

Perspectives Executive Summary

For the 12-month period beginning October 1, 2017



INFLATION OUTLOOK CALLS THE SHOTS

- The distinction between a gradual normalization of monetary policy and a more abrupt tightening is critical to the market outlook. For bonds, both scenarios should lead to higher yields. For equities, the distinction could mean the difference between positive and negative returns. Ultimately, inflation pressure, or its absence, will dictate how quickly central banks must remove accommodation.
- Global monetary policy and liquidity conditions should remain favourable throughout the forecast horizon. Although a new Chairperson at the U.S. Federal Reserve may bring some policy uncertainty early next year, a complete change of course is unlikely.

Equities versus Fixed Income

- If inflation remains under control, bond yields will rise gradually, risk appetite will remain high and equities will be further supported by robust earnings.

Loonie and Greenback

- The Canadian dollar is facing an uncertain outlook given the NAFTA negotiations and recent hikes from the Bank of Canada.
- We expect limited and only selective U.S. dollar strength over the coming year. For this to happen, however, the Fed has to stay on a gradual renormalization path.

Regional Markets

- **U.S.:** The U.S. may be running at full capacity, but structural forces seem to be keeping inflation pressures moderate. However, high equity valuations would become hard to justify if inflation surprises to the upside and bond yields spike.
- **International Developed Markets:** Apart from Japan, valuation of this group is not overly expensive compared to other developed markets, especially the U.S. We expect international equities to resume their outperformance, supported by valuation and cyclical conditions.
- **Emerging Markets:** Most EM economies are showing improving fundamentals in terms of external debt, current account balance and credit rating. EM economies are less cyclical and more resilient than in the past.
- **Canada:** Canadian equities have strongly underperformed year-to-date. Over the short term, there is room to catch up to other markets. The catalyst could be a stabilization in the Canadian dollar and the price of oil. However, the excess optimism evident in consensus earnings, and the low probability that recent economic strength will be repeated, make Canadian equities less attractive over a longer time frame.



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Expected Returns

| Expected returns for the one-year period beginning October 1, 2017 | In Canadian Dollars | | | In Local Currency | | |
|--|---------------------|------------------------|------------------|-------------------|------------------------|------------------|
| | Global Reflation | Policy Renormalization | Global Recession | Global Reflation | Policy Renormalization | Global Recession |
| Probabilities | 15.0% | 65.0% | 20.0% | 15.0% | 65.0% | 20.0% |
| Canada Money Market | 1.5% | 1.1% | 0.8% | 1.5% | 1.1% | 0.8% |
| Canada Bond | -0.4% | 1.6% | 4.8% | -0.4% | 1.6% | 4.8% |
| Canada Federal Government Bond | -0.7% | 1.4% | 5.8% | -0.7% | 1.4% | 5.8% |
| Canada Corporate Bond | 1.3% | 2.2% | 1.8% | 1.3% | 2.2% | 1.8% |
| Canada Real Return Bonds | 1.8% | -2.5% | 4.4% | 1.8% | -2.5% | 4.4% |
| Canada High-Yield Bond | 4.5% | 3.3% | -5.8% | 4.5% | 3.3% | -5.8% |
| International Government Bond | -5.6% | 0.5% | 8.1% | -3.8% | -1.0% | 5.3% |
| Canada Equity | 15.4% | 4.9% | -20.2% | 15.4% | 4.9% | -20.2% |
| United States Equity | 10.7% | 4.4% | -13.8% | 11.6% | 2.0% | -17.1% |
| International Equity | 14.4% | 6.3% | -17.5% | 16.5% | 5.8% | -17.5% |
| Emerging Equity | 17.2% | 10.8% | -22.1% | 18.6% | 9.0% | -18.4% |

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Asset Allocation Outlook

| Asset Class | Underweight | | Neutral | Overweight | |
|--|-------------|----------|---------|------------|-------------|
| | Significant | Moderate | | Moderate | Significant |
| Equity Relative to Fixed Income | | | ✓ | | |
| Fixed Income | | | | | |
| Canadian Money Market | ✓ | | | | |
| Canadian Government Bond | | | | | ✓ |
| Canadian Corporate Bond | | | | | ✓ |
| International Government Bond | | ✓ | | | |
| Equity | | | | | |
| Canadian Equity | | | ✓ | | |
| U.S. Equity | | ✓ | | | |
| International Equity (Developed Markets) | | | | | ✓ |
| Emerging Markets | | | | | ✓ |
| Currency (versus U.S. Dollar) | | | | | |
| Canadian Dollar | | | ✓ | | |
| Euro | | ✓ | | | |
| Japanese Yen | | ✓ | | | |
| British Pound | | | ✓ | | |
| Swiss Franc | | ✓ | | | |
| Australian Dollar | | ✓ | | | |
| Emerging Markets | | | | | ✓ |

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