Q1
2018

GLOBAL ECONOMIC & MARKET UPDATE

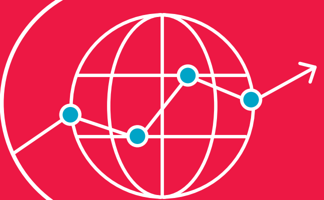
More Room to Run

ONTARIO TEACHERS' PENSION PLAN

We remain more constructive than the market consensus on the near term outlook for the global economy. This is due to our more optimistic view for the cyclical buoyancy in DM economies and the reinvigoration in ex-China EM's growth performance to be sustained. In the US, the added fiscal stimulus should provide a shot in the arm, delivering further near term growth impetus. Similarly, the improving backdrop in the Eurozone and Japan augurs well for growth. We are also a little more sanguine on the near-term outlook for China, where we look for a slightly "shallower" slowing in growth momentum than the current market consensus. Global growth is expected to accelerate towards the upper-end of the 3.75% to 4.0% y/y range. The near term risks are tilted to the upside.

Consistent with this sustained above-trend growth momentum, we see upside risks to inflation relative to the market consensus. With strong cyclical growth and inflation dynamics, we expect rates to increase as the central bank normalization proceeds apace, though global financial conditions should remain favourable, providing a supportive backdrop for risk assets and commodity prices.

Millan Mulraine, Chief Economist



SYNCHRONIZED GLOBAL GROWTH

Global growth dynamics remain encouraging, sustaining the positive thrust that has spread across a broad swathe of EM and DM economies. The nascent signs of an emerging global capex cycle suggest that the cyclical upswing may have more room to run.

CENTRAL BANK CONFIDENCE

With economic growth firming and cyclical inflation momentum beginning to reassert itself, we expect a more synchronized pivot towards monetary policy tightening by DM central banks. While we expect this pivot to be gradual and digestible, from an economic perspective, we are mindful of the medium term risks associated with a misstep eventually leading to a global slowdown.

INFLATION RISK TO RISE

As the pace of global slack absorption accelerates we expect cyclical inflation pressures to begin building. These inflationary pressures should be more evident in Canada, the U.S. and the U.K., where the business cycle is more advanced, particularly during the second half of this year.

RISK REVIEW

We remain constructive on the medium-term outlook. However, growth remains susceptible to potential headwinds, including central bank missteps, the rising threat of trade protectionism and geopolitical risks.

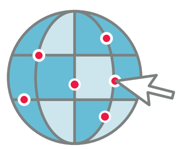
Eyes on the World

PHILOSOPHY

Our competitive edge stems from our unique access to key global decision-makers and a diverse platform of portfolio companies. This unique information gateway informs our view of the world, and provides a benchmark against which our global outlook (and associated risks) for growth, inflation and the discount rate (interest rates) can be judged. The underlying views are forged by an analysis of the interconnections between three key pillars of the economic infrastructure (namely the structural trends, cyclical dynamics and global adjusting forces) that shape the medium-term outlook for the global economy and financial market performance.

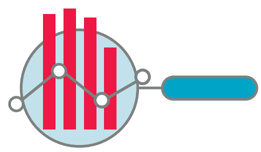
ONTARIO TEACHERS' GLOBAL MACROECONOMIC FRAMEWORK

Unique Information Gateway



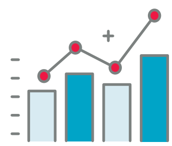
The Competitive Edge
- Portfolio companies
- Hedge fund partners
- Research community

The Analytical Framework



The Ontario Teachers' Tri-Cycle
- Structural Trends
- Cyclical Dynamics
- Global Adjusting Forces

Market Assessment and Outlook



The Investment Outlook
- Financial Market Outlook
- Global Macro Risk Monitor
- Global Scorecard

THE ONTARIO TEACHERS' TRI-CYCLE

1 Structural Trends

The long-term trends or secular regimes that define the investment environment, and influence the decision-making process of firms, households and non-market actors at both the individual and aggregate level.

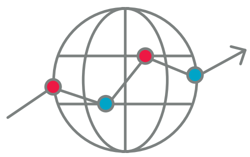
2 Cyclical Dynamics

Forces related to fluctuations in the economy, policy and credit regimes that are driving forces behind economic and asset market performance.

3 Global Adjusting Forces

These forces define the avenues for spillovers across economies and regions. In particular, they form the mechanism through which DM and EM economies and financial markets become integrated through trade and capital investment flow.

Global Macroeconomic Outlook



DEVELOPED MARKETS:

Sustained, Synchronized, Above-trend Growth:

We continue to be optimistic on the medium-term outlook for the global economy. And even as the consensus forecast has shifted in our direction, we see further near-term upside risks to our base-case for global growth to rise to the upper-end of the 3.75% to 4.00% range. The delta should come from the U.S., with Europe and EM (ex-China) growth momentum remaining strong.

Inflation Coming Out of Hibernation:

With the global output gap closing, cyclical inflation pressures should begin to gradually rise. A distinct risk is that as global labour markets tighten, wage growth accelerates sharply, leading to a faster rebound in inflation than is priced into the markets. In our view, the odds of this eventuality in late-2018 and early-2019 is reasonably high.

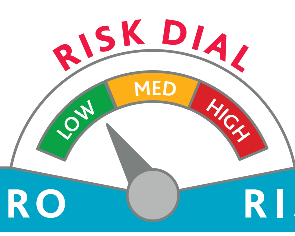
Central Banks Proceeding With Caution:

The DM monetary policy stance is beginning to shift towards synchronized tightening. However, the risks of a disorderly adjustment are limited by central bankers' willingness to adjust their policy stance to the economic reality. That said, we are mindful that a change in the balance of risks for inflation could quickly alter their reaction functions.

EMERGING MARKETS:

Most EMs in Cyclical Sweet-spot, With More Room to Run

We remain constructive on EMs, as cyclical growth prospects continue to improve thanks to lingering positive external conditions and more favourable domestic fundamentals. EMs' 2017 growth inflection was largely driven by exports. In 2018, we expect EM domestic demand to become a more important growth driver, fueled by a turnaround in the credit cycle. Importantly, China is no longer seen as a major destabilizer.



KEY GLOBAL MACRO RISK MONITOR	RISK LEVEL
1 U.S. encounters an economic recession over the next 12 months	
2 The Canadian economy enters a recession in the next 12 months	
3 Global geopolitical tensions rise owing to competitive devaluation and protectionism NEW	
4 A DM-led down-shift in the global business cycle over the medium term NEW	

Financial Market Outlook

EQUITIES: Fundamentals Remain Supportive

The fundamental backdrop for equities remains favourable, underpinned by supportive financial conditions, strengthening economic growth, and a positive fiscal impulse emanating from the U.S. And even as we enter a period of higher volatility, we see further modest upside going forward. Any correction will be short-lived.

OUTLOOK: Slightly Bullish

FIXED INCOME: Slight Upside Bias to Yields

The combination of robust cyclical economic activity, burgeoning inflation pressures, and central bank tightening should provide a lift to yields over the next year. From a strategic perspective, however, fixed income assets remain attractive given lingering secular headwinds to growth and inflation.

OUTLOOK: Cyclically Bearish

U.S. DOLLAR: Low Conviction

Our conviction on the medium-term USD outlook is low. Historically, strong global growth environments have coincided with a weakening greenback. If Europe and EMs continue to deliver positive growth surprises, we would expect portfolio flows to favour a weak dollar. However, interest rate differentials remain supportive.

OUTLOOK: Neutral

CREDIT: Risk-Reward Fails to Impress

Both DM and EM credit spreads remain anchored near their the post-GFC cycle lows, and we see limited scope for further compression. We are watching for signs of stress in credit markets, as they will provide an early warning signal that investors are becoming more concerned over global economic and financial risks.

OUTLOOK: Neutral

COMMODITIES: Firming Demand to Support Prices

We are still constructive on commodities. Supply-demand dynamics for many commodities (particularly oil) are beginning to re-balance, global demand is firming, and a potentially sustained USD weakening trend could provide further support. Financial demand may also rise, as investors seek more inflation protection.

OUTLOOK: Bullish

ON OUR RADAR

STRUCTURAL FACTORS

Changing global demographics, a weakening globalization impulse as well as ongoing deleveraging have been constraining forces on growth. Collectively, the net impact on interest rates and inflation has also been negative.

DISRUPTIVE TECHNOLOGY

The development and adoption of new revolutionary technologies is occurring at an unprecedented pace. The economic ramifications of these disruptive technologies are profound as they have the potential to transform the economic and financial market landscape in meaningful ways.

CENTRAL BANK POLICY

There is increased confidence among DM policymakers about the sustainability of growth and higher conviction around the need to begin removing policy support. The monetary pendulum is beginning to swing from synchronized global easing, to a synchronized, albeit gradual, global tightening – a major post-crisis inflection point. Risk of a misstep remains.

GEOPOLITICS

The global geopolitical risk level remains elevated, especially as the worst fears of a protectionist lurch by the Trump Administration resurface. Furthermore, the potential for a confrontation between the U.S. and China remains a non-trivial risk as tensions linger.

Global
Medium-term Scorecard

The scorecard reviews the directional impact of economic indicators ranging from structural trends like geopolitics and the regulatory backdrop to cyclical dynamics and global adjusting forces on the three key primitives – growth, inflation and interest rates. This is compared to our assessment of what the market is pricing in for these factors.

GLOBAL

		Growth	Inflation	Discount Rate
Structural Trends	Geopolitical Trends	−	+	+
	Regulatory Backdrop	−	+/−	+
	Secular Growth Drivers	+/−	+	−
Cyclical Dynamics	Credit Cycle	+	+	+
	Business Cycle	+	+	+
	Policy Cycle	+	+	+
Global Adjusting Forces	Investment Cycle	+	+/−	+/−
	Trade Cycle	+	+	+
	Capital Flow Cycles	+	+	+/−
Ontario Teachers' Bias		+	+	+
Relative to Market		+	+	+

CANADA

		Growth	Inflation	Discount Rate
Structural Trends	Geopolitical Trends	−	+	+
	Regulatory Backdrop	−	+/−	+
	Secular Growth Drivers	+/−	−	−
Cyclical Dynamics	Credit Cycle	+/−	+	+
	Business Cycle	+	+	+
	Policy Cycle	+/−	+/−	+
Global Adjusting Forces	Investment Cycle	−	+/−	+/−
	Trade Cycle	+/−	+	+
	Capital Flow Cycles	+	+	−
Ontario Teachers' Bias		+	+	+
Relative to Market		+	+	+

+ = Upward − = Downward +/− = Outcome uncertain

ONTARIO TEACHERS' PENSION PLAN

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