Monthly Market Insights

Data and opinions as of February 28, 2021

Stocks up, bonds crushed as reopening trade continues

Markets have been jittery about rising inflation ever since last November's vaccine announcements. Sure enough, long-term government bond yields have creeped up since then, which has mostly benefitted cyclical stocks as they offer some degree of hedge during periods of moderate inflation. Then in just February alone, government bond yields climbed nearly three times as much as November and January. This time, the rise in long-term yields was largely driven by rising real interest rates, and less so inflation expectations, which can start to pose a headwind for risk assets as costs of borrowing increase. Real rates typically rise as economic growth prospects improve. While it's difficult to pinpoint the exact cause, a few things are apparent: vaccine logistics appear to be improving, central banks remain widely accommodative, and more stimulus cheques are coming.

The NEI perspective

The bond market rout continued as the Treasury yield curve steepened, driven largely by rising real yields. This is a sign of encouraging economic conditions and a warning that markets may be pricing in a sooner-than-expected Fed rate hike.

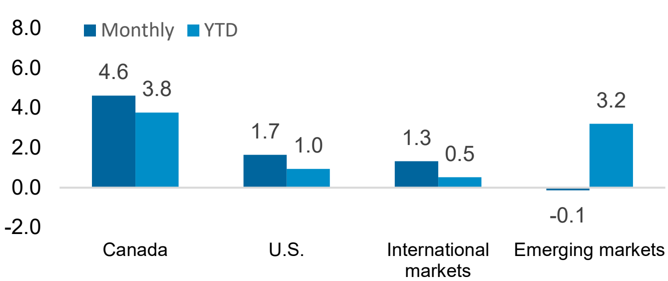
The impact of higher yields carried over to the equity market as well, which reversed its gains in the first half of February. Under the surface, value stocks continued their outperformance and beat growth stocks by nearly 7%.

We believe the Fed will remain accommodative and that it still has tools at its disposal to intervene if necessary. Also, more stimulus cheques are coming to Americans.

From NEI's Monthly Market Monitor for March 2021. [Click here to get the full report](#).

Equity

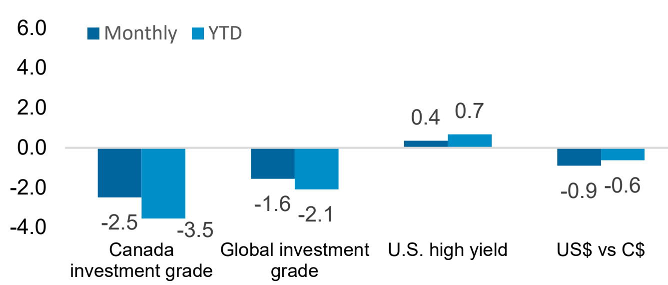
% return in C$



Canada: MSCI Canada; **U.S.:** MSCI USA; **International markets:** MSCI EAFE; **Emerging markets:** MSCI Emerging Markets. Source: Morningstar Direct.

Fixed income and currency

% return in C$



Canada investment grade: Bloomberg Barclays Canada Aggregate; **Global investment grade:** Bloomberg Barclays Global Aggregate; **U.S. high yield:** Bloomberg Barclays U.S. High Yield. Source: Morningstar Direct.

Thoughts on Bitcoin

The meteoric surge in Bitcoin prices has garnered a lot of attention. But there are important factors to consider before putting a dollar of your money in. We'll assume the reader already knows what a cryptocurrency is and how blockchain technology works. If not, there are plenty of great online resources as it is too complex a subject to explain in the limited space below. But perhaps that's the first warning sign right there. As Warren Buffett famously said, "Never invest in a business you cannot understand."

How does Bitcoin compare to traditional asset classes?

Bubble size = market capitalization (size), expressed in US$ trillions

Source: Bloomberg and Morningstar. Data as of February 28, 2021. Risk is calculated as annualzied standard deviation of monthly returns. For Bitcoin we used the total market value of all cryptocurrencies.

Bitcoin has seen a stellar annual return of 65% over the last three years. It has low correlation to gold and almost no correlation to stocks or bonds, so there can be diversification benefits. Moreover, Bitcoin can be an inflation hedge, as only 21 million units are ever coded into existence. However, as the chart above shows, Bitcoin is *six times* more volatile than stocks! To withstand such extreme short-term fluctuations, one would require either sufficient expendable capital or a long time horizon. There are also important environmental considerations, as mining Bitcoin requires immense computational power and energy. An estimated 60% of all Bitcoin mining occurs in China, where 58% of the nation's electricity is still generated from coal. While there is proven commercial application for the use of blockchain technology, from an investor's perspective, we will be staying on the sidelines for now.