Global Investment Forum Five-Year Outlook 2017 – 2022

BMO Global Asset Management

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Editorial summary

Welcome to BMO Global Asset Management's 5-Year Outlook 2017-2022.

Each year our Global Investment Forum (the 'Forum'), attended by a group of BMO's international investment leaders and strategists gather for two days of intensive briefing, fact finding and debate stimulated by the input of independent experts including chief economists, investment managers and academics. Our aim is to lift our eyes from the specific focus of our 'day jobs' and consider the wider investment world to seek out some of the key forces that will drive markets for years to come.

We firmly believe that this era of rapid change offers opportunities as well as threats, rewards as well as risks. As global investors with responsibility for the stewardship of your capital, we are committed to sharing our investment insights and expertise with you, our clients and customers. Looking to the future we consider a number of likely scenarios and the opportunities that they may bring to your portfolios' allocation strategies for under- or over-emphasis across asset classes and sectors.

In this year's Forum our discussion identified several persistent themes and we debated the potential impact of these forces over a 5-year time frame.

- The see-saw of monetary vs fiscal policy and the morphing of central banks into quasi-governmental roles, a potentially new paradigm;
- Populism – economic pessimism has seeped into wider society and a wave of populism and geopolitical disruption is sweeping across much of the world;
- Policy makers are searching for new gadgets in their policy toolboxes, as negative interest rates deliver mixed results and secular stagnation is becoming a mainstream theme;
- Disruptive technology – as the impact of automation and robotics is felt on long-standing business models and global industries;
- Bifurcation between manufacturing versus consumer economies, altering previous assumptions of emerging versus developed markets;
- Protectionism versus globalisation as broad trade agreements are being scrapped in favour of selective arrangements, closed markets and Special Economic Zones; and
- Humanitarian exposure – population shifts including the migrant crisis; warfare risks in South China Sea between U.S. and China; and the changing profile of the Middle East as the powerbase of who controls the world's energy supplies fragments, and the range of viable alternatives for oil widens (shale, LPG, non-fossil fuel etc).

Against this backdrop, we have arrived at a strong consensus regarding a baseline core scenario entitled 'Slow and Steady Wins the Race', which focuses primarily on the prospect of continued marginal incremental improvements in global economic growth (70% possibility). Our two alternative scenarios are 'Power to the People', reflecting the negative implications of populism and its associated ramifications (20% possibility); and 'All Pulling Together', in which collectivism triumphs and centralised policies are successful, stimulating global growth (10% possibility).

Annual scorecard: A look back at 2016

In last year's scenario casting we placed a 60% probability of our base case 'Firing on more than one cylinder' occurring over the coming years. On reflection, the key components we identified have broadly, so far been correct, albeit with some surprises caused by the surge of populism, a key consideration in our discussions this year. Key themes continue to evolve as follows:

- **Broadening of economic growth** – there has been some evidence of a broader distribution of growth, though not yet to the degree that we had anticipated. The U.S. continues to lead the expansion, while Japan and Europe are showing some signs of improvements.
- **Decline in energy prices** – we saw this as being a significant tailwind for a number of energy-consuming countries. However, not everybody benefited as responses differed regionally. In the U.S., in the face of lower oil prices the U.S. consumer acted unexpectedly, continuing to save and not spend, as seen in improving personal balance sheets. Also, the initial impact of lower energy-related capital expenditure had an immediately negative impact that was not offset by a typical U.S. consumer-led response to lower energy costs. Europe saw some expansion in consumer numbers, although in China, the benefits did not flow down to the consumer but stayed up at the state level.
- **Debt overhang as a headwind** – this remains the case, particularly where there is a high sovereign debt to GDP ratio and it continues to be a drag on growth potential. However, it is important to note that, consistent with our view coming out of our 2015 Forum, elevated debt levels remain a concern, but that there is a broader consensus that debt levels are sustainable for the foreseeable future, barring an unanticipated spike in interest rates.
- **For the U.S.**, we were calling for robust job gains and we got that spot on. We also thought housing prices would stay firm, and they picked up a little over the course of the year.
- **In Asia**, China has proven its ability to continue to grow and contain a crisis; GDP growth has slowed but without the hard landing many feared. We were right to highlight India as the BRIC nation that would disappoint the least.
- **Europe lower for longer** – this has broadly been the case, although the shock U.K. referendum decision was not anticipated and the long-term disruption remains unknown.

If we look at what we said regarding asset allocations, we suggested under-emphasising Canadian equities until the oil price was firm. Subsequently, we increased our Canadian equity rating late last year because we felt that oil prices had at last bottomed, moving into a position of over-emphasis. So we got that one correct too. Last October, we rightly suggested over-emphasising the following sectors: consumer discretionary, IT and industrials. Additionally, we recommended an over-weight in India, where equities have done better than in some developed markets. However, under-emphasising precious metals was not the right call in the last 12 months, and energy has been stronger than expected in the Canadian market.

On currencies, we predicted that the U.S. dollar was to be over-emphasised and it has strengthened overall. The U.S. dollar has had a volatile time, however, rising a little against the euro but weakening versus the yen.

Our 5-Year Outlook is a reflection of our commitment to add value through innovative ideas, solutions, support, and access to the insights of renowned global thought leaders.

State of the world

After eight years of growth (albeit moderate), and with signs of tightness in the labour market and deterioration in productivity, the U.S. economy appears to have entered the mature phase of the business cycle. But what are the prospects from here?

In the immediate term, there are some grounds for optimism. The U.S. is close to full employment, so modest wage rises are a possibility and these could support consumer sentiment and filter through into slightly higher inflation. Additionally, the impact of dollar strength is fading, and there is scope for profits to improve, so companies (unable to continue hiring so freely) could well increase capital expenditure.

Currently, the rate of expansion in the U.S. stands at around 2%, but longer term, there's an argument that secular themes could depress growth to around 1.5%. First, technology-related gains in productivity are moderating. Second, lower birth rates are combining with an ageing demographic to reduce the size of the working population.

Europe's economy is muddling through. Given its inherent diversity, it should be of little surprise that the region is characterised by marked divergence between the economic fortunes of its constituent nations. The European Central Bank remains proactive in its efforts to stimulate the economy but with rates already into negative territory, the future effectiveness of monetary policy is increasingly being questioned. Low interest rates have also had significant negative implications for key sectors such as banking. This naturally raises the possibility of shifting policy emphasis towards fiscal easing. Within the confines of the European Union, however, such a move is problematic as it implies a more coordinated federal structure which, in turn, runs counter to the wishes of domestic parliaments and stands in contrast to broader political developments. Brexit has heightened doubts over the longer-term feasibility of the E.U. project, and issues such as migration have contributed to the upturn in populist politics, with parties at both ends of the spectrum making gains. These themes have harmed both spending and investment, keeping the outlook for Europe's economy relatively lacklustre.

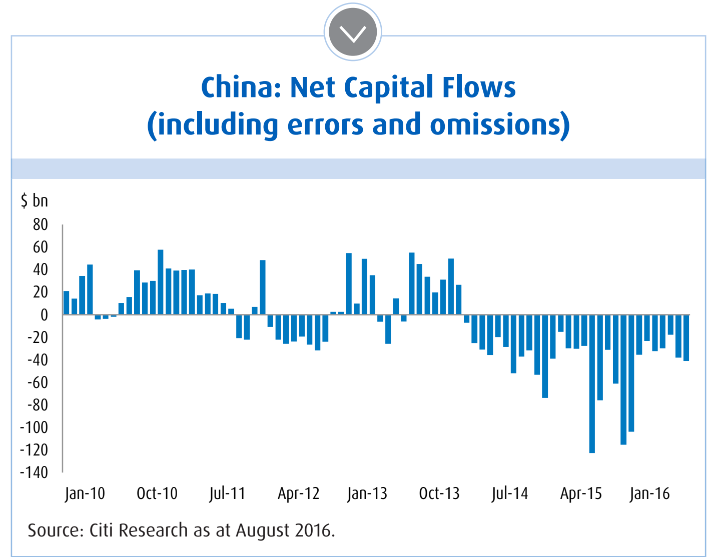
For the U.K., Brexit is likely to dominate in the short to medium term, with discussions over both the timing and negotiations affecting corporate decisions, U.K. stocks, and continuing to have a big impact on sterling. Despite this uncertainty, economic data has remained relatively robust with the purchasing managers' index showing continued expansion. Expectations for growth longer term are in a relatively wide range, but the general consensus is that the trend will be downwards from here, with short-term forecasts cut heavily post the referendum result.

The Bank of England was quick to act, post the referendum results, cutting base rates from 0.5% to 0.25%. However, there are a number of commentators who think this could have been more of a knee-jerk reaction to appear proactive and that the move was not necessary and could perhaps even be detrimental. Productivity is a cause for concern, and together with the more clouded outlook for inflation, this could spell a good time for policy to shift from monetary to fiscal, i.e. government spending and using the tax system to encourage private investment.

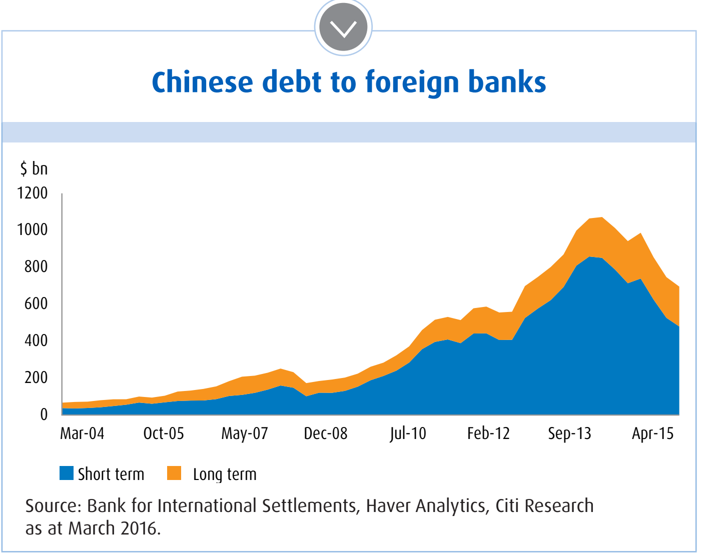
Turning to emerging markets, since mid-2013, a huge amount of money has been pulled out of emerging markets, and we have only just started to see this flow reverse. An improvement in sentiment has been driven by a whole host of factors, from the emergence from recession by Brazil and Russia to some structural reform stories in Argentina, Indonesia and India. This has been seen in emerging market debt spreads which peaked in February 2016 and have fallen materially since then.

2016 has also seen the convergence of two trends. The first is the fact that, for the first time since mid-2011, non-oil commodity prices have seen consistent, albeit small, upwards momentum. The second is that emerging market current account deficits began to fall from mid-2013, hence perceived risk fell, and returns rose. Therefore, it could be reasonably argued that emerging market fundamentals have troughed.

In China, capital outflows have contributed to problems in emerging markets. A big build-up of external debt between 2009 and 2013, originally accumulated to finance carry trades, is being unwound. The speed of that unwinding is affected by U.S. monetary policy as it was largely short-term U.S. dollar currency that was borrowed. Although capital outflows from China continue in 2016, it is not in a way that generates global risk aversion (as it did in 2015) largely because the People's Bank of China is pursuing a policy of moderate and gradual exchange rate depreciation. However, China's growth model is creaking and it has only limited policy tools available to engineer a soft economic landing.



Source: Citi Research as at August 2016.



Source: Bank for International Settlements, Haver Analytics, Citi Research as at March 2016.

Out of ammo – passing the baton

Since the financial crisis, central banks and their actions have been centre stage. Globally, central banks have deployed over $12.3 trillion since September 2008, in various quantitative easing initiatives, and cut interest rates towards zero (and even beyond). Can their efforts be judged a success? On balance, yes. Economies have grown, asset prices have increased and the threat of deflation has largely been mitigated.

Despite this progress the current lack of economic strength in many regions (and globally in aggregate) means that more needs to be done. After years of action, however, there is limited scope for monetary policy to provide further impetus, meaning that the likelihood of fiscal measures being employed has increased.

Fortunately, a period of austerity in countries like the U.K. means that there is greater flexibility to boost activity through spending in areas such as infrastructure. Indeed, the passing of the baton from central bankers to governments has already begun. Canada is already some way down the path; others will likely follow.

Shortly after his election, Prime Minister Trudeau outlined ambitious plans aimed at fighting off the recessionary threat by increasing Canada's deficit and spending big on infrastructure. In Japan, tax increases have been postponed, and in the U.K., the new government has shifted the emphasis from deficit reduction to a more flexible and pragmatic approach that includes greater spending. In the U.S., meanwhile, Donald Trump looks set to fulfill key promises from his election campaign to increase infrastructure spending.

Populism providing additional impetus

Shifts in the political backdrop have also helped drive the move towards fiscal measures. For many individuals, the period post the financial crisis has been one in which they have seen their wages fall while, at the same time, have become increasingly unsettled by factors such as automation and migration. Whether real or perceived, these factors have created greater scepticism towards centralised decision makers and structures like the E.U., and a shift away from the centre towards more populist rhetoric and policies. Those politicians and parties appealing to marginalised voters have gained ground, with protectionism and an increased willingness to spend and/or cut taxes: key themes on both sides of the Atlantic.

The law of diminishing returns

Response of policy makers to the financial crisis aimed to counter deflation, support asset prices and help economies.

Eight years on...

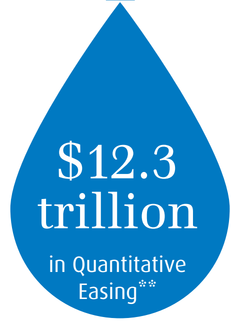
Inflation – subdued but in positive territory globally

Assets - many world markets at or above historic highs

Growth – lacklustre expansion with signs of weakening in global trade

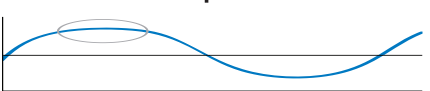
Debt – record global debt of $152 trillion*

Populism – disaffection drives shift from political centre ground



U.S.

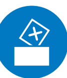
Low productivity + steady growth + tight labour market **= mature phase**



For illustrative purposes only

Europe

Brexit – eurozone uncertainty



2016/17 Elections
Italy, France, Germany, Netherlands, Austria

Emerging Markets

Fundamentals have troughed

Fund flows – investment in funds turning positive

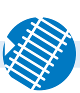
Globally low rates – little room for manoeuvre

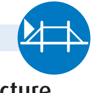
- **U.S.** 0.5%
- **Canada** 0.5%
- **U.K.** 0.25%
- **ECB** -0.4%
- **Japan** -0.1%
- **Australia** 1.5%

Time to pass the baton to...

Tax cuts

Fiscal stimulus





Infrastructure spend

Source: BMO Global Asset Management as at September 2016; *FT, **CNBC

Our scenarios

In the context of current global dynamics, we look to the future and consider a number of likely scenarios. This year within our Forum, we arrived at a strong consensus regarding a baseline core scenario entitled '**Slow and Steady Wins the Race**', which focuses on the prospect of continued marginal incremental improvements in global economic growth (70% probability). Our two alternative scenarios are '**Power to the People**', reflecting the negative implications of populism and its associated ramifications (20% probability); and '**All Pulling Together**', in which collectivism triumphs and centralised policies are successful, stimulating global growth (10% probability).

70% probability

'Slow and Steady Wins the Race', which focuses on the prospect of continued marginal incremental improvements in global economic growth.

20% probability

'Power to the People', reflecting the negative implications of populism and associated ramifications.

10% probability

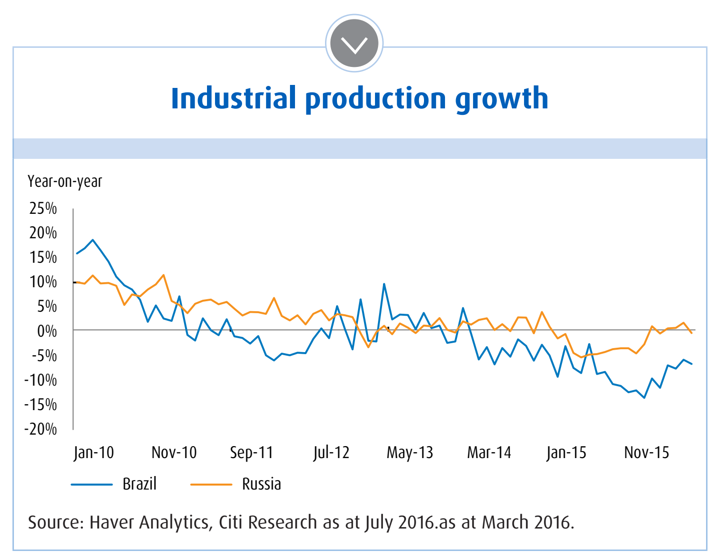
'All Pulling Together', in which human nature triumphs and centralised policies are successful, stimulating global growth.

Slow and Steady Wins the Race (70% probability)

For our base case scenario, we believe that, although the global recovery remains subdued, the benefits of a slow and steady strategy will enable the U.S. to avoid a recession and that the rest of the world will remain stable and achieve modest levels of growth.

Incremental growth

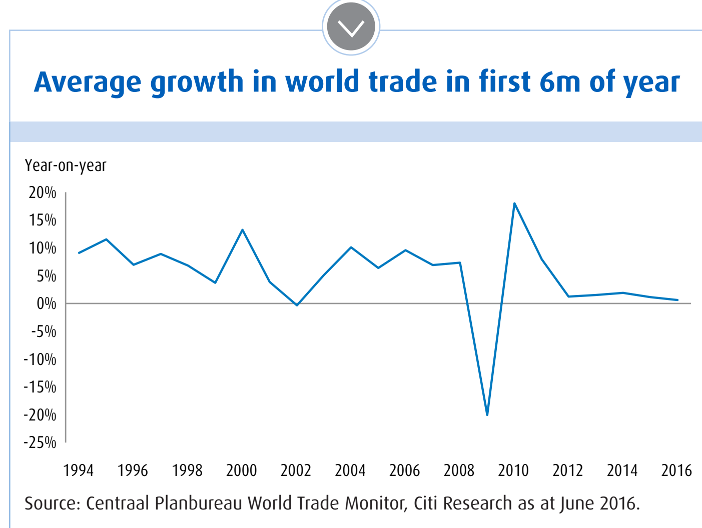
Alongside achieving slow and low growth in the U.S. and Europe (without stalling), we have hopes for stronger global growth in emerging markets, which have struggled in recent years with the collapse of the oil price and other commodity markets. As countries like China and India become bigger global growth engines, stronger output in these economies will power the global recovery forward. This is anticipated to drive a third of the expected recovery over the coming years, while the end of recessions in emerging markets such as Brazil and Russia should also lift growth.



Industrial production growth

Source: Haver Analytics, Citi Research as at July 2016.as at March 2016.

A full worldwide recovery will, however, be challenged by diminishing volumes of global trade as reflected by the slowing in productivity and an increase in protectionism, although closed markets such as India and those with selective trading partners appear to be faring better than more open markets.



Average growth in world trade in first 6m of year

Source: Centraal Planbureau World Trade Monitor, Citi Research as at June 2016.

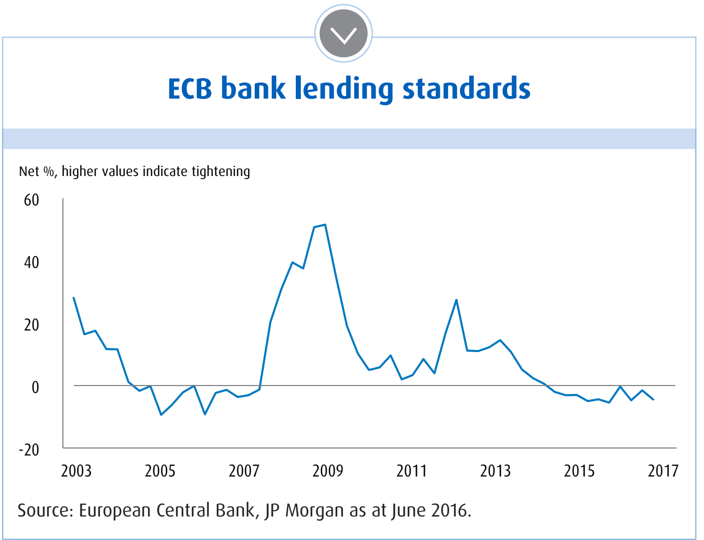
In a story accredited to the ancient Greek slave Aesop, writing between 620 and 564 BC, there was once a speedy hare who bragged about how fast he could run. Tortoise challenged him to a race. All the animals gathered to watch. Hare quickly ran off then stopped for a rest, thinking himself safely in the lead. Meanwhile, tortoise just kept walking, never pausing. He reached the finish line well ahead of the sleeping hare who woke to the sound of the crowds cheering that 'slow and steady had won the race'.

Handing over the policy baton

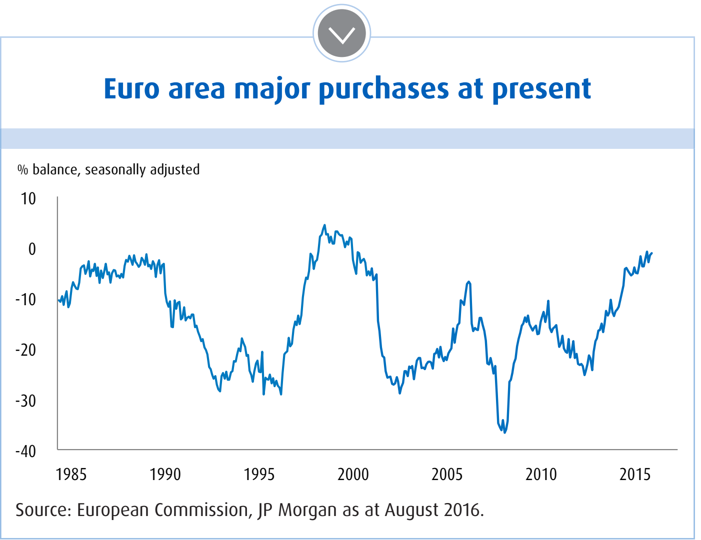
In our twist to the old story of the tortoise and the hare (see inset on page 9), as the hare was sleeping, there is a switch of runners as the exhausted Monetary Policy tortoise hands the baton over to a fresher tortoise wearing the Fiscal Policy team colours.

As we outlined earlier, we believe that monetary policy has been increasingly running out of ways to ease deflationary pressure and reflate assets. Low or negative interest rates have been described as a dire financial tool, but better than the others available, although, in practice, their effect has been limited. The theory – that interest rates below zero should reduce borrowing costs for companies and households thereby driving demand for loans – has proven somewhat successful in Europe, which has remained resilient in the face of the Brexit shock. However, central banks, in trying to prevent the risk of deflation, can't seem to kick-start growth. Since the European Central Bank ('ECB') and Bank of Japan ('BoJ') cut rates into negative territory and drove long end yields much lower through aggressive quantitative easing, monetary policy has started to have adverse impacts on certain parts of the economy – the financial and insurance sectors in particular. More broadly, negative interest rates appear to have caused many consumers to restrain spending and to increase their savings rate, as low or negative interest rates cause their savings for retirement to be lower. This is exactly the opposite effect that central bankers were looking to initiate.

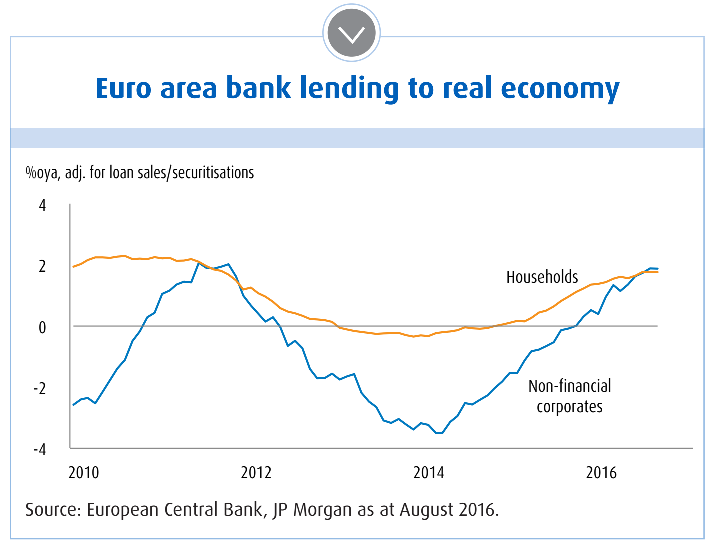
There is a growing sense that more initiatives are needed to stimulate productivity and that fiscal policies will be able to deliver the step-change that is required. Although in Japan, government spending measures have lowered the probability of recession, the possibility of deflation has increased, partly due to the recent appreciation of the yen.



Source: European Central Bank, JP Morgan as at June 2016.



Source: European Commission, JP Morgan as at August 2016.



Source: European Central Bank, JP Morgan as at August 2016.

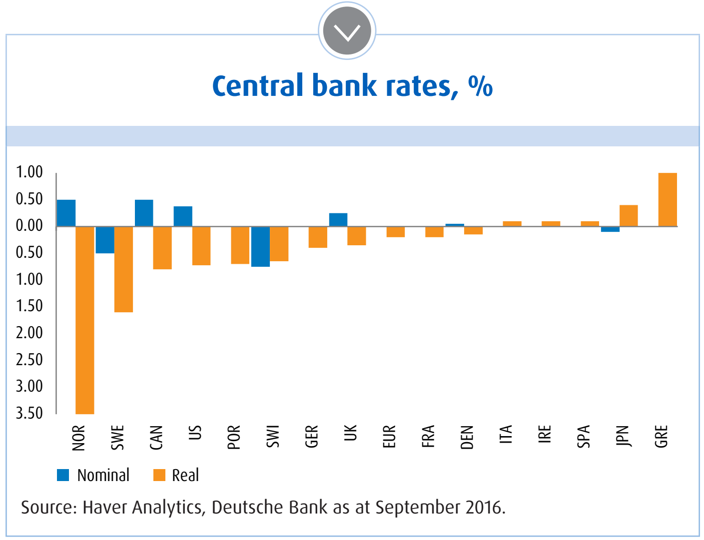
The recovery will be challenged by diminishing volumes of global trade, reflecting the slowing in productivity and increase in protectionism.

Although paradoxically, closed markets such as India and those with selective trading partners seem to be faring better than more open markets.

> "We have to adapt to the new reality of lower potential growth. The faster we do this, the safer the financial system will be."
>
> **Carolyn Wilkins,**
> **Senior Deputy Governor, Bank of Canada**

In Canada, with the benchmark interest rate currently at 50 basis points, Senior Deputy Governor Carolyn Wilkins has noted that monetary policy in Canada remains quite stimulative, although less so than it would have been a decade ago when the base rate was higher[1].

Central bank rates, %



Source: Haver Analytics, Deutsche Bank as at September 2016.

The evolving role of central banks

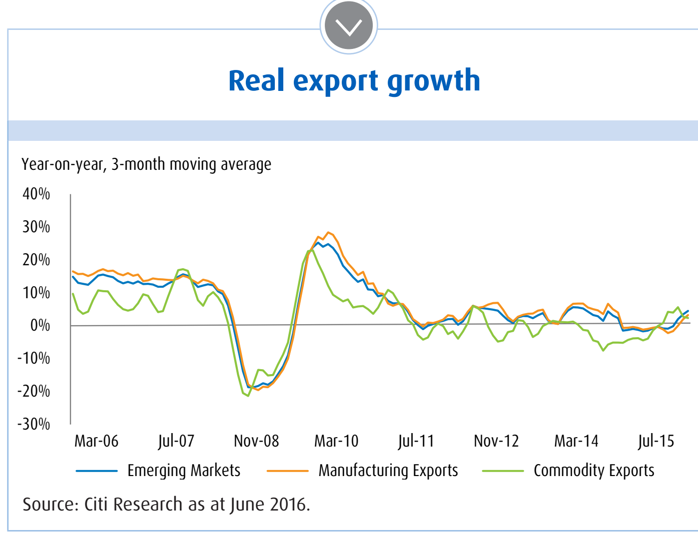
In the 'Slow and Steady' scenario, we also consider that central banks and governments will become increasingly aligned, and a new paradigm may be emerging as we make the shift from a sole focus on monetary policy to a mix that includes fiscal policy initiatives. With central banks becoming more closely linked to fiscal expansion, some commentators are asking whether central banks have taken on too many responsibilities. Their impact is significant as can be seen when a small shift in base rates results in very marginally effective stimulus. Consequently, there remains scope for slightly more aggressive tightening of rates from the Federal Reserve to stimulate productivity – the equivalent of offering a subsidy to banks.

[1]Source: Bank of Canada, Data and Statistics office, Average base interest rate for 2005: 2.92% and for 2006 4.3% (Jan – Dec).

Low return world

We remain broadly positive on equities, but in line with the generally slow tempo of this scenario, we are predicting a continued period of lower returns as the prospect of increasing fiscal policies creates a business unfriendly environment (with pressure on labour to be paid more at the cost of margins). This is better than the outlook for bonds which, we believe, will continue to deliver modest total returns due to generationally low interest rates, although equities' growth may prove better able to deliver dividends as an income substitute.

We are also predicting an increasing bifurcation between manufacturing economies versus consumer economies, altering previous assumptions of emerging versus developed markets, with our scenario favouring the commodity importers over exporters. This, in turn, is also reflected in our belief in the strength of the U.S. dollar over other currencies.



Source: Citi Research as at June 2016.

Elsewhere, in this scenario, the benefits of automation versus the disruption effect of new technologies are netted out and not felt to be performance enhancing overall.

Powerful population

In our fable, the influence of the other animals plays an important role as it is their vociferous involvement which helps drive Team Tortoise on to achieve the goal.

We have seen, through the rise of extreme political parties and unexpected voting results, that a sizeable portion of the populations in the U.S. and across Europe are signalling a need for change, almost regardless of a real understanding of the implications. These results are reflecting a disenfranchised and marginalised population – the so-called 'inequality theme'. The realities of a sluggish economy are that businesses make less profits, which translates to weaker pay growth and lower living standards. This, in turn, spirals into a growing interest in protectionism and support for the scrapping of trade deals and the imposing of tariffs, ultimately impacting international trade.

However, in our fable, it was the cheering of the wider population that woke the sleeping hare. Similarly, we believe it will be the increasing influence and passion of the population and individual voters that pushes governments to take the steps to effect changes manifested through fiscal stimulus, while on the flip side contributing to uncertainty and volatility.

We believe that the increasingly aligned actions of governments and central banks would include tax reforms and large-scale investment in economic and social infrastructure projects including transport, utilities and energy.

However, in the 'Slow and Steady' scenario (in marked contrast to the 'Power to the People' scenario detailed below), we believe that the long-term impact of the rise of populism is relatively limited. We believe that the positive response of policy makers (both central banks and governments) will generate appropriate remedial incentives to address the root causes of concern. Importantly though, it remains the most unpredictable and volatile of the various dynamics that we discussed.

For possible asset allocation implications of this scenario, see **Section 8** for our Under- and Over-emphasis tables.

We have seen through the rise of extreme political parties and unexpected voting results, that a sizeable portion of the populations in U.S. and across Europe are signalling a need for change – almost regardless of a real understanding of the implications.

Power to the People (20% probability)

Power to the People is our downside scenario, in which we consider the negative outcome when monetary and fiscal policies' failures fan the burning embers of an already disaffected and alienated population across global markets.

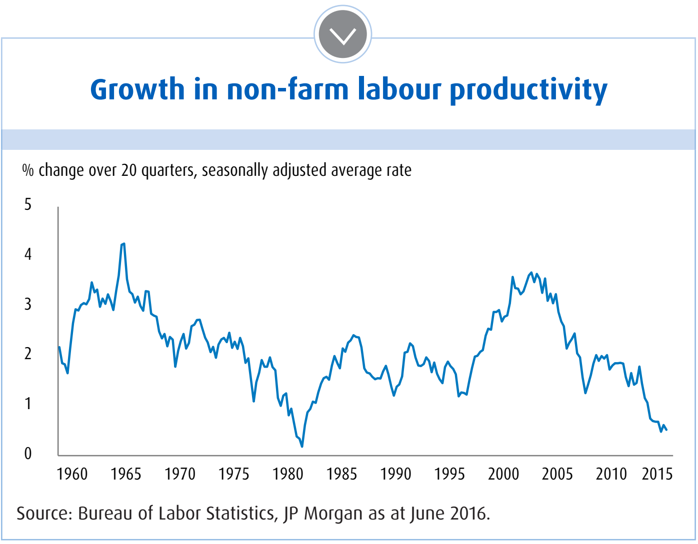
We are giving this scenario a probability of 20% as several of the events on which it is predicated are scheduled to occur. What we are unable to predict is which event will be the catalyst.

In this scenario, there is a sense of our vulnerability to the increasingly unpredictable outcome of human sentiment, with polls becoming less reliable, the significant global penetration of social media and shifting patterns of demographics.

Given the shock waves following the result of the U.K.'s referendum on membership and Trump's victory in the race for the White House, there is a heightened awareness of the need to give serious consideration to the risk of seemingly unexpected outcomes.

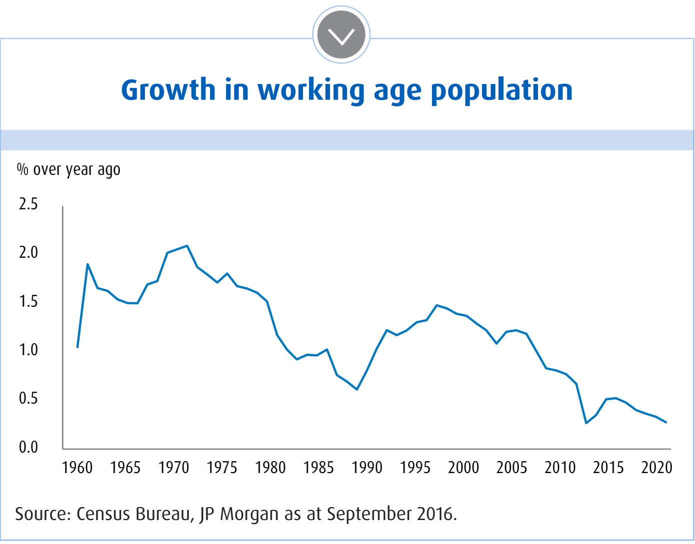
Growth stalls

One of the events that would lead to a populist backlash is the possibility that current low levels of U.S. growth falters, with productivity maintaining the current downward trend, aggravated by the falling levels of the working-age population. We anticipate that this stall in productivity would trigger a U.S. recession.



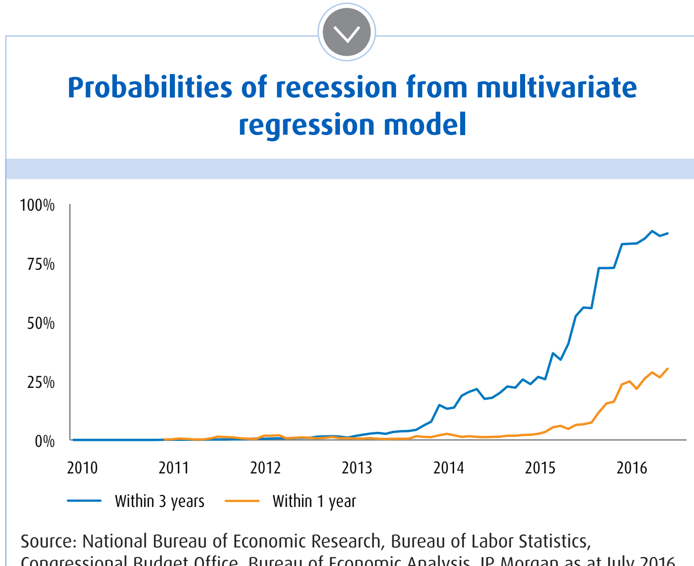
Growth in non-farm labour productivity

Source: Bureau of Labor Statistics, JP Morgan as at June 2016.



Growth in working age population

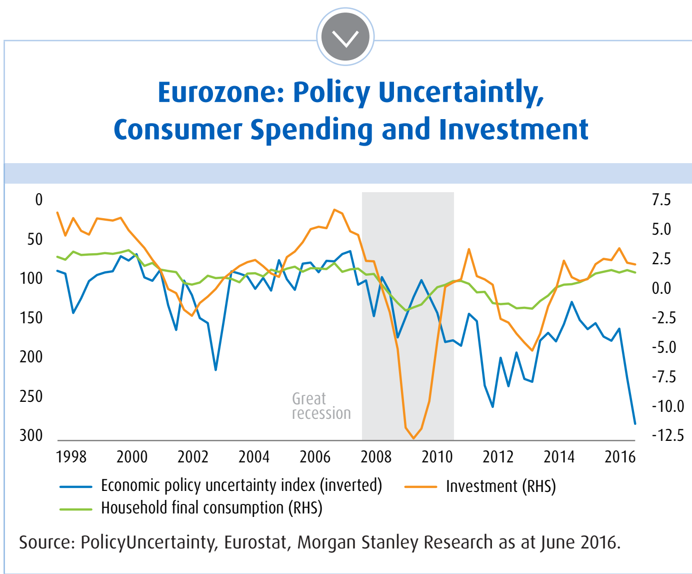
Source: Census Bureau, JP Morgan as at September 2016.



Probabilities of recession from multivariate regression model

Source: National Bureau of Economic Research, Bureau of Labor Statistics, Congressional Budget Office, Bureau of Economic Analysis, JP Morgan as at July 2016.

Similarly, in Europe, as we've mentioned previously, the reality of not being a single country or federation is creating a politically fragmented and volatile environment that is not conducive for growth. We can see that higher policy uncertainty harms consumer spending and leads firms to scale back their investment plans.



Eurozone: Policy Uncertaintly, Consumer Spending and Investment

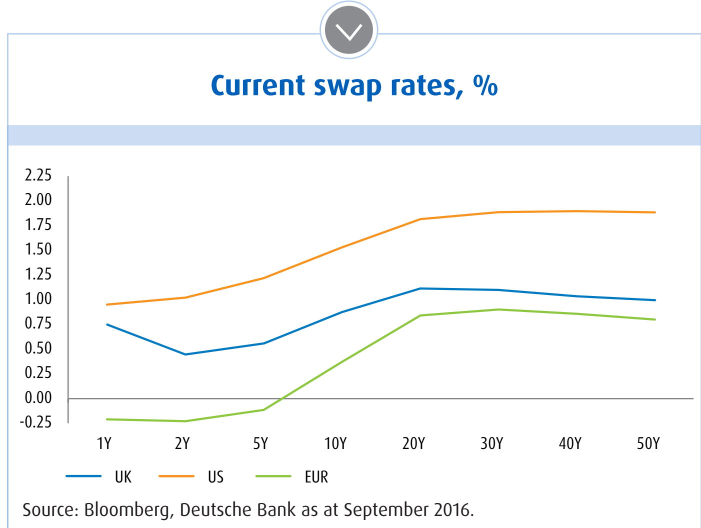
Source: PolicyUncertainty, Eurostat, Morgan Stanley Research as at June 2016.

Dropping the baton

Elsewhere, we've looked at the prospective shift between existing monetary policies, implemented by central banks with varying degrees of success, and the move towards governments' increasing fiscal stimulus.

In this scenario, in response to the global stalling of growth we anticipate that there will be several knee-jerk reactions, including the continued application of the negative interest rate policy.

This will eventually create a populist backlash against the lack of economic growth, persistent un- and under-employment of the labour force aggravated by increasing cost-saving automation, and impoverishment of savers. In response, where governments do move to implement fiscal stimulus, what they do is too little too late.



Current swap rates, %

Source: Bloomberg, Deutsche Bank as at September 2016.

Populism x Population stagnation x Protectionism = a globally explosive chain reaction

Populist politics are widespread in their impact. In Europe, this scenario predicts a Brexit-contagion effect as other countries push for votes to leave and begin to pull out of the European Union.

In the U.S., the disruption and volatility caused by the vitriolic Trump vs Clinton election campaign has long-term implications for the implementation of new policies and an increased requirement of politicians (of both parties) to accommodate the demands and views of marginal voters. Although it remains to be seen how Trump's campaign rhetoric translates into actual policy.

The continued problems in the Middle East are a source of concern to governments. As political and economic refugees continue to flood into the European Union, the migrant crisis is also causing further pressure on the E.U.'s open borders policy, making it a bone of contention between increasingly protectionist voting factions. Also, there is the threat of deteriorating national relationships given the large number of countries with vested interests in the area including Russia and the U.S. Elsewhere, in Asia, warfare also remains a tension as relationships between China and the U.S. flare up in the South China Sea.

In manufacturing economies and emerging markets, growing protectionism delays global trade agreements and increases tariffs, just as some emerging markets are coming out of long periods of recession.

Seeking opportunities

In these deflating conditions we would anticipate that equities would go into a tail spin although the outlook would be more positive for bonds.

Rates will not have had sufficient time to rise from current low levels before the potential downturn anticipated in this scenario. Therefore, central banks will be constrained to drop rates further unless they move to the negative interest rate policy. It is likely that investors would chase gold in this scenario, moving to a physical asset in preference to receiving no or negative interest. Other yield generating assets, such as income equities and property, have the potential to outperform the market on a relative basis.

The upshot of this extreme reaction is uncertainty. This in turn leads to investors saving more and investing less, which stalls economies further.

For possible asset allocation implications of this scenario, see **Section 8** for our Under- and Over-emphasis tables.

The impact of new technologies, while increasingly described as disruptive, have the potential to deliver a positive step change to industry.

Examples include the advancement in battery storage technology in combination with the improvement in efficiency and effectiveness of power generation through wind and solar.

All Pulling Together (10% probability)

If the 'Power to the People' scenario, reflects the negative impact of populism, then 'All Pulling Together', is an optimistic scenario in which countries find ways to work together to address trade; political parties find constructive, unifying solutions to issues; and the labour force globally is invigorated. This scenario sees the successful implementation of centralised policies overcoming the downward pressures on productivity and employment to stimulate growth.

The policies work

In a repeat of a theme that was also drawn out last year, this scenario assumes that policymakers around the globe get it right for longer i.e. where monetary policy has been implemented it gains traction and we see that its effect has lagged rather than been absent. Equally, where fiscal policy is implemented it is done smoothly and has a positive impact. Infrastructure projects are able to get up and running without the usual time lags from concept to delivery and their impact delivers positive changes.

In Europe, we anticipate that effective implementation of centralised policies will see financial improvements through recapitalisation and reflation. Investment injections work as businesses with fully employed workforces begin to invest. Globally, productivity picks up in response to the policy stimuli and has a beneficial effect on consumer confidence and sentiment, encouraging people to spend rather than save. Increased market confidence means that the labour supply is at capacity.

In emerging markets, the structural commodity problems are left behind and the consistent increase in growth seen through 2016 continues. The threat to global trade recedes as countries regain confidence in the idea of globalisation and currency wars become less necessary.

Stimulating effect of new technology

The current low yield environment and reasonably high savings ratio across the developed world gives new ventures easy access to capital.

The impact of new technologies, while increasingly described as 'disruptive' have the potential to deliver a positive step change to industry. Examples include:

- the sharp pick up in internet penetration driven by the rise of the smartphone;
- the advancement in battery storage technology in combination with the improvement in efficiency and effectiveness of power generation through wind and solar; and,
- the development of 3D printers which reduces working capital needs and makes replication easier.

We can also see the rise of the sharing economy (e.g. ZipCar and Uber) is improving the efficiency with which assets are used.

New business models are also very asset-light e.g. Airbnb and Uber (again), which further accelerates their development and stimulates existing established markets to also evolve to become more responsive.

For possible asset allocation implications of this scenario, see **Section 8** for our Under- and Over-emphasis tables.

Strategic asset allocation: Over and under emphasis tables

			Slow and Steady			Power to the People			All Pulling Together		
			Under	Neutral	Over	Under	Neutral	Over	Under	Neutral	Over
Equities											
Developed Markets (DM)	U.S.				●		●				●
	Euro			●		●					●
	U.K.			●		●					●
	Japan			●		●					●
	Canada				●	●					●
	Non-resource cyclicals	Information Technology			●	●					●
		Financials		●		●					●
		Consumer Discretionary			●	●					●
		Industrials			●	●					●
	Commodity / cyclicals sectors	Energy		●		●					●
		Base metals		●		●					●
		Precious metals		●		●					●
	Income sectors	Utilities	●					●	●		
		Pipelines	●					●	●		
		Telecom	●					●	●		
		Health care	●					●	●		
		REITs	●					●	●		
Emerging Markets (EM)	EM overall			●		●					●
	India				●	●					●
	China		●			●				●	
	Russia			●		●					●
	Brazil			●		●					●
	Commodity importers			●				●	●		
	Commodity exporters			●		●					●

Strategic asset allocation: Over and under emphasis tables (continued)

		Slow and Steady			Power to the People			All Pulling Together		
		Under	Neutral	Over	Under	Neutral	Over	Under	Neutral	Over
Fixed Income										
DM	U.S.		●				●	●		
	Euro	●					●	●		
	U.K.	●					●	●		
	Japan	●					●	●		
	Canada		●				●	●		
	Inflation-linked bonds		●		●					●
	Nominal Rates		●				●	●		
	Sovereign	●					●	●		
	Credit products – investment grade		●		●					●
	Credit products – high yield		●		●					●
	Canadian preferred equity		●		●					●
	EM – overall		●		●					●
Alternatives										
	Commodity related		●		●					●
	Fixed (non-duration and credit)		●				●			●
	Global Macro	●					●			●
	Gold		●				●			●
	Infrastructure			●			●			●
	Long-short relative value strategies		●				●			●
	Private equity			●			●			●
	Real estate		●		●					●
	Style premia		●				●			●
Currencies										
	USD		●				●			●
	CAD		●		●			●		
	EUR	●			●			●		
	YEN	●			●			●		
	GBP		●		●			●		

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