Economic and Financial Outlook

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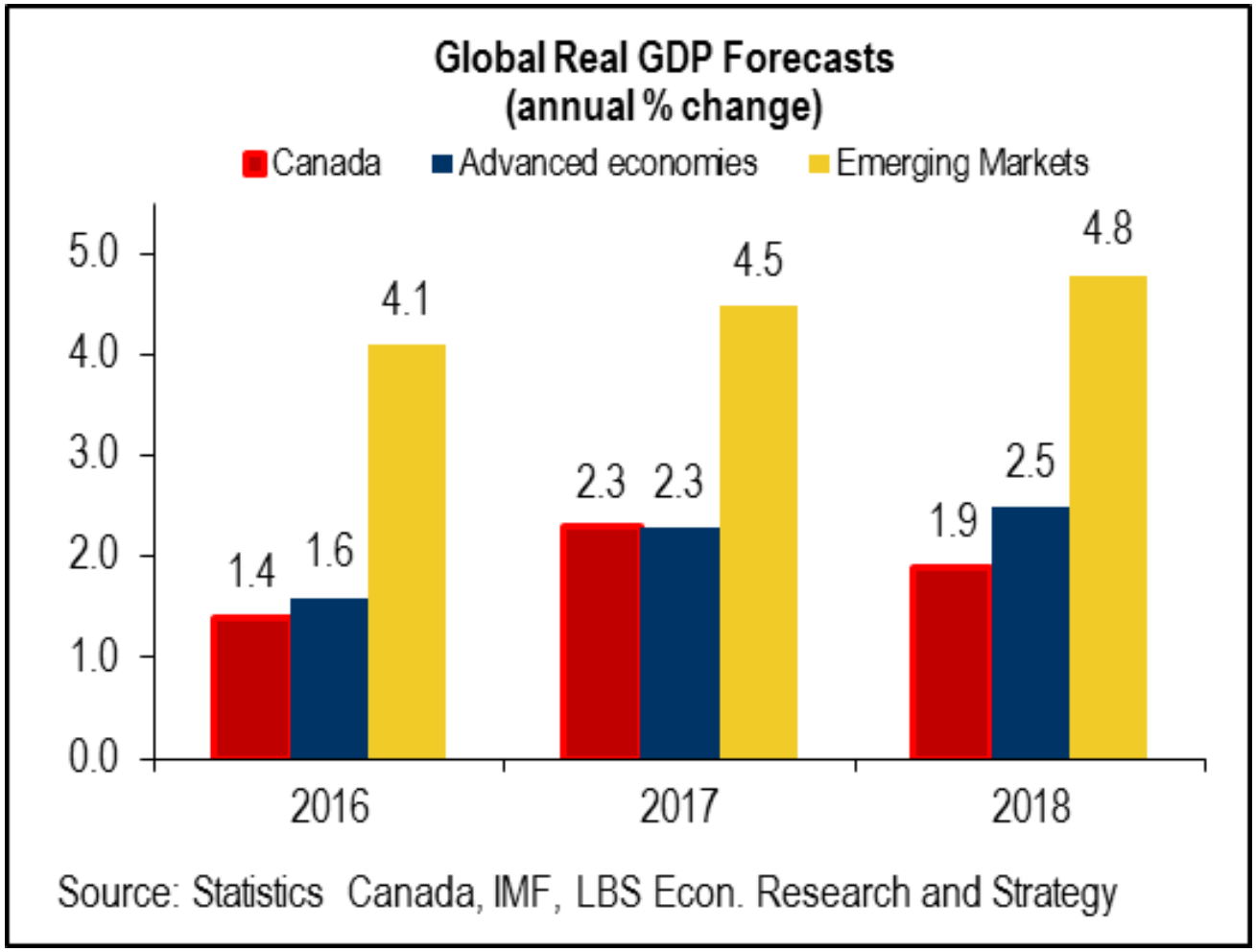
LAURENTIAN BANK SECURITIES

Spring 2017

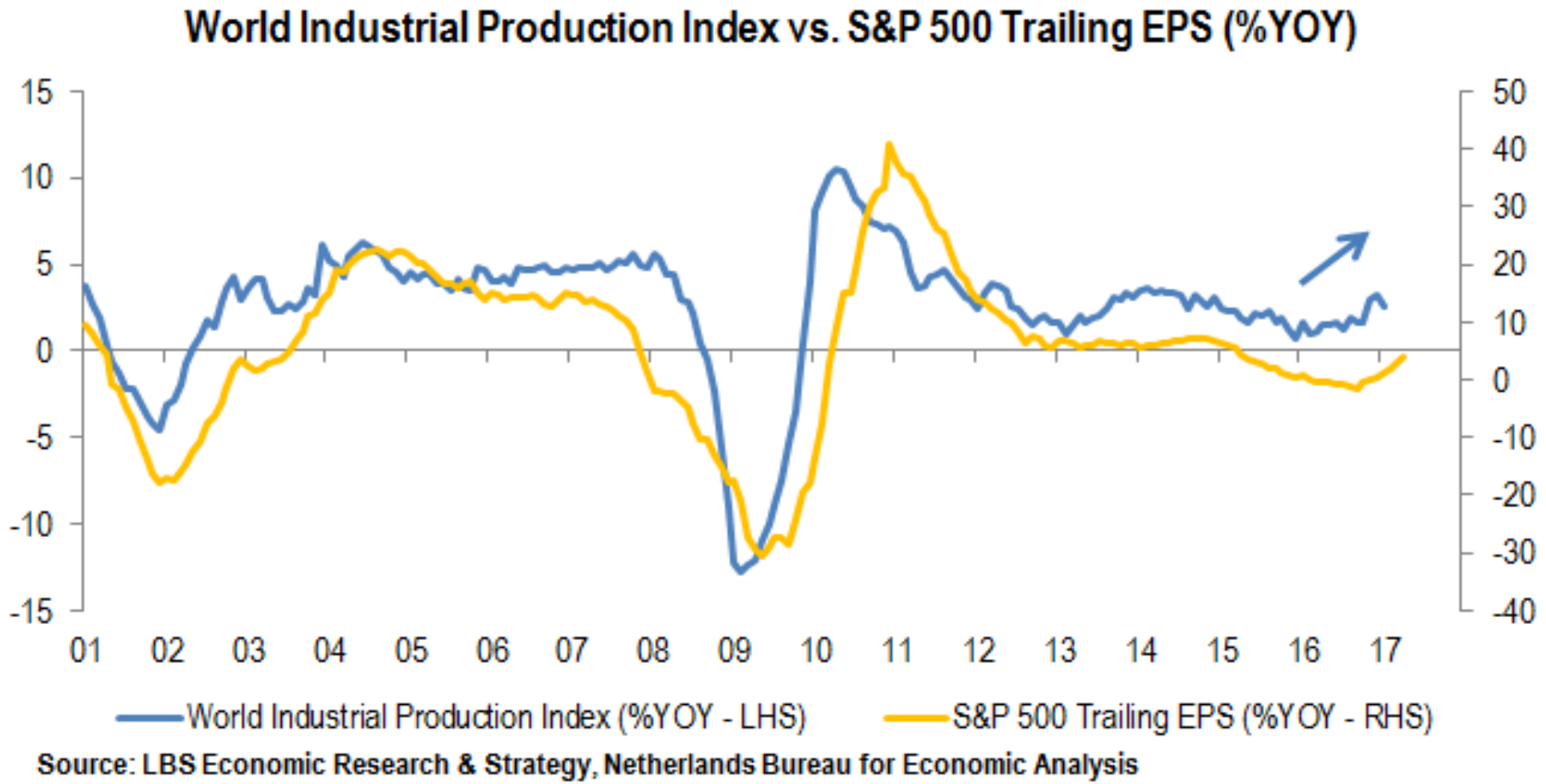
Economy gaining momentum, acceleration broad based

Support the case for a continuation of the earnings acceleration phase



Global industrial production on the rebound

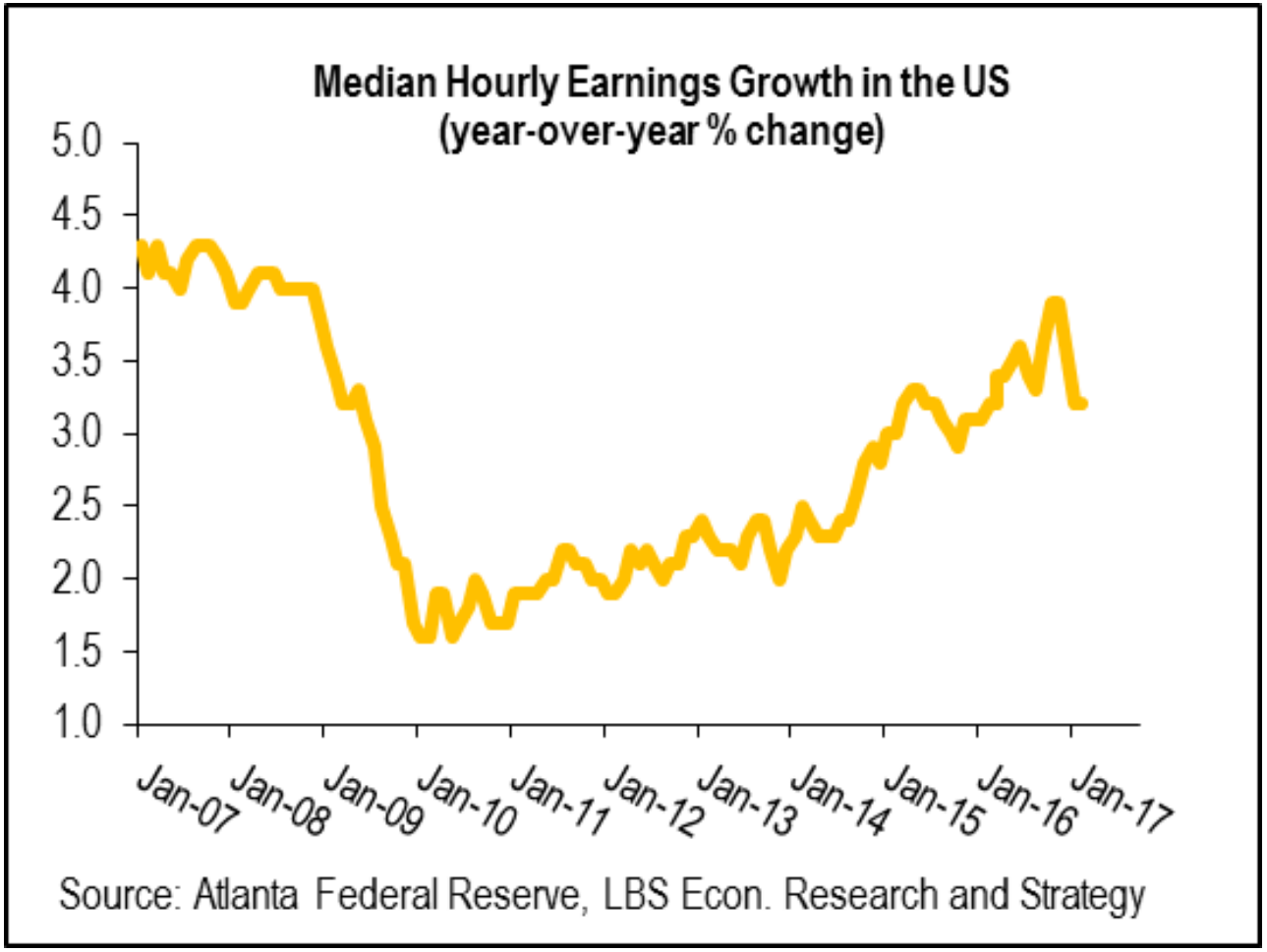
Supportive for earnings and equities as long as the economic momentum continues



Source: LBS Economic Research & Strategy, Netherlands Bureau for Economic Analysis

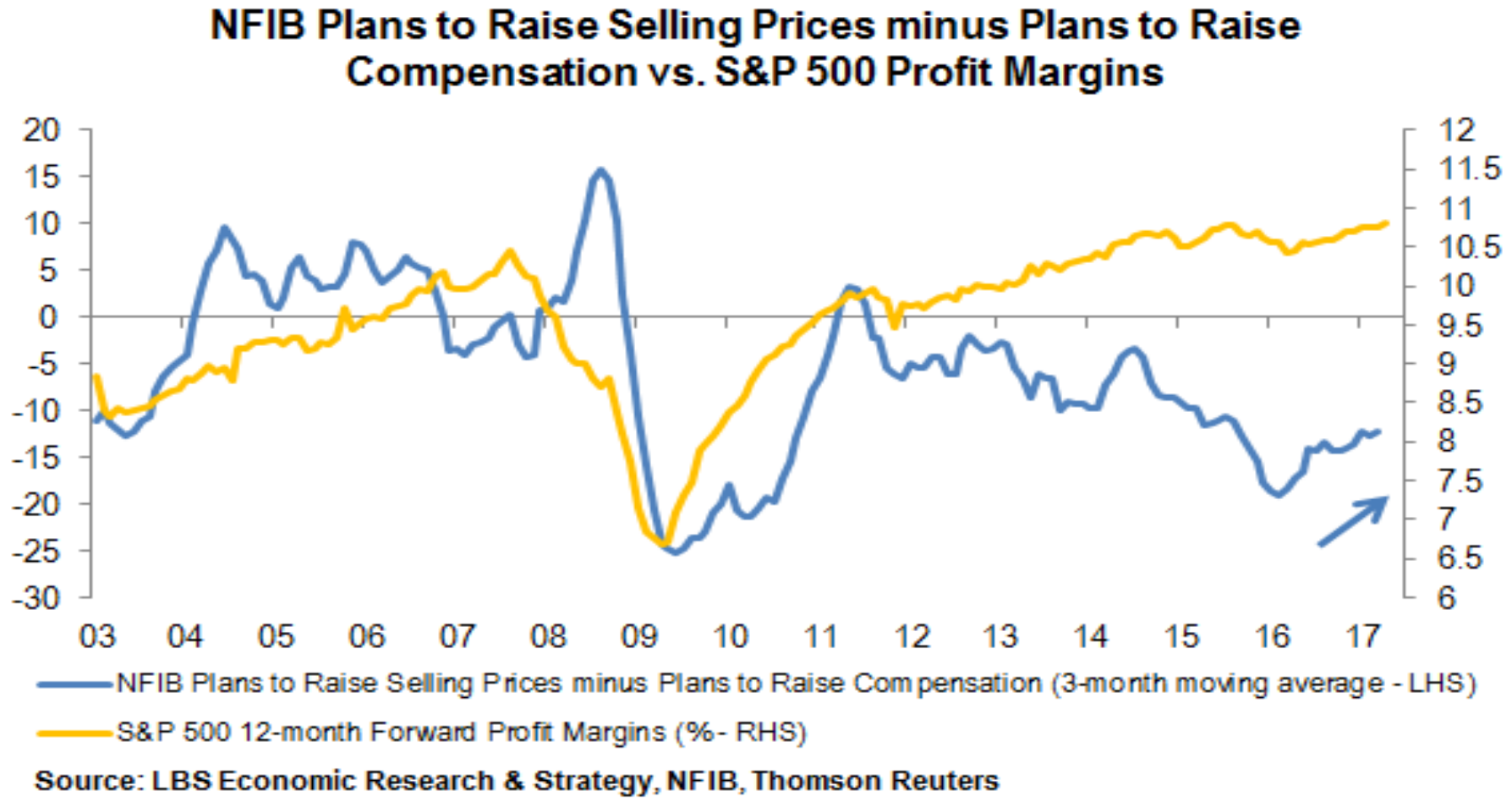
Positive momentum in advanced economies led by the U.S.

Labour market conditions are generally continuing to improve



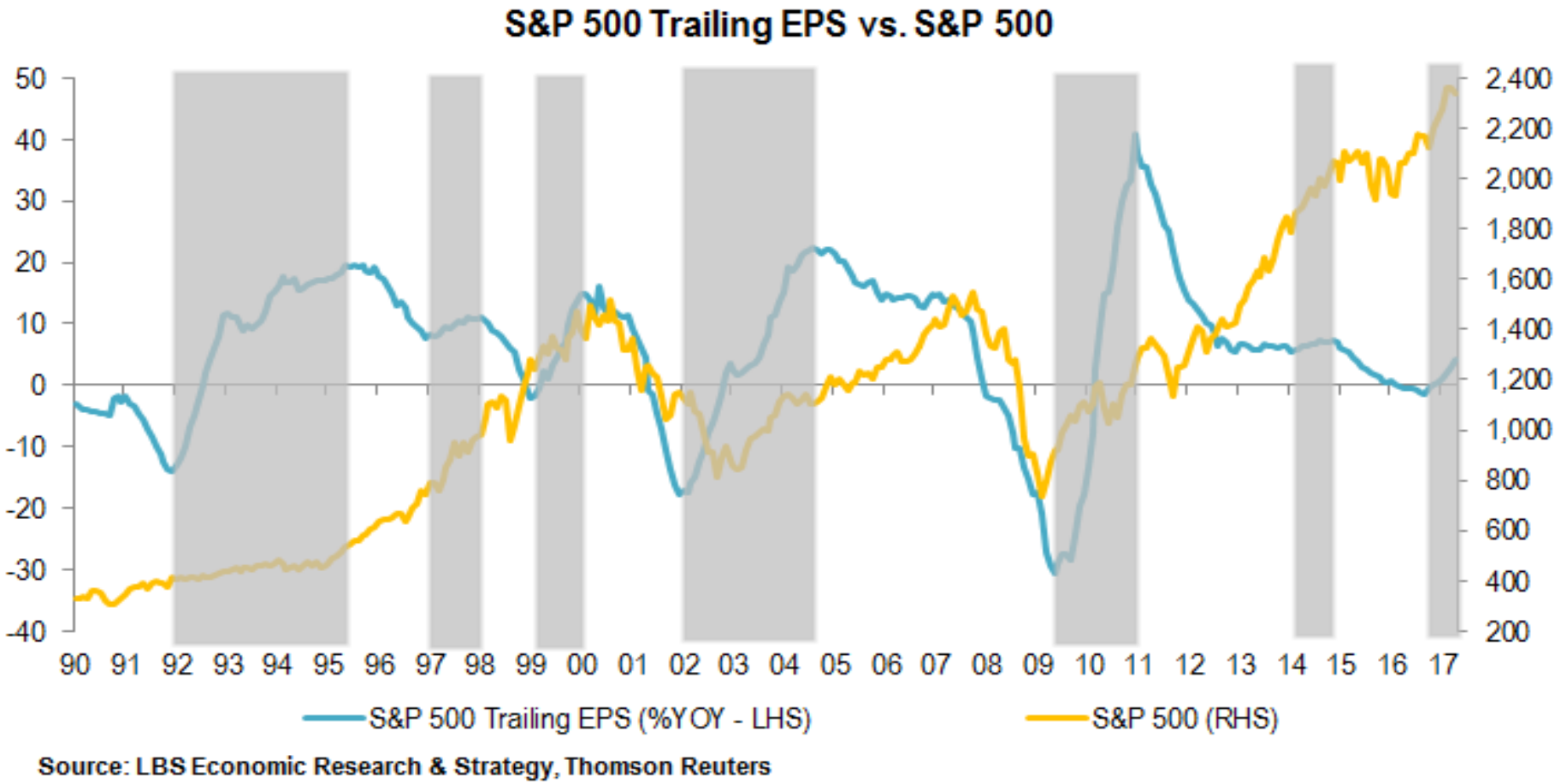
Pricing Power: U.S. CPI Inflation is also starting to rise

Positive tailwind for profit margins in the U.S.



A continuation of the earnings acceleration

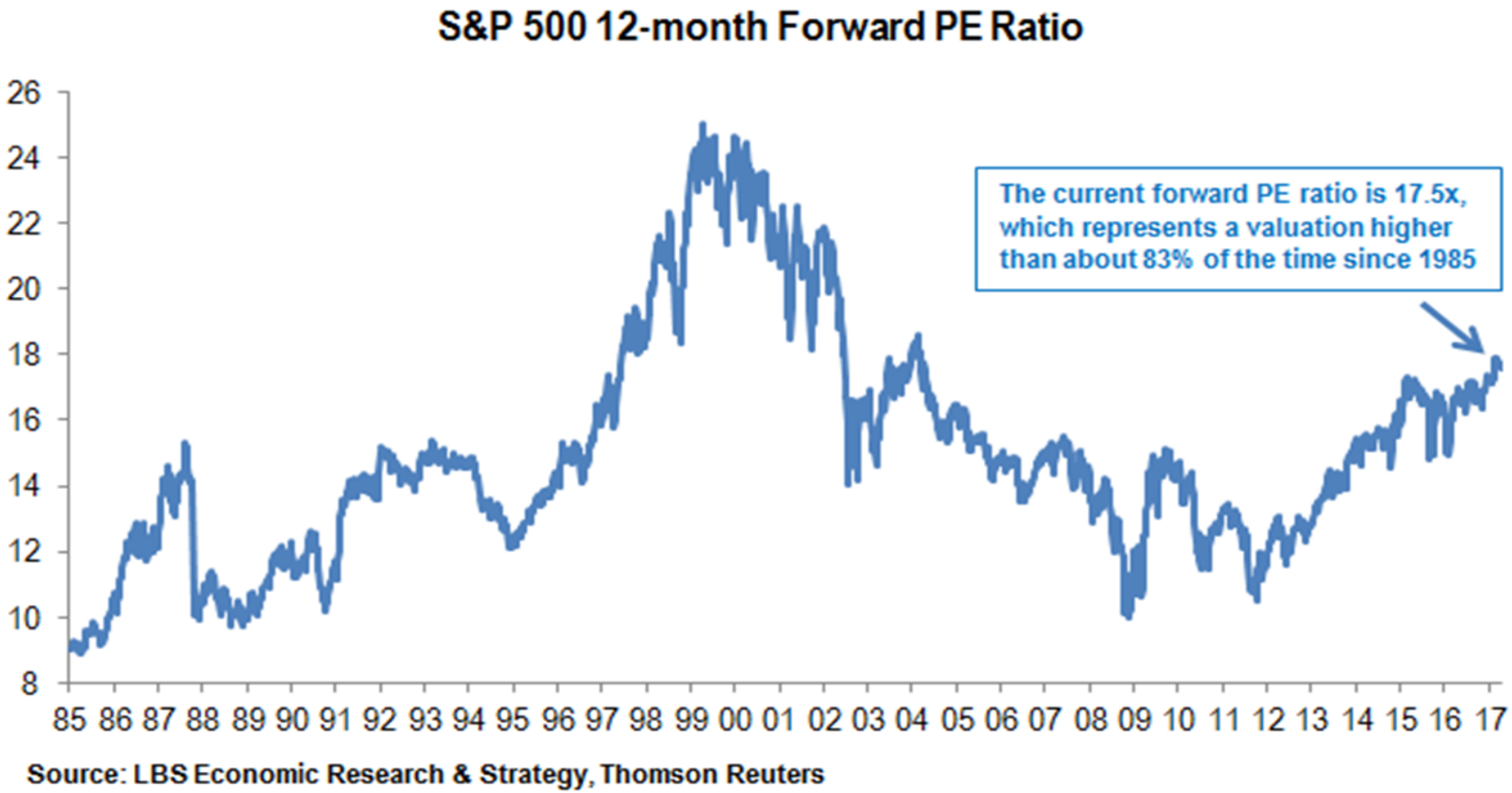
Good news for U.S. equities



Source: LBS Economic Research & Strategy, Thomson Reuters

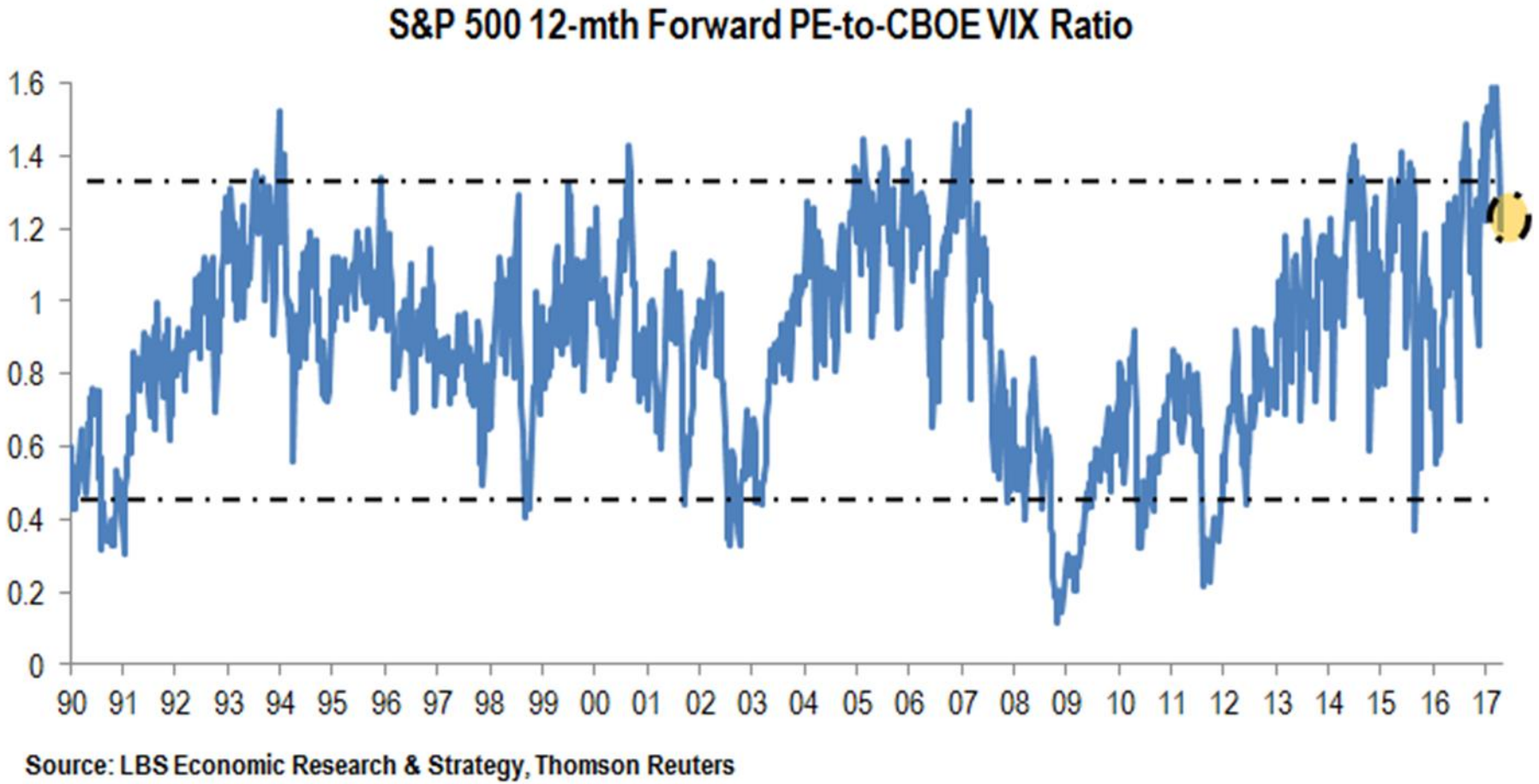
The situation is not perfect for U.S. equities

Valuation is not as attractive as the positive momentum in earnings



The situation is not perfect for U.S. equities

Growing signs of market complacency



Bottom Line: Neutral on U.S. equities

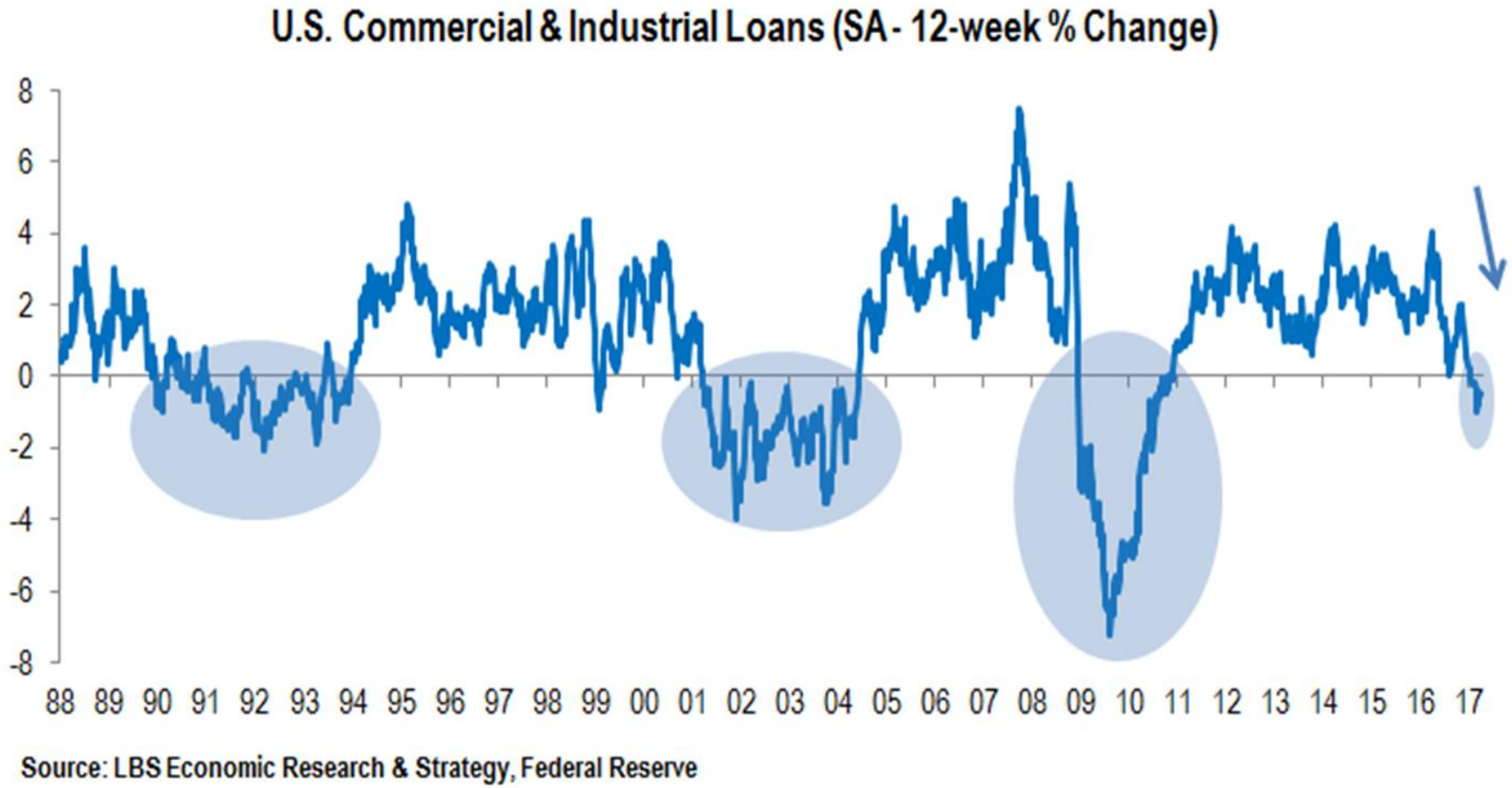
Dashboard a notch less positive than 6 months ago

Dashboard	
Factors	**Current Assessment**
Earnings Expectations	+
Valuations	= / +
Market Internals	-

What to watch for: the U.S. equity outlook

Does the economy continue to surprise on the upside?

Beginning of a downturn in U.S. C&I Loans

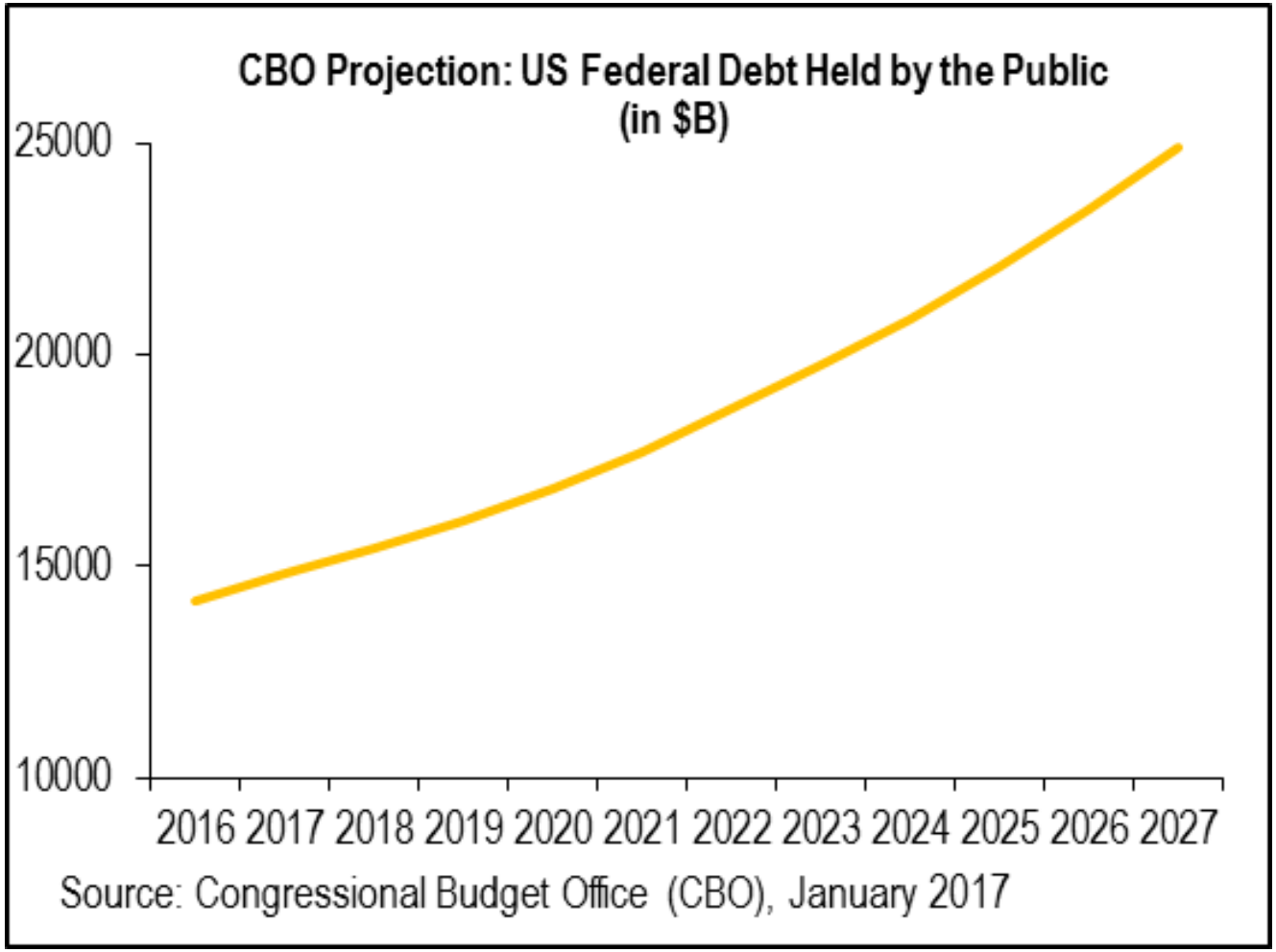


What to watch for: the equity, interest rates and FX outlook

1. Legislative agenda: Immigration, healthcare and deregulation
2. Economic agenda: Lower taxes and infrastructure
3. International agenda: trade, climate and geopolitical crises

The financing of new U.S. fiscal policies still a question mark

Brings a new source of volatility, notably on the bond market

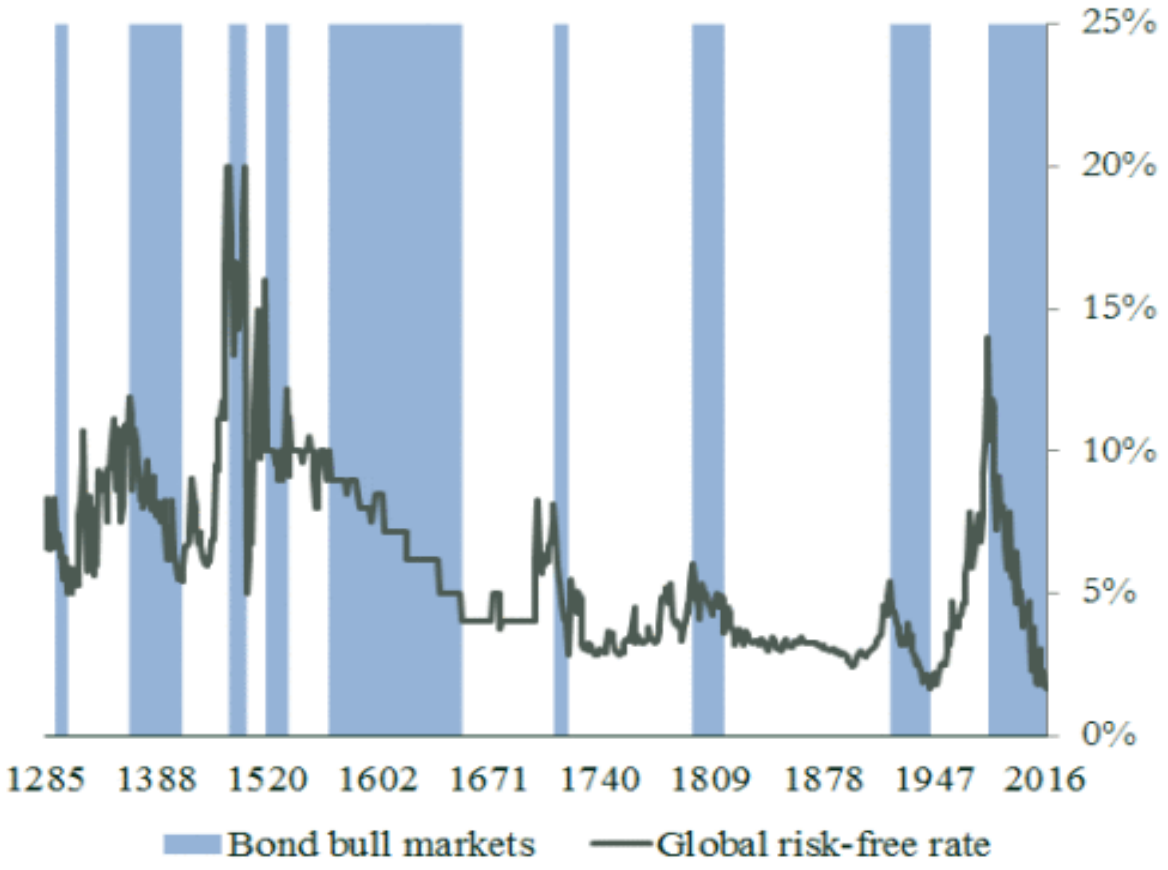


Slightly higher interest rates environment in sight

After the 2nd largest bond bull market in history

5-year federal bond yield in Canada :

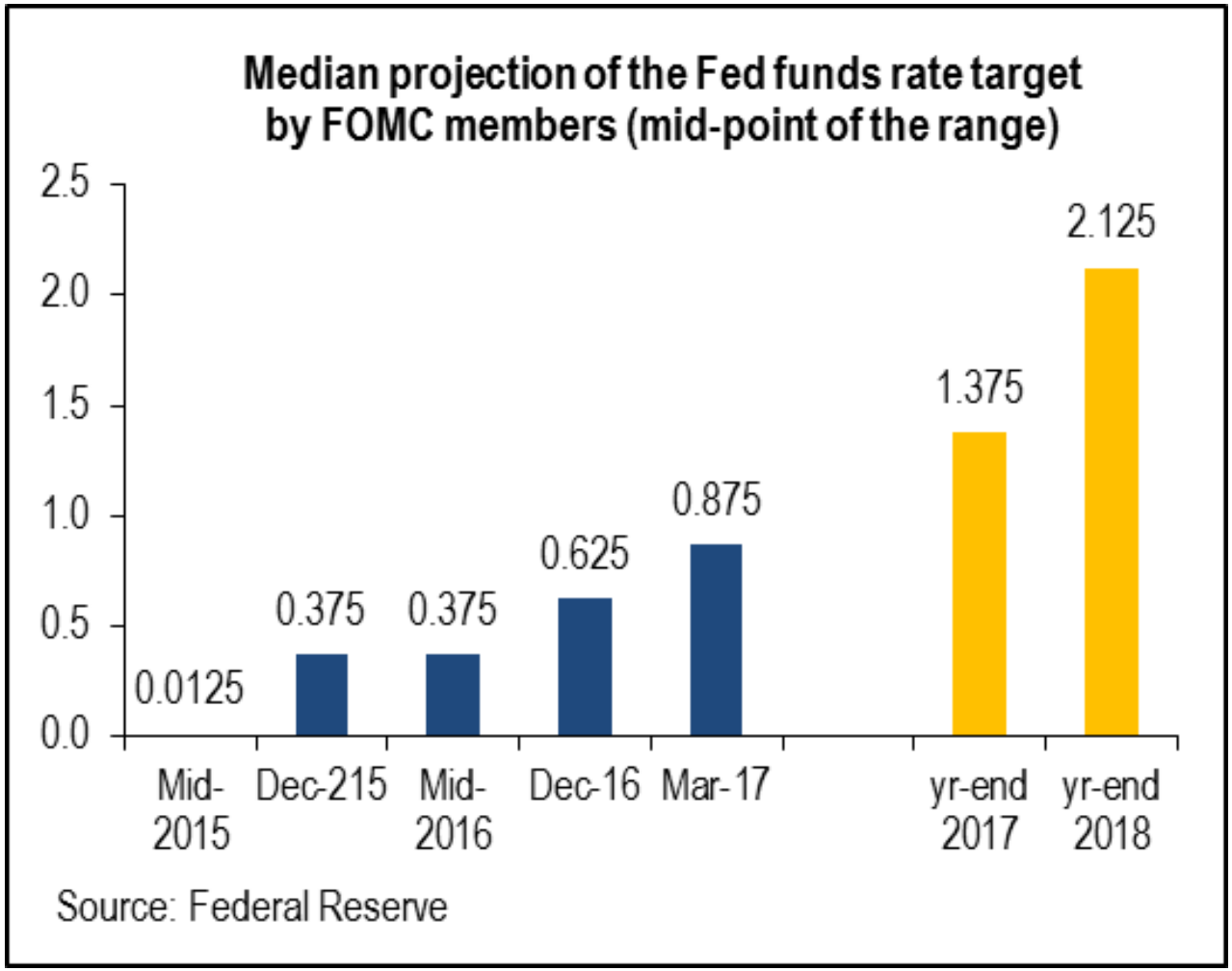
- **Brexit mid-2016: 0.60%**
- **Trump Dec. 2016: 1.11%**
- **Fed hike March: 1.28%**
- **Easter April: 1.03%**
- **Yr-end 2017: 1.25%**
- **Yr-end 2018: 1.40%**



Source: Paul Schmelzing, Bank of England

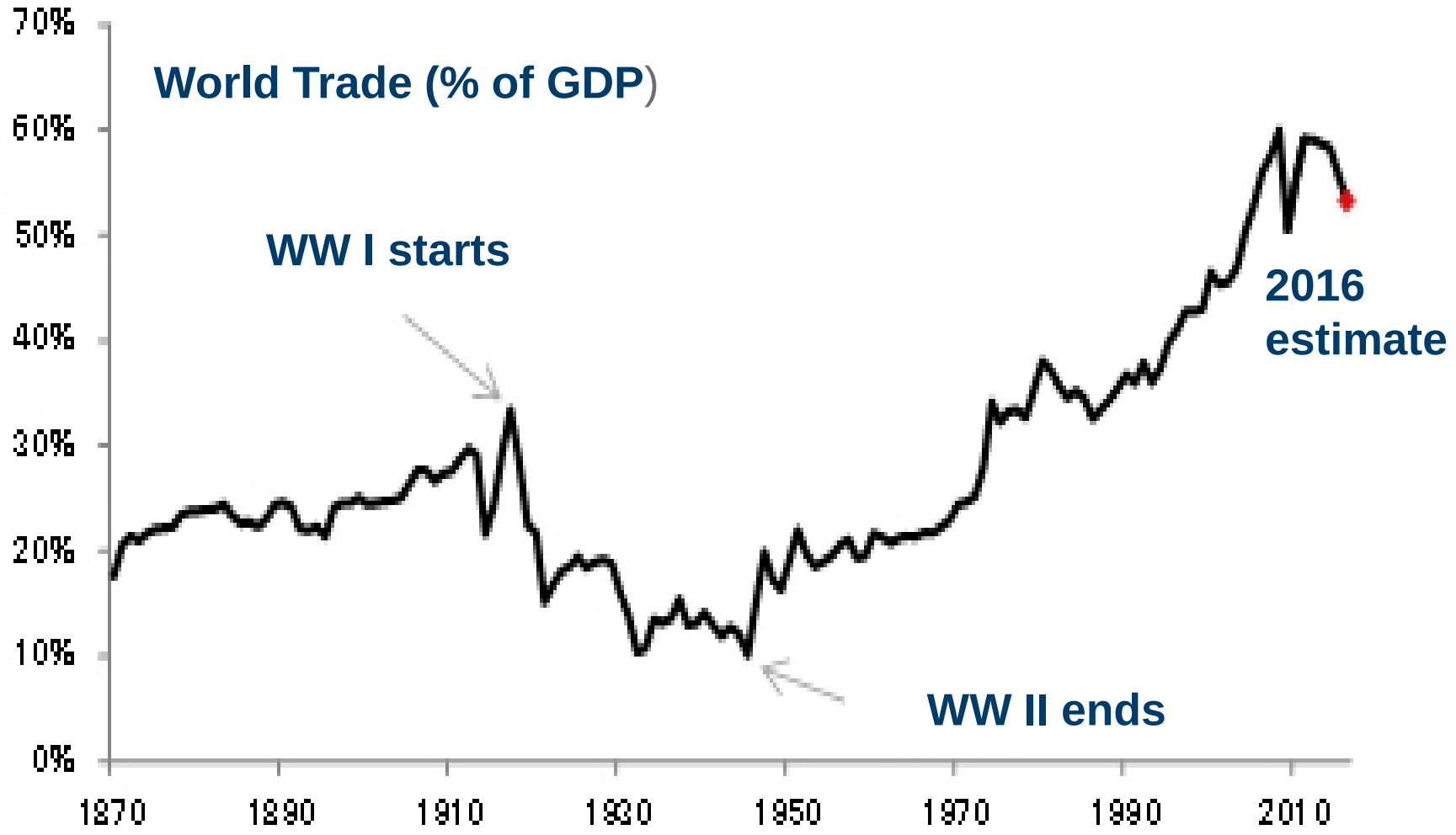
Federal Reserve Bank: 2 hikes in 3 months; 2 more in 2017?

Full-employment and rising inflation supportive for further gradual tightening



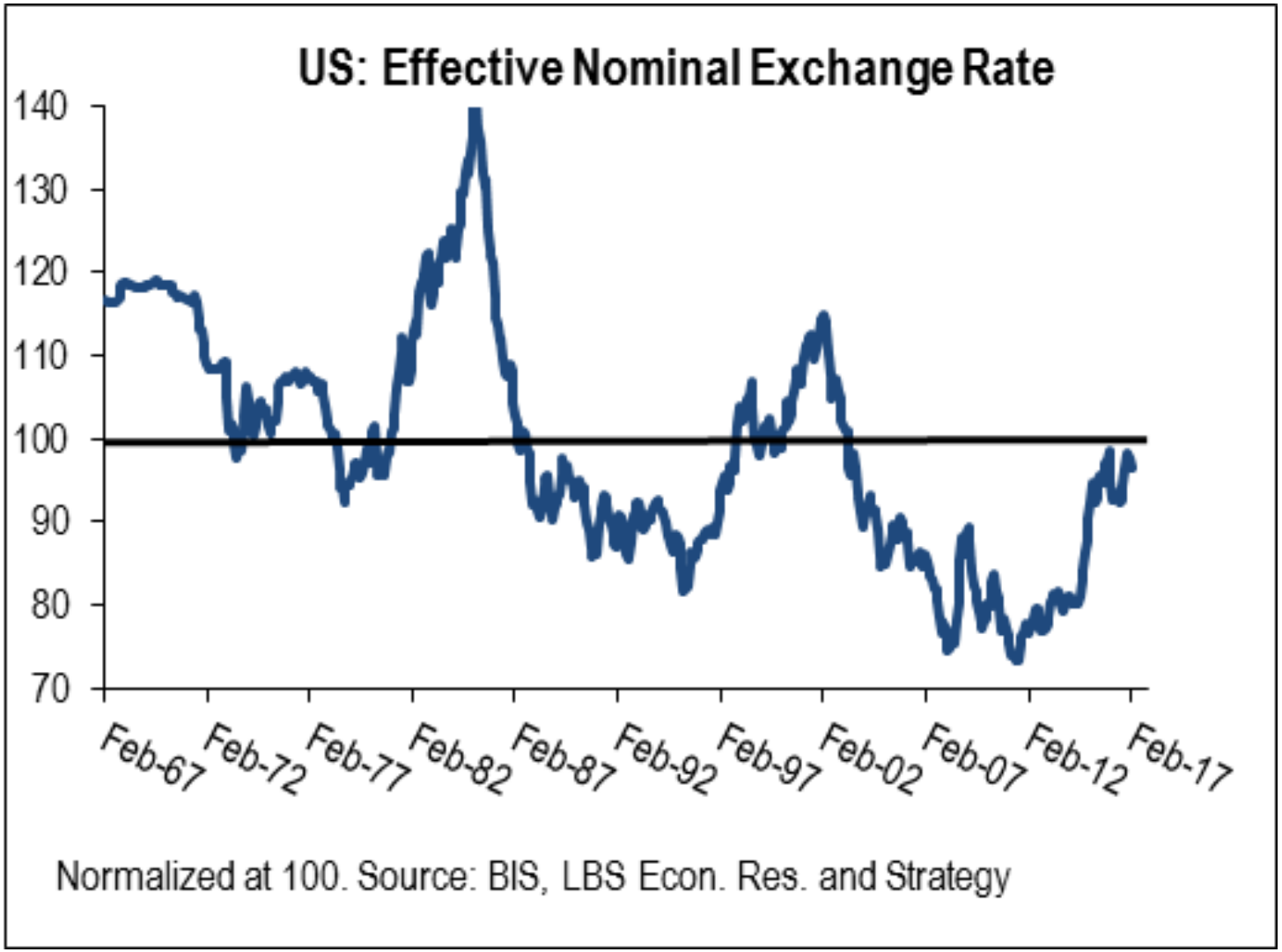
Deglobalisation? Difficult to unwind recent decades

Trade barriers increasing, but not tarrifs yet



Difficult to improve U.S. competitiveness with low USD policy

A severe USD adjustment could disrupt the financial system



Asset Allocation – Spring 2017

Top Overweight Sectors	
Canada	U.S.
Information Technology	Information Technology
Telecommunication Services	Consumer Staples
Industrials	Real Estate
Materials	Telecommunication Services
Energy	Materials
	Energy

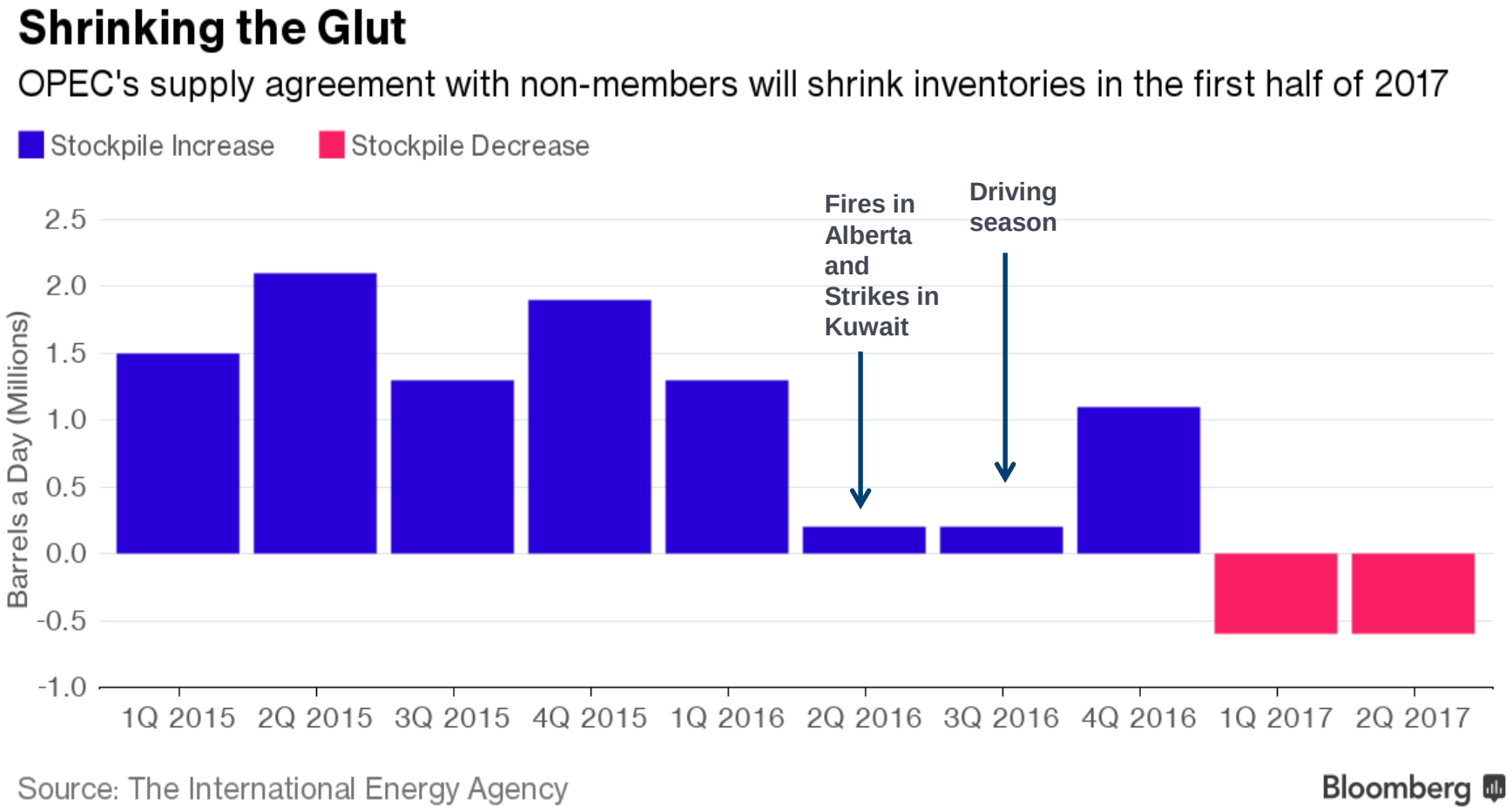
Asset Allocation – Spring 2017

Neutral on U.S. equities; still overweighting Canadian equities

Model Portfolio as of April 2017				
Asset Classes & Regions	Recommended Weightings (%)	Benchmark Allocation (%)	Over/Underweights (%)	Recommendation
Bonds	50.0	50.0	0.0	=
Government	30.0	34.2	-4.2	-
Corporate	20.0	15.8	4.2	+
Equities	50.0	50.0	0.0	=
Canada	25.0	20.0	5.0	+
United States	14.0	16.0	-2.0	-
Other Developed Markets	8.6	11.6	-3.0	-
Emerging Markets	2.4	2.4	0.0	=

Crucial to a balanced market

OPEC's agreement with members and non-members needs to hold

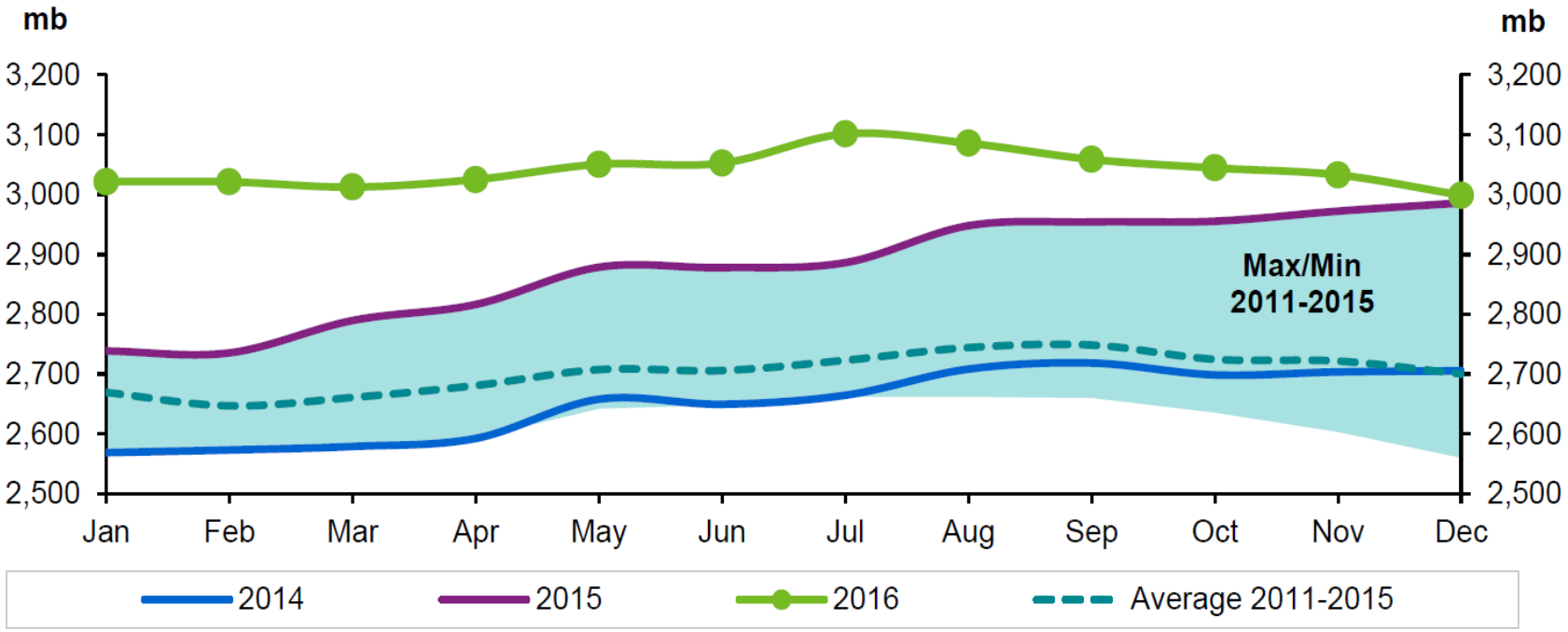


OECD commercial inventories

Getting within 5-year range before the cuts

Graph 9.1

OECD's commercial oil stocks



Sources: Argus Media, Euroilstock, IEA, METI, OPEC Secretariat and US Energy Information Administration.

Crude oil outlook is positive

Several themes will dominate in 2017 and beyond

- Higher demand (medium term trend)
- Shrinking non-OPEC supply (medium term)
- Aramco's IPO
- Lower investments (medium to long term)
- Geopolitical risk and disruption (at all times)

In spite of:

- Excess inventories (short term)
- OPEC cohesion or lack thereof (short term)
- Iran, Nigeria and Libya's return to market (medium term)
- U.S. shale oil production return to market (medium term)
- Technology (long term)
- Alternative energies (long term)
- Environmental concerns (long term)

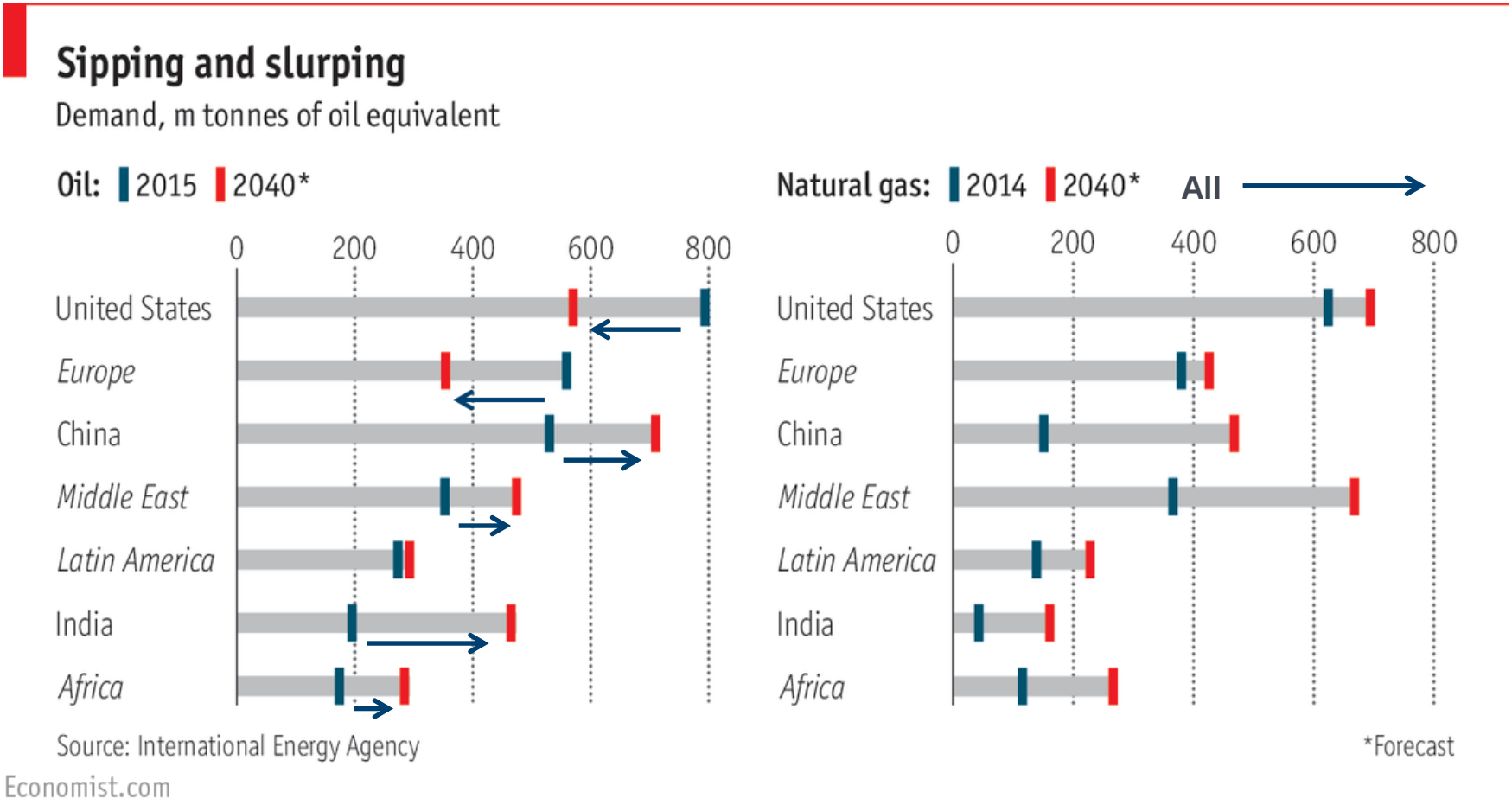
The crude price outlook beyond 2017

Surplus will stop accumulating even without OPEC agreements

- Production in the rest of the world (ex-OPEP and ex-NAM) will be flat unless prices remain above $70 for a sustained period
- China produces less and consumes more oil. In India, oil consumption is rising rapidly.
- U.S. shale oil production will have been flat over a 3 year period when it is back to 9,5 mb/d next year.
- U.S. crude consumption is still increasing.
- Geopolitical and production disruptions will persist.
- Crude oil will remain the dominant source of energy at least until 2030, especially in transportation

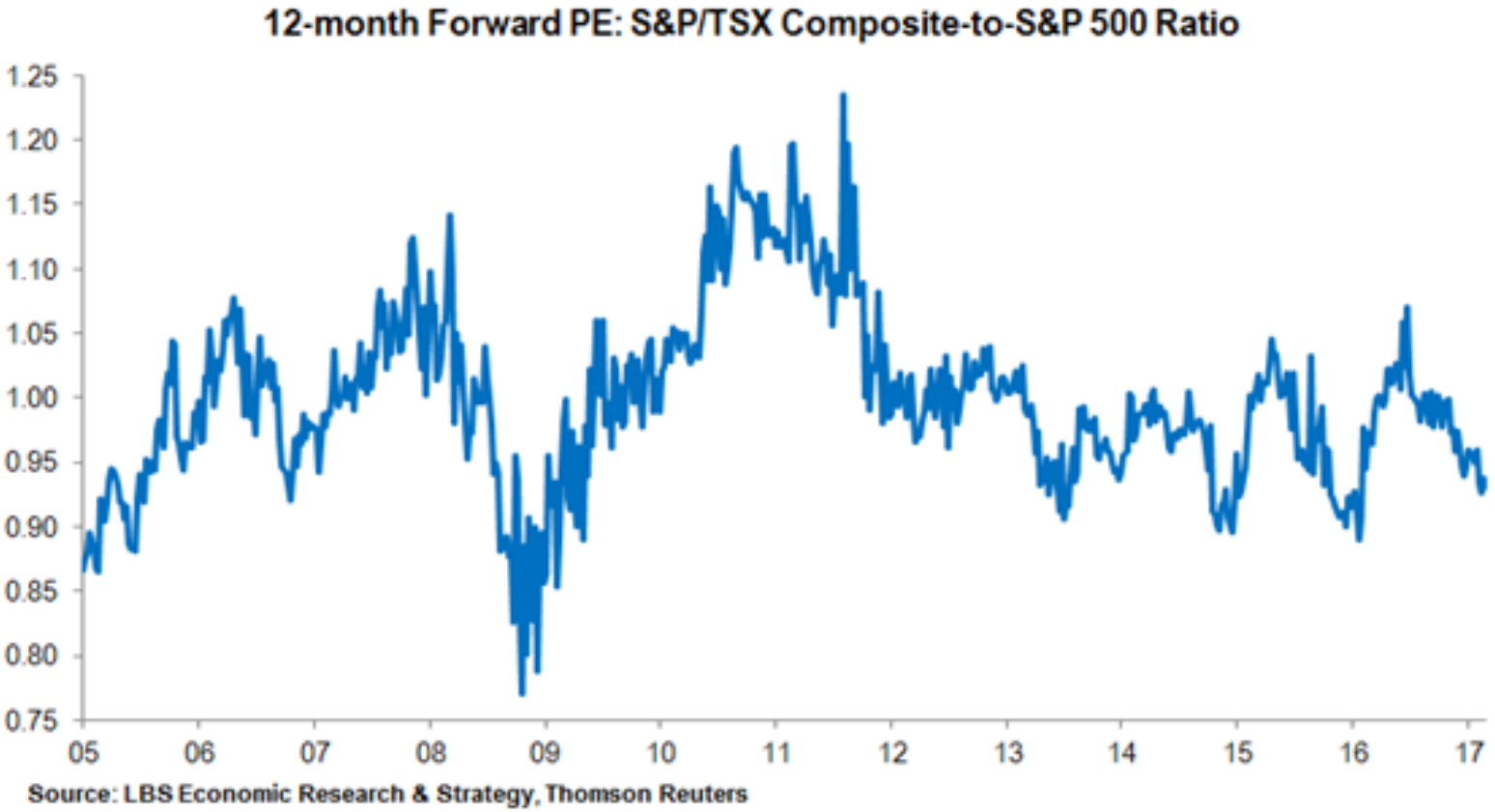
Oil demand growth will eventually slow down (by 2040)

And natural gas demand still expected to grow fast



Asset Allocation – Overweighting Canadian equities

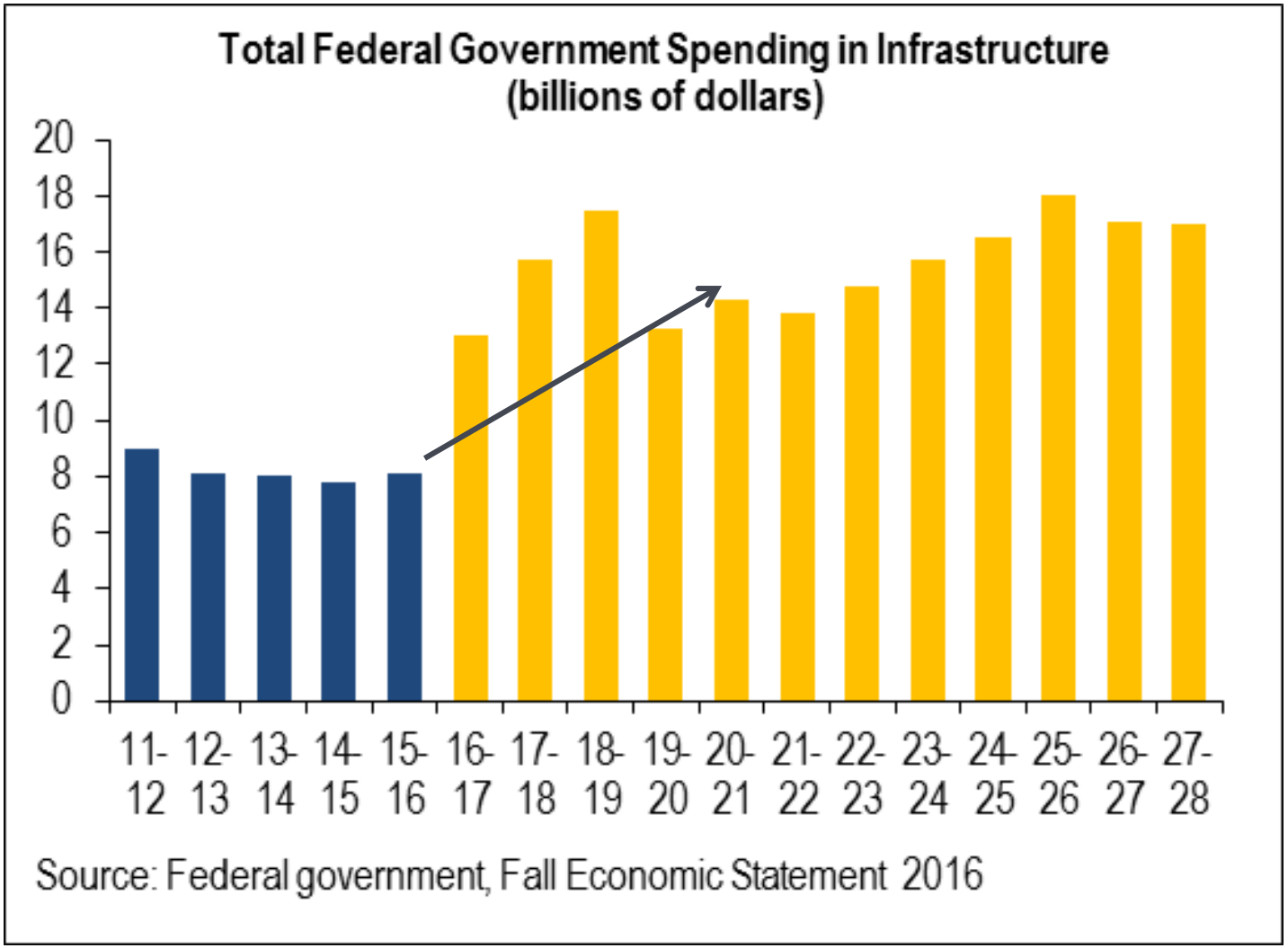
Low TSX/S&P500 12-month forward PE ratio



Canada: Real GDP growth projected to be above potential in 2017-18

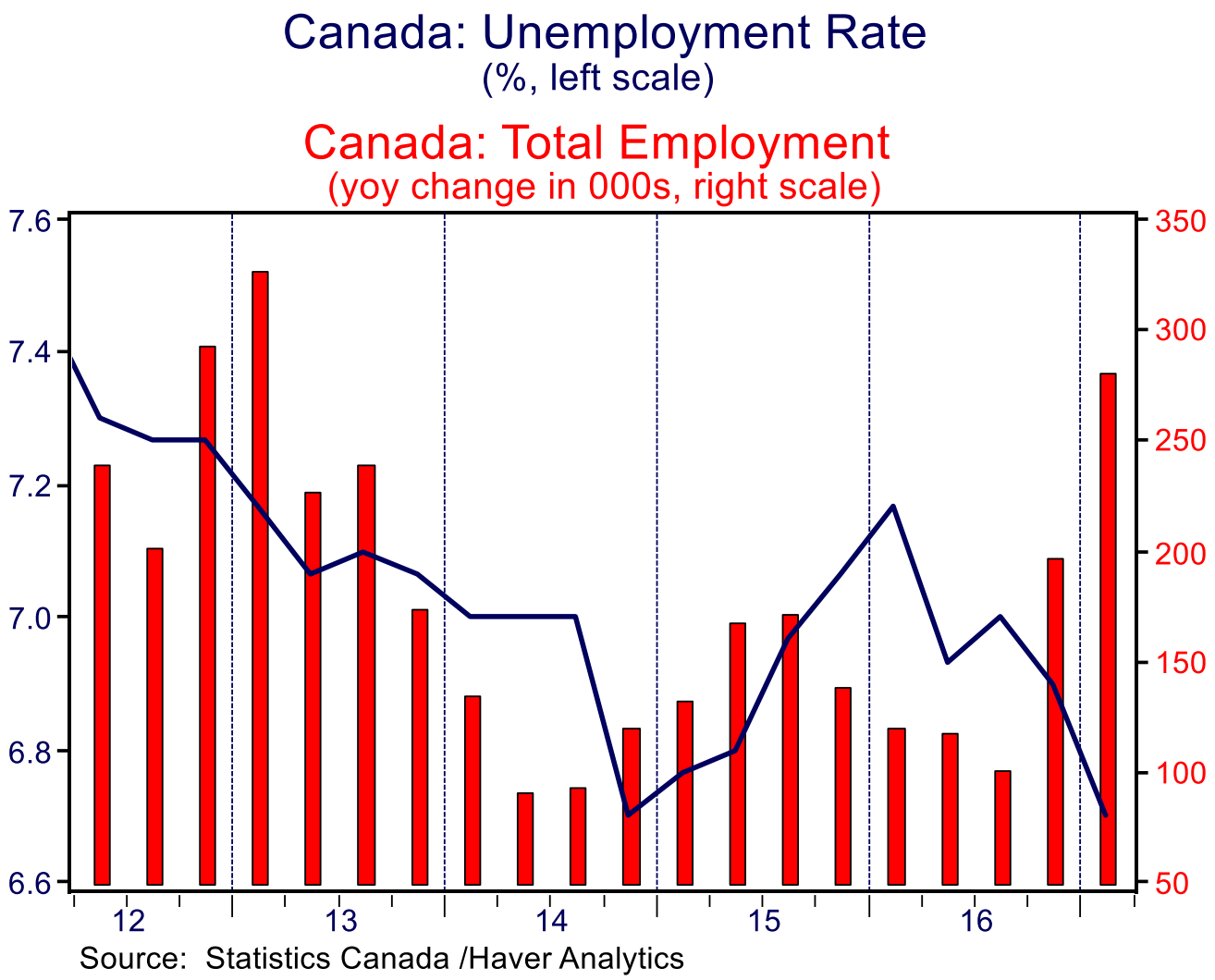
But growing dependence on household spending and debt

Infrastructure spending in Canada



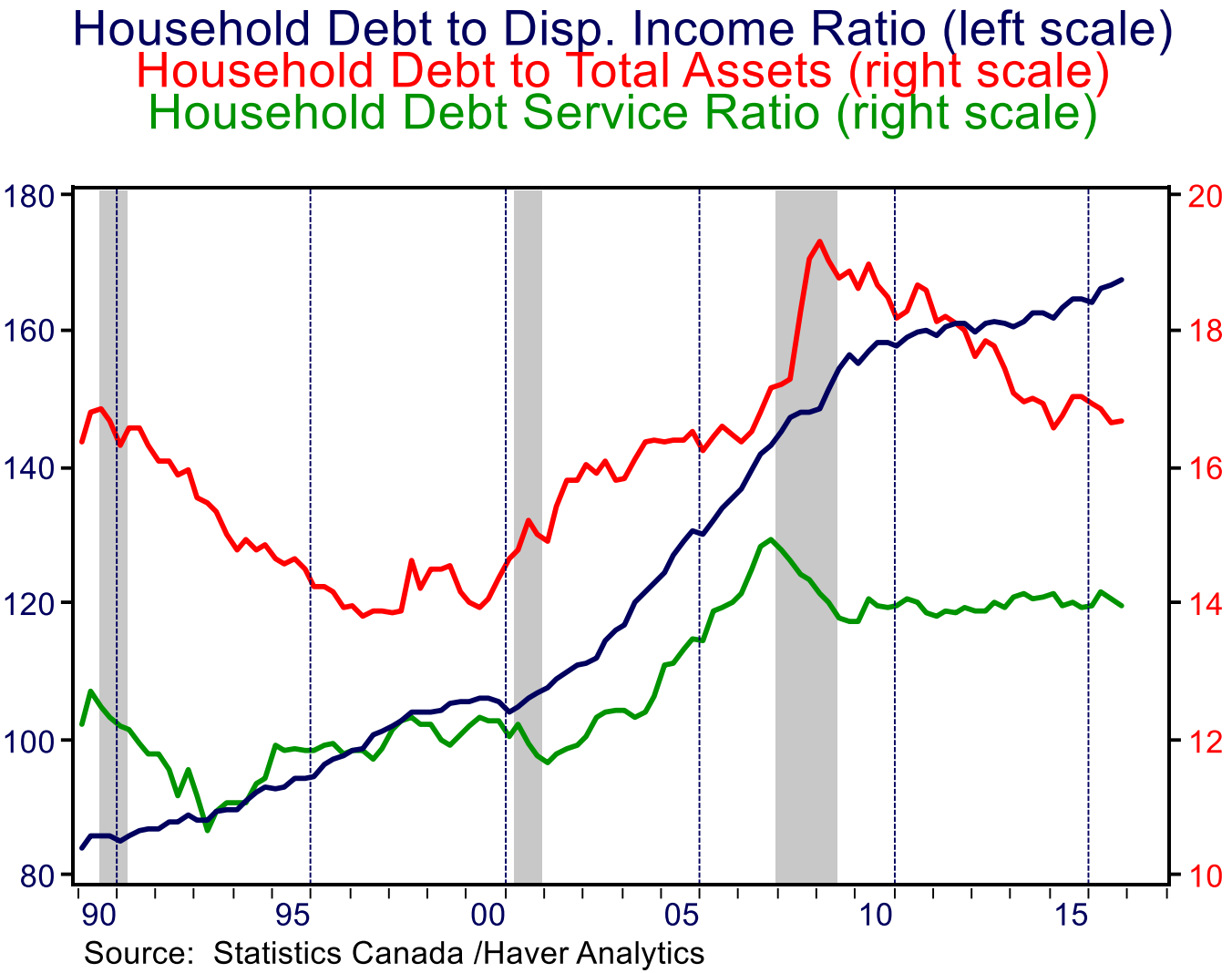
Labour market conditions supportive for credit demand

Unemployment back to pre-oil shock level due to the diversified economy



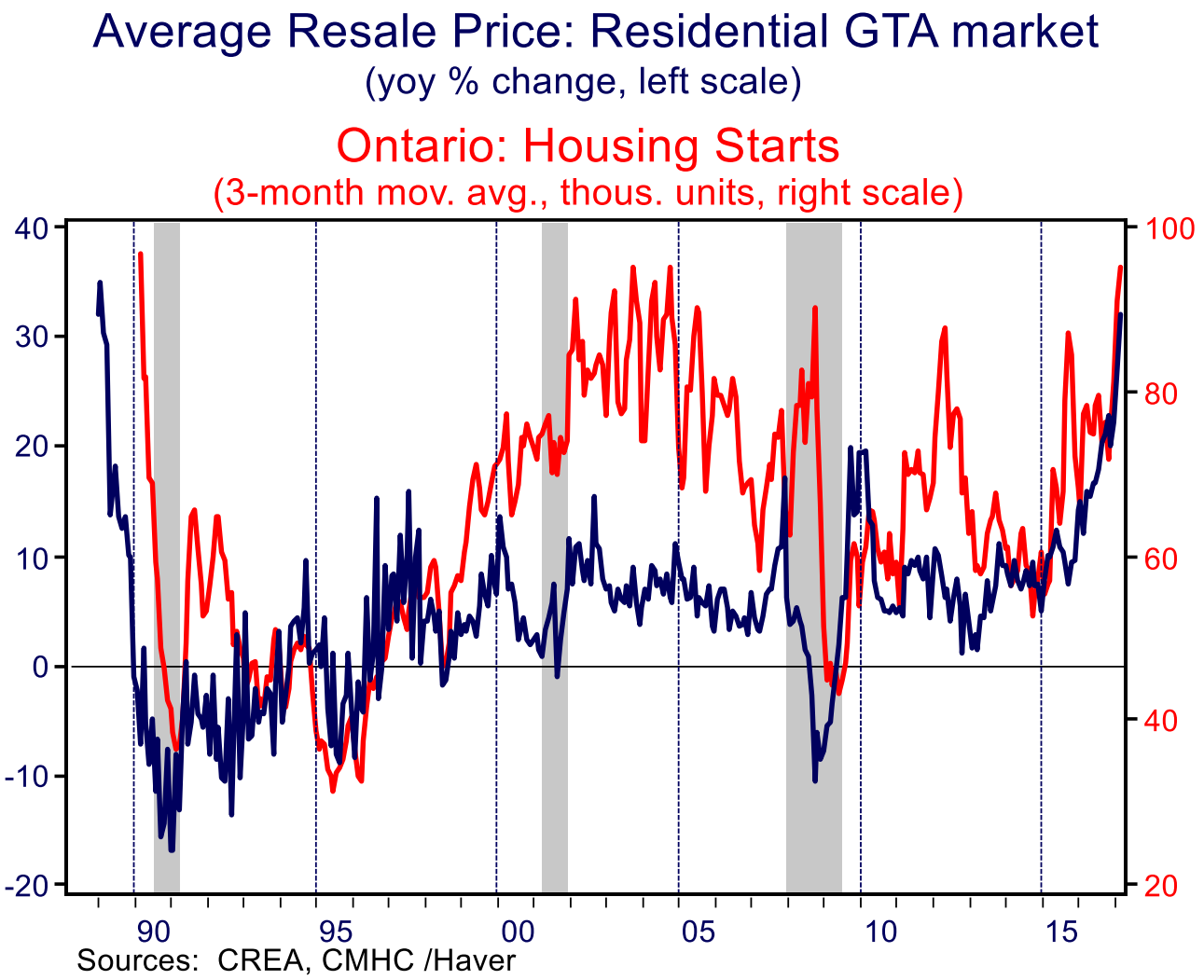
Improving household net wealth due to appreciation in equities and housing

Lower interest rates have maintained the DSR stable



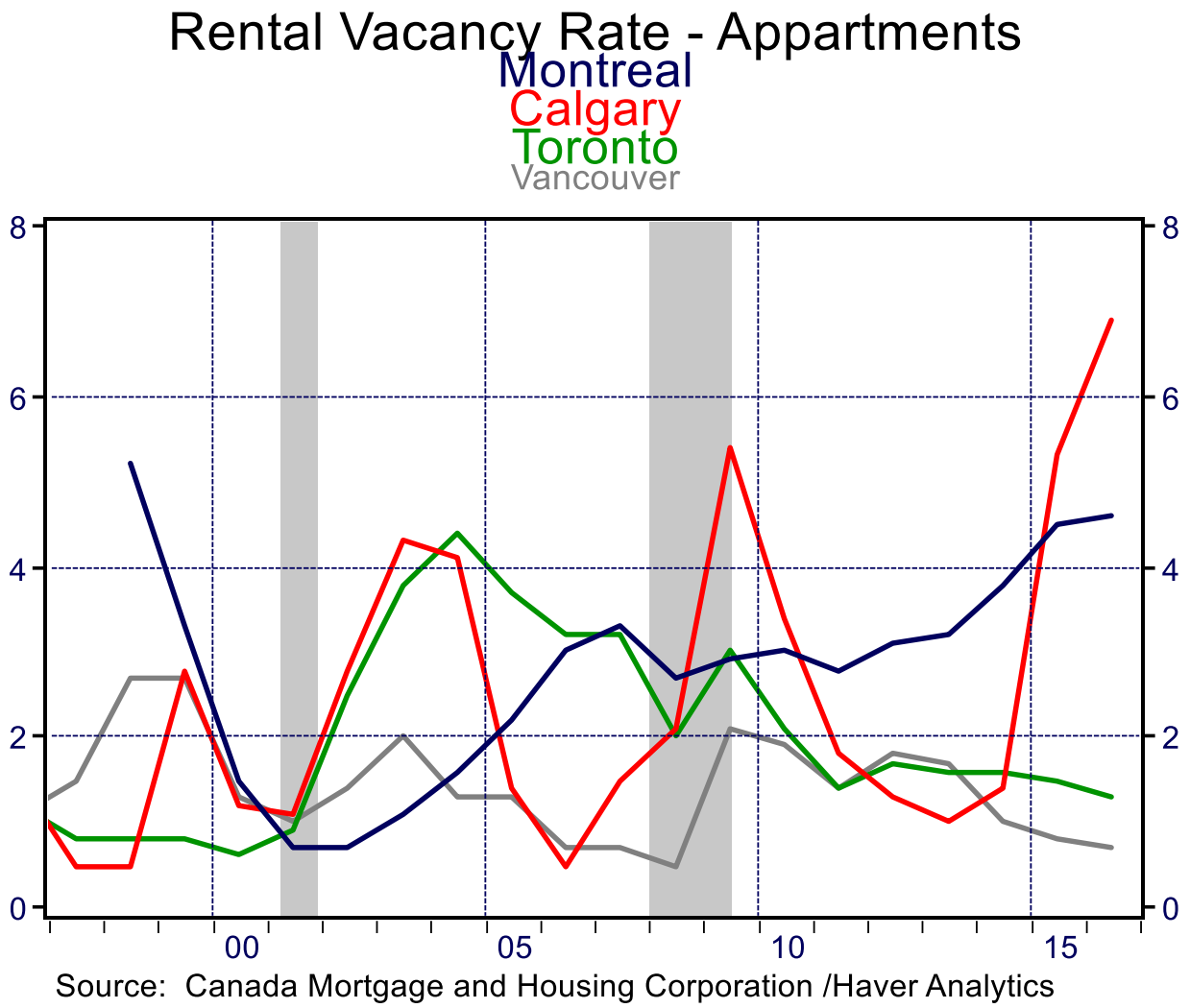
Further ajustments in the housing sector are necessary

New measures to cool down speculative activities necessary



Affordability issues, tighter mortgage rules

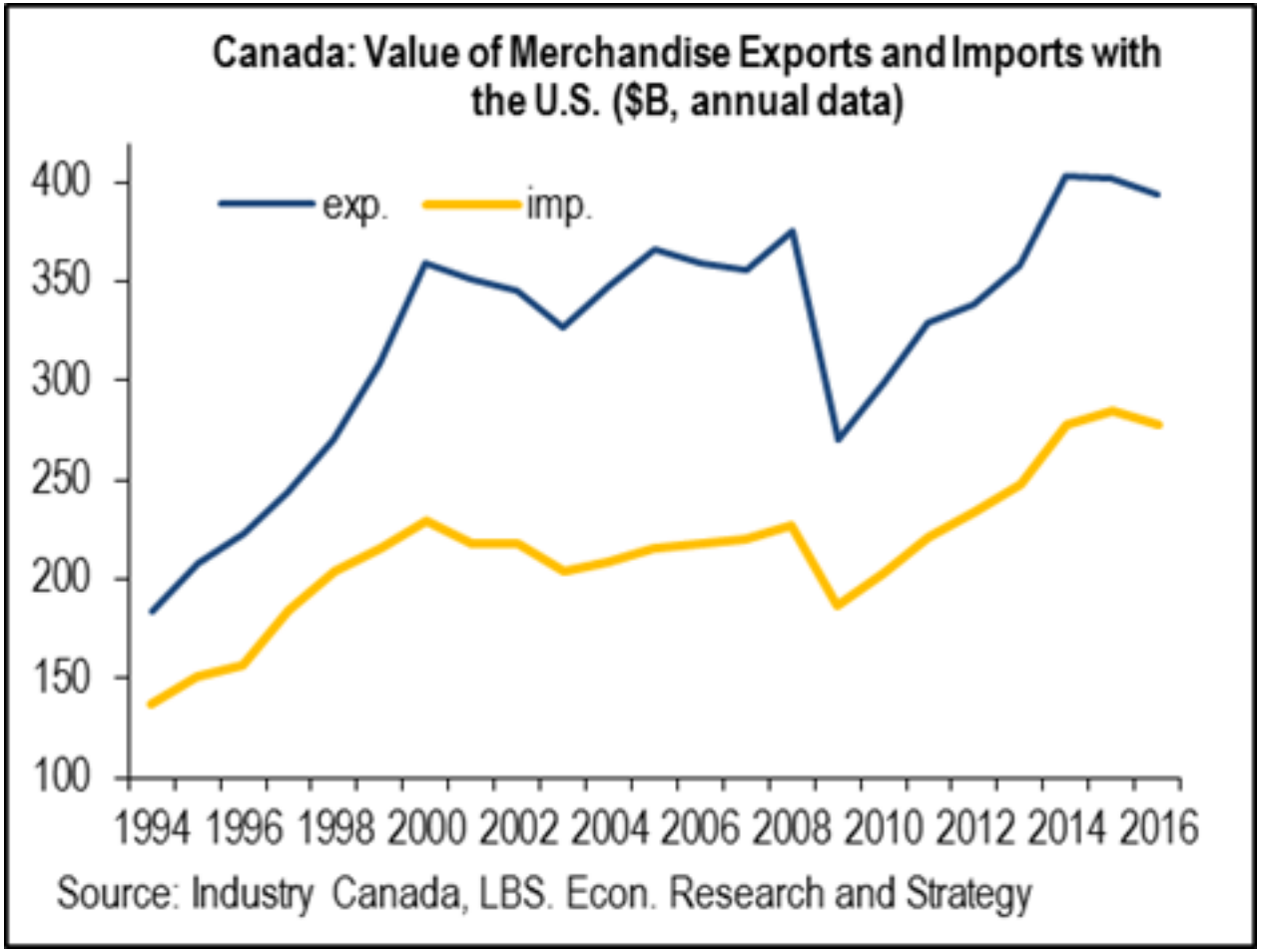
Improving the relative price of rental (REITs) vs. homeownership



Source: Canada Mortgage and Housing Corporation /Haver Analytics

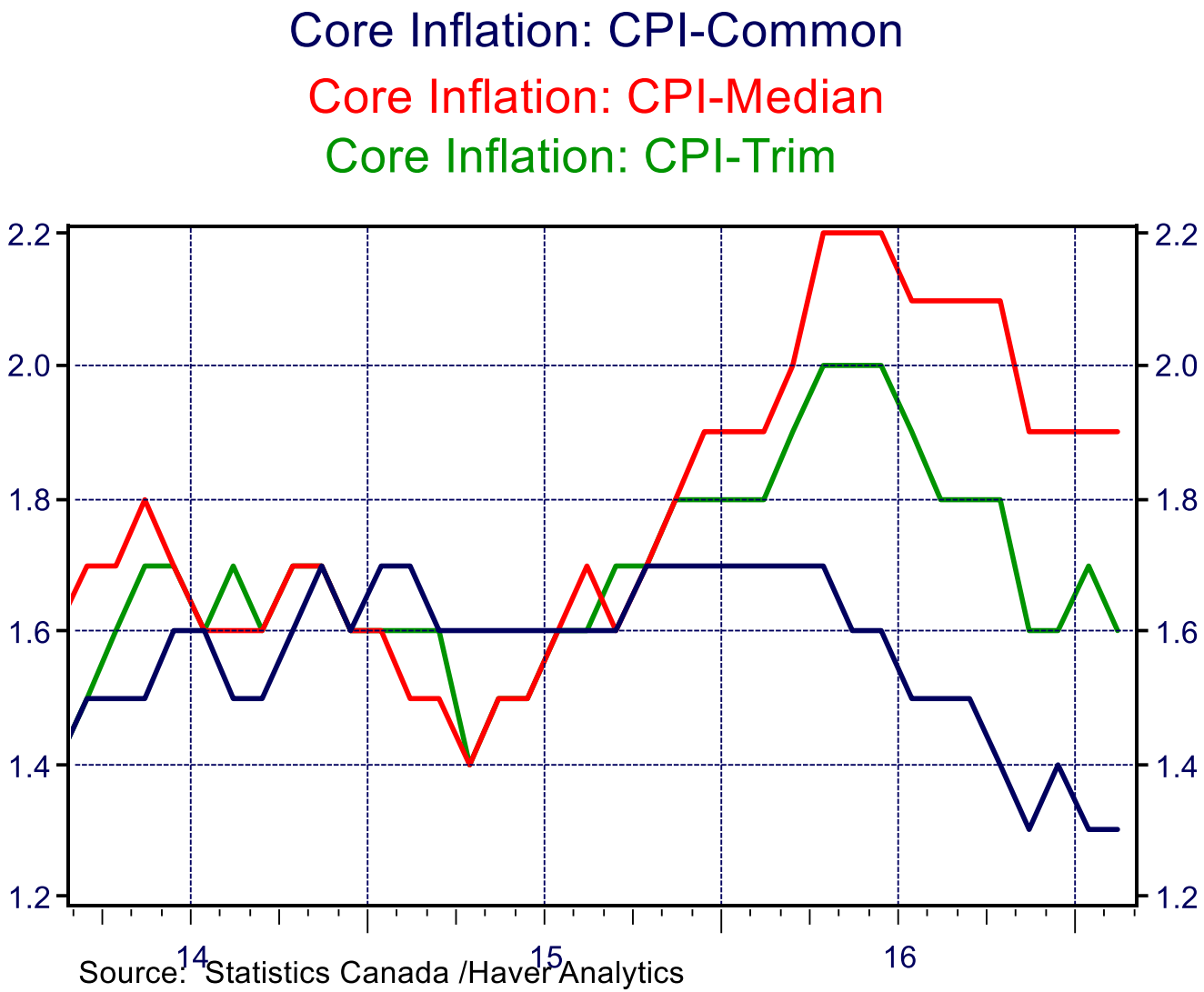
Canada: More vulnerable to U.S. trade protectionism than most countries

Considerable uncertainty for exports and business investment



BoC to keep its accomodative stance due to global risks to the outlook

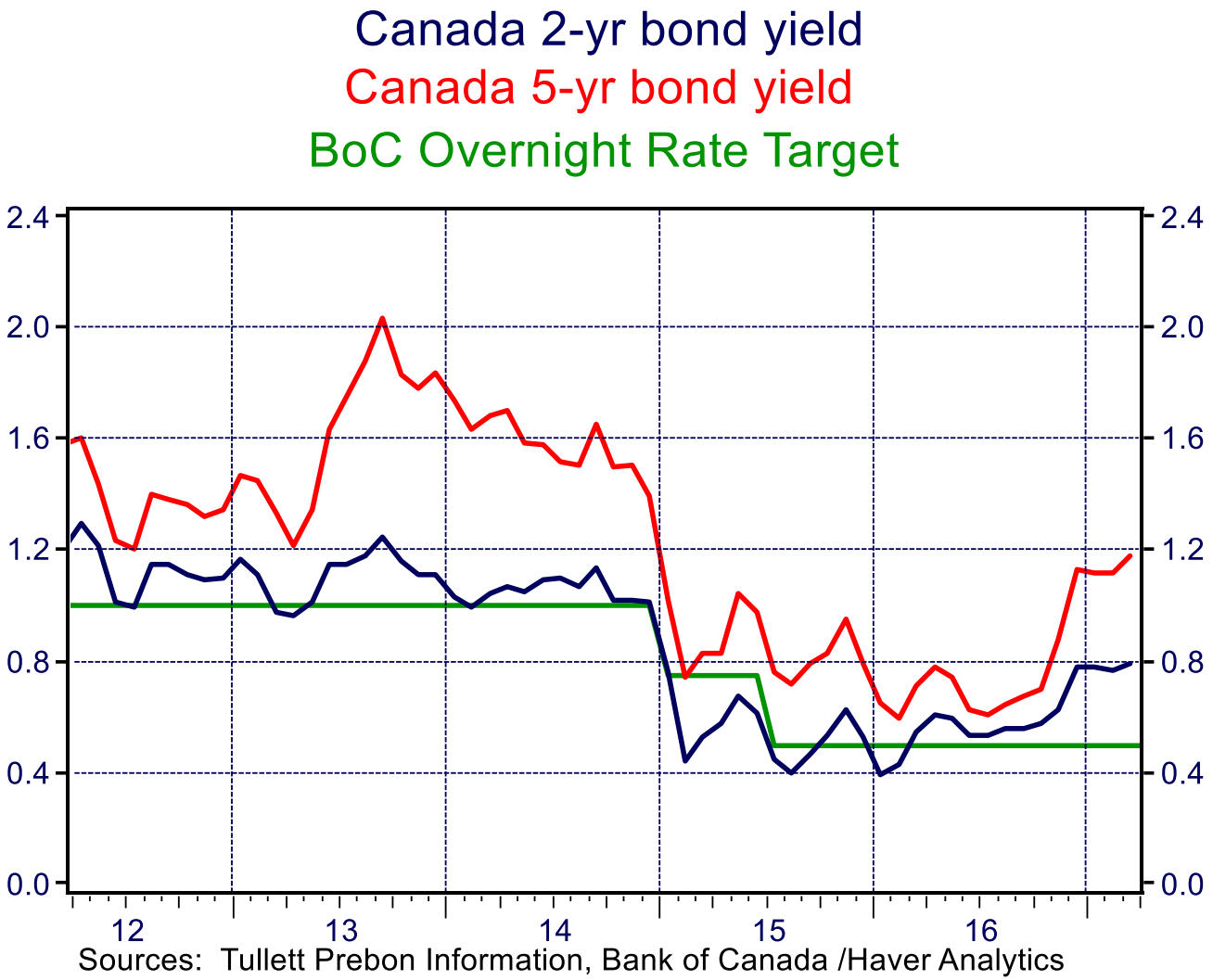
In contrast to the Fed, no upward pressures on core inflation measures



Source: Statistics Canada /Haver Analytics

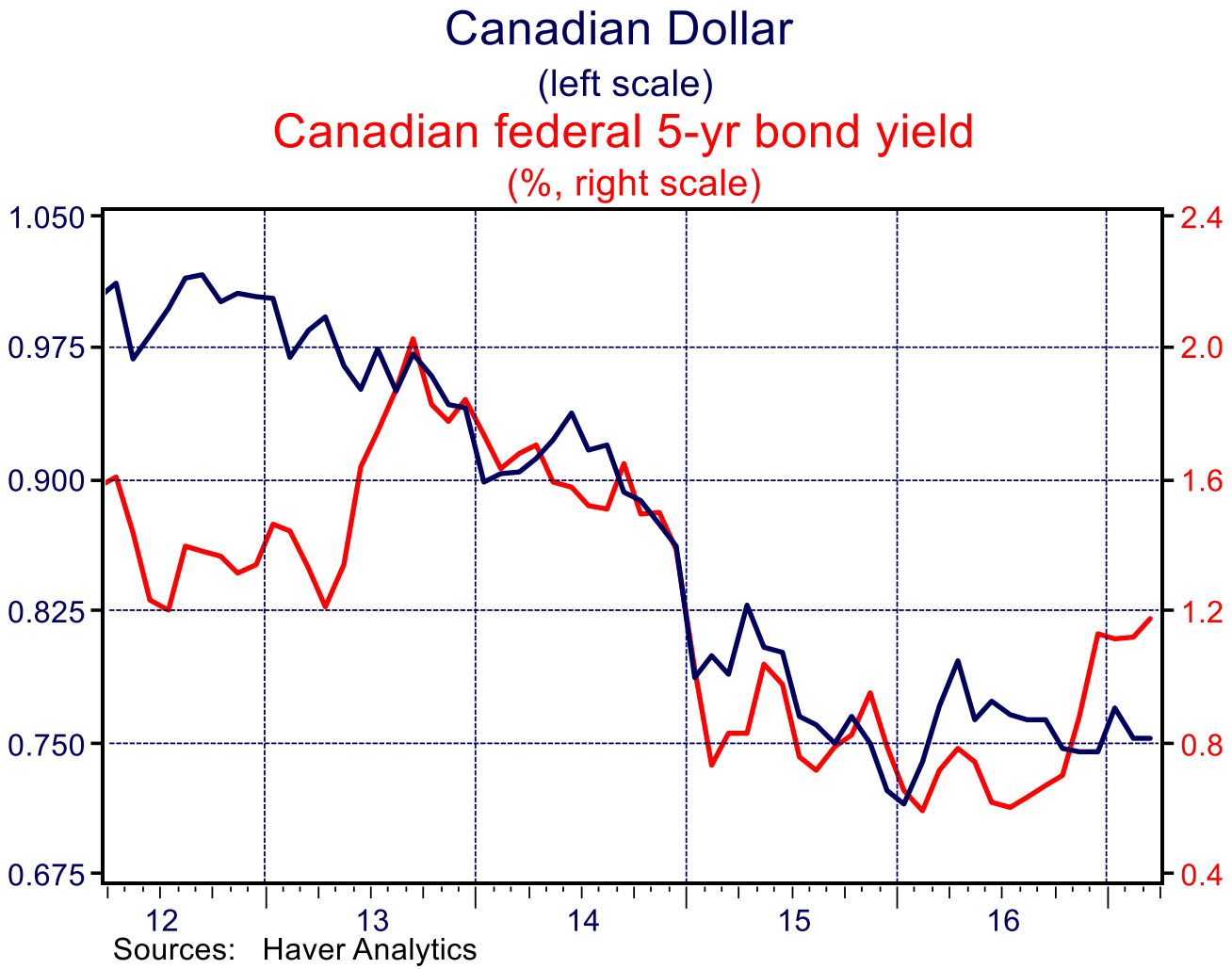
BoC to keep its accomodative stance

Canada is a price taker on the bond market



BoC to keep its accomodative stance

Tightening in financial conditions coming from the CAD as well



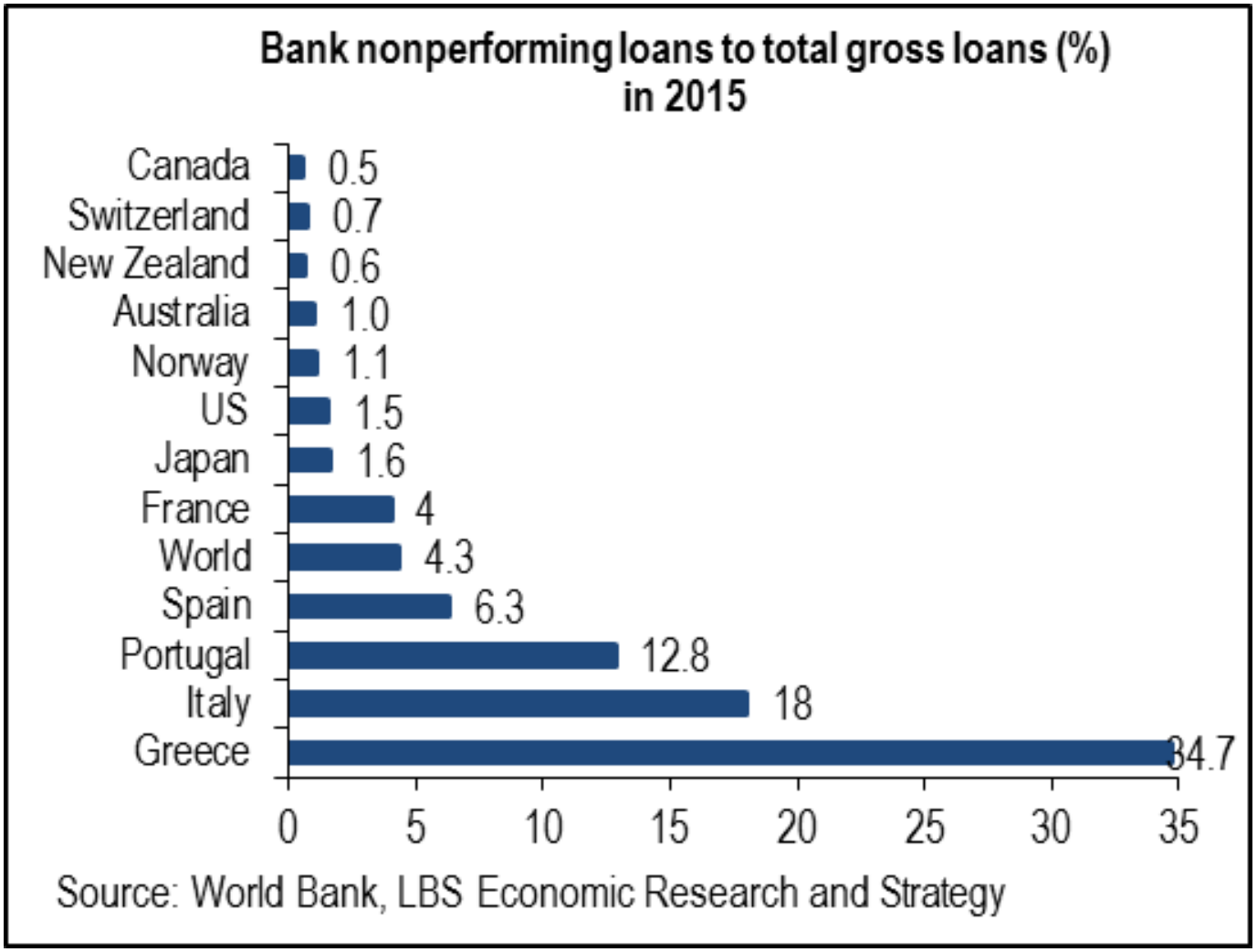
Financial Forecasts – Spring 2017

Financial Forecasts

	14Q4	15Q1	15Q2	15Q3	15Q4	16Q1	16Q2	16Q3	16Q4	17Q1	17Q2	17Q3	17Q4
Canada													
Overnight Rate Target	**1.00**	**0.75**	**0.75**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**
3-Month Treasury Bills	0.91	0.55	0.58	0.43	0.51	0.45	0.50	0.52	0.48	0.54	0.50	0.50	0.60
2-Year Bond	1.01	0.51	0.49	0.53	0.48	0.54	0.52	0.54	0.74	0.75	0.80	0.90	0.80
5-Year Bond	1.34	0.77	0.81	0.81	0.73	0.68	0.57	0.61	1.11	1.11	1.20	1.35	1.10
10-Year Bond	1.79	1.36	1.68	1.45	1.39	1.23	1.06	1.19	1.72	1.62	1.75	1.95	2.05
30-Year Bond	2.33	1.99	2.31	2.21	2.15	2.00	1.71	1.85	2.31	2.30	2.35	2.50	2.60
United States													
Federal Funds Rate Target*	**0.125**	**0.125**	**0.125**	**0.125**	**0.375**	**0.375**	**0.375**	**0.375**	**0.625**	**0.875**	**0.875**	**1.125**	**1.125**
3-Month Treasury Bills	0.04	0.03	0.01	0.00	0.16	0.21	0.22	0.33	0.61	0.74	0.85	1.00	1.15
2-Year Bond	0.67	0.56	0.64	0.64	1.06	0.76	0.59	0.76	1.18	1.25	1.40	1.65	1.80
5-Year Bond	1.65	1.37	1.63	1.37	1.76	1.21	1.00	1.24	1.93	1.93	2.10	2.30	2.40
10-Year Bond	2.17	1.94	2.35	2.06	2.27	1.78	1.46	1.59	2.44	2.39	2.55	2.80	2.85
30-Year Bond	2.75	2.54	3.11	2.87	3.01	2.61	2.28	2.31	3.07	3.01	3.10	3.35	3.45
Canadian Dollar (US$/C$)	**0.86**	**0.79**	**0.80**	**0.75**	**0.72**	**0.77**	**0.76**	**0.76**	**0.75**	**0.75**	**0.77**	**0.78**	**0.79**
S&P 500 Index	2059	2068	2063	1920	2044	2060	2099	2168	2239	---	---	---	2500
TSX Index	14632	14902	14553	13307	13010	13494	14064	14726	15288	---	---	---	16500
Oil WTI (US$/barrel)	53.5	47.7	59.5	45.1	37.0	38.3	48.3	48.2	53.7	50.7	59	63	67

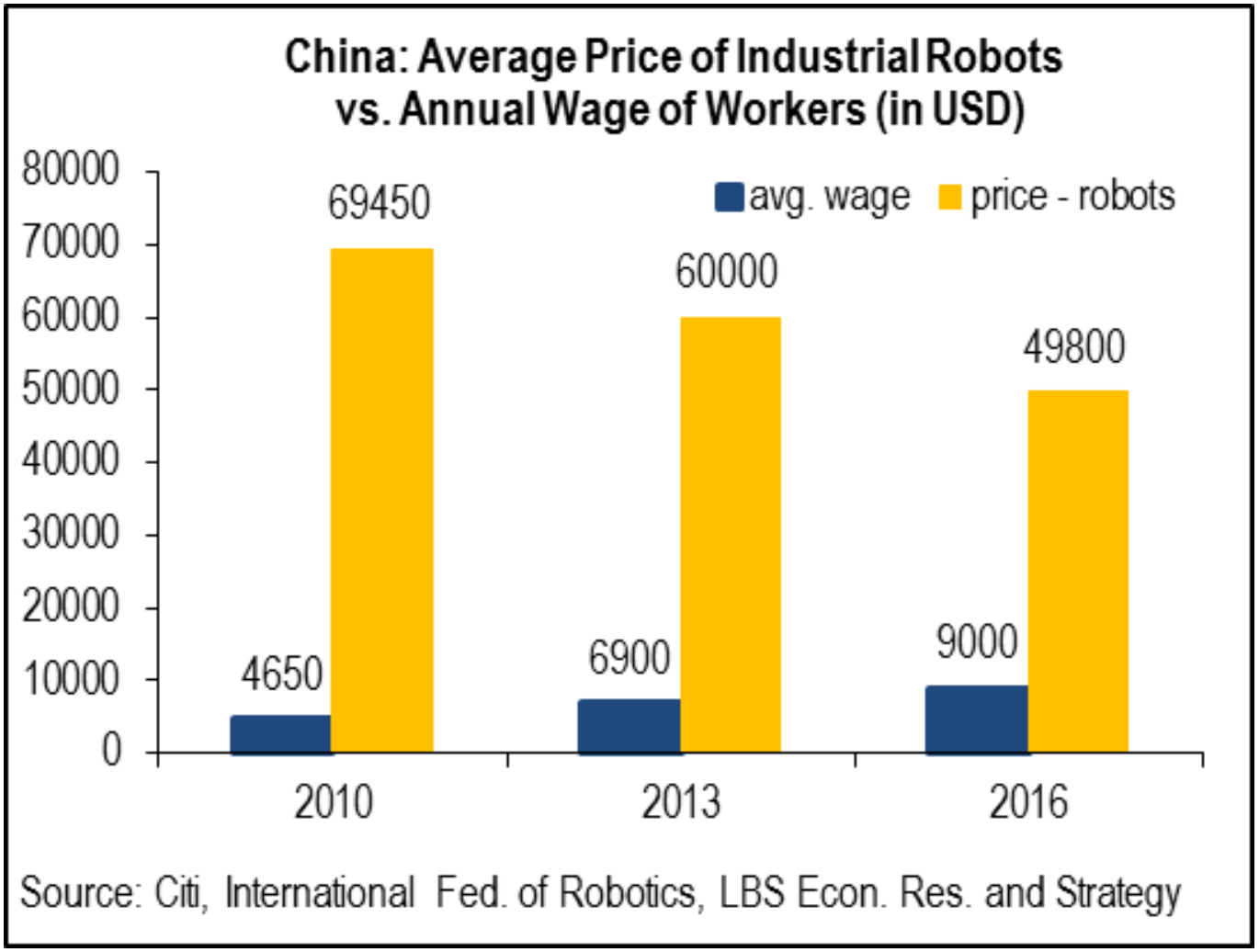
Europe: Beyond Brexit and elections

Vulnerable financial system



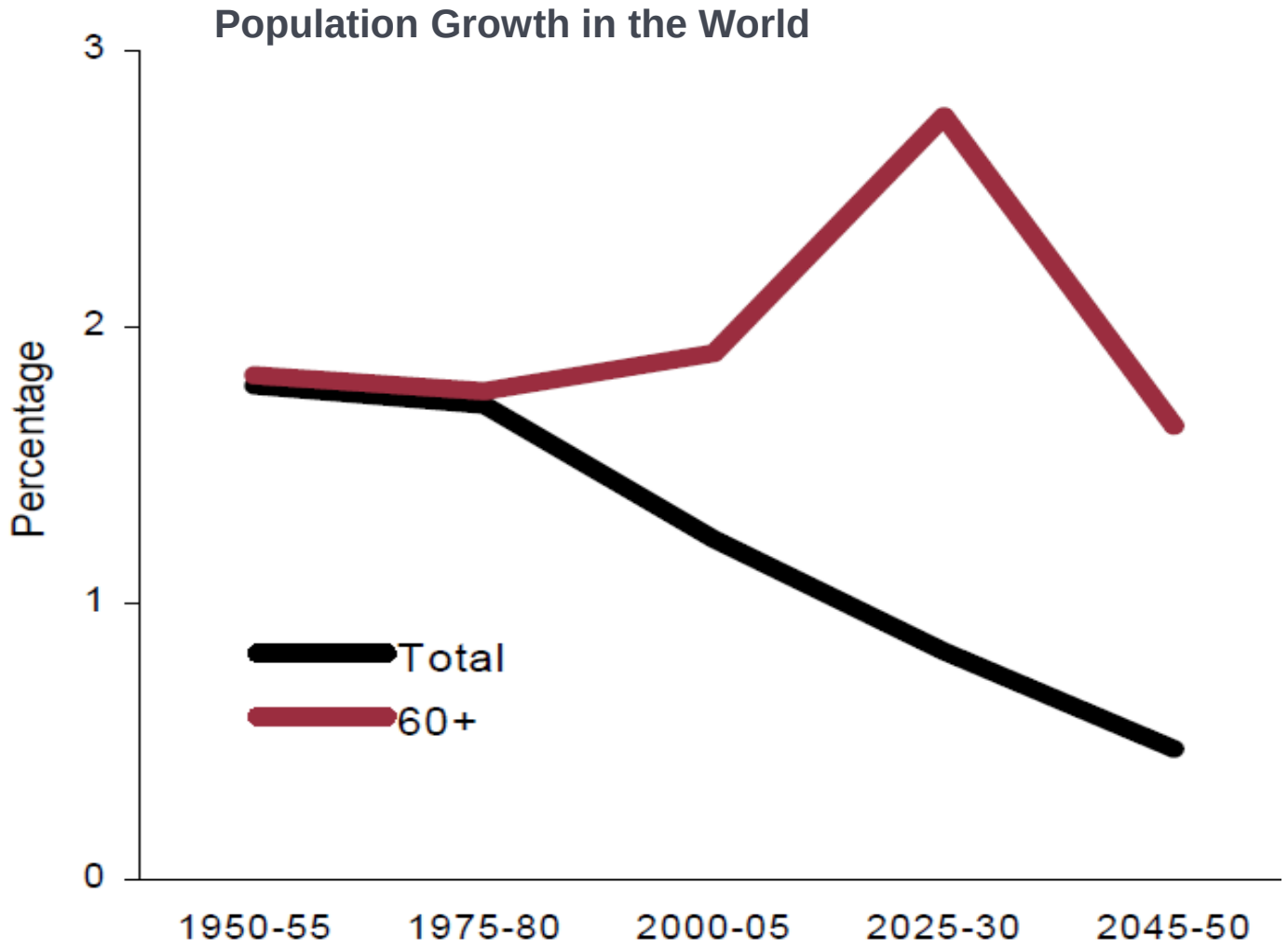
After the globalisation era, the emergence of robotisation

A new source of productivity gains for companies



The Silver Economy: 2 billion persons aged 60 yrs+ in 2050

Baby Boomers: Wealthy; Younger generation: student and housing debt



Source: United Nations

The world grew since 1960

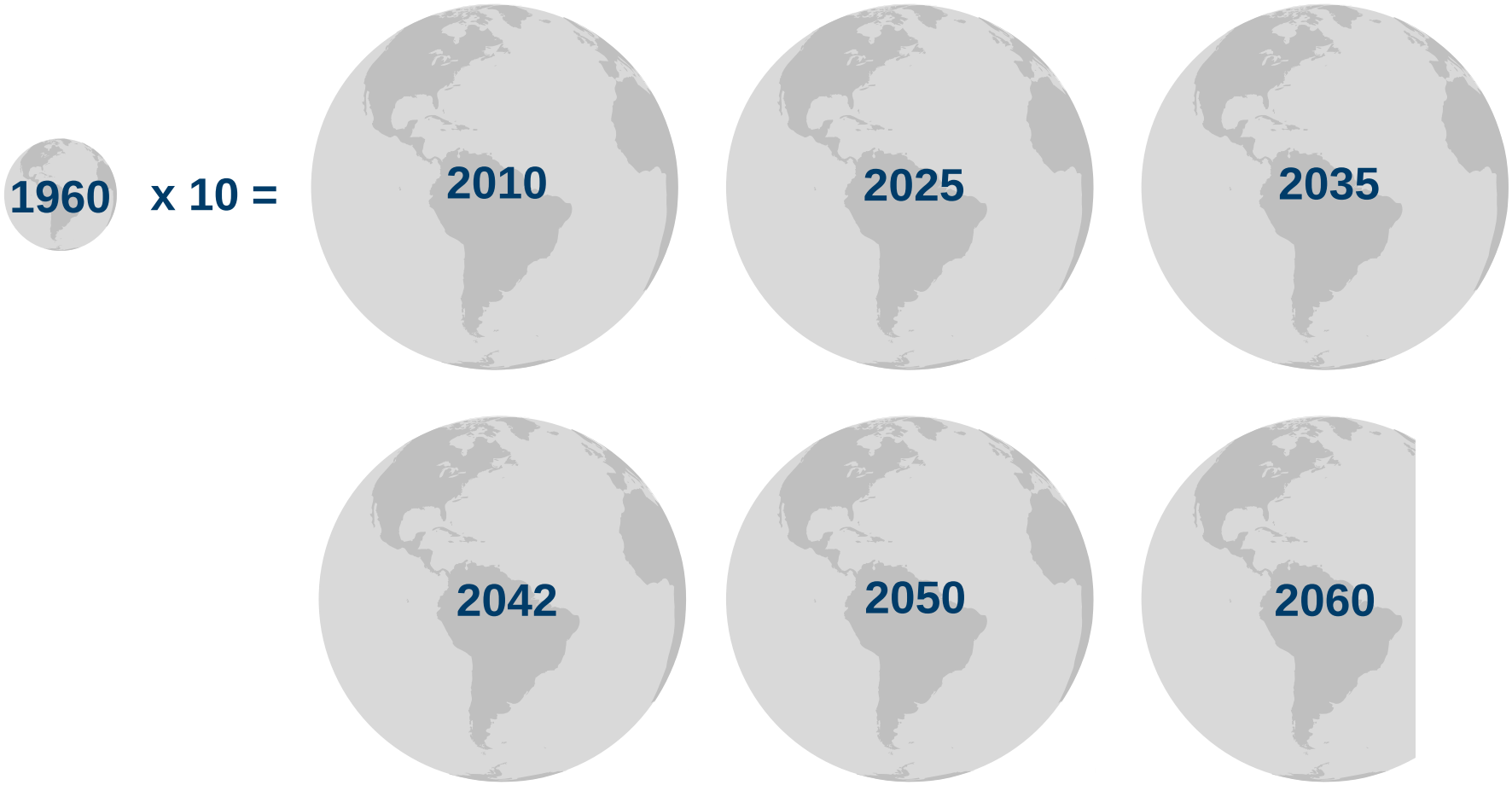
Global GDP is now 8 times what it was in 1960

This is not the moon

The relative size of the planet in 1960

Realistically assuming 3.5% global real GDP growth

We will need more than 5 planets …

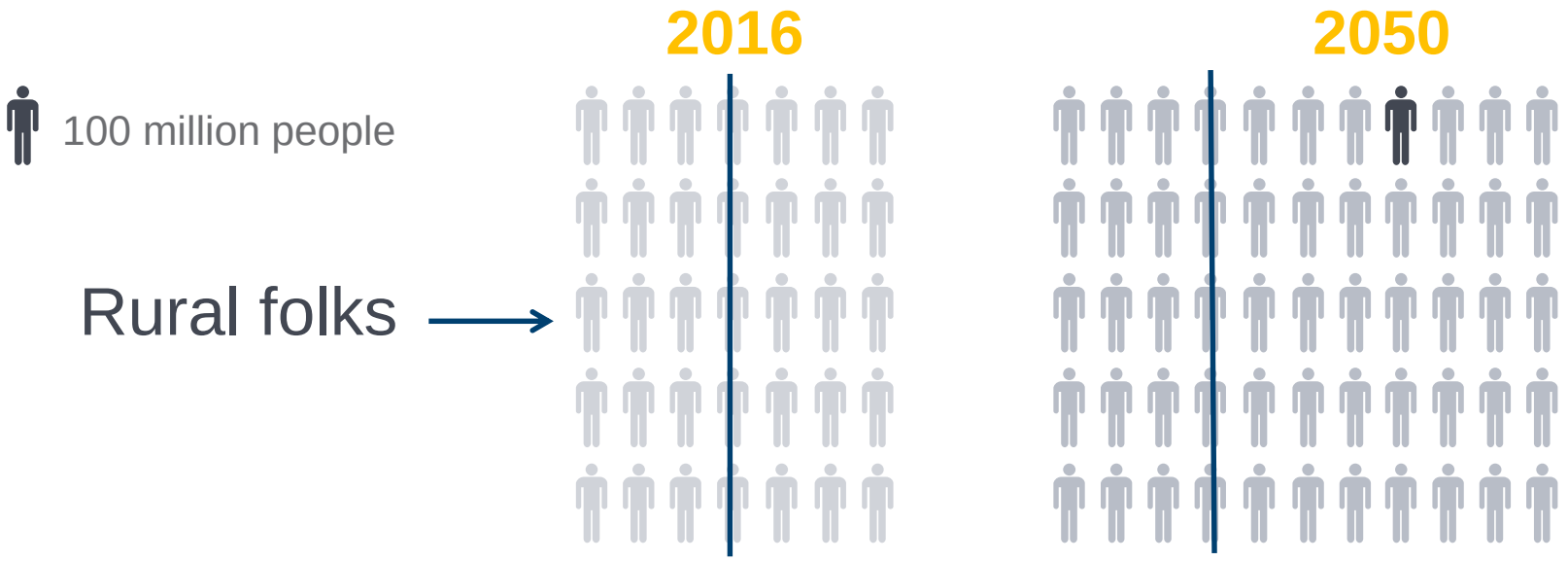


… by **2060**

Source: LBS estimates

Urban population growth

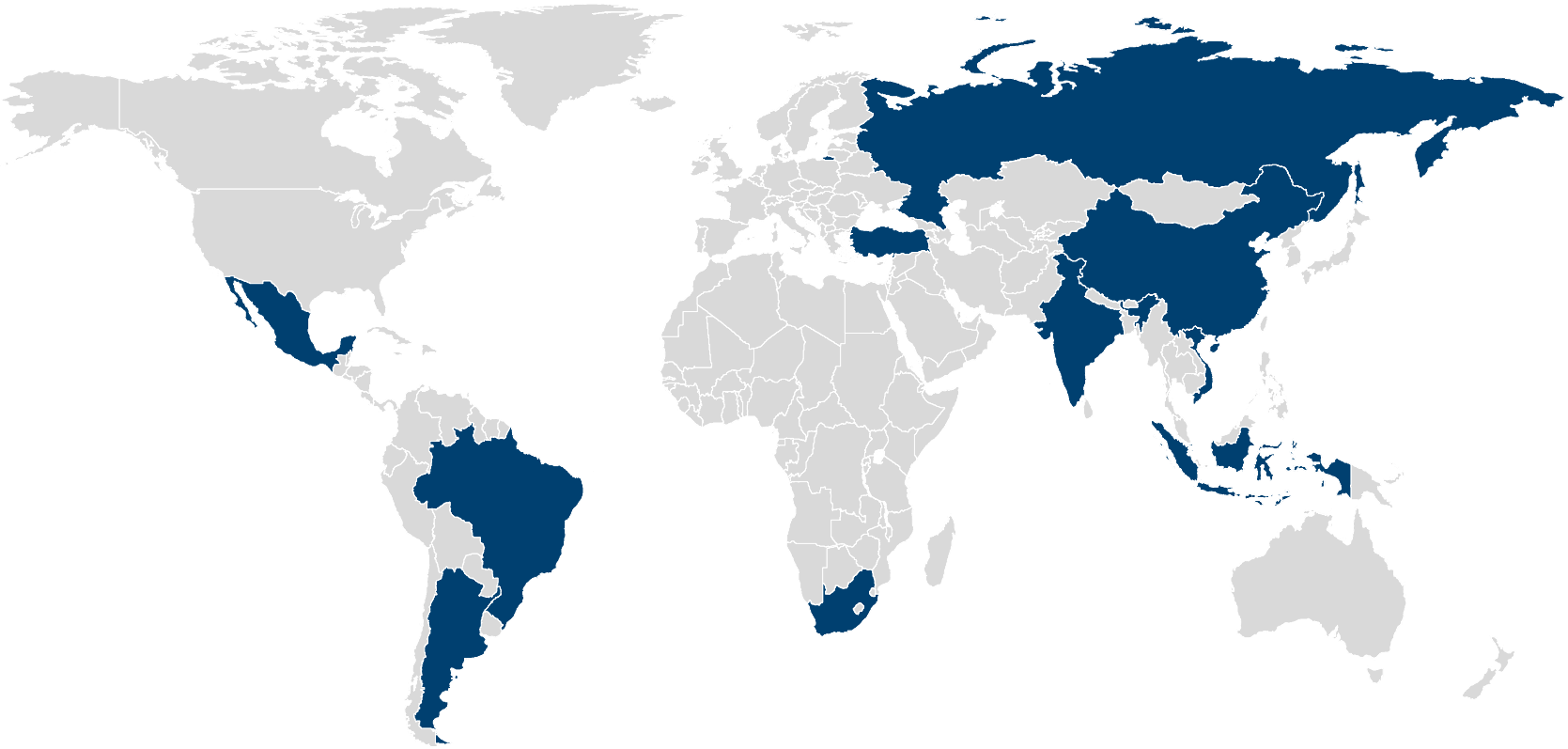
From **3.5 today** to **7.0 billion** in 2050



While rural population will be stable at **3.5 billion**, **100 million** new urban dwellers every year for next 35 years

Where will most this growth take place?

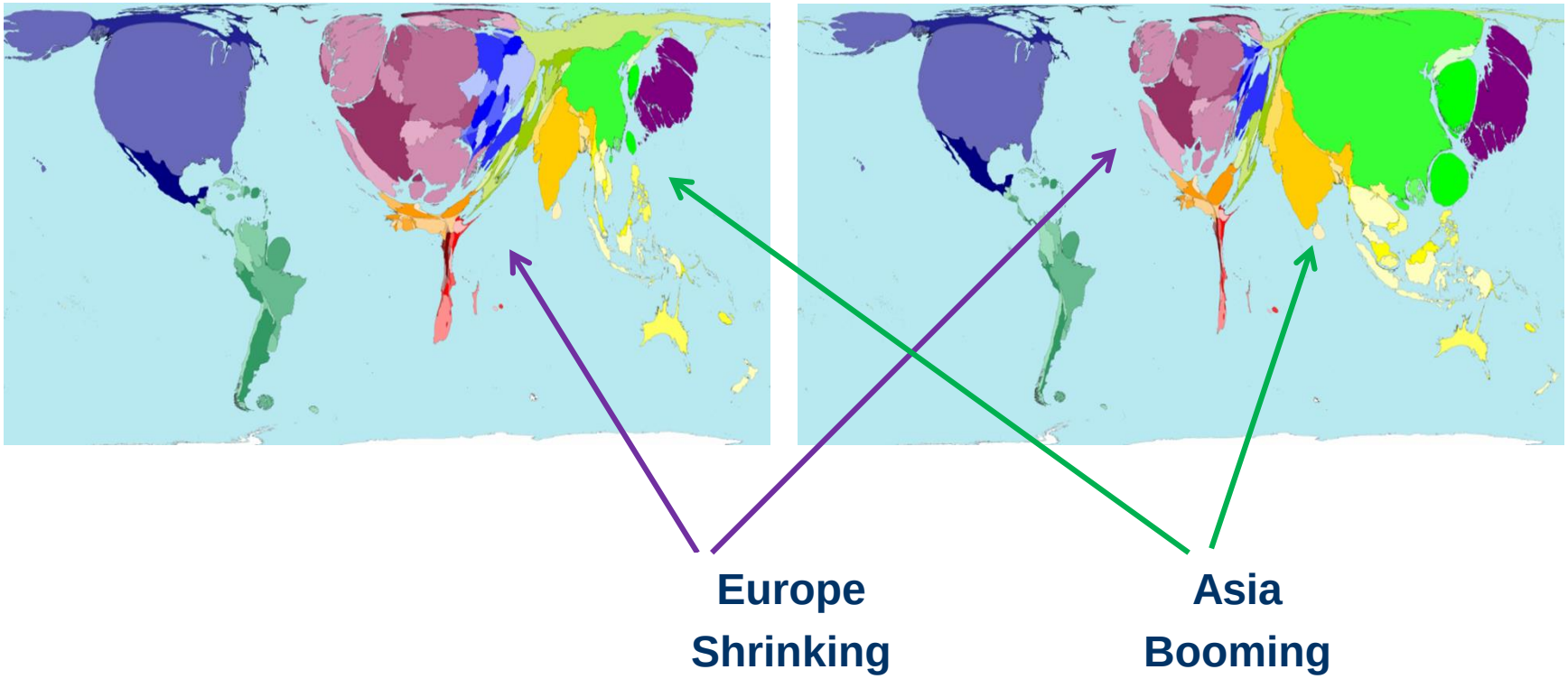
In Emerging Markets



Multi-polar world ahead

The Economic World

1960 vs. 2010



Europe
Shrinking

Asia
Booming

Source : *www.worldmapper.org*

Thank you
Questions?