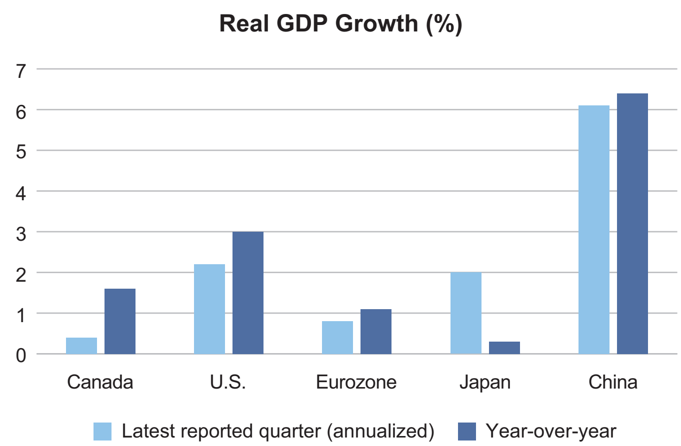
ECONOMIC OVERVIEW

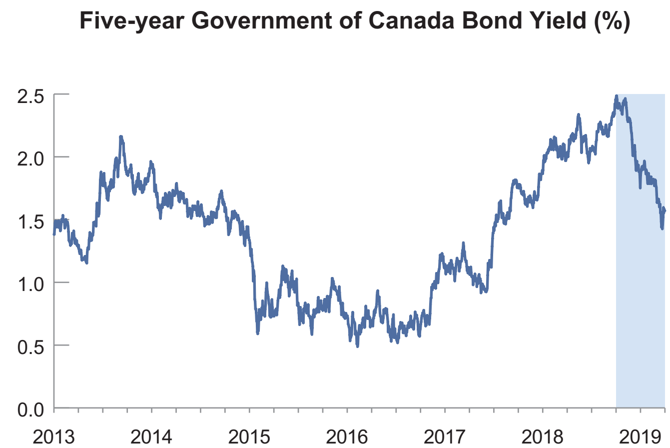
March 31, 2019

World economic growth is expected to continue to decelerate in 2019 as many economies are reaching the latter end of their economic expansions. The global economy, however, is still being positively impacted by relatively tight labour markets, a pause in central banks' monetary tightening, temporary declines in longer term interest rates and additional fiscal and financial stimulus in China and select other countries.



Source: Bloomberg

performance in 2018. In contradiction to more than a few financial market pundits, a recession does not appear to be imminent in 2019 as the Bank of Canada recently indicated that a pause in its tightening cycles is warranted. Certainly, several economic challenges remain over the balance of the year, including trade relations with China and the health of the Alberta energy sector. The consensus growth outlook is calling for 1.7% economic growth in 2019, but only an annualized 0.7% to 1.0% in the first quarter.



Source: Bloomberg

Canada

The economic weakness experienced at the end of 2018 carried on into the first quarter of 2019. Domestic growth has certainly slowed, weighed down by the combination of lower investment spending, slower household spending and a fall in exports. Further weighing on growth were the usual suspects: global trade tensions and geopolitical uncertainties. Responding to these events, interest rates fell throughout the quarter.

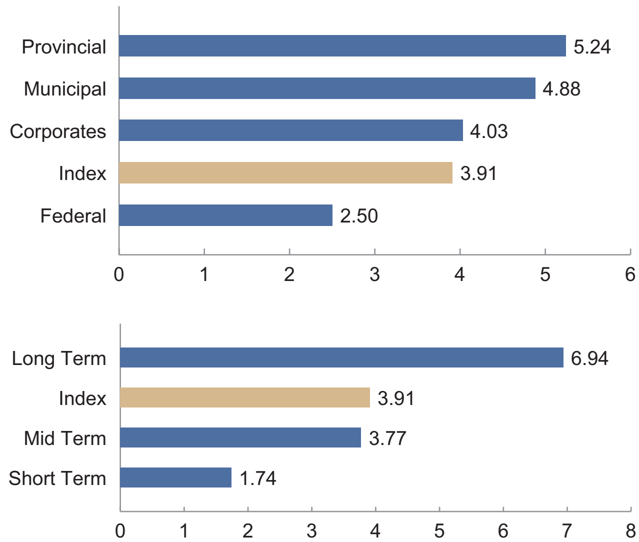
Despite the slowdown, Canada is still performing adequately and had been expected to slow after the improved economic

Shorter-dated yields dropped modestly more than longer-dated yields reflecting the growing sentiment that North American central banks have reached the end of their respective rate hiking cycles. The benchmark 10-year Government of Canada bond yield fell by approximately 35 basis points in the quarter and the two-year to 30-year yield spread widened modestly.

Credit performed well as both provincial and corporate bonds exceeded the performance of federal bonds as risk assets in the financial markets rebounded from the economic forecast weakness at the end of last year.

Performance of FTSE Canada Universe Bond Index Sectors and Term Structure (%)

(Three months ending March 31, 2019)



Source for both graphs: FTSE Canada

U.S.

The latest data showed that the U.S. economy slowed in the fourth quarter of 2018 due in part to the federal government shutdown orchestrated by President Donald Trump. Additional headwinds included weaker consumer spending and a slowing housing market. Nevertheless, business investment during the same period helped offset the slowdown to some degree. The most recent data pertaining to the first quarter of 2019 indicates ongoing weakness in economic growth. Softer retail sales, limited wage growth and the ongoing housing challenges all characterized a retreat by the consumer. Business investment appears to be slowing, based on preliminary data. Trade issues with China remain a sticking point, but if resolved, should result in a lift to U.S. GDP.

The consensus outlook for 2019 suggests a continued real GDP slowdown to an annualized level of 2.4%. Major government spending programs appear to be tailing off which will contribute to the expected lower GDP growth along with the continuing inflated levels of both government and corporate indebtedness.

Europe

Europe continues to suffer from weaker economic growth, with recent data barely picking up from depressed levels in the fourth quarter of 2018. Europe, especially Germany, usually the powerhouse of export growth, has been hurt by sluggish global demand, declining consumer sentiment, threatened U.S. trade wars, and unresolved Brexit negotiations. However, as occurs when economies are in the latter stages of their growth cycles, several countries' retail sales continue to support growth. Some additional support is coming from a tightening labour market, contained inflation, and a relative easing in European Central Bank (ECB) monetary policy which may partially offset the continuing economic slowdown.

U.K.

The fourth quarter of 2018 showed some broad improvements in the consumer sector across areas such as employment and wage growth. However, early data points for the first quarter of 2019, including purchasing managers indexes (PMIs), are implying only a modest advancement. Recent retail sales figures are showing some support for positive GDP. As expected, Brexit continues to present a massive overhang to both near- and long-term growth prospects. Uncertainty on whether a deal can be struck with the European Union continues and has contributed to reduced investment. Going forward, a no-deal outcome will likely trigger a material economic retrenchment while the consummation of a deal should advance consumer spending, restore business investment and, more importantly, remove the existing economic uncertainly. Because of Brexit, consensus economic growth for the year is forecast at 1.3%.

Japan

Japanese GDP growth rebounded in the fourth quarter of 2018 but recent economic reports appear to show more weakness ahead. The manufacturing PMI hit a two-year low due to continued weakening in exports related to the growth slowdown in China. This may be reversed later this year as China has initiated another round of monetary and fiscal stimulus. Consumer confidence measures and capital goods orders continued to decline. In March, the government downgraded its economic outlook for the first time in several years. With an Upper House election scheduled for July, Prime Minister Shinzo Abe could be prompted to institute some positive economic measures before then. Additionally, investment-related spending in advance of the Tokyo 2020 Olympic games and a ramp-up in consumer spending ahead of the planned October sales tax increase may offset a portion of the above-mentioned economic headwinds.

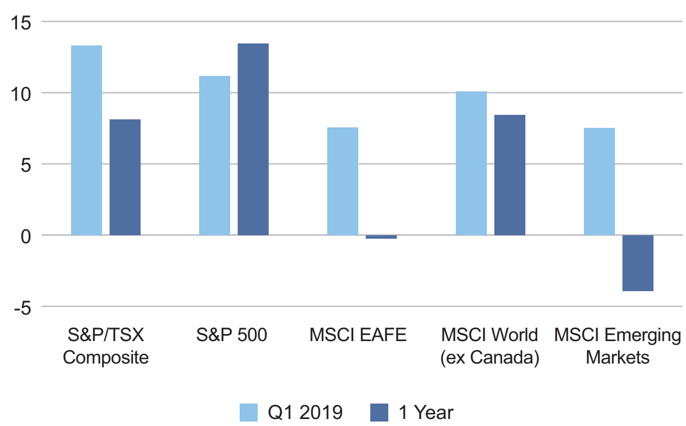
Emerging Markets

Considering recent financial stresses, in part driven by the strong U.S. dollar, growth in emerging markets has lost some momentum. Trade tensions have been an economic drag on many emerging economies, as have been reduced volumes of commodity shipments, falling investment, and the inflationary effects of rising oil prices. Some central banks have raised policy interest rates to offset domestic currency depreciation.

Notwithstanding fiscal stimulus in China designed to head off higher tariffs imposed by the U.S., it appears the Chinese economy will still slow. On the other hand, India is expected to advance as its restrictive monetary policy moderates. Central and Eastern European emerging economies are expected to grow only modestly due to a contraction in Turkey given its weak fiscal position.

The economies of the emerging markets are forecast to demonstrate a wide range of economic advancement in 2019. Consensus growth expectations range from 1.4% in Russia, 2.3% in Brazil, 6.2% in China, and 7.3% in India. Overall, the powerhouse BRIC members – Brazil, Russia, India, and China – are expected to grow 5.6% as a group.

Equity Index Performance (%) (CAD)
at March 31, 2019



Source: TD Securities, MSCI