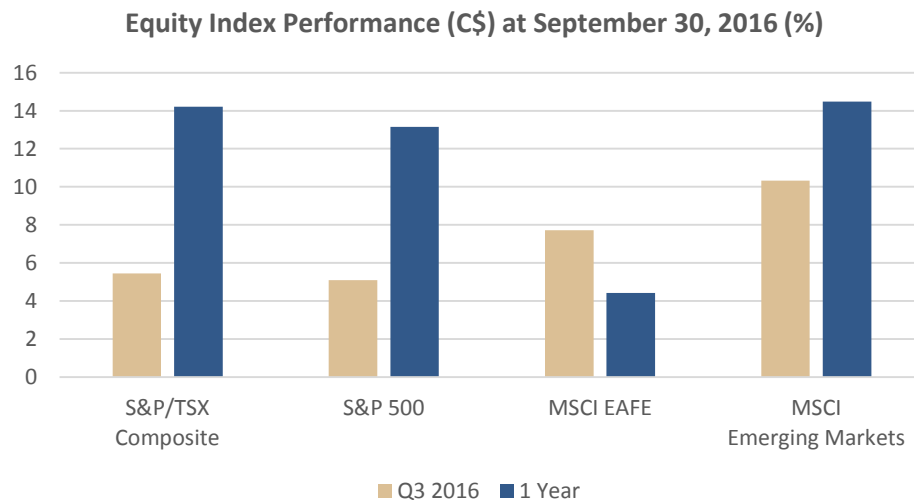


Q3 2016 Global Economics Overview

Economic Overview

Many central banks continued to struggle to improve economic growth and stimulate inflation via increased quantitative easing (QE) initiatives. At the same time, promised fiscal stimulus packages in many countries have been slow to build momentum. These delays were the result of increased political uncertainty, including the pending U.S. federal election, more posturing on the potential for a “hard Brexit”, continued terrorist activities, and political scandals in select emerging market countries. As the World Bank noted in a recent review: “The global outlook faces pronounced risks of another stretch of muted growth.” Despite these downstream risks, major global equity markets rallied strongly in the third quarter.



Source: Bloomberg

Inflation and GDP Growth as of June 30, 2016				
	Canada	US	EAFE	EM
CPI (YoY)	1.50%	1.00%	0.42%	3.14%
Real GDP (YoY)	0.90%	1.30%	1.85%	3.34%

Valuation Multiples as of September 30, 2016				
	S&P/TSX	S&P 500	EAFE	EM
P/B	1.85x	2.85x	1.59x	1.59x
P/E (Fwd)	19.3x	17.2x	15.1x	13.9x

Source: Bank of Canada, Statistics Canada, U.S. Bureau of Labor Statistics, Bloomberg, BNY Mellon

Canada

Economic growth had been held back by a substantial first quarter decline in oil prices followed by the Alberta wildfires in the second quarter and a less than robust U.S. economic expansion. More recently, Canadian GDP growth has shown some signs of improvement as oil prices are up about 50 percent from their February lows and select other commodities have increased in price. Although also up from its February lows, the current depressed level of the Canadian dollar is aiding export performance. Select consumers are also enjoying the benefits of the enhanced monthly Canada Child Benefit. Unfortunately, business capital spending remains subdued, acting as a major headwind for GDP growth. Some of this may be offset by planned fiscal stimulus, but the economic effect of any such spending will take time to be felt by the economy as a whole. In this environment, the Bank of Canada is not likely to follow the U.S. Federal Reserve (the Fed) in potentially increasing short-term rates this coming December. However, Canada is experiencing some signs of inflation, so longer term interest rates may drift slightly higher as the year draws to a close.

The U.S.

The United States appears to be on track for slightly improved growth for the remainder of the year after an economically challenging first half of 2016. A strong dollar, suppressed capital investment, and weak productivity growth remain major impediments to a significant surge in real GDP. Additionally, the ebb and flow of the pending elections and the threat of a December Fed Funds rate increase adds further uncertainty to the outlook. A firm job market and inventory rebuilding should offset some of these negatives, resulting in real GDP growth in the 1.5% to 2% range.

Europe

Economic growth and inflation through the major European economies remains weak. The European Central Bank (ECB) has continued to expand its QE program. This action has resulted in negative interest rates in several countries. Negative yields are putting financial pressure on the banking system to such an extent that rumours abound that the ECB may be considering a tapering of its QE actions. The growing complexity of future Brexit negotiations remains a wildcard for the economic and market outlook.

The U.K.

The U.K. economy continued to advance in the quarter despite fears to the contrary after the June Brexit vote. The decline in the pound sterling to near quarter-century lows supported growth in the export sector of the economy. As the quarter progressed, Prime Minister Theresa May took an aggressive stance on future Brexit negotiations. She implied that the two-year exit negotiations with the European Union would begin in March 2017. Her approach resulted in the market coining the term “Hard Brexit”, further unsettling markets.

Japan

Japan remains mired in what seems to be an endless cycle of debt, deflation, and demographically induced low growth. The Bank of Japan has shifted its QE strategy from buying a specific quantity of bonds and other financial instruments each month, to one of targeting a 0% yield on its 10-year government bonds. The markets are skeptical of the efficacy of this new approach.

Emerging Markets

Emerging markets remain as volatile as ever. China is again dealing with an overheated property market. Brazil confirmed the dismissal of its leftist president, Dilma Rousseff, who was replaced by a more centrist president. As a result, sentiment in Brazil has improved. At a time of economic slowdown, South Africa continues moving towards political uncertainty, with municipal electoral losses for the ruling African National Congress.

Turkey experienced a failed coup attempt which resulted in more power for its president, Recep Tayyip Erdogan, a result which is positive for the short term but negative for the long term. Risk in the Philippines has increased, with the new president, Rodrigo Duterte, making waves globally with his approach to curbing drug trafficking and his shifting alliance from the U.S. towards Russia and China.

Bonds

Despite a small rise in yields in mid-September, global yields generally fell in the quarter. Central banks remain an obstacle to higher, more sustainable interest rates. Negative interest rates overseas have put substantial pressure on the future stability of the banking system. As noted above, the ECB may be considering a reduction in future QE stimulus.

North American interest rates remain in positive territory, but offshore purchases of Canadian and U.S. bonds have slowed as currency hedged purchases now result in a negative overall yield. There are some signs of potential inflation as the U.S. and Canadian economies show improvement, but a significant increase is not likely. Interest rates are expected to drift slightly higher as the quarter progresses.

Canadian Bond Market Performance		
	Third Quarter 2016	1 Year
TMX Universe Bond Index	1.2%	6.3%
TMX Short Term Bond Index	0.5%	2.0%
TMX Long Term Bond Index	2.4%	12.6%
Canadas	0.6%	4.1%
Provincials	1.5%	8.7%
Investment Grade Corporate	1.6%	6.3%
High Yield Corporate	5.7%	10.0%

Source: FTSE TMX