

PULLING THE PLUG ON GLOBAL LIQUIDITY

While it took much longer than in past business cycles, we've finally reached the point where excess liquidity is being drained from the global financial system. This is a turning point, with the Fed shrinking its balance sheet, the ECB about to stop buying assets and the BOJ in tapering mode. While the policy-induced global economic slowdown will likely be relatively mild, global financial markets may have trouble coping as central banks turn off the global liquidity tap.

EQUITIES VERSUS FIXED INCOME

Equity returns should remain positive but are increasingly at risk. Bond yields are still below fair value and should continue to gradually move up as bond prices decline.

TRADE WAR VIEWS (SPECIAL SECTION)

Trade tensions between the U.S. and its trading partners have intensified in recent months. Financial markets are weighing the probability that the dispute will trigger a reversal of globalization. Very few tariffs have actually been imposed so far, but a material economic problem doesn't have to exist to produce volatility in financial markets.

(the full Perspectives document lays out the trade issues in more detail)

Ultimately, aside from negotiation tactics, all parties understand that intensifying trade frictions will not be positive for growth, inflation or votes! The financial markets have other issues to consider such as tight labour markets, wage pressures and major central banks' renormalization. These are the areas that should attract more market attention over the coming months.

LOONIE

Canada is vulnerable to tightening U.S. credit conditions and any U.S. policies aimed at widening Canada's overall trade deficit. For these and other fundamental reasons, we believe it is too early to call a bottoming for the Canadian dollar.

REGIONAL MARKETS

U.S.: The U.S. continues to face headwinds from both high valuation and shrinking profit margins—these will likely limit returns for the foreseeable future.

Canada: The outlook for Canadian equities is mildly positive. Earnings growth is expected to decelerate as economic growth continues to slow, but the S&P/TSX index benefits from a relatively good dividend yield of 2.9%.

International Developed Markets: The UK, Sweden, Spain and France offer the best value in Europe, while the most attractive markets in Asia are Australia, Singapore and Hong Kong. Dividend yields are also attractive at 3.1%, and should contribute substantially to total returns.

Emerging Markets: Valuation arguments still favour emerging markets over other global regions.

EXPECTED RETURNS

Expected returns for the one-year period beginning July 1, 2018

	IN CANADIAN DOLLARS			IN LOCAL CURRENCY		
	Global Reflation	Policy Renormalization	Global Recession	Global Reflation	Policy Renormalization	Global Recession
Probabilities	20.0%	50.0%	30.0%	20.0%	50.0%	30.0%
Canada Money Market	1.8%	1.5%	0.9%	1.8%	1.5%	0.9%
Canadian Bond	-0.4%	0.8%	3.6%	-0.4%	0.8%	3.6%
Canadian Federal Govt. Bond	-0.3%	1.1%	5.7%	-0.3%	1.1%	5.7%
Canadian Corp. Bond	1.5%	1.3%	1.0%	1.5%	1.3%	1.0%
Canadian RRB	-0.6%	-0.8%	-0.9%	-0.6%	-0.8%	-0.9%
Canadian High Yield	6.3%	5.0%	-6.8%	6.3%	5.0%	-6.8%
International Govt. Bond	-6.5%	-2.2%	11.2%	-3.3%	-2.1%	5.8%
Canada Equity	14.3%	6.4%	-17.7%	14.3%	6.4%	-17.7%
United States Equity	4.1%	0.2%	-13.0%	10.9%	3.8%	-16.4%
International Equity	12.3%	7.7%	-17.2%	14.0%	5.8%	-20.0%
Emerging Equity	16.6%	8.3%	-24.7%	15.6%	8.2%	-24.5%

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ASSET ALLOCATION OUTLOOK

as at July 1, 2018

ASSET CLASS	UNDERWEIGHT		NEUTRAL	OVERWEIGHT	
	SIGNIFICANT	MODERATE		MODERATE	SIGNIFICANT
EQUITY RELATIVE TO FIXED INCOME					
Canadian Money Market					
Canadian Government Bond					
Canadian Corporate Bond					
International Government Bond					
Canadian Equity					
U.S. Equity					
International Equity (Developed Markets)					
Emerging Markets					

CURRENCY (VERSUS U.S. DOLLAR)	UNDERWEIGHT		NEUTRAL	OVERWEIGHT	
	SIGNIFICANT	MODERATE		MODERATE	SIGNIFICANT
Canadian Dollar					
Euro					
Japanese Yen					
British Pound					
Swiss Franc					
Australian Dollar					
Emerging Markets					

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