow on Brexit and the ECB and other central banks pushing governments towards more fiscal stimulus the coronavirus will dominate direction for the month of February. It would certainly be bad karma to call for an epidemic so I think if authorities get a handle on the virus and transmission slows the higher beta currencies like the Antipodeans and the Scandies will catch a nice bid and retrace some of the January losses while the USD declines. If the outbreak escalates I would expect the flight to safety to continue and the USD move higher to extend into February, longer than some of the technicals suggest.

USD Index and G10 FX

Mark Engelking CFA, Director FX Trading

- The US dollar index recovered into the end of 2019 and early part of 2020
- Momentum is trending in the greenback's favour right now, with stochastics on the subchart above the 50 line
- However, we do note that stochastics made a series of lower-highs since 2018 even as the DXY made new highs - **pointing to triple momentum divergence** (green arrows on top, red arrows on bottom)
- The early part of February will be critical - if the index can't get back above at least the 98.50 high from December 2019, then selling will likely increase and a larger move below 96 and then 94 could come into play



Source: Bloomberg, ATB Financial Markets

WTI Crude Oil

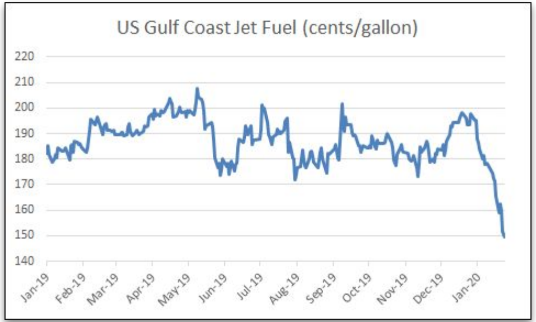
JP Dore, Markets Analyst

Global crude prices have certainly suffered to start the year with prompt WTI posting a -18% drop for January as we went to press. That is the worst monthly performance for oil since November 2018's -24% decline. So, what's causing all the turmoil?

Fears over the spread of the coronavirus (nCov) and its impact to oil demand growth have gripped the market and certainly put a stop to the idea that the global economy is set for a rebound following the US/China Phase 1 trade deal. Global manufacturing PMI's and local Chinese data (monthly crude imports, Caixin PMI, vehicle sales) were all trending in the right direction as we entered 2020; and along with the supply issues in the middle east (Iran/US, Libya), and a surprise OPEC supply cut to end 2019, had created expectations of rising near term prices, steepening backwardation, and long term prices anchored near US$50/bbl.

That outlook is now in flux. The forward curve as a whole has shifted lower and we are seeing contango in the prompt four months as time spreads weaken and near term prices move lower than far dated prices. That is a distinct sign that the outlook for crude has shifted dramatically: and falling jet fuel, gasoline, and refinery crack spreads all support that notion.

Jet Fuel Price Decline Since the Outbreak



Source: Bloomberg, ATB Financial Markets

Oil demand growth in China for 1Q20 is expected to take a hit of between 150-400k bpd by some estimates. Will that loss of demand last?

If we look at the SARS epidemic, we can get some guidance. During that 2003 outbreak, monthly visitor arrivals to China dropped by 128 million during April and May following the official notification by China to the WHO (chart next page). Oil prices dropped right alongside arrivals, falling 18% in April - however, prices then stabilized quickly and posted a 13% gain for May. China's raw oil demand during SARS dropped by 350k bpd and rebounded just as quickly before resuming its previous growth trend. Those aspects are encouraging, and when we couple that with the comprehensive quarantine procedures that have already been put in place during nCov, and the fact that some 80 million people in mainland China have been told to stay home and restrict travel, we could see the pace of new cases start to slow very soon.

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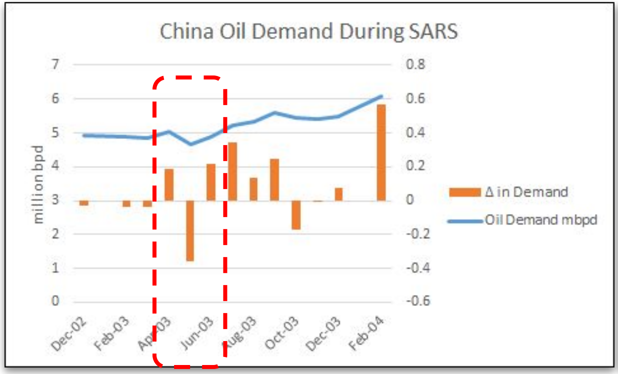
WTI Crude Oil

JP Dore, Markets Analyst

And that is the aspect that needs to be considered most closely. In 2003, once the pace of new infections (the “epicurve” in technical virology parlance) started to slow, we saw a corresponding rebound in crude and asset prices. Are we at the peak of the epicurve? That is unknown. What is known, is that of the 14,700 infections to date, 98% of them have been in China, and 58% of those have been in the Province of Hubei where the city of Wuhan is, or ground zero. That indicates to me that the response from Chinese officials thus far has been robust enough to ensure that new cases will not spread beyond China’s borders at the same exponential pace that they have within them. This is an encouraging sign, though an aspect that is unlikely to cool the selling seen across the crude complex in the very near term.

That said, I would suggest that we are close to an area on the front of the curve where we could start to see some meaningful consolidation. The US$50-52/bbl area has held up well over the past year and is also the area where the back end of the curve has been anchored for the past number for years. The next week will be critical to how this unfolds, but once we start to see information that indicates the epicurve has started to slow, I would not be surprised to see crude prices rebound just as quickly as they have declined.

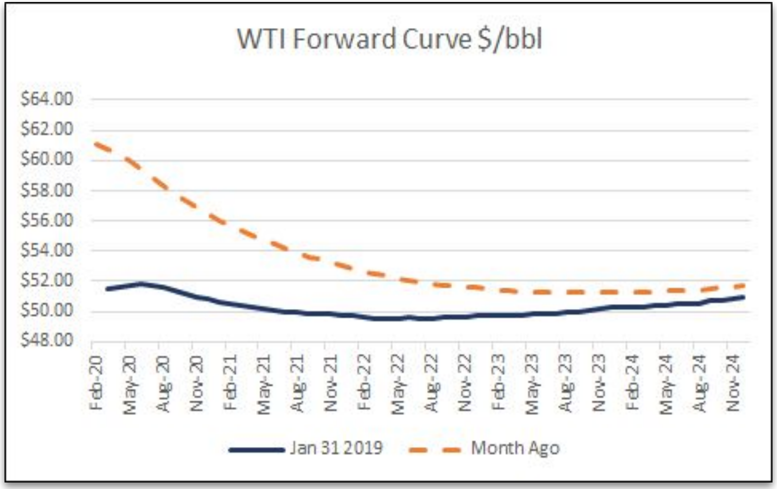
Chinese Oil Demand and GDP wobbled during SARS, but returned to growth very quickly

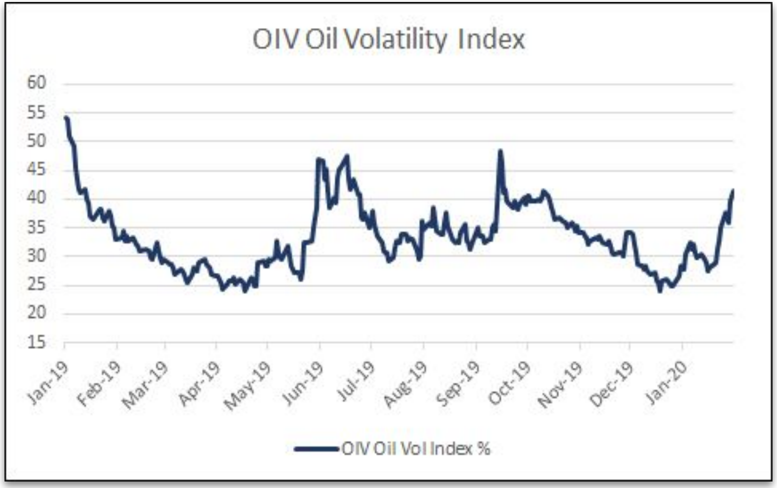


Source: Bloomberg, ATB Financial Markets

WTI Crude Oil

JP Dore, Markets Analyst



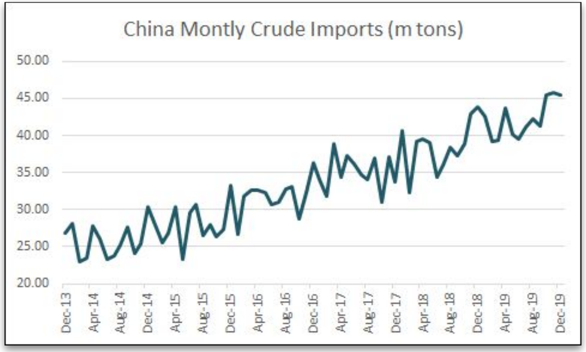


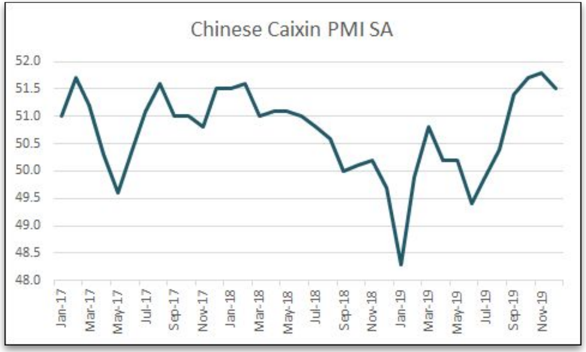
Source: Bloomberg, ATB Financial Markets

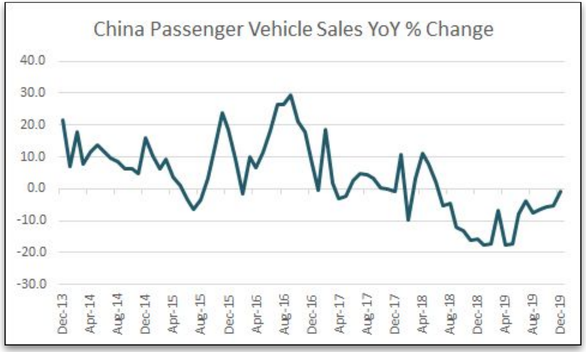
- The WTI forward curve has flattened in the past few weeks and is showing signs of contango in the front as demand destruction is priced in over the near term
- Volatility has surged and is above levels seen during the recent US/Iranian tensions, though still below the 1-yr highs from early 2019 and the spike in September following the Saudi drone attacks

WTI Crude Oil

JP Dore, Markets Analyst







- The Phase 1 trade deal was shaping up as an incremental positive for Chinese growth prior to the nCov outbreak…

- ….Crude imports, manufacturing data, and an uptick in domestic passenger vehicle sales were all acting as tailwinds prior to virus hitting the domestic economy

Natural Gas

CJ Hilling MBA, Associate Director Commodities/FX

It was a volatile month for Aeco prices, as we got blasted with Arctic temperatures the week of Jan 13th. However, overall temperatures have been quite mild this winter/year and the sentiment is that forecasters are expecting to see above-normal temperatures ahead.

Intra Alberta demand, East Gate deliveries, and fields receipts are all back to levels prior to the pre-cold period but storage withdrawals have stayed relatively strong this week and it has affected day prices. Summer 2020 and next winter fixed prices have declined to late November levels at $C 1.56 and 1.93/gj respectively but the basis has held relatively strong at $US (0.88) and (0.91)/MMbtu.

Dawn storage has decreased to 188 Bcf, down 15 Bcf on the week and inventory is 10% higher than last winter same period and the spread versus last year same period has increased to 29 Bcf.

NGTL reported production is 11.675 Bcf. There seemed to be a jump in linepack from 18.194 to 19.072 Bcf over the day. This could be added linepack in preparation for North Montney Mainline which is expected to come on Feb 1st. The market will be watching for the change in production and adjust prices accordingly.

The EIA inventory report for the week of Jan. 24th showed a 201 Bcf weekly withdrawal from U.S. natural gas stocks, to the higher side of expectations, but a futures market already depressed by mild winter weather reacted with disappointment.

Weekly EIA Inventory as of Jan 24th 2020

Stocks in billion cubic feet (bcf)			
Region	Current	Previous	Change
East	638	696	-58
Midwest	761	815	-54
Mountain	143	151	-8
Pacific	210	220	-10
South Central	995	1065	-70
Salt	297	328	-31
Nonsalt	698	737	-39
Total	**2746**	**2947**	**-201**

The 201 Bcf withdrawal, recorded for the week ended Jan. 24, compares with a 171 Bcf withdrawal recorded in the year-ago period and a five-year average pull of 143 Bcf.

With one eye closed, producers, bankers, and ancillary service providers watched the continued free fall of natural gas over the first month of 2020. We broke below the $2/MMBtu mark earlier than expected this year and now, as one analyst noted, the commodity faces a “gasmageddon” that could see prices stay below $2 on average through 2020.

Some major trading houses have also dropped their forecast to $1.99 on average. Reasons cited for the reduced forecast are mild weather conditions, continued renewable generation capex and buoyant liquefied natural gas (LNG) exports.

Natural Gas

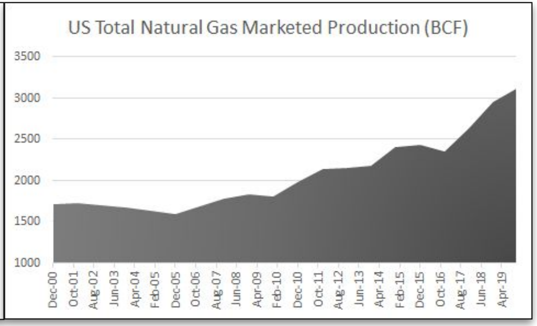
CJ Hilling MBA, Associate Director Commodities/FX

Higher inventories heading into the 2019/20 winter meant the market "needed early and sustained cold weather" to even have a chance of sustaining higher prices. Once the November cold spell was over, the warm weather brought forward the price free fall.

Despite an "impressive" 8 Bcf/d ramp-up in LNG exports over the past four years that has been bolstered further by about 2 Bcf/d of growth in exports to Mexico, these demand gains have been dwarfed by roughly 22 Bcf/d in production growth since January 2016. To continue the pile on, the Energy Information Administration's (EIA) updated their Annual Energy Outlook, and 2020 shows natural gas prices stuck below the $4 mark out to 2050.

The agency expects sub-$4 pricing to persist because "of an abundance of lower cost resources, primarily in tight oil plays in the Permian Basin. These lower cost resources allow higher production levels at lower prices during the projection period." Lower for longer remains the mantra...

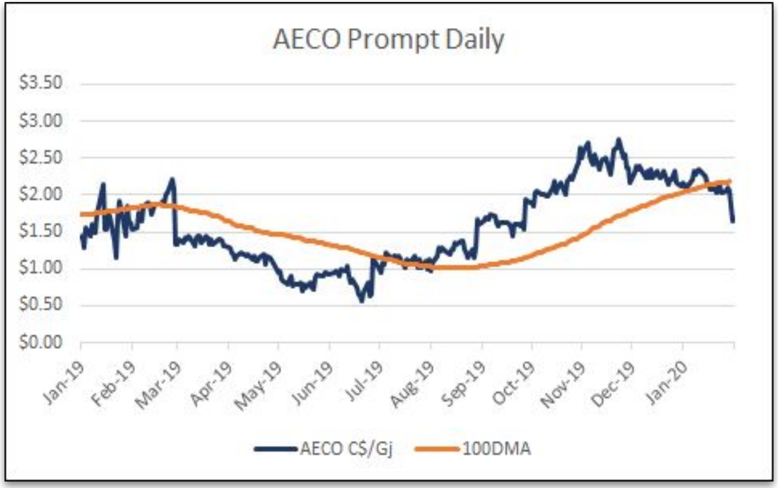
AECO Basis has tightened to Henry Hub; US Production Continues to Surge

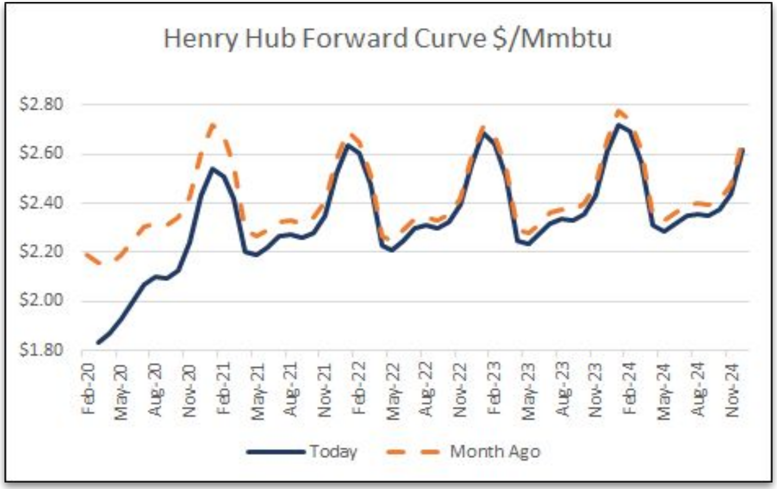


Source: Bloomberg, ATB Financial Markets

Natural Gas

CJ Hilling MBA, Associate Director Commodities/FX





Source: Bloomberg, ATB Financial Markets

- AECO cash prices were well supported from last summer, although recent warm weather and increased Canadian rig counts have started to act as headwinds
- The Henry Hub forward curve has really suffered in the front part with significant damage done to the prompt 12 month strip

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CHARTPACK

Monthly and YTD Returns

January FX Spot Returns % Against USD	
Japanese Yen	0.38%
Swiss Franc	0.37%
British Pound	-0.36%
Euro	-1.06%
Danish Krone	-1.09%
Canadian Dollar	-1.89%
Swedish Krona	-2.70%
New Zealand Dollar	-3.87%
Norwegian Krone	-4.57%
Australian Dollar	-4.63%

Source: Bloomberg, ATB Financial Markets

12M FX Spot Returns % Against USD	
Swiss Franc	3.20%
British Pound	0.74%
Japanese Yen	0.50%
Canadian Dollar	-0.85%
Euro	-3.10%
Danish Krone	-3.20%
Swedish Krona	-6.00%
New Zealand Dollar	-6.54%
Australian Dollar	-7.99%
Norwegian Krone	-8.38%

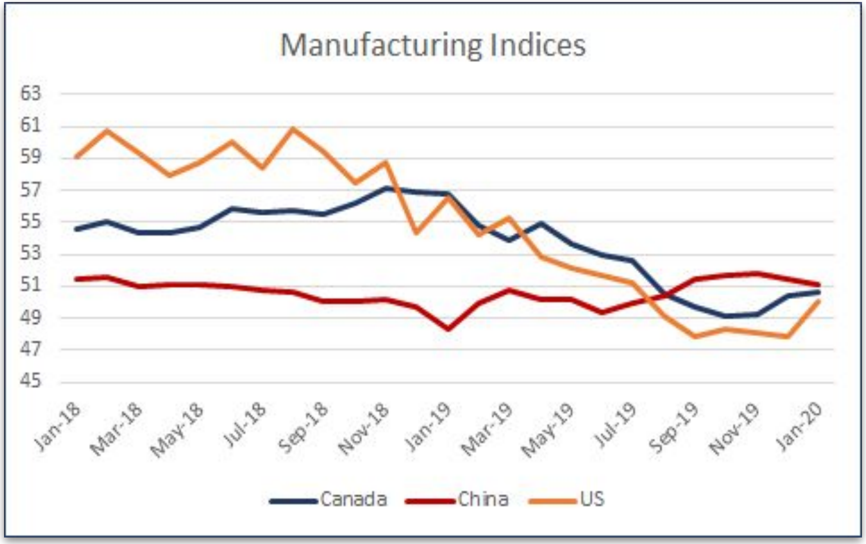
YTD Cross Asset Returns %	
Nasdaq 100	4.62%
S&P500	3.50%
MSCI World Index	2.00%
WTI	0.99%
TSX	-0.68%
Gold	-9.08%
Soybeans	-10.56%
Copper	-11.70%
TSX Energy	-17.90%
Natual Gas	-18.70%

- The Japanese Yen and Swiss Franc eked out gains against the USD as the safe-have trade drove flows to begin 2020
- CAD was a mid-performer, although it still had a rough month with steady losses
- Commodities took it on the chin in January, and the TSX Energy Index keeps moving lower despite attractive valuations; Nasdaq outperforms as AAPL, AMZN, MSFT surge

Global PMI Data

PMI Heat Map	Jan-18	Feb-18	Mar-18	Apr-18	May-18	Jun-18	Jul-18	Aug-18	Sep-18	Oct-18	Nov-18	Dec-18	Jan-19	Feb-19	Mar-19	Apr-19	May-19	Jun-19	Jul-19	Aug-19	Sep-19	Oct-19	Nov-19	Dec-19	Jan-20
Canada	54.6	55	54.3	54.4	54.7	55.9	55.6	55.7	55.5	56.2	57.1	56.9	56.8	54.8	53.9	54.9	53.6	53	52.6	50.5	49.7	49.1	49.2	50.4	50.6
China	51.5	51.6	51	51.1	51.1	51	50.8	50.6	50	50.1	50.2	49.7	48.3	49.9	50.8	50.2	50.2	49.4	49.9	50.4	51.4	51.7	51.8	51.5	51.1
US	59.1	60.7	59.3	57.9	58.7	60	58.4	60.8	59.5	57.5	58.8	54.3	56.6	54.2	55.3	52.8	52.1	51.7	51.2	49.1	47.8	48.3	48.1	47.8	50.9

- Readings of global economic activity are represented here by Purchasing Managers Indices (PMI) from Canada, China, and the US
- Readings above 50 indicate an overall expansion of activity, below 50 would indicate an outright contraction
- Activity had slowed markedly in the US and Canada during 2H19 and was looking to turn a corner into 1H20
- Chinese readings were rather stable and were picking up ahead of the nCov pandemic - 1Q20 could be a bumpy ride



What Kind of Rally is This?

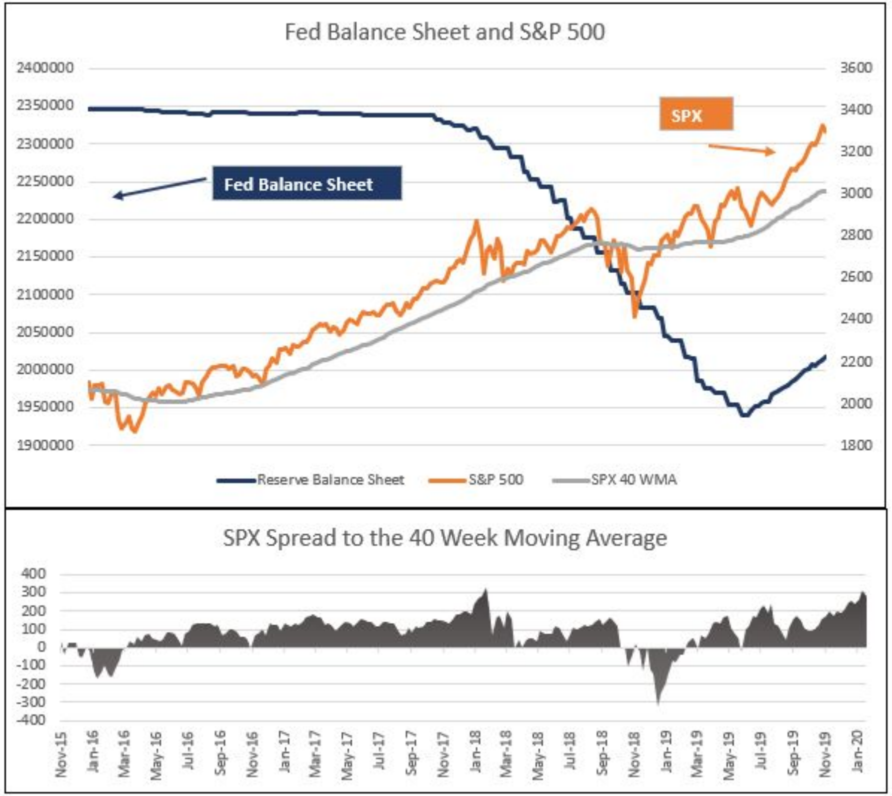
- You may have noticed that equities, particularly in the US, have been on a tear recently

- You can see that the rally in the S&P 500 that kicked off in earnest in Aug/Sep 2019 coincided almost exactly with an increase in in the Fed's balance sheet...

- The extra liquidity in the system led to increased risk taking and pushed the market to lofty valuations

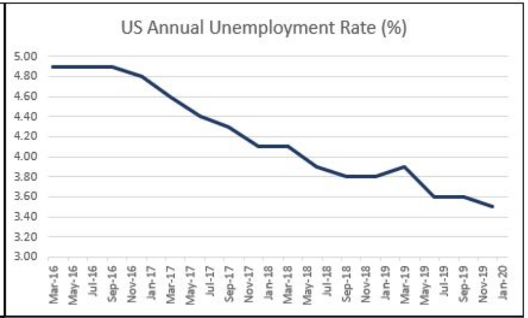
- In January, US companies came through with solid earnings for Q4, that meet and/or exceeded the high expectations the market had priced in

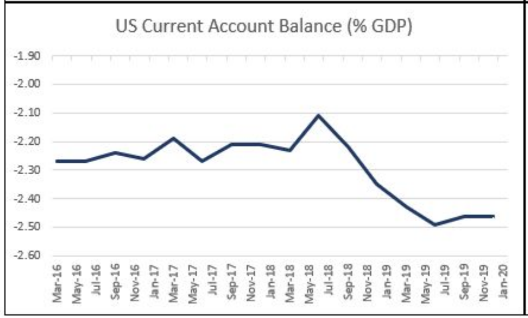
- If the concern over the Coronavirus dissipates quickly, then this rally really has some legs: The Fed is keeping rates low and is still expanding its balance sheet....risk-on continues to be the mantra

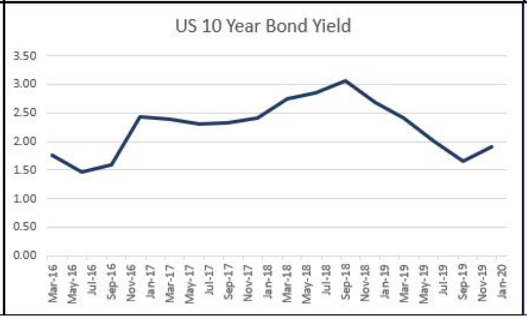


Source: Bloomberg, ATB Financial Markets

US Country Snapshot







Source: Bloomberg, ATB Financial Markets

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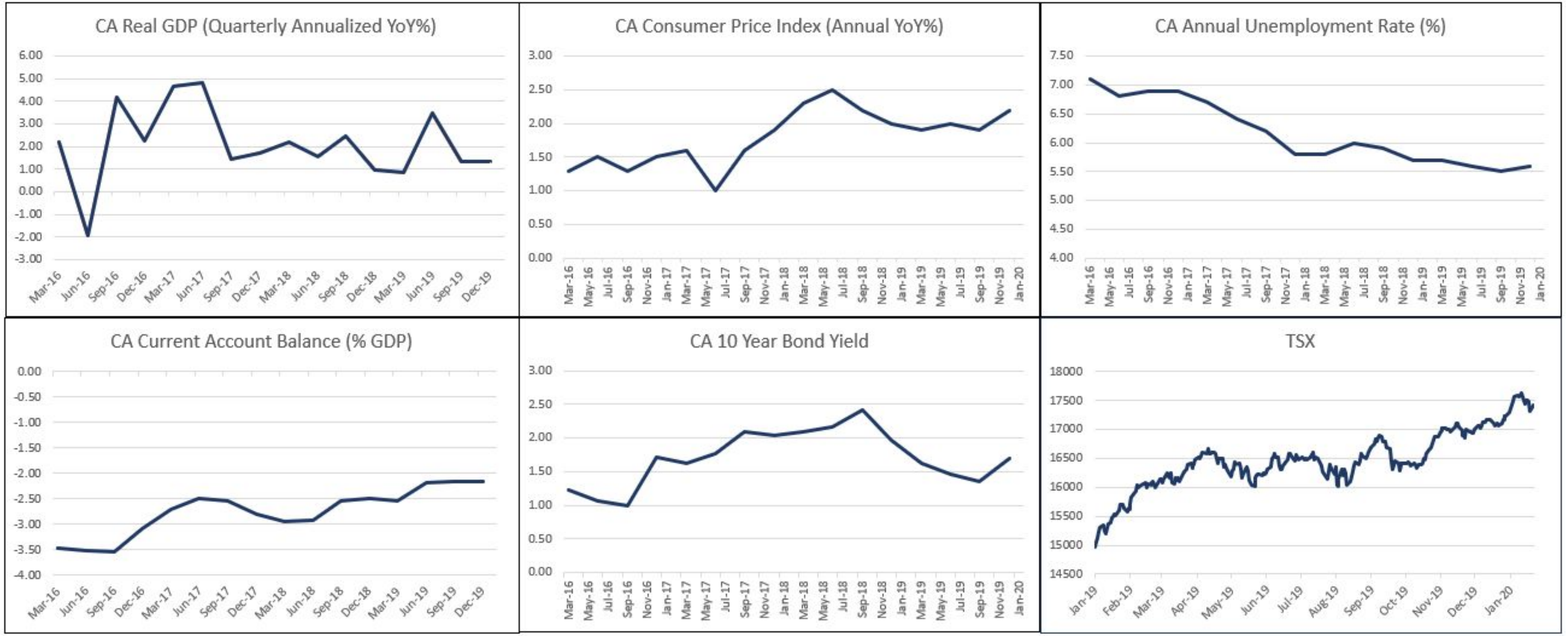
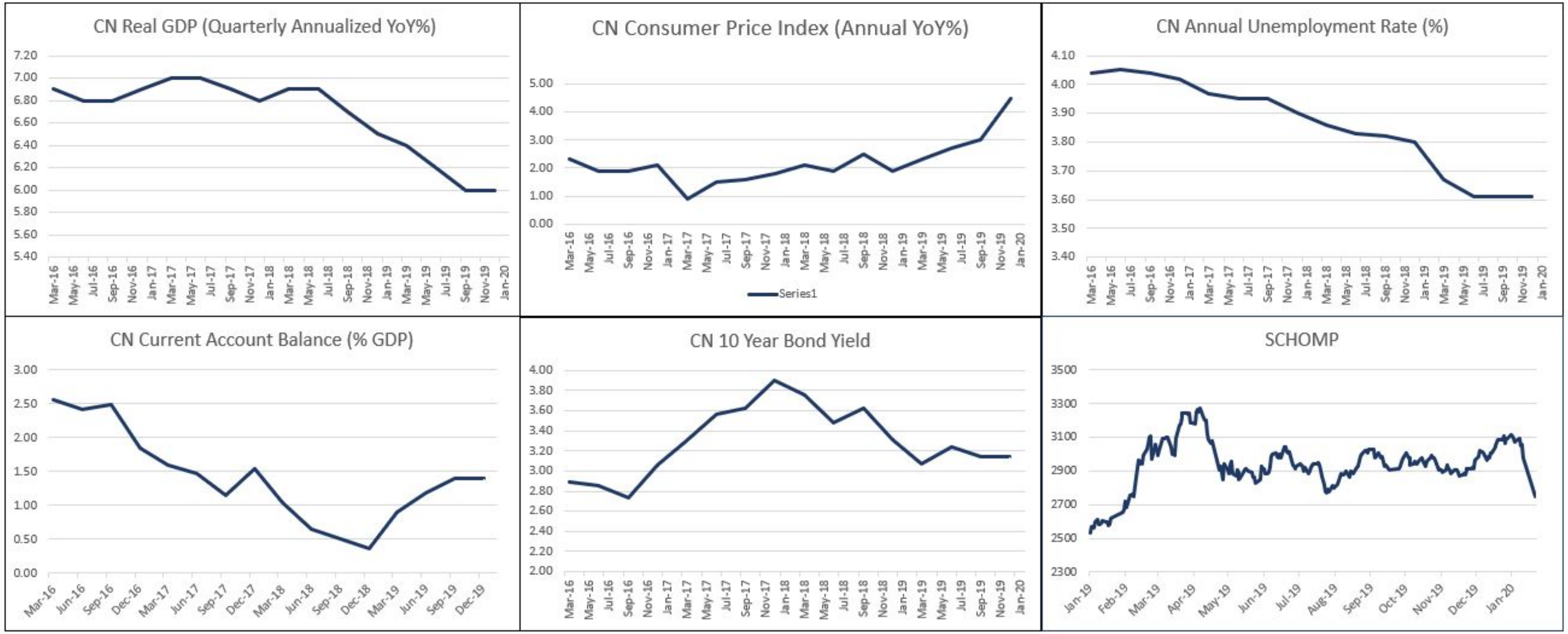
Canada Country Snapshot



Source: Bloomberg, ATB Financial Markets

China Country Snapshot



Source: Bloomberg, ATB Financial Markets

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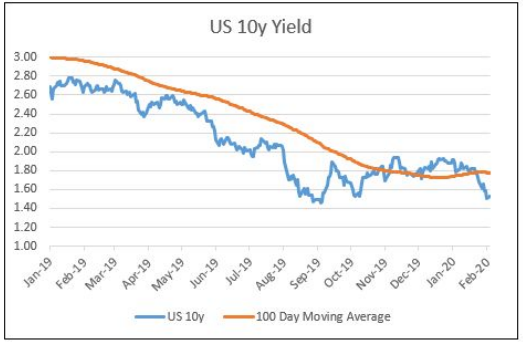
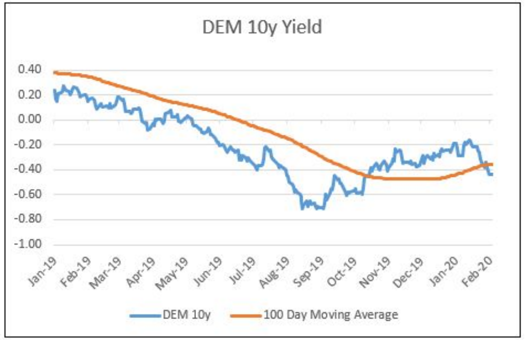
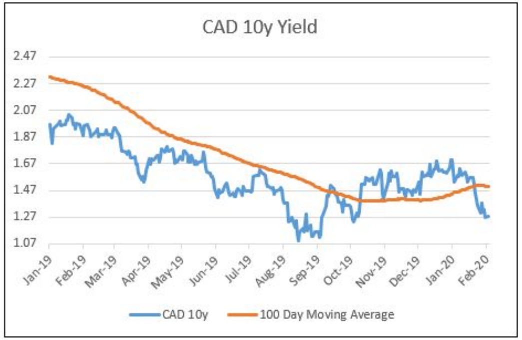
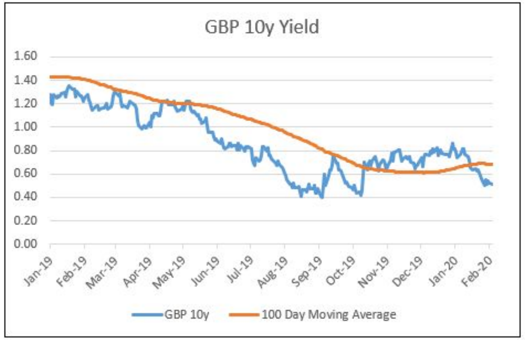
Developed Market 10 Year Yields

- Developed market 10 year bond yields continue to trend lower
- All majors are below their respective 100 day moving averages and not showing much signs of slowing down
- The market has priced in an almost 90% chance of another cut by the Fed this year and as such we could see the committee start to walk back their commitment to holding rates at current levels in the near term









Source: Bloomberg, ATB Financial Markets

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WTI Model - In Search of “Fair-Value”

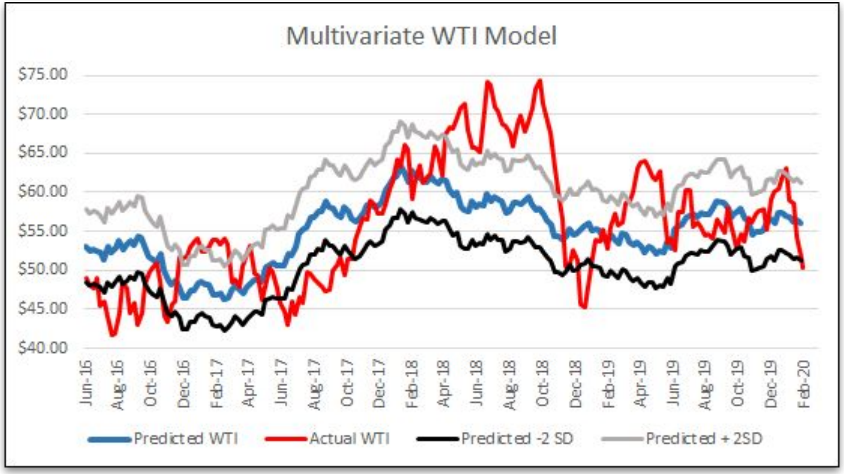
- Several factors influence oil prices, making it hard to consistently predict changes in market pricing.

- We have focused on 5 fundamental drivers of oil price to model the elusive search for “fair-value”:

    1) **S&P500**: Diversified equity market for a robust picture of risk appetite. **(+Correlation to Oil)**
    2) **Gold**: Investable commodity offering a ‘hedge’ against inflation. **(+Correlation to Oil)**
    3) **USD Index**: Weighted index of the USD. **(-Correlation to Oil)**
    4) **Baltic Dry Shipping Index**: Bulk cargo ocean freight rates - a leading indicator of economic activity. **(+Correlation to Oil)**
    5) **US Total Crude Inventories**: A good indicator of the overall level of supply and demand in US oil markets. **(-Correlation to Oil)**

- We then regressed WTI prices to these inputs to arrive at an multivariate model of a “fair-value” price for WTI

- **At current levels for each input, our model implies a price of US$56.67/bbl**



Source: ATB Financial Markets Group

“Dude, Where’s my Loonie (Going)?”

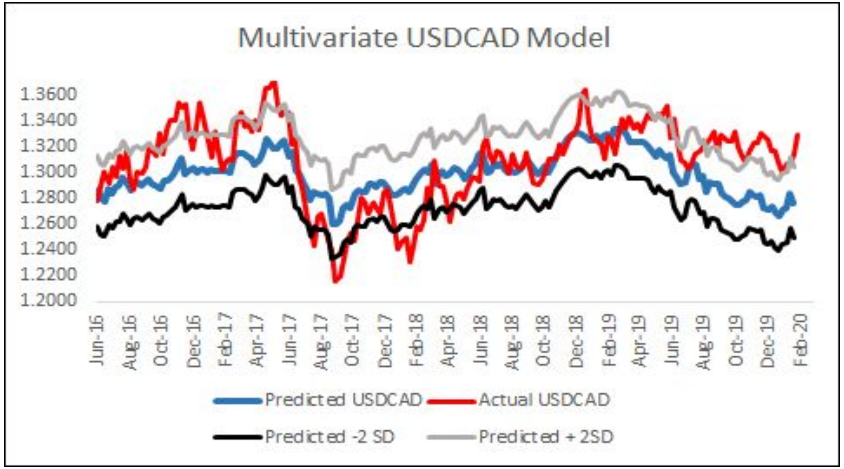
- Modelling currency values is rather difficult as well, though FX rates do tend to exhibit lower volatility than commodities.

- We have focused on 3 main drivers to inform our “fair-value” estimate of USDCAD:

    1) **S&P500**: Diversified equity market for a robust picture of risk appetite. **(+Correlation to USDCAD)**
    2) **WTI**: Investable commodity and one of Canada’s largest exports. **(-Correlation to USDCAD)**
    3) **US/CA 2y Yield Spreads**: Sovereign bond yield spreads reflect the level of interest rate expectations between two countries, and can be a good indicator of relative economic performance, foreign direct investment, and thus demand for a given currency. **(+Correlation to USDCAD)**

- We then regressed USDCAD to these inputs to arrive at an multivariate model of a “fair-value” price for USDCAD

- **At current levels for each input, our model implies USDCAD at 1.2775. We note that there is considerable divergence from the model to actual price at present, which has been a decent contrarian indicator in the past, let’s see how this develops in the next few weeks.**

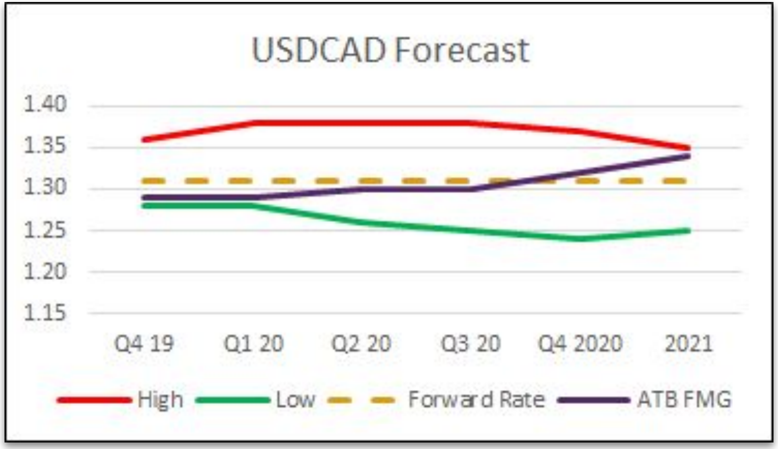


Source: ATB Financial Markets Group

USDCAD Forecast

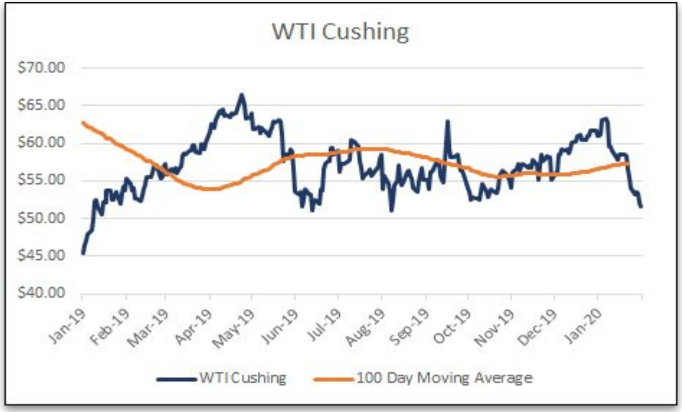
	USDCAD Forecast					
	Q4 19	Q1 20	Q2 20	Q3 20	Q4 2020	2021
High	1.36	1.38	1.38	1.38	1.37	1.35
Low	1.28	1.28	1.26	1.25	1.24	1.25
Forward Rate	1.31	1.31	1.31	1.31	1.31	1.31
ATB FMG	***1.32***	***1.32***	***1.33***	***1.33***	***1.34***	***1.34***

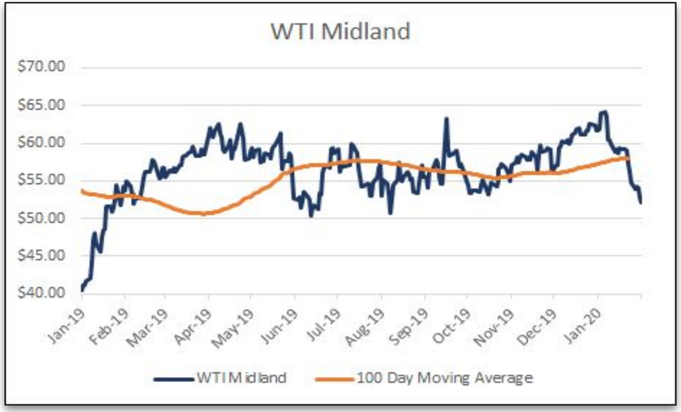
*Source: Bloomberg, ATB Financial Markets Group *This is ATB's official forecast as submitted to Bloomberg*

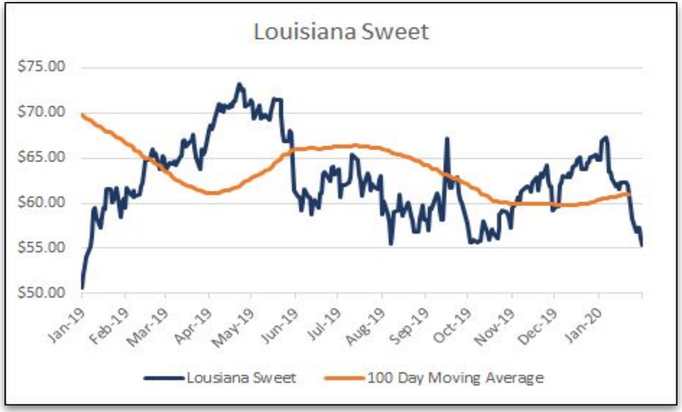


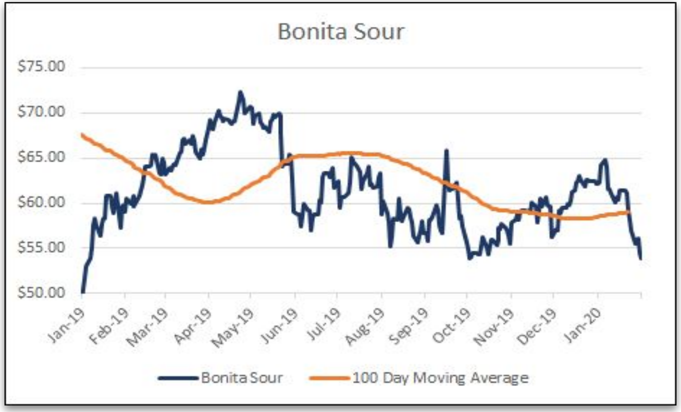
- Despite our model flashing signals that we could see moderate CAD appreciation, our base case is that USDCAD will continue to gravitate close to the prevailing spot rate before gradually rising
- We view the recent change in tone from the BoC coupled with simultaneous status quo by the Fed, and of course the negative impact of the Coronavirus, as negating any positive developments on the trade front in the near term

US Crude Prices ($/bbl)



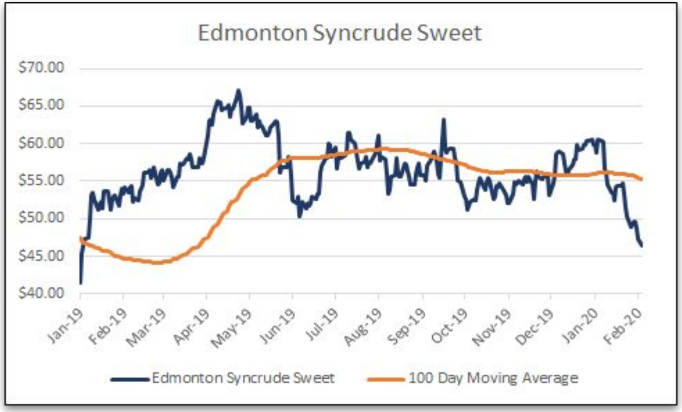


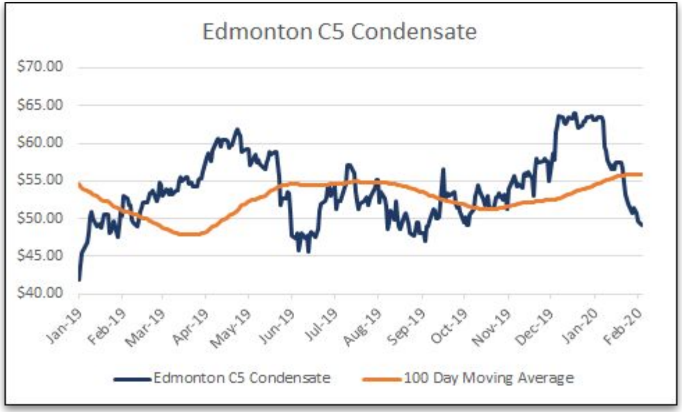


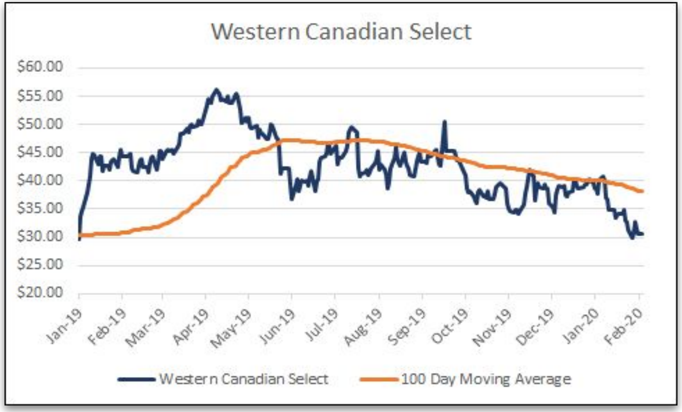


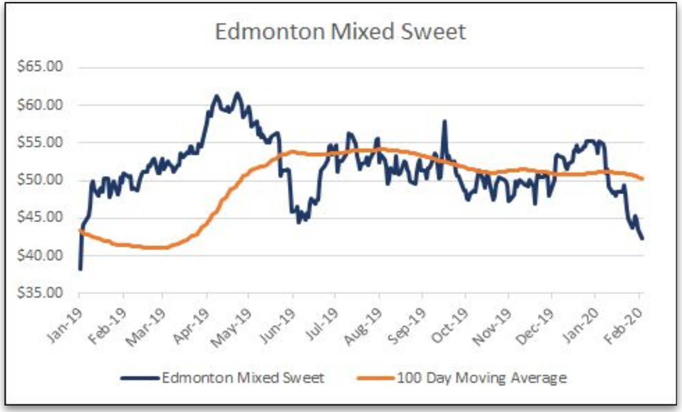
Source: Bloomberg, ATB Financial Markets

Canadian Crude Prices ($/bbl)









Source: Bloomberg, ATB Financial Markets

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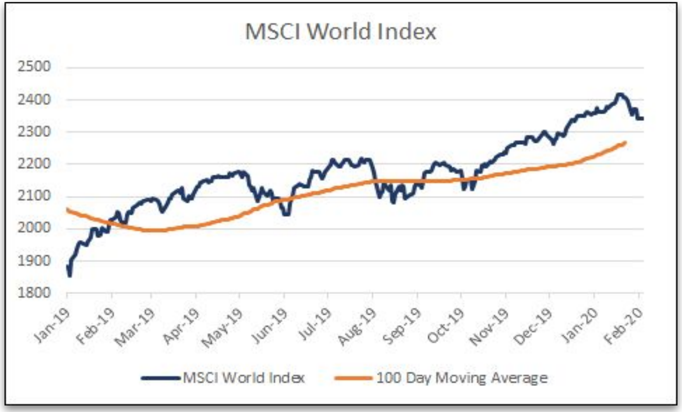
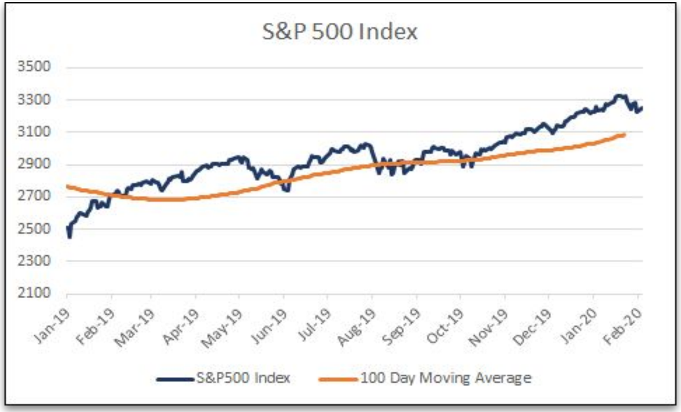
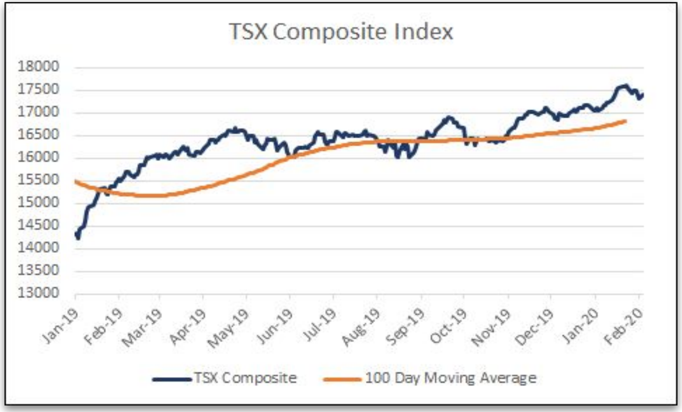
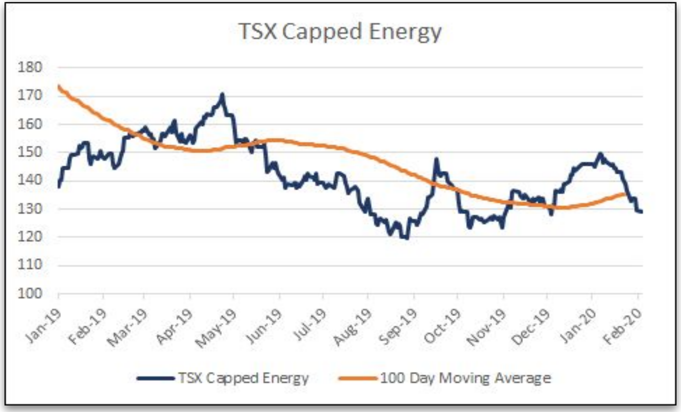
Equities At Record Highs, Energy Lags



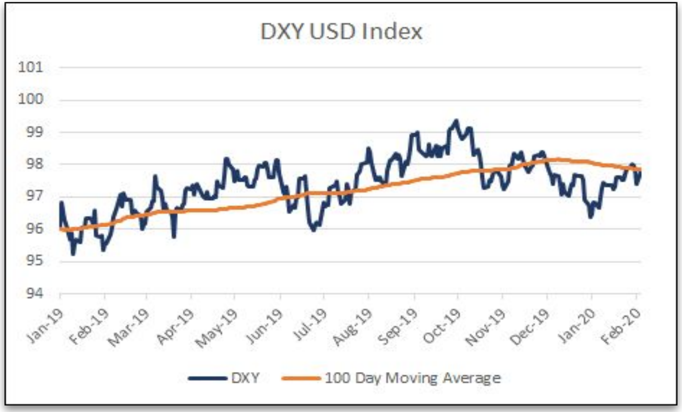


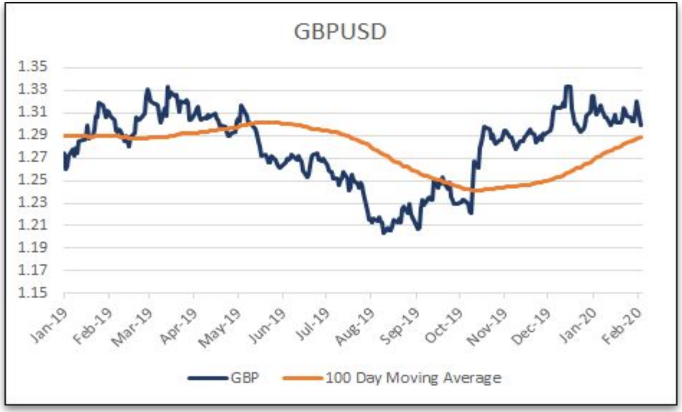


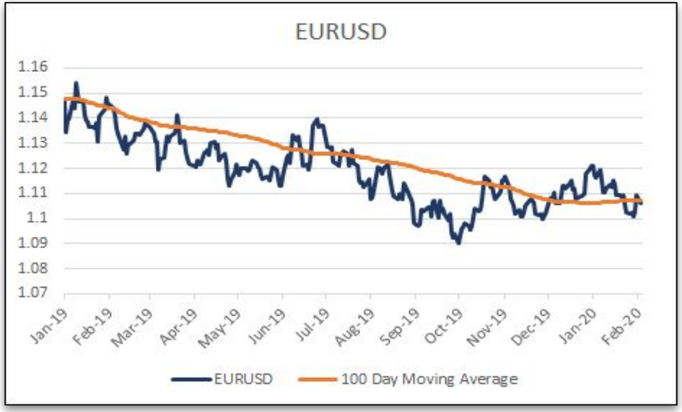


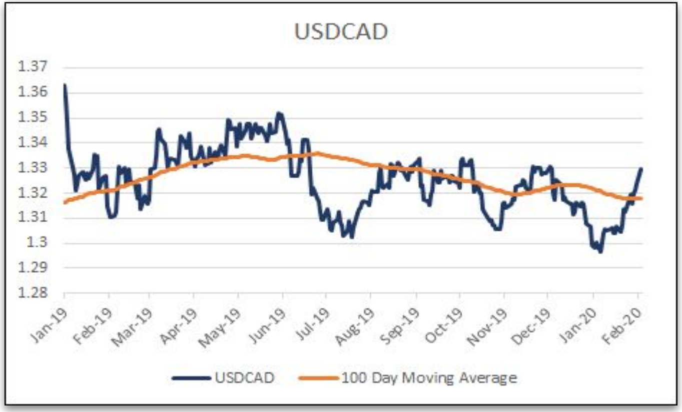
Source: Bloomberg, ATB Financial Markets

G10 FX Charts - USD Moving Higher









Source: Bloomberg, ATB Financial Markets

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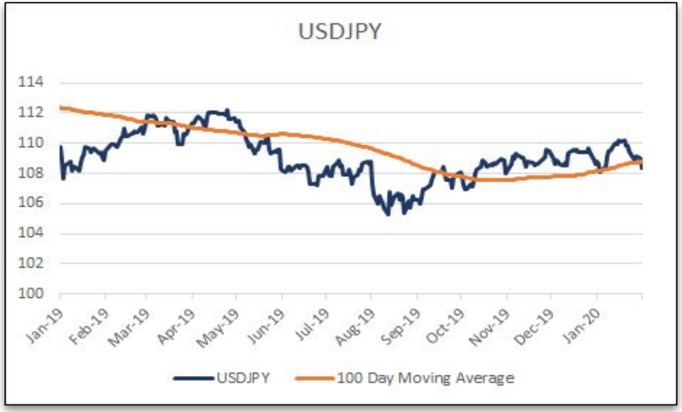
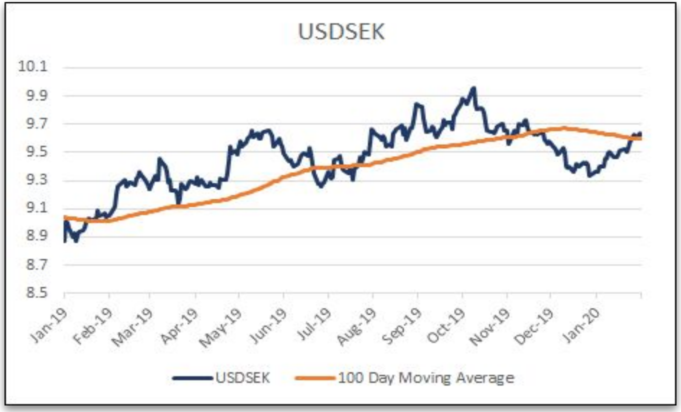
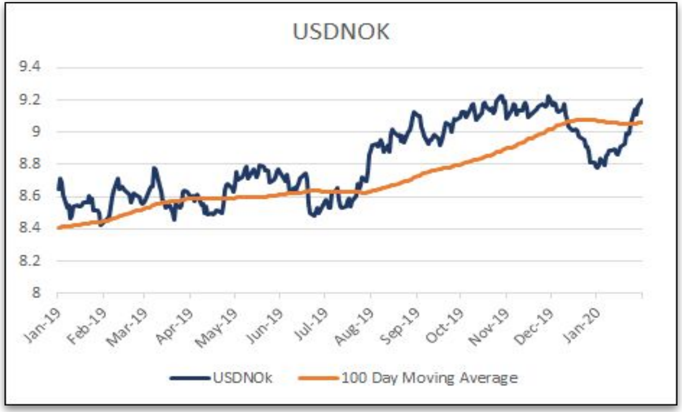
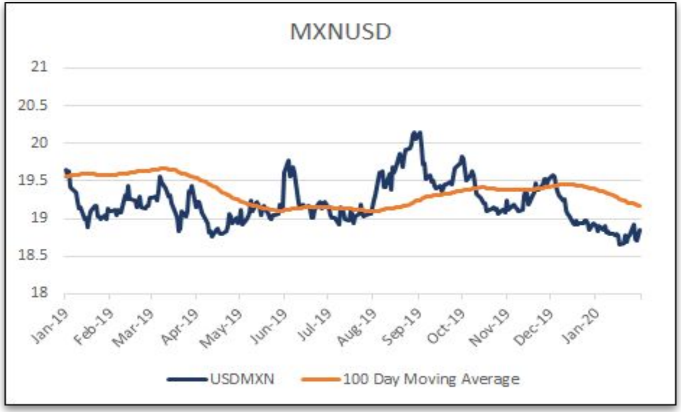
G10 FX Charts - USD Moving Higher



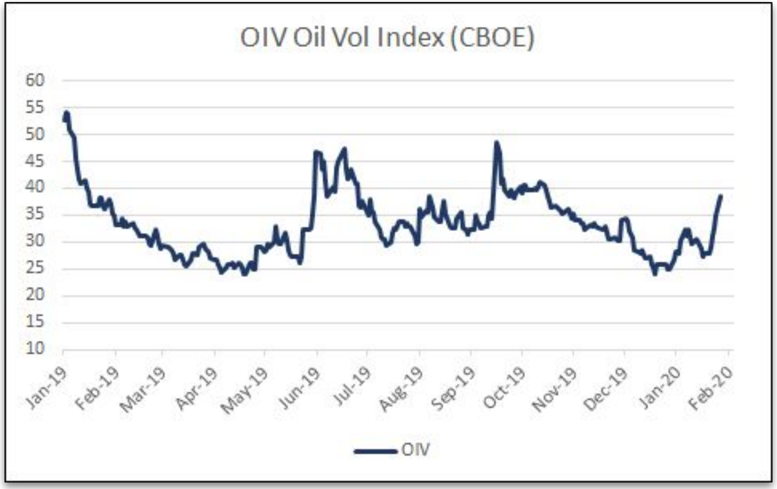


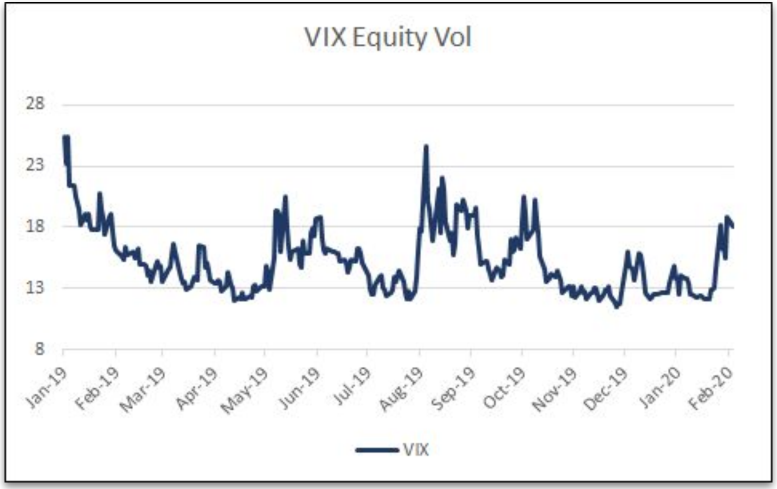




Source: Bloomberg, ATB Financial Markets

Volatility Spikes to Begin 2020





Source: Bloomberg, ATB Financial Markets

- Volatility levels in oil and equities have jumped higher to start 2020, although we are still below 2019 highs
- Volatility is mean reverting so let’s see how persistent this bout proves to be…

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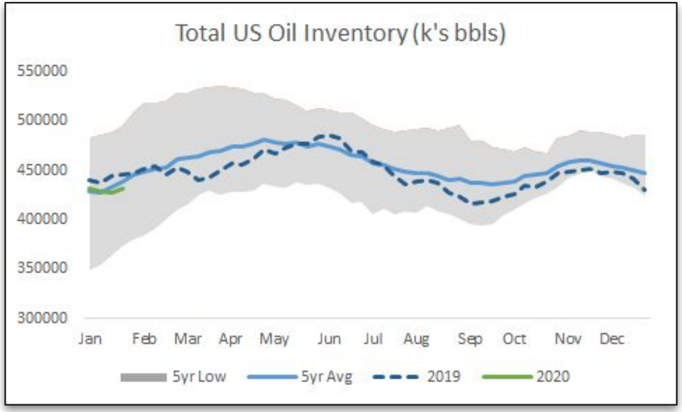
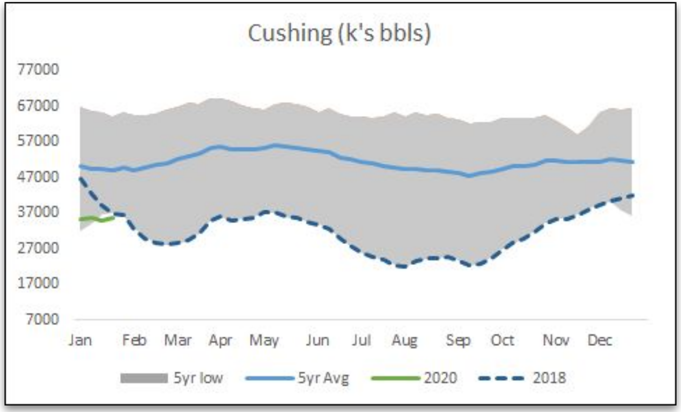
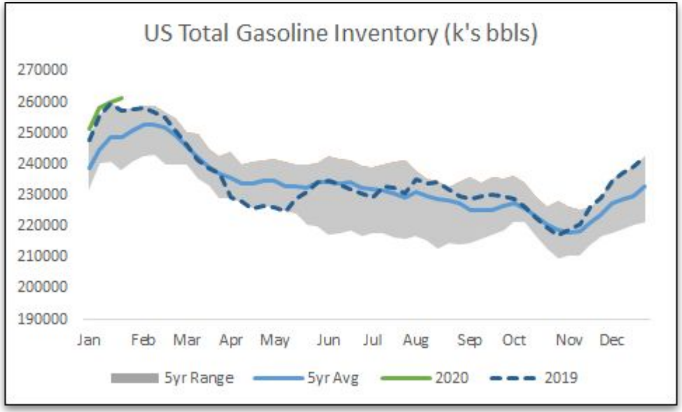
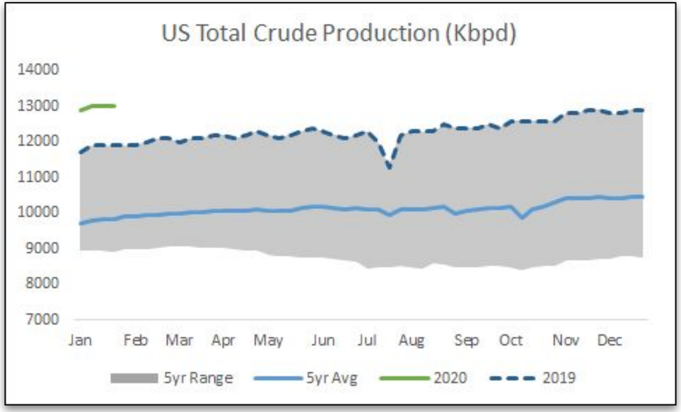
Oil Storage and Production Charts



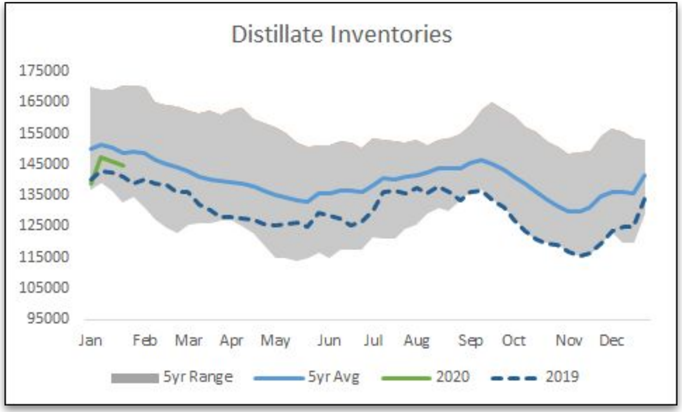


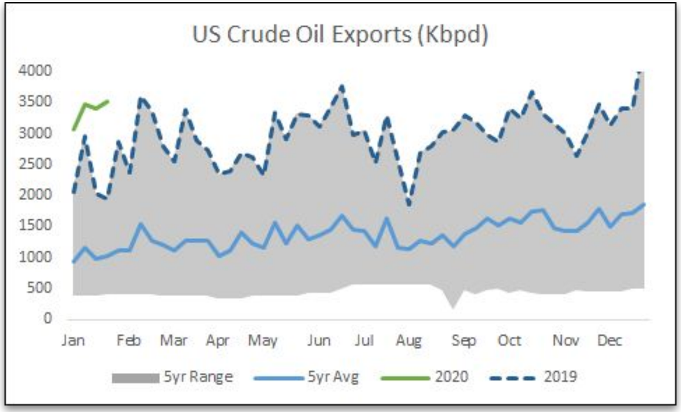


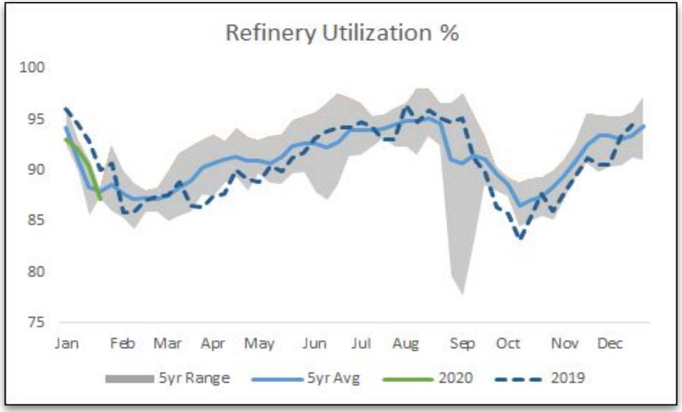


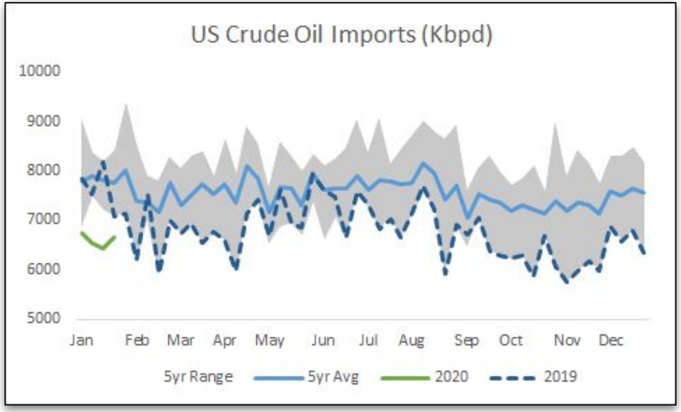
Source: DOE, ATB Financial Markets

US Oil Exports, Imports, Refining



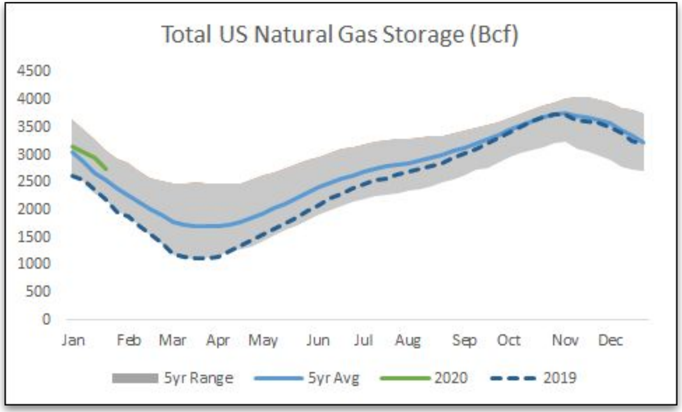


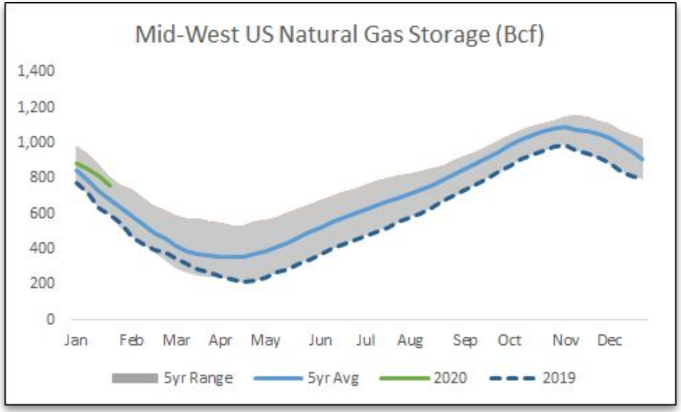


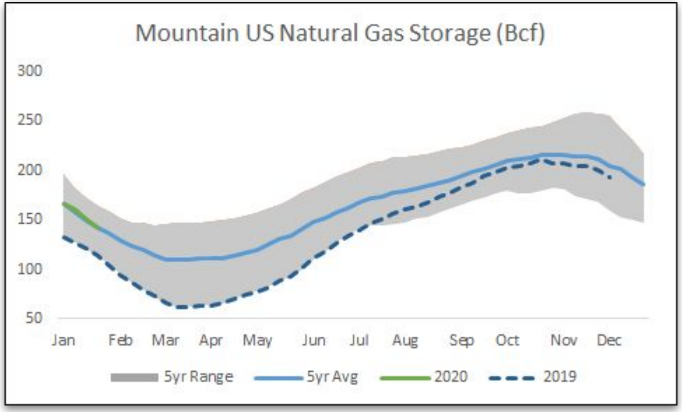


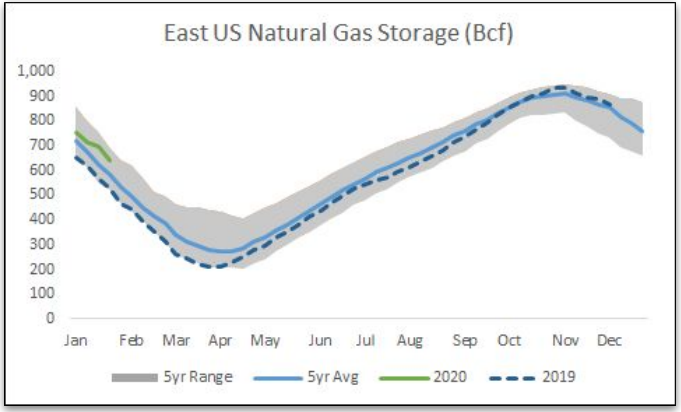
Source: DOE, ATB Financial Markets

Natural Gas Storage Charts



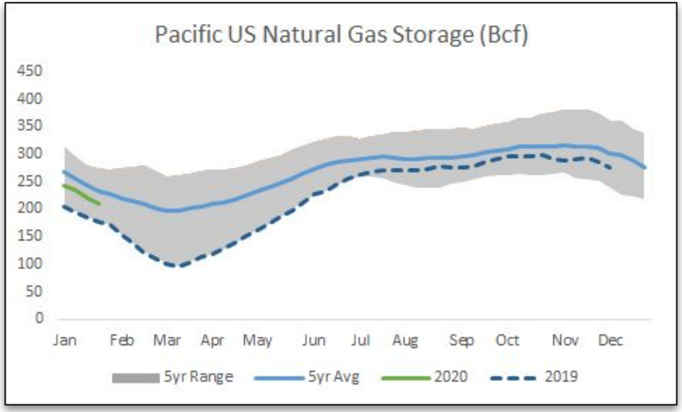


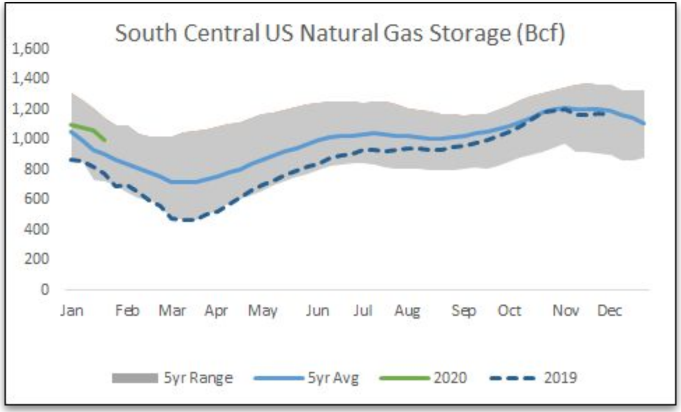


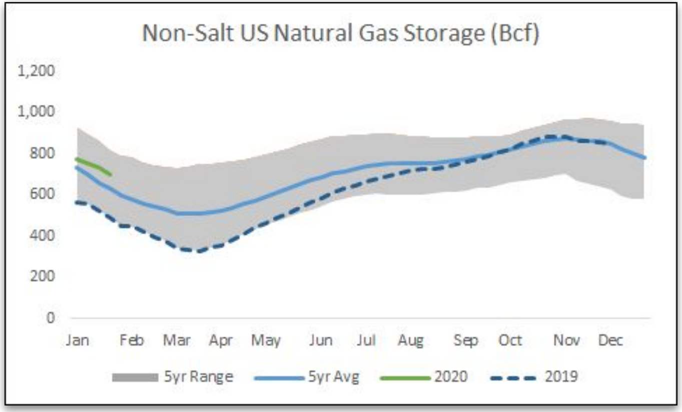


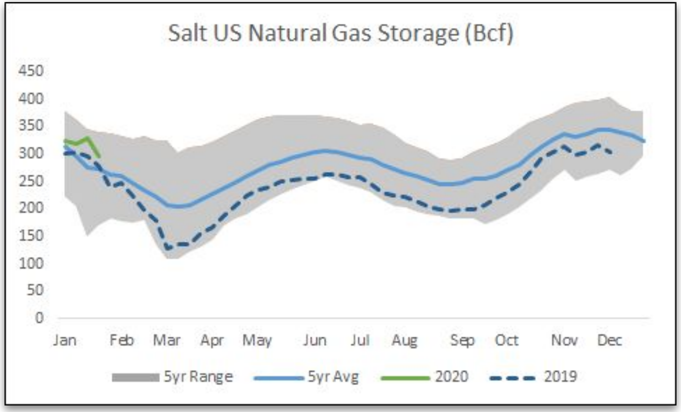
Source: DOE, ATB Financial Markets

Natural Gas Storage Charts









Source: DOE, ATB Financial Markets

Markets Near Term Outlook

	Bullish	Neutral	Bearish
Currency	**EUR**	**CAD, GBP**	**USD, JPY**
Energy		**WTI, Brent, WCS**	**AECO, Henry Hub**
Rates		**BoC**	**Fed, ECB**
Equities	**S&P500, TSX**		**SCHOMP**

**Near Term Outlook is the desk view of the Financial Markets Group and not representative of ATB Financial or its subsidiaries*

Looking to hedge your risk?

Identify Exposure → Specify your goals → Develop a plan → Choose your tools → Evaluate your results

Talk to us…we’re here to listen.

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ATB listens

We can *transform banking*
Reimagine it MAKE BANKING
WORK FOR PEOPLE
Because we carry the *outrageous*
belief that banking can change
PEOPLE'S LIVES FOR THE BETTER
Make their time richer
their aspirations closer
THEIR HAPPINESS DEEPER
HOW WILL WE DO THIS? By doing things other banks wouldn't do
By being ever loyal to our customers *relentlessly inventive*
and steadfastly genuine in our pursuit
of Albertans' greater good
BY USING BANKING TO CREATE HAPPINESS
WHY HAPPINESS?
Because good things happen when happiness becomes your purpose
that's why ATB
will always
BE MORE
than a bank