

# Investment Strategy

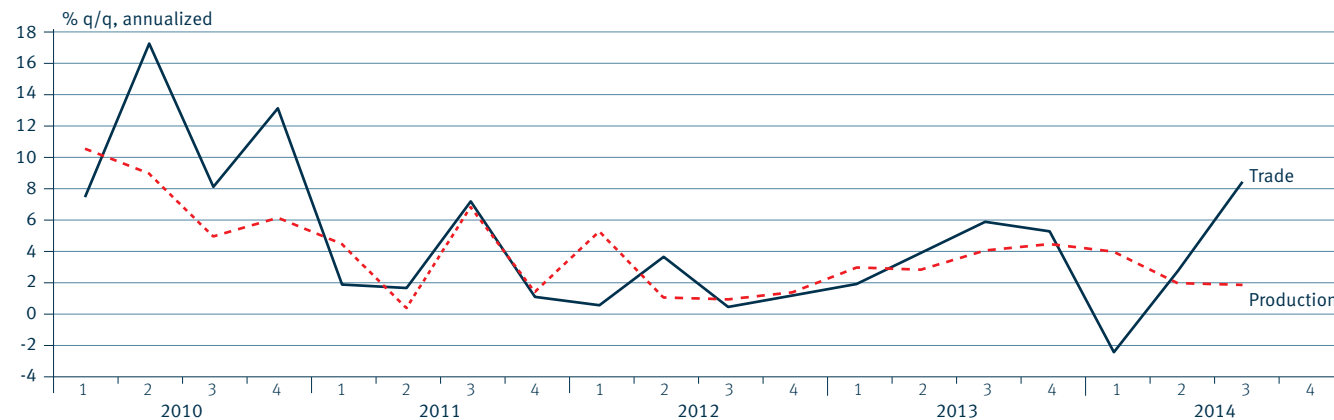
## Global Economy

Despite uncertainty about the outlook for regions such as the euro zone and Japan, the global economy continues to expand. Global trade volume jumped 2% in September, and for the third quarter as a whole was up 8.4% annualized, the best quarterly showing in four years. If the slide of oil prices is bad news for crude-exporting countries (especially those with fixed exchange rates), it is a boon to the world as a whole. First, it will help rebalance the global economy by improving the current accounts of oil-importing countries, which are often in deficit, at the expense of big oil exporters, which usually run large

surpluses. More important, lower oil prices constitute an oxygen pump for the global economy. The biggest beneficiaries will be large importers like China and India, where oil accounts for up to a third or more of imports. In short, there are grounds for concern about the world economy but the positives should not be underestimated. A resurgent U.S. will lead the advanced economies and emerging economies like India's will gain lift from improved demand, U.S.-dollar appreciation and lower energy costs. We foresee a slight acceleration of world GDP growth next year, to 3.6%.

### World: Trade flows rebound

Volume trade flows and industrial production



NBF Economics and Strategy (data via CPB)

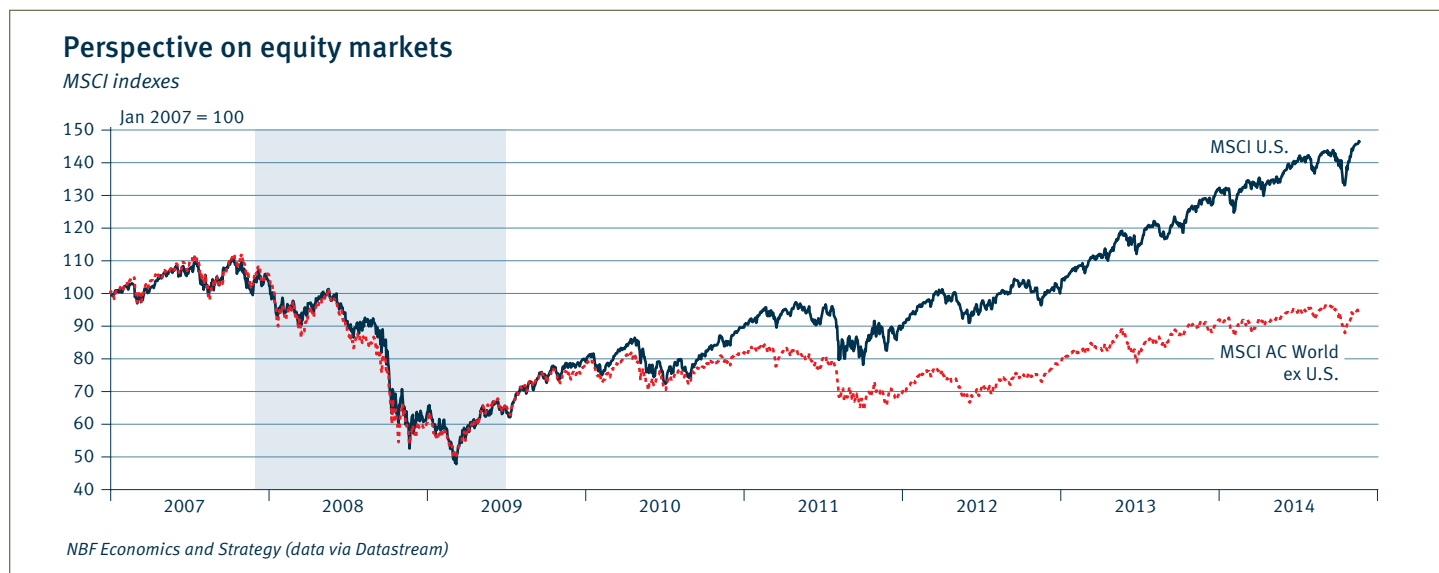
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## Financial Markets

Global equity markets have once more avoided a correction (decline of more than 10%). In the recent turbulence, the maximum pullback of the MSCI All-Country World index was 8.3%. Since then, the index has regained all the lost ground and gone on to new all-time highs. Despite geopolitical uncertainty, the odds continue to favour

economic expansion in the coming quarters. Credit market spreads (for high-yield bonds and emerging-country debt) remain narrow, and low inflation is prompting a number of central banks to increase liquidity in order to maintain an environment of very low interest rates.



## Investment Strategy

Despite a multitude of risks ranging from the war against the Islamic State, protests in Hong Kong, the propagation of the Ebola disease and fears of an economic slowdown in Europe, global stock markets managed to limit the damage in the fourth quarter, even if the U.S. Federal Reserve (the “Fed”) decided to end its bond purchasing program. It must be said that the U.S. economy continues to show remarkable resilience, with growth of over 4% on average over the last two quarters. It must also be said that for the first time since the great recession of 2008, the European Central Bank (ECB) and the Bank of Japan finally seem determined to take over and plan to significantly boost their respective balance sheets. The People’s Bank of China has also joined in with an unexpected drop in key interest rates. This massive injection of capital from central banks has enabled major stock markets around the world to rebound strongly and end the year at record levels. In this environment of uncertainty, government bonds remained popular, German and French reference rates even falling below 1%. However, the real safe haven proved to be the U.S. dollar, which appreciated against all currencies, pushing commodity prices down at the same time. Of them all, the price of crude oil was the most affected, an imbalance between supply and demand pushing it down more than 30%.

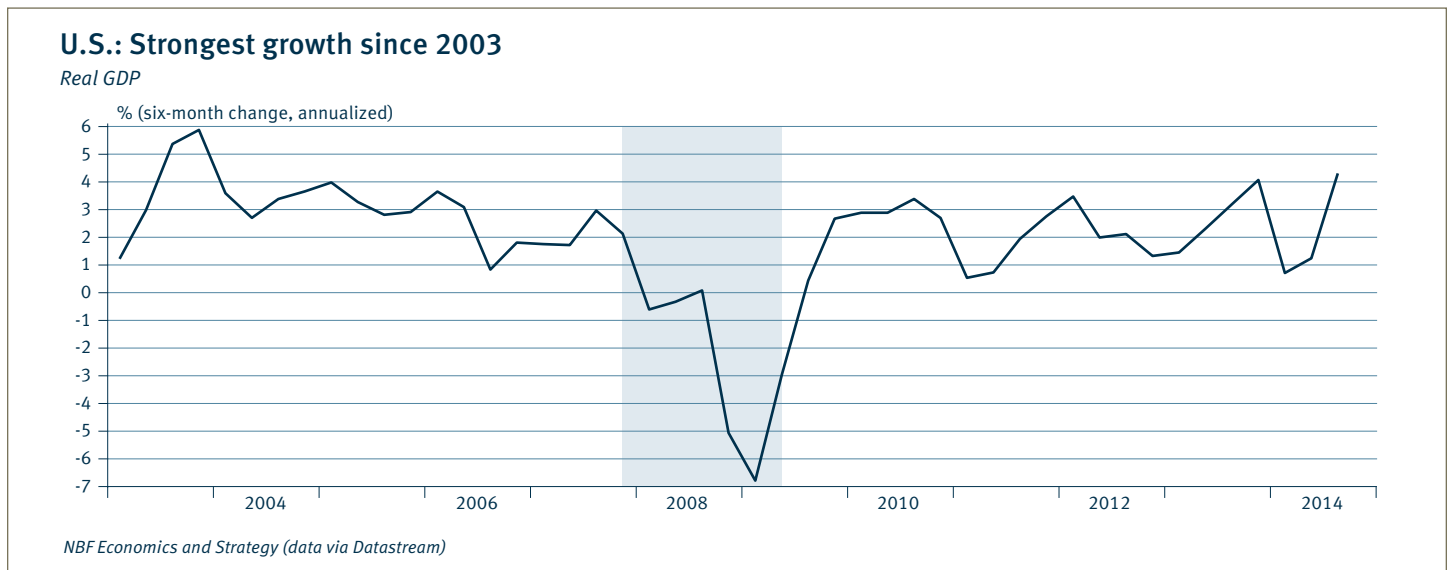
To start 2015, we continue to focus on excess liquidity and ongoing improvements in economic activity in the United States. Certainly, the European slowdown is worrying and the arising deflation risks are as well. However, the latest statistics indicate that fears of a triple-dip recession in Europe may be exaggerated. Furthermore, stabilizing effects, such as the sharp drop in gasoline prices in the United States and the impact of stimulus measures in China on other emerging countries should help the U.S. economy to maintain its composure. Under these conditions, we continue to recommend an overweight position in the stock markets for all risk profiles.

As for fixed income, interest rates should remain low in an environment where inflation is virtually absent. However, the negative effect of the drop in oil prices on inflation could rapidly reverse in the event of an increase in demand. Therefore, at current levels, expected returns on bonds are unattractive. In the short term, North American yields will remain depressed because of the downward pressure exerted by the European rates. However, in the context in which the improvement in the U.S. economy will force the Federal Reserve to gradually tighten monetary policy, the balance of risks seems skewed towards an increase in interest rates.

## United States

After a calamitous first quarter, the U.S. economy picked up strongly in the second and third. Real growth rebounded to 4.6% annualized in Q2 and held at 3.9% in Q3 – the best six-month showing since 2003. The third quarter ended with industrial production at an all-time high, about 4% above the pre-recession peak. Domestic demand seems well positioned for the months ahead and consumer confidence is the highest in years, buoyed by a strengthening labour market and the decline of gasoline prices. Moreover, investment is also on the rise, fuelled by a stronger growth outlook, and trade continues to add to GDP growth. Though the expansion can be expected to cool in the

months ahead, that development will be neither surprising nor worrisome after the performance of the last several months. The longer-term U.S. prospect remains upbeat. We are staying with our forecast of 2.9% GDP growth in 2015 – provided, however, that Congress does not once again throw sand in the gears by sowing uncertainty, let alone by shutting down the government as it did last year. The risk of such moves was increased by the Republican capture of the Senate as well as the House of Representatives in the November elections.



## Canada

The Canadian economy beat expectations for a second straight quarter in Q3, expanding at an annual rate of 2.9%. Domestic demand was again solid, with contributions to growth from all the main components and notably from business investment, which has finally rebounded after a long period of disappointing sluggishness. Though the savings rate was unchanged, consumption was well supported by growth of disposable incomes. Trade again contributed to growth, fuelled no doubt by resurgent U.S. demand. That said, the Canadian economy can be expected to decelerate somewhat over the months

ahead. The fall of crude oil prices is bad news for Canada as a whole, since if it persists, the consequences will be felt beyond the oil patch. However, the effect on oil producers has been softened to some extent by depreciation of the loonie. In short, the slump in the price of oil is manageable for the moment. Moreover, Ottawa recently announced that its anticipated surpluses will be used to stimulate the economy in 2015. Under these conditions, we remain confident of our forecast that Canadian GDP growth will accelerate to 2.5% in 2015.

Income Portfolio	Asset Class	Minimum/Maximum	Benchmark	Recommended Weighting	Change from Previous Quarter
<b>Investor Profile:</b> You want to preserve your capital or establish a source of periodic income to finance ongoing expenses. You do not find the stock market very attractive because of its volatility, but you are not against the idea of investing a small part of your portfolio in stocks, mainly to counteract the effects of inflation. Your tolerance for risk is low.	Cash equivalents	0% to 20%	5.0%	3.0%	0.0%
	Fixed-income (duration: 5 years) <sup>1</sup>	60% to 100%	70.0%	66.0%	0.0%
	Canadian equities	0% to 30%	7.5%	8.5%	-0.5%
	US equities		7.5%	11.5%	0.0%
	Foreign equities		5.0%	6.0%	0.5%
	Alternative investments <sup>2</sup>	0% to 10%	5.0%	5.0%	0.0%
<b>Conservative Portfolio</b>					
<b>Investor Profile:</b> On the whole, you want your portfolio invested in fixed-income securities. Although you can tolerate limited volatility to ensure that your assets will grow, you prefer having a portfolio consisting mainly of fixed-income investments for reasons of stability. Your tolerance for risk is low.	Cash equivalents	0% to 15%	5.0%	3.0%	0.0%
	Fixed-income (duration: 5 years) <sup>1</sup>	45% to 80%	55.0%	51.0%	0.0%
	Canadian equities	20% to 45%	14.0%	15.5%	-0.5%
	US equities		14.0%	17.5%	0.0%
	Foreign equities		7.0%	8.0%	0.5%
	Alternative investments <sup>2</sup>	0% to 10%	5.0%	5.0%	0.0%
<b>Balanced Portfolio</b>					
<b>Investor Profile:</b> You give equal weight to income and capital growth. You can tolerate moderate volatility to ensure the growth of your capital, but you prefer having a portfolio with a significant exposure to fixed-income securities for reasons of stability. Your tolerance for risk is average.	Cash equivalents	0% to 20%	5.0%	1.0%	0.0%
	Fixed-income (duration: 5 years) <sup>1</sup>	30% to 65%	40.0%	36.0%	0.0%
	Canadian equities	30% to 65%	17.5%	19.0%	-0.5%
	US equities		17.5%	22.5%	0.0%
	Foreign equities		10.0%	11.5%	0.5%
	Alternative investments <sup>2</sup>	0% to 20%	10.0%	10.0%	0.0%
<b>Growth Portfolio</b>					
<b>Investor Profile:</b> Your main goal is capital growth. Although you can tolerate greater volatility in order to increase the value of your assets, you are not prepared to invest your entire portfolio in stocks. Your tolerance for risk is high.	Cash equivalents	0% to 25%	0.0%	0.0%	0.0%
	Fixed-income (duration: 5 years) <sup>1</sup>	25% to 45%	35.0%	28.0%	-0.5%
	Canadian equities	40% to 75%	20.0%	21.0%	0.0%
	US equities		20.0%	25.0%	0.0%
	Foreign equities		15.0%	16.0%	0.5%
	Alternative investments <sup>2</sup>	0% to 25%	10.0%	10.0%	0.0%
<b>Maximum Growth Portfolio</b>					
<b>Investor Profile:</b> You want to maximize the eventual return on your capital by investing all or most of your portfolio in the stock market. In doing so, you accept higher volatility of your investment returns in the hope that these returns will ultimately be higher. Your tolerance for risk is high.	Cash equivalents	0% to 30%	0.0%	0.0%	0.0%
	Fixed-income (duration: 5 years) <sup>1</sup>	0% to 30%	20.0%	11.5%	-0.5%
	Canadian equities	55% to 100%	22.5%	24.5%	0.0%
	US equities		22.5%	28.0%	0.0%
	Foreign equities		20.0%	21.0%	0.5%
	Alternative investments <sup>2</sup>	0% to 30%	15.0%	15.0%	0.0%

1 Dex Universe Index

2 Includes Hedge funds, Global real estate and Infrastructure, and Commodities.

FORECAST	Forecast				December 2014		June 2015		December 2015	
	2012	2013	2014	2015	Canada	US	Canada	US	Canada	US
	<b>Gross Domestic Product %</b>					<b>Rate %</b>				
Canada	1.9	2.0	2.4	2.5	Short-term rates (T-Bills, 91-Day)					
US	2.3	2.2	2.2	2.9	0.96	0.03	0.96	0.52	1.47	1.40
<b>Inflation %</b>					10-year bond yields					
Canada	1.5	0.9	2.0	1.6	1.91	2.23	2.11	2.67	2.57	2.74
US	2.1	1.5	1.7	1.4	2.45	2.97	2.60	3.38	3.00	3.36
					<b>Canadian dollar</b>		<b>US \$0.87</b>		<b>US \$0.85</b>	

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