Greystone Quarterly Market Update

Q3-2018

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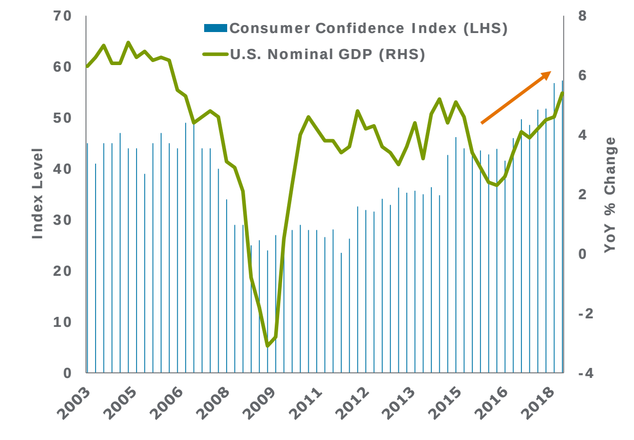
Chief Executive Officer & Chief Investment Officer

In August, the current economic recovery became the second longest in recorded history. While lengthy, the recovery has also been one of the shallowest in history. As the cycle marches on, our outlook for continued earnings and economic growth has not changed materially. What is catching our attention is the relatively few headline risks on the horizon. The shortlist of risks includes contagion from any further emerging markets stress, a housing slowdown, Italian deficits and a full blown trade war between the U.S. and China. While not to be ignored, these risks appear minor when compared to the global risks navigated over the past decade. Corporate debt levels are also worth monitoring but are likely to remain a quiet issue until the next downturn.

Signposts pointing towards economic expansion are more widespread, headlined with nominal U.S. GDP growth tracking between 6-7% for Q3, following similar figures from Q2. Strong levels of U.S. nominal growth has driven strong sentiment for an economy that, in recent years, has been tuned towards lower real economic growth and lower inflation. Unemployment rates, financial conditions, strength in manufacturing, modest inflation, corporate profitability and fiscal stimulus remain as tailwinds for investors.

Figure 1: Nominal Growth Fuels Positive U.S. Consumer Sentiment



Source: Bloomberg.

We believe that oil prices may return to view for Canadians following recent quarters of relative calm. We are monitoring a technical breakout towards higher Brent oil prices amid declining Iranian production and falling inventories in the U.S. and Saudi Arabia. Canada is unfortunately at risk of lagging further behind global energy producers, with a large price discount on Western Canadian Select crude, until delivery issues are alleviated.

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Investment momentum will be an important indicator in the coming months absent any change in the fundamental outlook. As the positive outlook is priced in by a growing number of investors, we will look for pricing signals that could potentially indicate full valuation of positions that have performed well. Within equities, our view calls for a regional bias to the U.S. as well as a focus on leaders within Health Care, Information Technology and non-North American Energy sectors. Pricing power and market expansion will be increasingly important as tightening labour capacity places pressure on wages.

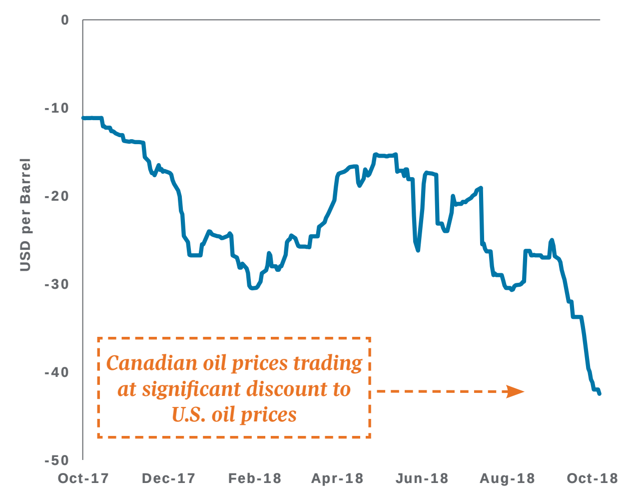
Momentum will also play an important role in fixed income markets, which witnessed a re-acceleration towards higher yields in September. Short-term bonds will likely see higher yields as the Bank of Canada continues to raise interest rates, while longer-term rates are also at risk of rising from late cycle inflationary pressures. Support for bond prices may be close at hand given debt levels in Canada. Our assessment of the fair value on Government of Canada 10-year bonds is near 2.5% and we view the peak for this cycle near 3.0%.

While our bias is to hold on to positions that have performed well, scaling of risks will be an important portfolio management function in light of our assessment. An absence of material risks may breed complacency in the market place. We are also monitoring the pace of interest rate increases, which could create pressure on valuations for stocks. There have been very few instances of simultaneous losses in stocks and bonds; however, this historically occurs when inflation and interest rates rise faster than expected. Real assets will play an important role in stabilizing portfolios if stocks and bonds witness simultaneous pressure.

We are seeing increasing capital flows into private real asset markets, as institutional investors increase their allocation to alternatives. Within private markets, the late stages of the economic cycle are presenting strong opportunity to deploy capital in high-quality assets. These high-quality assets tend to exhibit greater capital preservation over a full market cycle. Moreover, the income spreads being generated from real estate, private debt and infrastructure continue to be attractive versus public markets.

Our asset mix positioning is conscious of market volatility potentially rising with only modest tilts towards equities over bonds. Regionally we have a bias to U.S. equities over Canadian and international. Investors with long-term real asset exposure will likely benefit from late cycle deal availability and stable return profiles if public markets witness price pressures.

Figure 2: Western Canada Select vs. West Texas Intermediate Price Differential



Source: Bloomberg.

Multi-Asset Class Total Returns

Calendar Year						Q3-2018
2013	2014	2015	2016	2017	YTD	3-Month
Glo. Eq 35.2	Long Bonds 17.5	Glo. Eq 18.9	Cdn. Eq 21.1	EM Eq 28.3	Glo. Eq 8.8	Glo. Eq 3.2
Cdn. Eq 13.0	Glo. Eq 14.4	Infrastructure 11.5	Infrastructure 8.6	Infrastructure 18.8	Real Estate 6.0	Real Estate 2.4
Infrastructure 12.9	Infrastructure 10.6	Real Estate 7.8	EM Eq 7.3	Glo. Eq 14.4	Infrastructure 3.7	Infrastructure 1.4
Real Estate 10.6	Cdn. Eq 10.6	Mortgages 4.0	Real Estate 6.1	Cdn. Eq 9.1	Cdn. Eq 1.4	Cash 0.3
EM Eq 3.9	Bonds 8.8	Long Bonds 3.8	Glo. Eq 3.8	Real Estate 7.2	Cash 0.9	Mortgages -0.2
Mortgages 1.3	Real Estate 7.0	Bonds 3.5	Long Bonds 2.5	Long Bonds 7.0	Mortgages 0.5	Cdn. Eq -0.6
Cash 1.0	EM Eq 6.6	EM Eq 2.0	Mortgages 1.8	Bonds 2.5	Bonds -0.4	Bonds -1.0
Bonds -1.2	Mortgages 6.0	Cash 0.6	Bonds 1.7	Mortgages 0.9	Long Bonds -1.5	Long Bonds -2.4
Long Bonds -6.2	Cash 0.9	Cdn. Eq -8.3	Cash 0.5	Cash 0.6	EM Eq -4.8	EM Eq -2.8
Market Portfolio[5]						
			4.9	10.4	3.9	0.9

Benchmarks

- S&P/TSX
- MSCI World (Net)[1]
- MSCI Emerging Markets (Net)[1]

- Infrastructure[2]
- REALpac/IPD Canada - All Assets[3]
- Custom Mortgage Benchmark[4]

- FTSE TMX Cda 91 day T-bill
- FTSE TMX Cda Universe
- FTSE TMX Cda LT Overall

Source: FactSet, Preqin, Greystone. As at Sep 30, 2018.
Returns in Canadian dollars, excluding Infrastructure (U.S. dollars). Gross of investment management fees. May be subject to rounding. Past performance is not necessarily a guide to future results.
[1] MSCI, net of foreign dividend withholding taxes.
[2] Infrastructure returns are the Preqin Infrastructure Quarterly Index up to Q4 2017 and are Greystone Infrastructure Fund (Canada) LP returns thereafter.
[3] Real estate returns are the REALPAC/IPD Canada Quarterly Property Index - All Assets up to its most recent publication, Q2 2018 and are Greystone Real Estate Fund Inc. returns thereafter.
[4] Custom Mortgage Benchmark: FTSE TMX Cda Short Term Overall 60%, FTSE TMX Cda Mid Term Overall 40% + 0.5% per annum.
[5] The Market Portfolio is the Greystone Balanced Plus fund.

Looking for a Multi-asset Class Solution Investment Partner?

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Greystone Managed Investments Inc.

Greystone Managed Investments Inc. is an institutional money manager with multi-asset solutions proudly serving its clients since 1988. Headquartered in Regina, with additional offices in Toronto, Winnipeg and Hong Kong, Greystone manages over C$35 billion[1] on behalf of institutional clients.

Greystone has in-house expertise in the following areas:

MULTI-ASSET
- Balanced
- Balanced Plus
- Target Date Plus
- Alternative Plus[2]

FIXED INCOME
- LDI
- Term
- Plus
- Sector

ALTERNATIVES
- Real Estate
- Infrastructure

PRIVATE DEBT
- Mortgages

PUBLIC EQUITIES
- Canadian & U.S.
- International
- Global
- China

[1] As at Sep 30, 2018.

[2] The Greystone Alternative Plus Solution is an integrated open-ended alternatives mandate where a client invests in the Greystone Infrastructure Fund (Canada) LP, the Greystone Mortgage Fund and the Greystone Real Estate Fund Inc. or the Greystone Real Estate LP Fund. Greystone holistically manages the underlying cash flows and liquidity of the allocation as well as the asset mix between the underlying strategies.

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