

RBC Global Asset Management

Economic Outlook



Andrew Sweeney, Vice President & Portfolio Manager

Phillips, Hager & North Investment Management



Central Banks to the rescue!!!



“Do you swear to calm the jittery financial markets, all the jittery financial markets and nothing but the jittery financial markets, so help you God?”

Key macro themes



Risk assets rebounded as central banks came to the rescue



Headwinds: Protectionism, cycle age, fading U.S. fiscal



Tailwinds: Central banks, global fiscal stimulus, U.S. speed limit rising



Canada limited by oil, housing, competitiveness



Late in business cycle



Recession risk substantial, but not happening yet



China slowing but government stimulus to provide temporary relief



Brexit delayed; uncertainty high

Source: RBC GAM

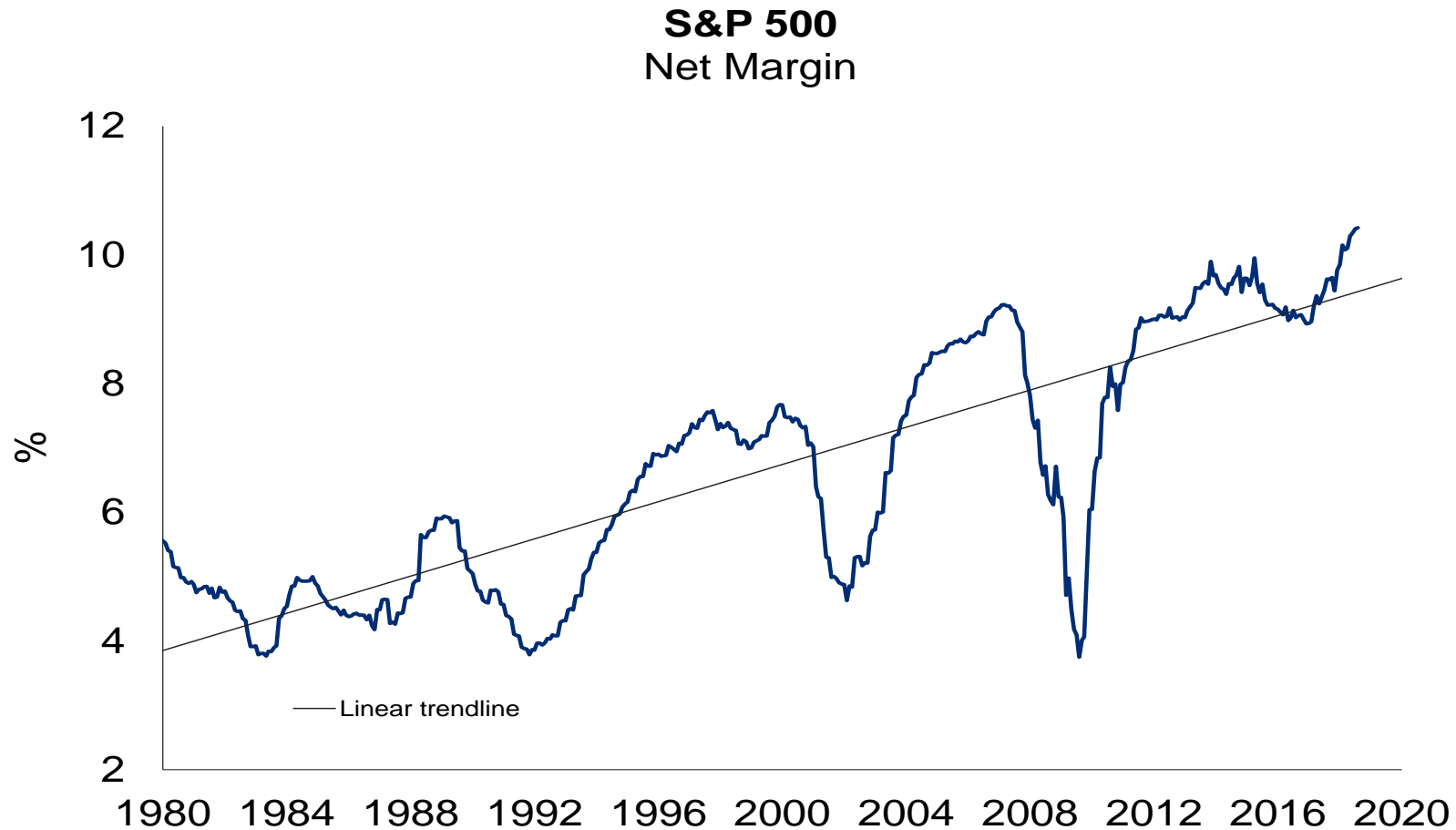
In spite of trade fears, stock market still near highs



Note: As of 8/30/2019. Source: WSJ, Haver Analytics, RBC GAM

Corporate margins running above trend

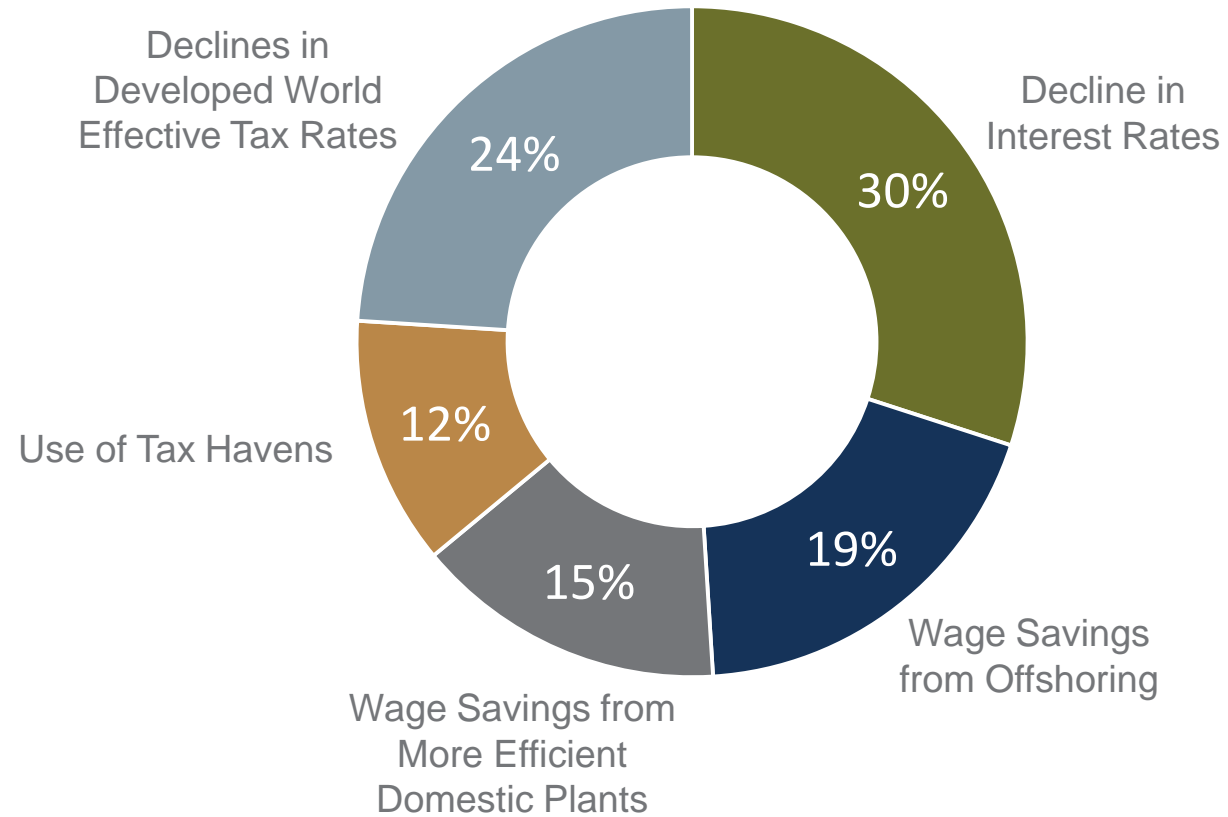
Tend To Mean Revert During Economic Contraction



Source : RBC Capital Markets, RBC GAM

How have margins expanded so much?

**S&P 500 Index Manufacturers
Sources of Profit Margin Improvement Since 2000**



Bond yields falling globally

Canada 10 year yield has fallen dramatically



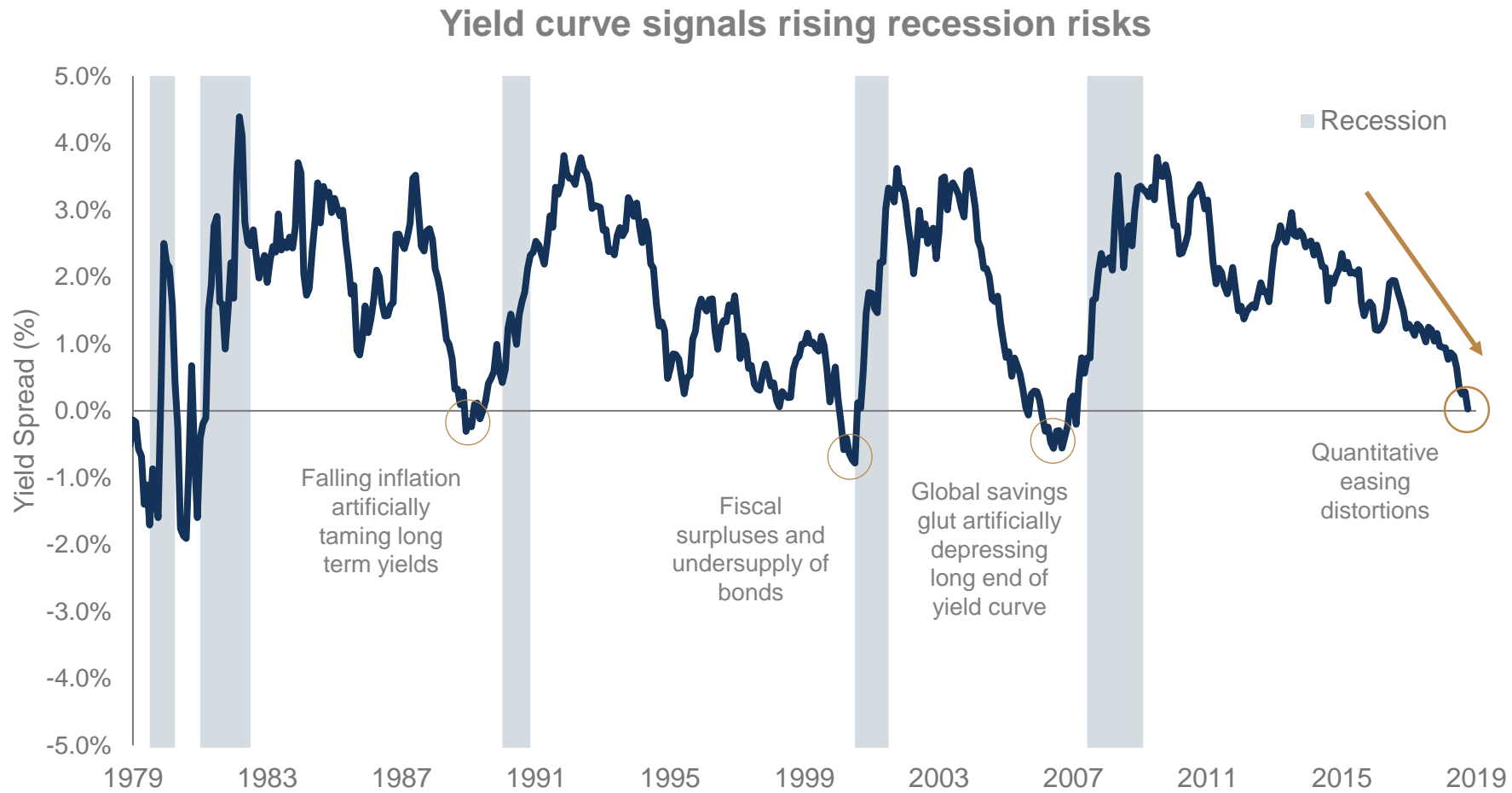
Source: Bloomberg

Developed Country Yields (%)

Country	5 Year	10 Year	30 Year
Canada	1.19	1.16	1.43
U.S.	1.33	1.46	1.95
U.K.	0.27	0.38	0.92
Japan	-0.73	-0.28	0.11
Germany	-0.92	-0.74	-0.21
France	-0.75	-0.40	0.44
Spain	-0.35	0.09	1.00
Italy	0.31	0.88	1.93

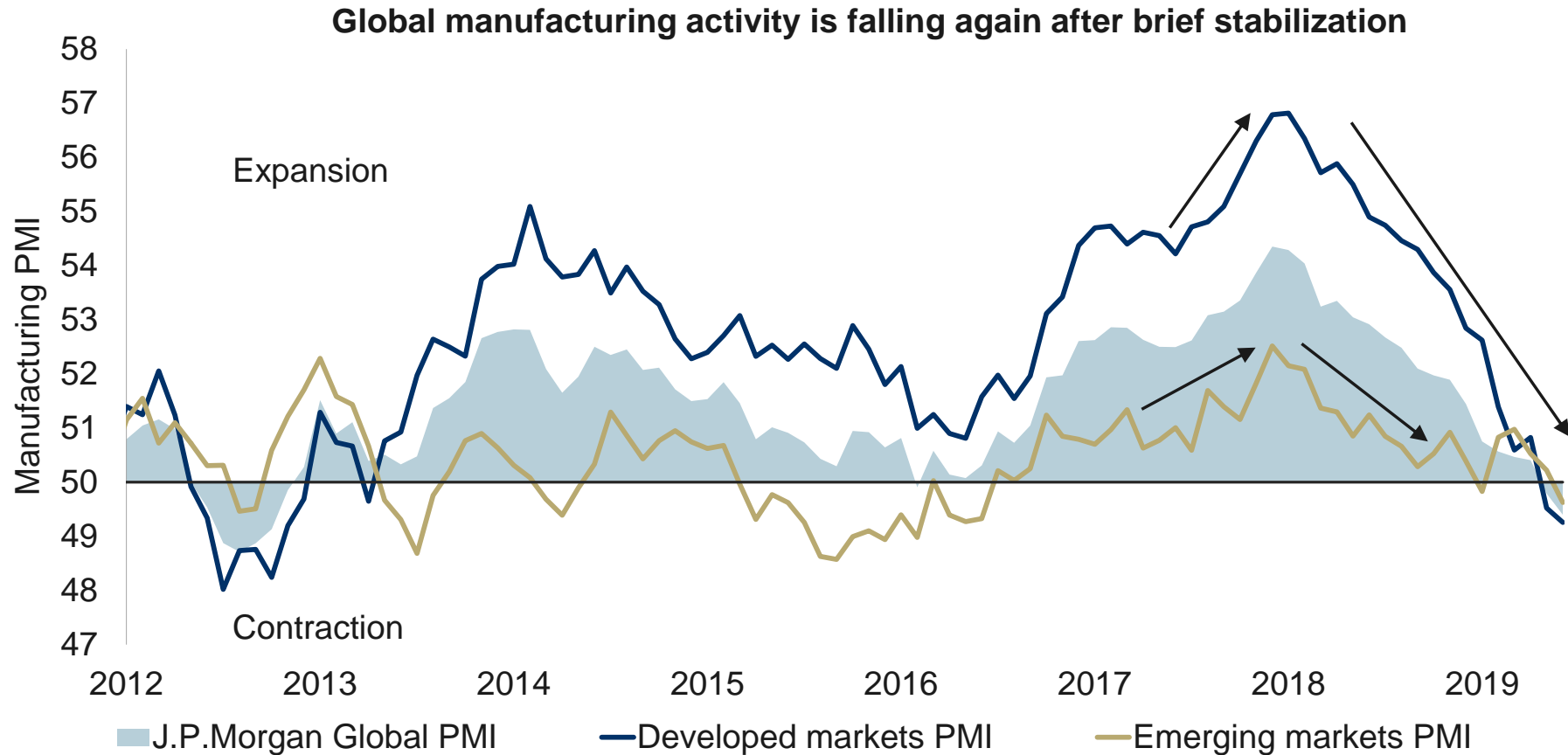
Source: Bloomberg As of August 31, 2019

Yield curve inverted: recession risk warning



Source: Bloomberg

Cyclical economic trends: Economic deceleration



Note: As of Jun 2019. PMI refers to Purchasing Managers Index for manufacturing sector, a measure for economic activity.
Source: Haver Analytics, RBC GAM

U.S. is “Late Cycle”

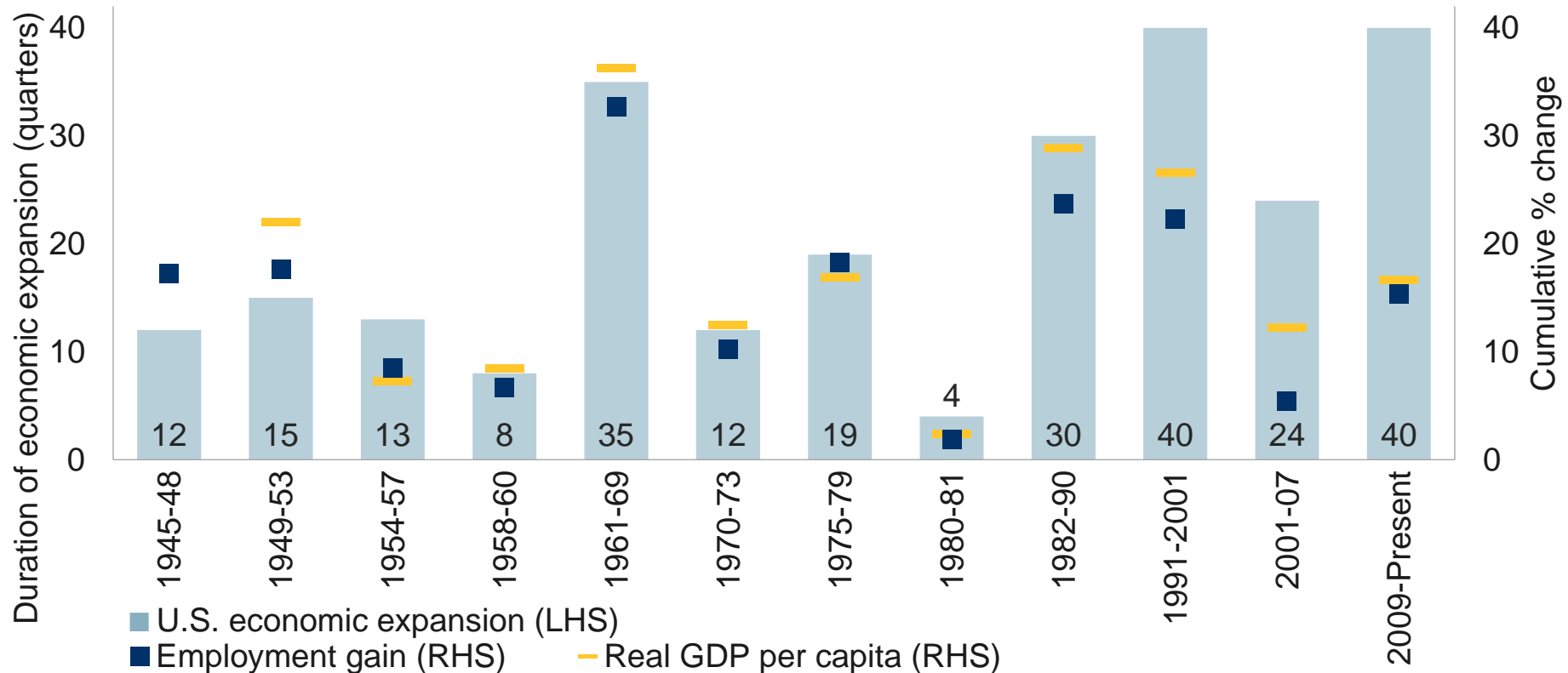
U.S. business cycle scorecard

	Start of Cycle	Early cycle	Mid cycle	Late cycle	End cycle	Recession
Consumer						
Leverage						
Business Investment						
Employment						
Corporate Profitability						
Credit						
Inventories						
Prices						
Housing						
Economic Trend						
Volatility						
Sentiment						
Economic Slack						
Equities						
Cycle Age						
Monetary Policy						
Bonds						
Scores for each stage of the business cycle	0	0	5.5	13	8.5	1.5

Note: Dark shading indicates the most likely stage of business cycle (full weight); light shading indicates alternative interpretation (0.5 weight)

U.S. achieving longest expansion / cycle is old

Current economic expansion in historical context



Note: Duration of economic expansion up to Q2 2019, cumulative employment gain as of May 2019, cumulative change in real GDP per capita as of Q1 2019. Source: NBER, Macrobond, RBC GAM

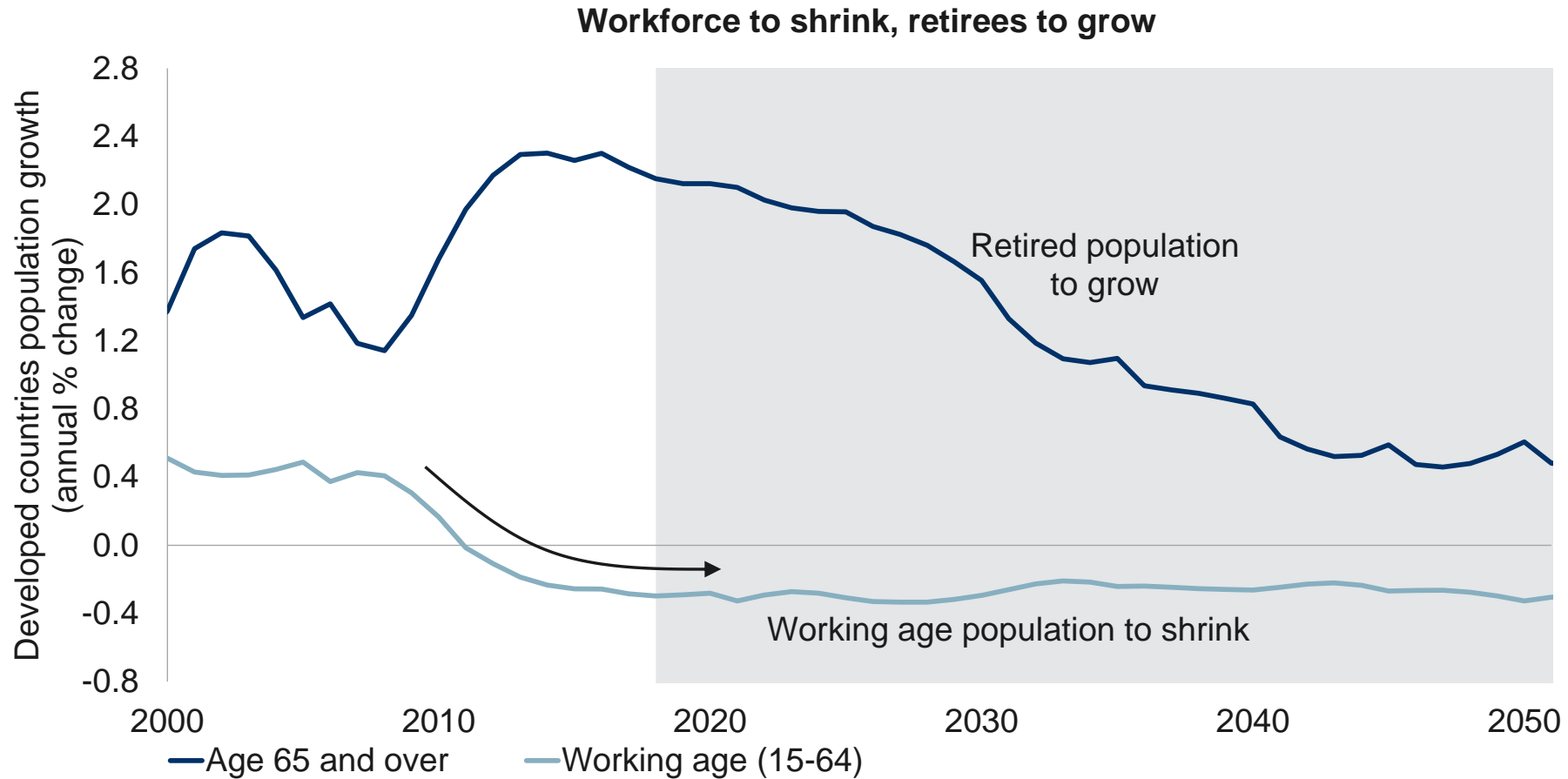


Structural headwinds to economic growth

Human factors	Economic structure	Post-crisis
<ul style="list-style-type: none"> • Demographics: <ul style="list-style-type: none"> • Slower pop. growth • Rising retired % • Decelerating gains in: <ul style="list-style-type: none"> • Education • Health • Urbanization • Rising complacency: <ul style="list-style-type: none"> • Low labor mobility • More segregated • Less risk-taking • Falling societal trust • Higher inequality 	<ul style="list-style-type: none"> • Fading globalization • Declining creative destruction: <ul style="list-style-type: none"> • Lower firm turnover • Higher firm concentration • Goods → services • Maturing EM economies <div data-bbox="975 963 1569 1035" style="background-color: #003366; color: white; text-align: center; padding: 5px;">Technology</div> <ul style="list-style-type: none"> • Running out of big new innovations? 	<ul style="list-style-type: none"> • Populism/protectionism • Secular stagnation: <ul style="list-style-type: none"> • Diminished expectations • Less business investment • Skill decay • Debt excesses: <ul style="list-style-type: none"> • Servicing • Deleveraging

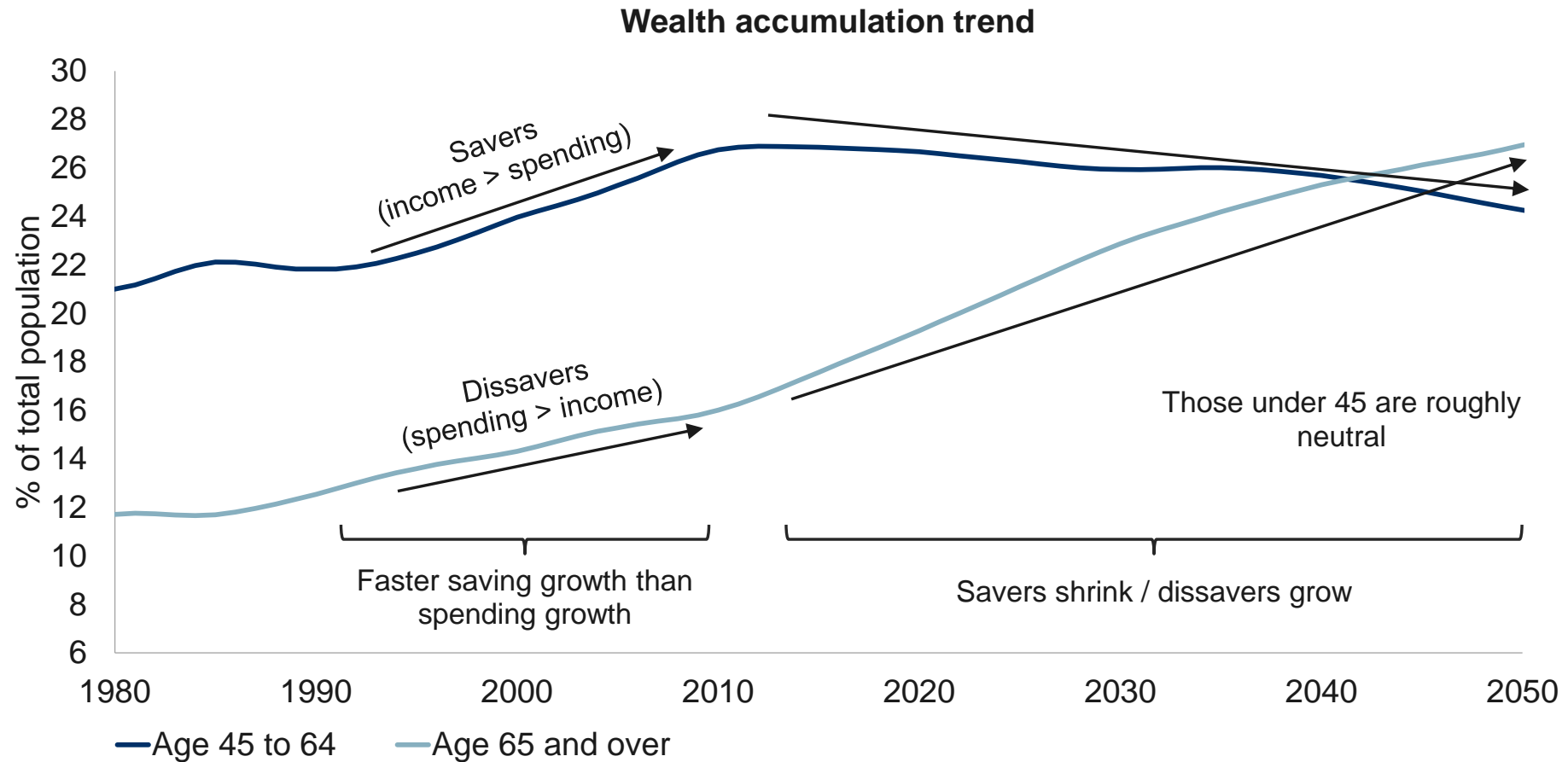
Source: RBC GAM

Adverse demographic trends



Note: Shaded area represents UN projections. Source: United Nations, Haver Analytics, RBC GAM

Composition of aging population to tilt away from savers



Note: Population of developed countries. Source: United Nations, Haver Analytics, RBC GAM

Populism → protectionism

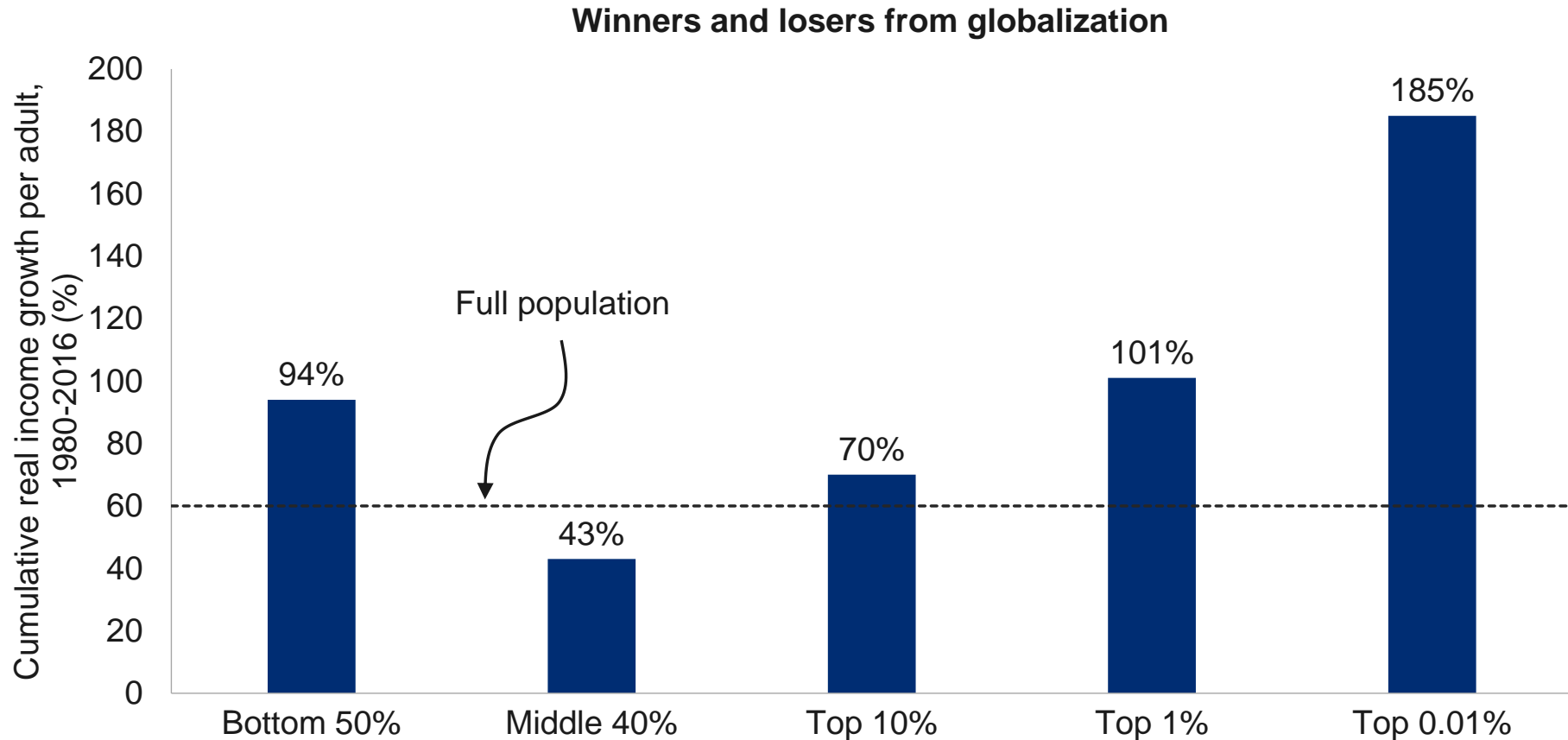
Why populism?	Policy implications	Economic implications
<ul style="list-style-type: none">• Financial crises• Slow growth era• High inequality• Globalization losers	<ul style="list-style-type: none">• Less free trade• Less immigration	<ul style="list-style-type: none">• Less economic growth• More inflation• Worse market returns

Evidence of populist attitudes

- Brexit
- Populist governments in Greece, Italy, polling elsewhere
- U.S. presidential election
- Rising protectionism, immigration fears

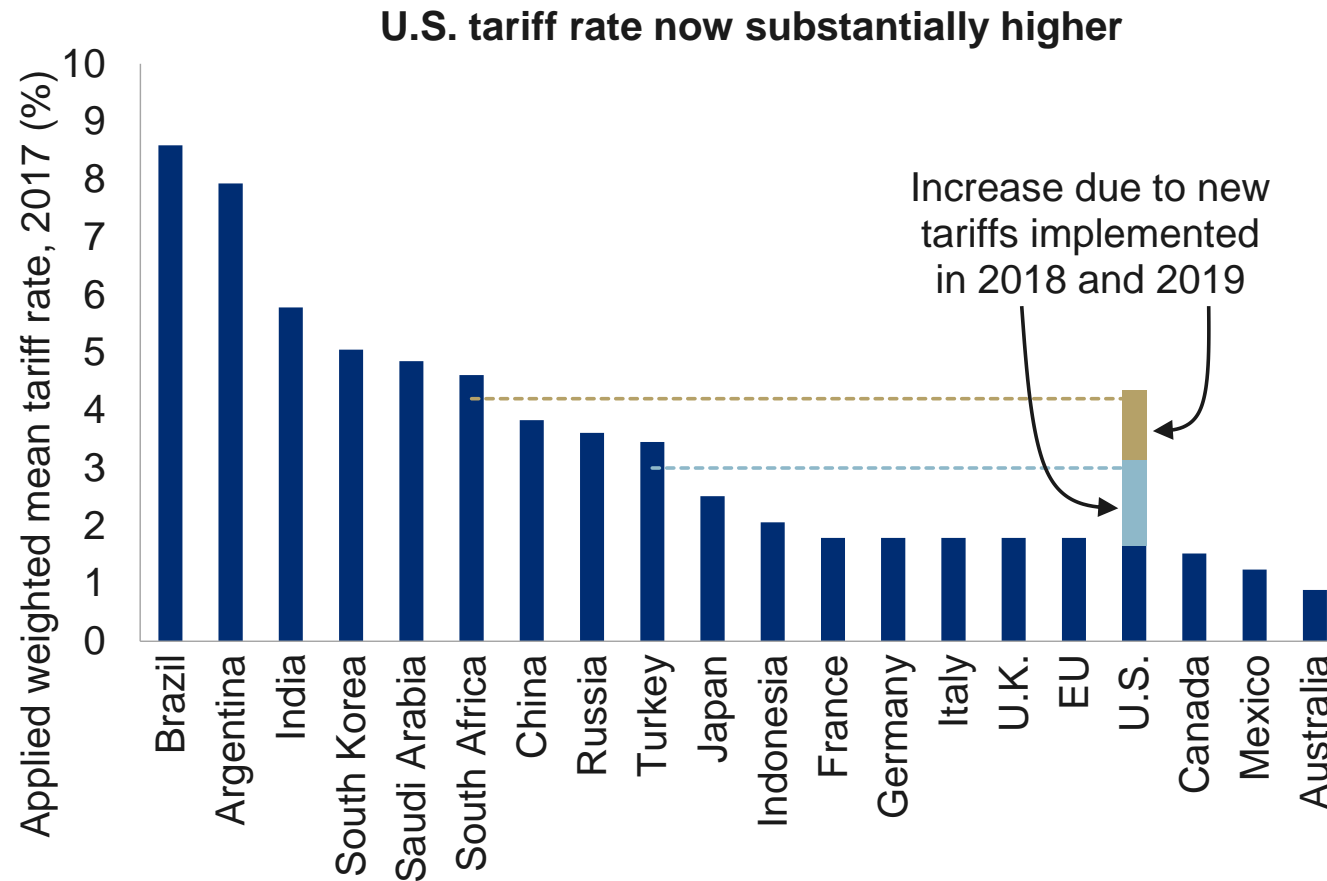
Source: RBC GAM

Increasing inequality at national level, falling inequality globally



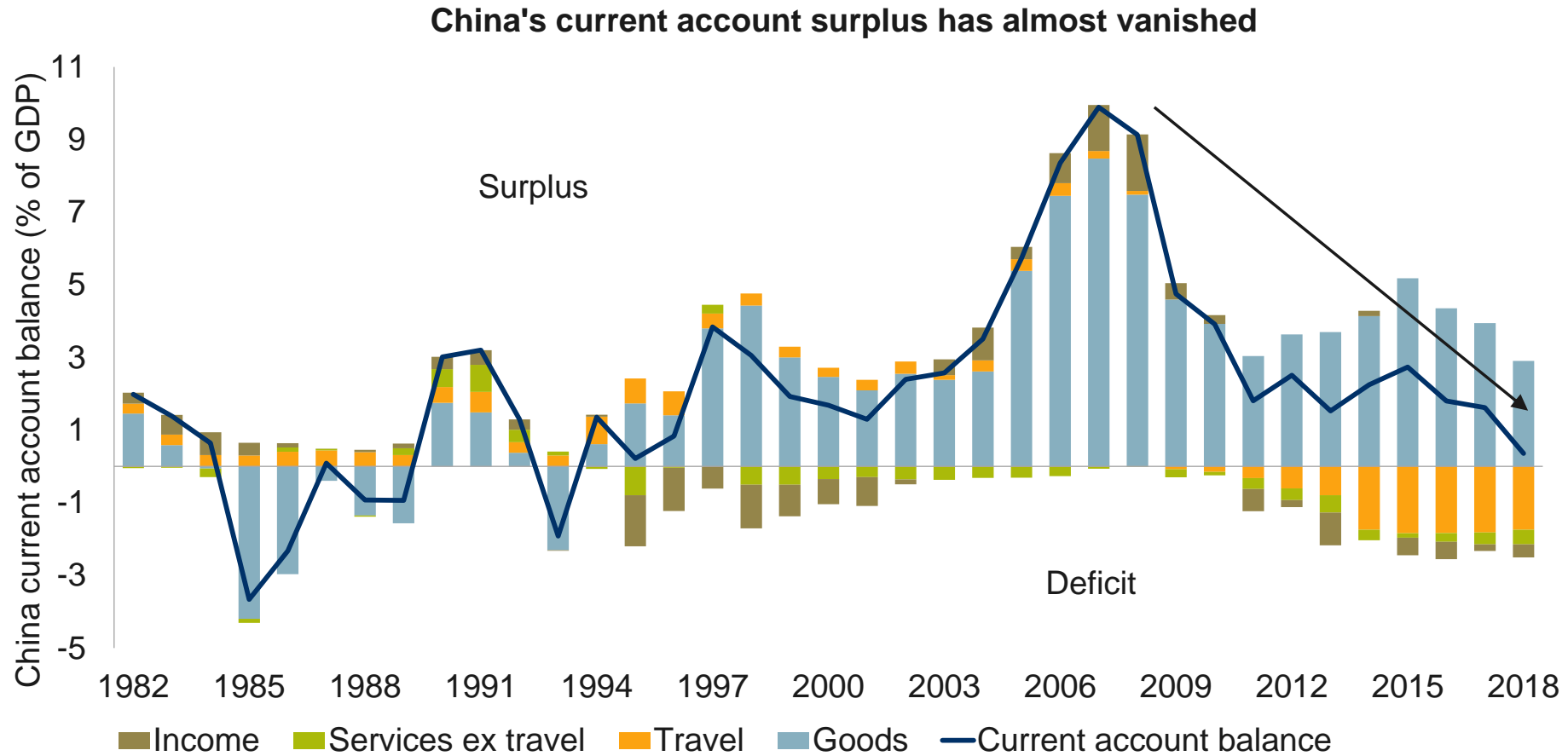
Note: Cumulative growth of average income of each income group of the world population. Source: World Inequality Database, RBC GAM

U.S. tariffs in context



Note: Applied weighted mean tariff rates for all products. Deutsche Bank estimates for 2018 and 2019 U.S. tariff rates based on additional tariffs announced up to October 2018.
Source: Deutsche Bank, World Bank, Haver Analytics, RBC GAM

China's current account surplus is nearly gone, but the goods trade surplus remains



Note: As of 2018. Source: Macrobond, RBC GAM

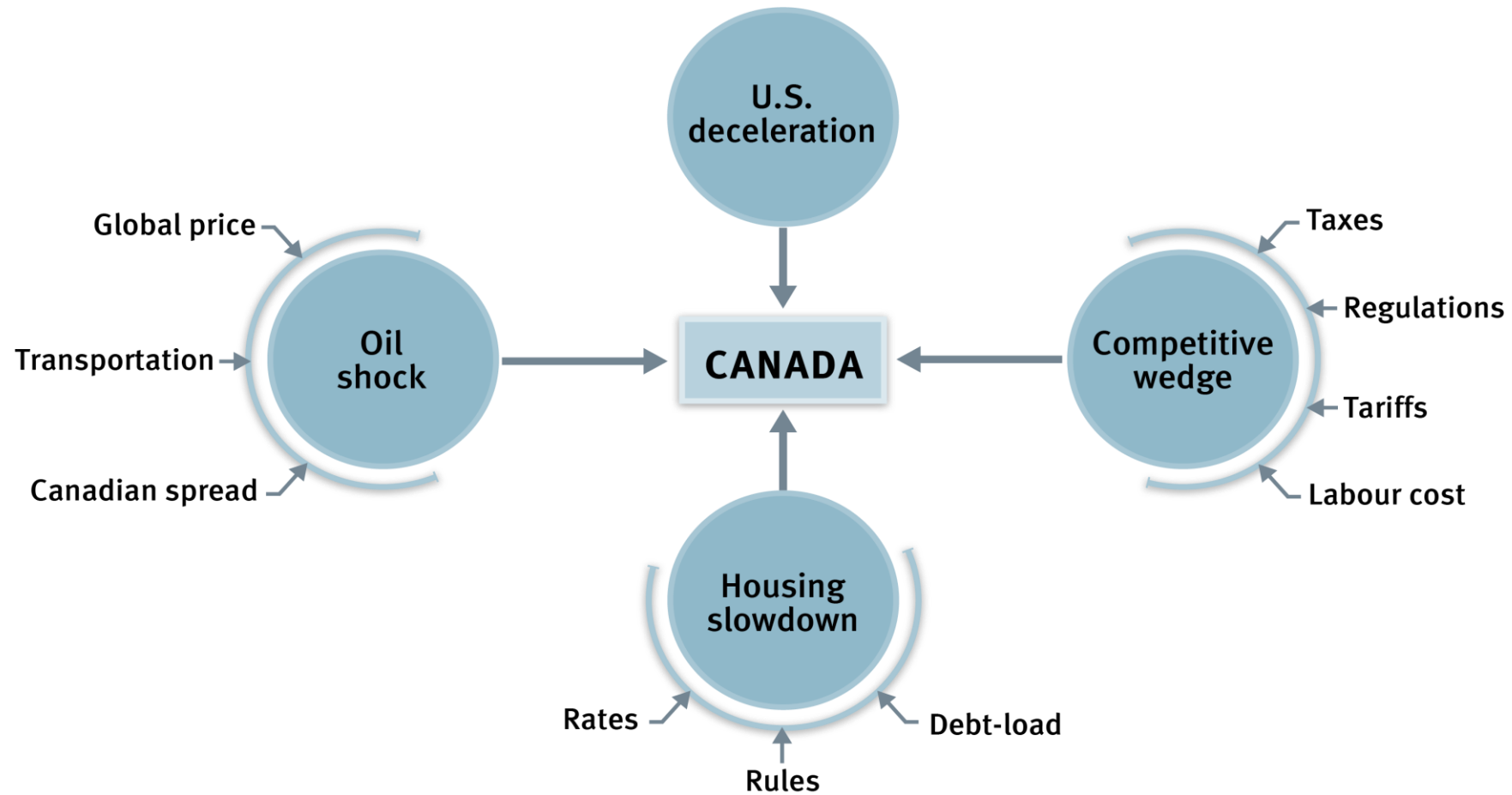
Canadian provinces operating at different speeds

Province	Current GDP growth rate (YoY % change)
Manitoba	2.4
British Columbia	2.1
Quebec	2.1
Nova Scotia	2.0
Newfoundland and Labrador	1.9
Prince Edward Island	1.9
Ontario	1.7
Saskatchewan	1.2
Alberta	1.0
New Brunswick	0.8

Note: RBC GAM estimate of provincial GDP year-over-year growth rate as of Mar 2019.

Source: Macrobond, RBC GAM

Canadian macro challenges



Source: RBC GAM

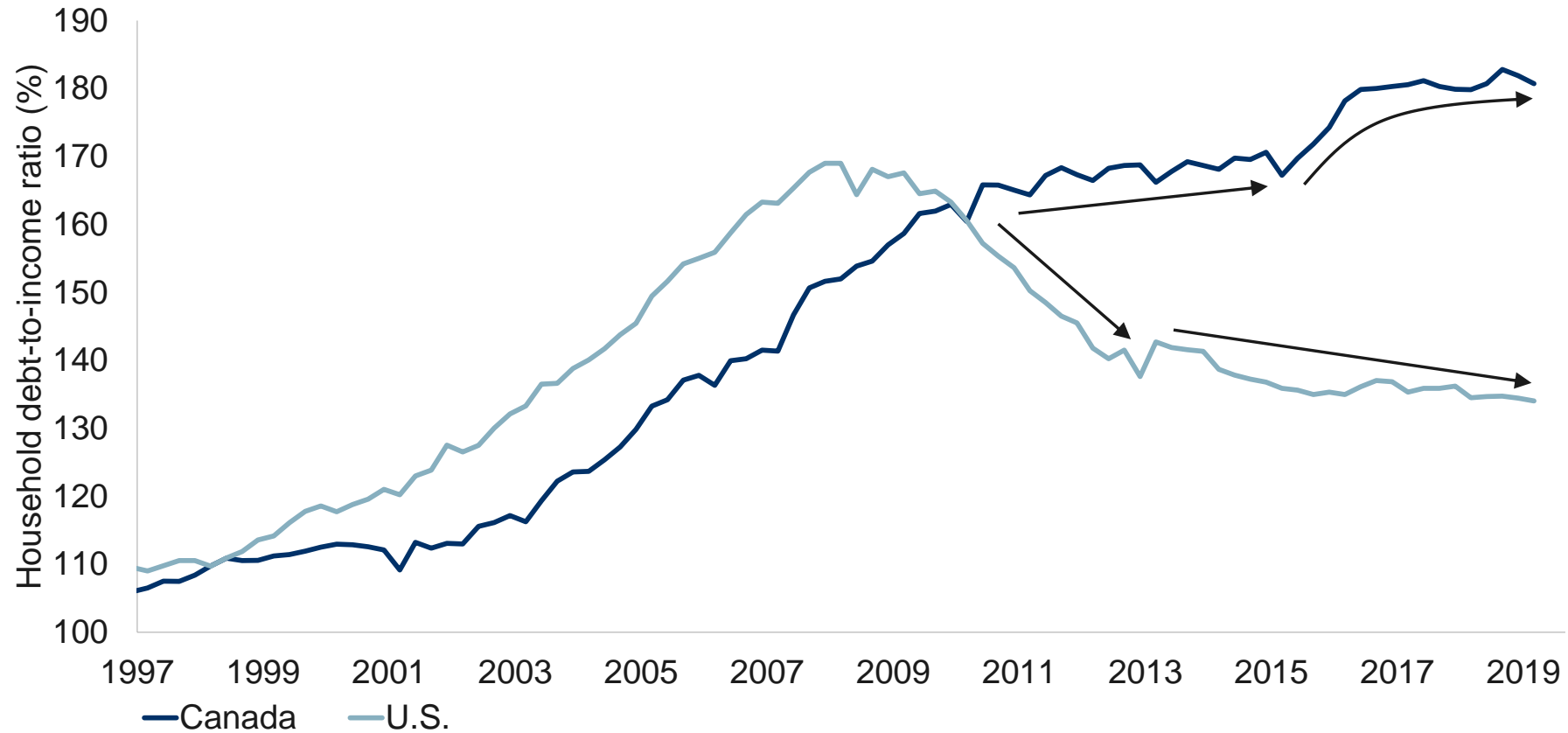
Canada is losing its competitive edge

How Canada stacks up			
Measure	Canada's international ranking (percentile)		
	2007-2008	2017-2018	Change
Public Policy	93.8	92.2	↓
Labour	92.5	92.0	↓
Innovation	91.8	84.7	↓
Composite	93.0	90.2	↓

Note: The composite ranking is a weighted average of the three measures. Ranking for each measure is an average of percentile rankings of the underlying components. Public policy is composed of World Governance Indicators, Ease of Doing Business, and Global Competitiveness Index (GCI). Labour is made up of GCI Higher Education and Training Subindex, GCI Labour Market Efficiency Subindex, and Global Human Capital Index (GHCI). Innovation comprises GCI Technological Readiness Subindex, GCI Innovation Subindex, and Global Innovation Index. GHCI 2013 data used in the calculation of the innovation measure for the 2007-2008 period. Source: GII database, Cornell, INSEAD, WIPO, World Bank, World Economic Forum, RBC GAM

Canadian households are leveraged






























Household leverage has climbed in Canada, but declined in U.S.



Note: As of Q1 2019. Source: Haver Analytics, RBC GAM

Canadian provincial elections reveal clear rightward trend

Latest provincial elections

Province	Latest election	Prior government	Latest government	Change
Newfoundland and Labrador	05/16/2019			
Prince Edward Island	04/23/2019			
Alberta	04/16/2019			
Quebec	10/01/2018			
New Brunswick	09/24/2018			
Ontario	06/07/2018			
Nova Scotia	05/30/2017			
British Columbia	05/09/2017			
Manitoba	04/19/2016			
Saskatchewan	04/04/2016			

Note: Red flag represents left-wing parties (non-BC Liberal, NDP), blue for right-wing parties (Conservatives, BC Liberals, Quebec CAQ, Alberta UCP).

Source: Wikipedia, RBC GAM

Disclosure

This document has been provided by RBC Global Asset Management (RBC GAM) for informational purposes only and may not be reproduced, distributed or published without the written consent of RBC Global Asset Management Inc. (RBC GAM Inc.). In Canada, this document is provided by RBC GAM Inc. (including Phillips, Hager & North Investment Management). In the United States, this document is provided by RBC Global Asset Management (U.S.) Inc., a federally registered investment adviser. In Europe, this document is provided by RBC Global Asset Management (UK) Limited, which is authorised and regulated by the UK Financial Conduct Authority. In Asia, this document is provided by RBC Global Asset Management (Asia) Limited, to professional, institutional investors and wholesale clients only and not to the retail public. RBC Global Asset Management (Asia) Limited is registered with the Securities and Futures Commission (SFC) in Hong Kong.

RBC GAM is the asset management division of Royal Bank of Canada (RBC) which includes RBC GAM Inc., RBC Global Asset Management (U.S.) Inc., RBC Global Asset Management (UK) Limited, RBC Global Asset Management (Asia) Limited, and BlueBay Asset Management LLP, which are separate, but affiliated subsidiaries of RBC.

This document has not been reviewed by, and is not registered with any securities or other regulatory authority, and may, where appropriate, be distributed by the above-listed entities in their respective jurisdictions. Additional information about RBC GAM may be found at www.rbcgam.com.

This document is not intended to provide legal, accounting, tax, investment, financial or other advice and such information should not be relied upon for providing such advice. The investment process as described in this document may change over time. The characteristics set forth in this document are intended as a general illustration of some of the criteria considered in selecting securities for client portfolios. Not all investments in a client portfolio will meet such criteria. RBC GAM takes reasonable steps to provide up-to-date, accurate and reliable information, and believes the information to be so when printed. RBC GAM reserves the right at any time and without notice to change, amend or cease publication of the information.

Any investment and economic outlook information contained in this document has been compiled by RBC GAM from various sources. Information obtained from third parties is believed to be reliable, but no representation or warranty, express or implied, is made by RBC GAM, its affiliates or any other person as to its accuracy, completeness or correctness. RBC GAM and its affiliates assume no responsibility for any errors or omissions.

All opinions and estimates contained in this document constitute RBC GAM's judgment as of the indicated date of the information, are subject to change without notice and are provided in good faith but without legal responsibility. Interest rates and market conditions are subject to change.

Return estimates are for illustrative purposes only and are not a prediction of returns. Actual returns may be higher or lower than those shown and may vary substantially over shorter time periods. It is not possible to invest directly in an unmanaged index.

A note on forward-looking statements

This document may contain forward-looking statements about future performance, strategies or prospects, and possible future action. The words "may," "could," "should," "would," "suspect," "outlook," "believe," "plan," "anticipate," "estimate," "expect," "intend," "forecast," "objective" and similar expressions are intended to identify forward-looking statements. Forward-looking statements are not guarantees of future performance. Forward-looking statements involve inherent risks and uncertainties about general economic factors, so it is possible that predictions, forecasts, projections and other forward-looking statements will not be achieved. We caution you not to place undue reliance on these statements as a number of important factors could cause actual events or results to differ materially from those expressed or implied in any forward-looking statement made. These factors include, but are not limited to, general economic, political and market factors in Canada, the United States and internationally, interest and foreign exchange rates, global equity and capital markets, business competition, technological changes, changes in laws and regulations, judicial or regulatory judgments, legal proceedings and catastrophic events. The above list of important factors that may affect future results is not exhaustive. Before making any investment decisions, we encourage you to consider these and other factors carefully. All opinions contained in forward-looking statements are subject to change without notice and are provided in good faith but without legal responsibility.

® / TM Trademark(s) of Royal Bank of Canada. Used under licence.

© RBC Global Asset Management Inc., 2019

Publication date: July 5, 2019