RBC Global Asset Management

Economic outlook

SUMMER 2024

Falling inflation tees up rate cuts

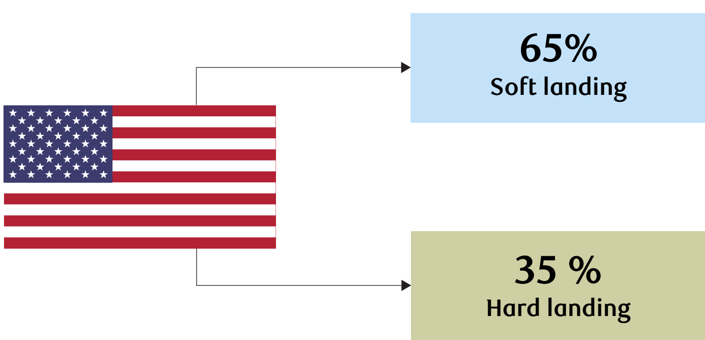
Eric Lascelles
Managing Director & Chief Economist
RBC Global Asset Management Inc.

The global economy has again demonstrated its impressive resilience by surviving another quarter of elevated interest rates. This reinforces our opinion that a recession can be avoided over the year ahead. We now assign a 65% likelihood that the economy manages a soft landing versus just a 35% risk of a hard landing – another term for a recession (Exhibit 1). The business cycle appears to be in the mid- to late-cycle phase, consistent with about two to five years of further economic growth.

After inflation staged an unwelcome revival in early 2024, it is heartening that the latest data (Exhibit 2) points to the resumption of the prior downward trend. Inflation is still too high, but it is becoming incrementally less so.

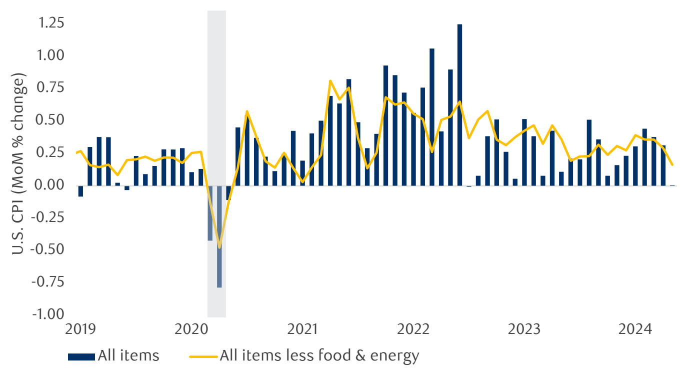
In turn, while interest-rate-cut expectations have been delayed relative to expectations at the beginning of the year, several central banks have already begun their monetary easing, and most of the rest are in a position to cut rates later in the year. The pace of rate cutting should be only gradual

Exhibit 1: Soft landing still most likely for the U.S., but not certain



Source: RBC GAM

Exhibit 2: U.S. CPI monthly trend is decelerating again



Note: As of May 2024. Shaded area represents recession. Source: BLS, Macrobond, RBC GAM given the resilience demonstrated by the economy and inflation, but it nevertheless promises to significantly reduce the main headwind blowing against economic growth over time.

U.S. growth is enduring despite concerns around a handful of softening indicators (Exhibit 3). The consumer should be able to weather rate-related pressures. Granted, the U.S. economy is looking less exceptional in the context of its peers than it did in 2023. This is in part due to a modest deceleration in the U.S., and in part because much of the rest of the developed world has managed a slight acceleration.

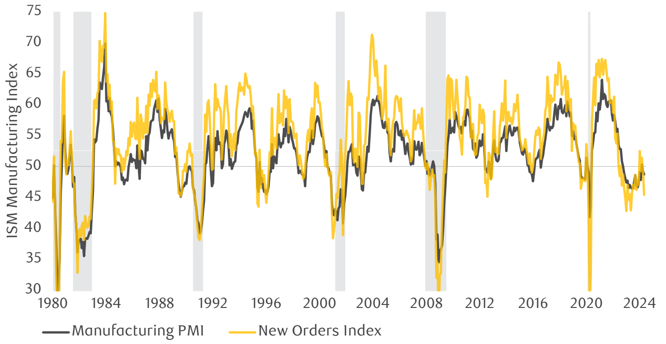
Downside risks cannot be ignored, highlighting why a hard landing remains a possibility. Interest-rate-related pain continues to mount in some corners of the economy and it may worsen still. Moreover, the risk remains that inflation will become stuck at elevated levels. Geopolitical risks are also higher than normal: the November U.S. election, Middle East conflict, China-U.S. tensions and the war in Ukraine together pose challenges for continued global stability and low inflation.

For markets, every major asset class has a measure of allure right now. Cash offers its highest yield in over a decade, though this is now beginning to ebb. Fixed income similarly operates with coupons near their highest in a decade, offers the potential for small capital gains as central banks cut rates and serves as portfolio protection should the economy stumble. Equities, meanwhile, normally provide moderate returns at this point in the business cycle. Valuations are somewhat stretched in the U.S., but reasonable elsewhere. The fact that the risk premium between stocks and bonds is smaller than normal makes the case for our slight bond overweight relative to equities.

Economy continues to advance

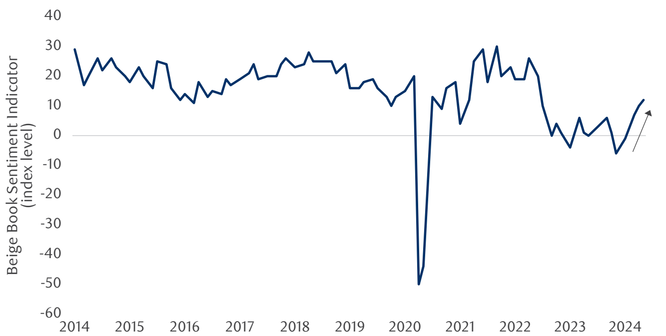
Economic activity continues to advance, a welcome development given lingering fears of a recession and the persistence of high interest rates. This progress is visible across a wide range of indicators, from first-quarter GDP figures that were reliably positive across the developed world; to descriptive surveys like the Fed's Beige Book, which confirms growth in the U.S. (Exhibit 4); to real-time alternative indicators such as the favourable signal emitted by an X (formerly Twitter) -based economic sentiment index (Exhibit 5).

Exhibit 3: U.S. manufacturing is wobbling



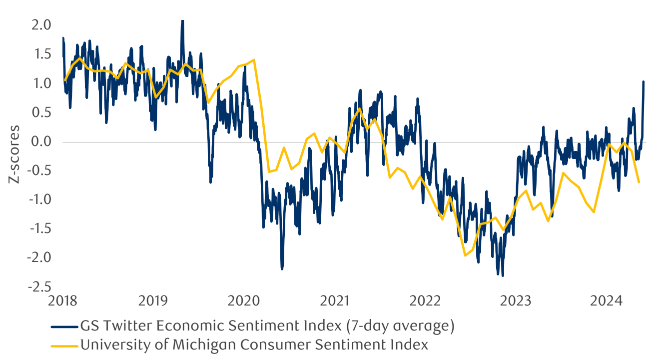
Note: As of May 2024. Shaded area represents recession. Source: ISM, Macrobond, RBC GAM

Exhibit 4: Beige Book Sentiment Indicator shows a revival



Note: As of May 2024. The indicator quantifies the sentiment of local contacts by assigning different weights to a spectrum of positive and negative words used to describe overall economic conditions in the Fed Beige Book. Source: U.S. Federal Reserve, RBC GAM

Exhibit 5: Twitter Economic Sentiment in the U.S. suggests more optimism ahead

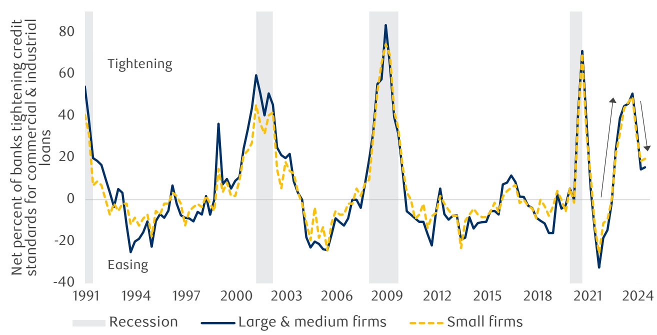


Note: Twitter Economic Sentiment Index as of 05/29/2024, University of Michigan Consumer Sentiment as of May 2024. Source: Goldman Sachs Global Investment Research, University of Michigan, Macrobond, RBC GAM

Our economic modelling indicates that growth should be sustained over the year ahead. A number of the recession signals that had been blinking red last year have reversed, including now-easing lending standards (Exhibit 6), newly rising profit margins and reviving global trade (Exhibit 7). References to the word "recession" in S&P 500 Index company transcripts have continued to fall and are now at their lowest level in two years (Exhibit 8). These developments articulate the case for a soft landing over a hard landing.

The U.S. economy was strong for much of 2023, enjoying the fruits of robust consumer spending, stronger-than-expected fiscal stimulus and population growth (Exhibit 9). Meanwhile, most of the rest of the developed world effectively stagnated during that period (Exhibit 10).

Exhibit 6: U.S. business-lending standards are reversing helpfully

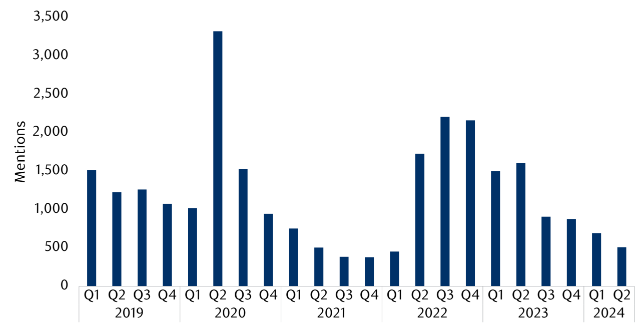


Note: April 2024 Senior Loan Officer Opinion Survey on Bank Lending Practices. Source: Federal Reserve Board, Macrobond, RBC GAM

Exhibit 7: Global trade is reviving

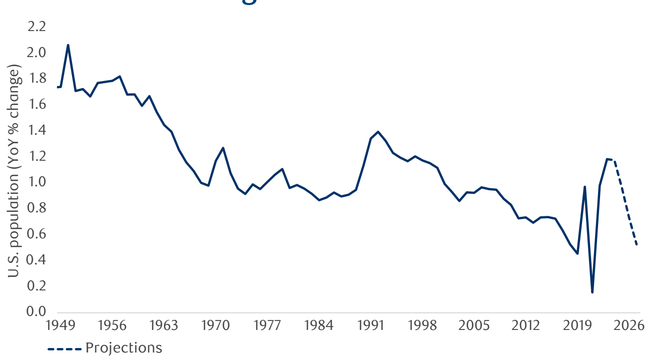
Note: As of Mar 2024. Shaded area represents U.S. recession. Source: CPB Netherlands Bureau for Economic Policy Analysis, Macrobond, RBC GAM

Exhibit 8: Mentions of "recession" in S&P 500 company transcripts have fallen steadily



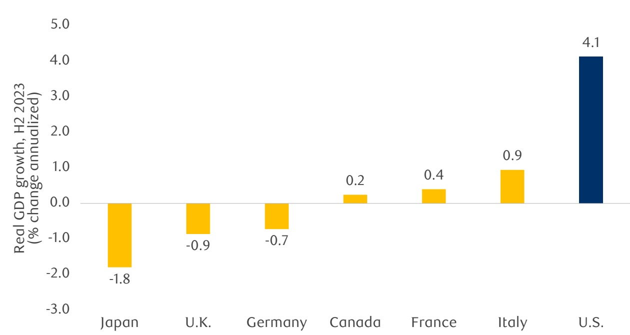
Note: As of Q2 2024 (partial data used for the quarter). Includes transcripts from all investor calls, investor days and capital markets days for S&P 500 companies. Source: Bloomberg, RBC GAM

Exhibit 9: U.S. population boom driven by undocumented immigrants



Note: Data for 2022-2027 estimated based on RBC GAM assumptions. Source: U.S. Census Bureau, Congressional Budget Office, Macrobond, RBC GAM

Exhibit 10: U.S. growth exceptionalism



Source: Macrobond, RBC GAM

But that U.S. economic exceptionalism appears to be fading in 2024, in part as fiscal outlays stabilize. At the same time, other developed economies have accelerated from effective stagnation to a moderate clip. The eurozone, the UK and Canada all recorded improved GDP growth in the first quarter of 2024, alongside an assortment of other upgraded economic indicators. This convergence can perhaps best be conveyed by the fact that global economic surprises are no longer more negative than in the U.S. (Exhibit 11).

Updated growth forecasts

You wouldn't think that economic growth has materially converged between the U.S. and several other developed countries simply by looking at their respective 2024 GDP forecasts. The U.S. is still anticipated to significantly outpace the rest, with 2.4% growth versus 1.3% in Canada, and just 0.9% in the UK and 0.8% in the eurozone.

But those figures exaggerate the divide, as the U.S. managed such extraordinary growth in late 2023 (and the others experienced such pitiful stagnation) that the economic handoff into 2024 relatively flatters U.S. growth this year. In actuality, we anticipate quite a similar growth rate of just under 2% annualized per quarter across the entire set of countries.

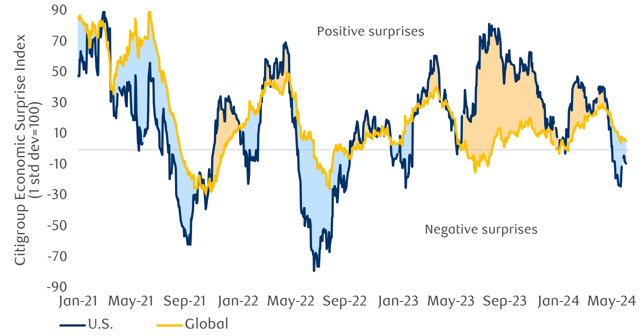
Providing further context, the 2024 U.S. growth outlook remains unchanged from a quarter ago while the rest of the developed world enjoyed an approximately half-percentage-point forecast upgrade.

Our growth forecasts are mostly a bit above the consensus outlook, informed by the view that a recession can be avoided, that inflation can likely descend somewhat further, and that interest-rate cuts can provide some assistance to the economy (Exhibit 12).

For 2025, the economic outlook remains largely the same as a quarter ago and is approximately on consensus. Modest growth stabilizes unemployment rates at healthy but not rock-bottom levels, allowing inflation to fall further. There is scope for growth to pick up somewhat over the latter part of the year as interest rates continue their descent.

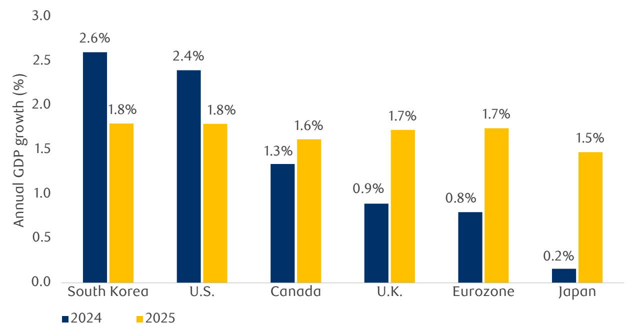
In emerging markets, the 2024 growth outlook has improved slightly and is ahead of the consensus by virtue of superior expectations for Chinese and Indian growth (Exhibit 13). Growth should then decelerate somewhat into 2025.

Exhibit 11: Global economic surprise gap reverses



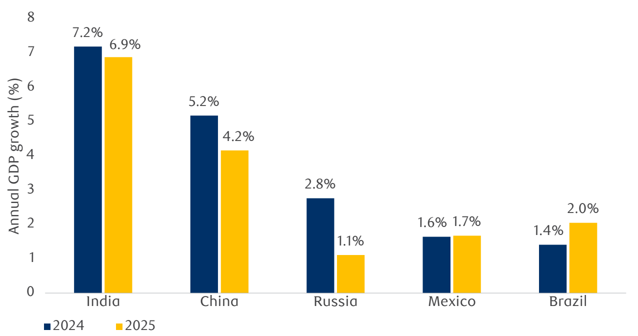
Note: As of 06/03/2024. Source: Citigroup, Bloomberg, RBC GAM

Exhibit 12: RBC GAM GDP forecast for developed markets



Note: As of 05/30/2024. Source: RBC GAM

Exhibit 13: RBC GAM GDP forecast for emerging markets



Note: As of 05/30/2024. Source: RBC GAM

Inflation begins to settle, again

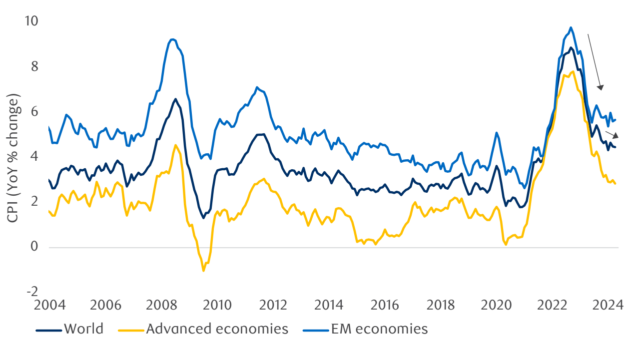
After impressive progress between the middle of 2022 and the end of 2023, inflation proved somewhat stickier over the first several months of 2024 (Exhibit 14). This was especially true in the U.S., but also visible in other markets.

Inflation's flare resulted from higher gasoline prices, still-robust service-sector inflation and – in the U.S. – some seasonal distortions in the first quarter. It is undeniably a more difficult path downward for inflation if economies manage to avoid recession, as they have so far done.

The good news is that, since that unwelcome spurt, inflation has tentatively begun to decline again. The April and May inflation numbers have improved, and real-time inflation data suggests that future months should also manage incremental improvements (Exhibit 15).

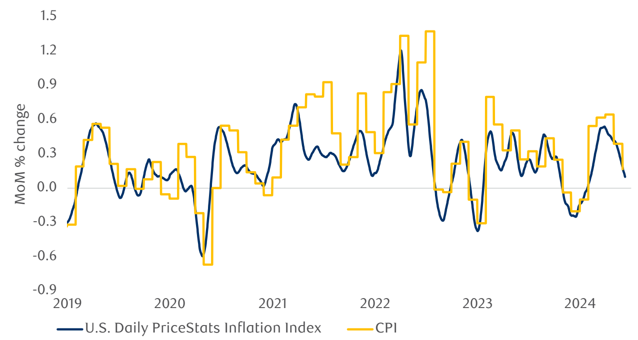
Although labour markets remain tight, wage growth is gradually decelerating from robust rates (Exhibit 16). The largest single driver of inflation – shelter costs – has room to continue slowing as lengthy lags play out. Non-shelter inflation can probably ease somewhat as insurance inflation peaks – a view motivated by the component's historically lagged relationship to broader price pressures, and by the reversal of some of the acute factors that recently drove insurance costs so high (Exhibit 17).

Exhibit 14: Global inflation has declined but remains sticky



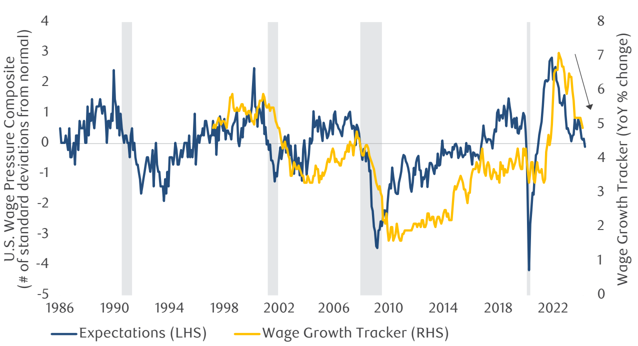
Note: As of Apr 2024. Source: Haver Analytics, Macrobond, RBC GAM

Exhibit 15: Real-time inflation continues to fall



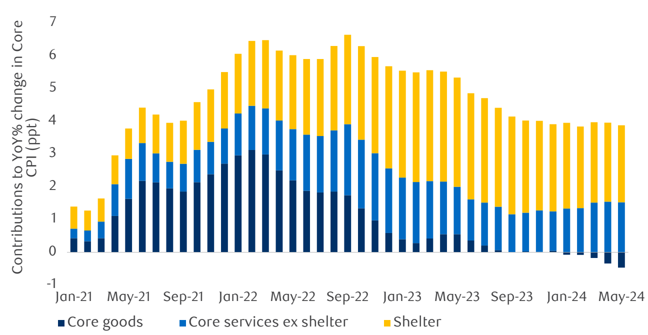
Note: PriceStats Inflation Index as of 05/31/2024, CPI as of May 2024. Source: State Street Global Markets Research, RBC GAM

Exhibit 16: Wage pressure in U.S. is easing



Note: Atlanta Fed Wage Growth Tracker as of Mar 2024, wage expectations as of May 2024. Wage Pressure Composite constructed using business intentions to raise wages. Shaded area represents recession. Source: Macrobond, RBC GAM

Exhibit 17: Shelter and core services are now the drivers of inflation in U.S.



Note: As of May 2024. Source: BLS, Haver Analytics, Macrobond, RBC GAM

There is evidence that more conservative consumers are starting to erode corporate pricing power, with the result that retail-level price cuts are becoming more common: This trend is another aid for inflation in the coming months, if less celebrated in C-suites.

Our 2024 inflation forecast has increased for the U.S. given recent upside inflation surprises, but it remains largely unchanged elsewhere. This is to say: Inflation should remain too high in 2024, but on a downward trend across the remainder of the year (Exhibit 18). We further assume that it takes a significant part of 2025 to bring inflation sustainably down to the realm of central banks' 2.0% targets.

Note that the lower inflation numbers recently achieved in the UK and eurozone versus North America largely reflect differences in how inflation is defined. The critical difference is that the U.S. and Canada include shelter costs in their inflation indexes, whereas the European nations do not.

Central banks start cutting

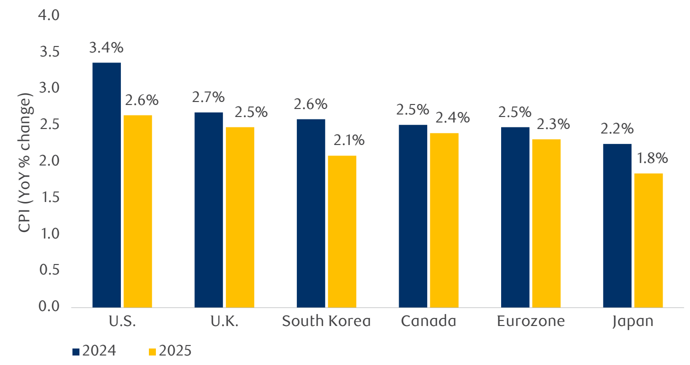
Policy rates are extremely high by the standards of the past decade and a half, and with good reason given the recent inflation shock. But now, with inflation declining, central banks are beginning to ease policy rates.

A number of emerging-market central banks have already begun the downward journey. This is an important development, as they were a helpful leading indicator on the way up. A mounting number of developed-world central banks including the European Central Bank, the Bank of Canada, the Swiss National Bank and Sweden's Riksbank have also begun their rate-cutting journey (Exhibit 19).

The Bank of England could begin easing as soon as August after the UK's national elections take place. The U.S. Federal Reserve (Fed) is dragging its heels given that inflation is higher there than elsewhere, but it is nevertheless plausibly on track for some exploratory rate cutting this fall, possibly as early as in September (Exhibit 20).

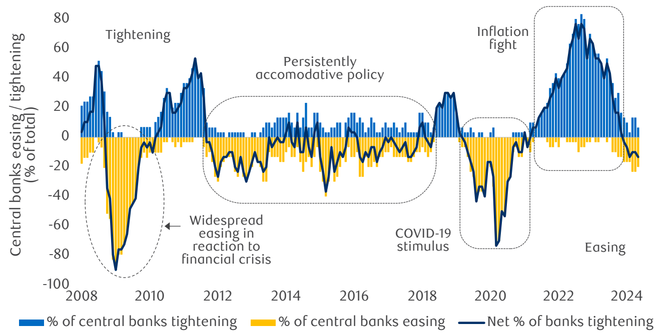
This broadly based pivot is momentous, as it is high interest rates that have constituted the primary threat to the global economy. Beginning the process of removing that threat is therefore quite helpful, despite a lag until the full benefit is felt.

Exhibit 18: RBC GAM CPI forecast for developed markets



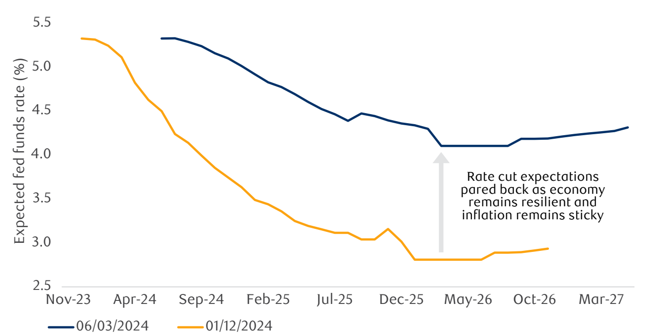
Note: As of 05/30/2024. Source: RBC GAM

Exhibit 19: Central banks are pivoting to rate cuts



Note: As of 05/31/2024. Based on policy rates for 30 countries. Source: Haver Analytics, RBC GAM

Exhibit 20: Market shaves off a number of rate cuts in 2024



Note: As of 06/03/2024. Source: Bloomberg, RBC GAM

Two caveats are in order.

First, it would be foolish to suggest that the trajectory for central banks can be mapped out far in advance. There have already been major revisions to expectations just this year, with far less easing anticipated today than at the beginning of 2024. Stubborn inflation and resilient growth have led to delays. There will certainly be more plot twists on the way to lower policy rates. But, as a general idea, central banks credibly want to make interest rates lower and believe they can begin to do so over the remainder of 2024.

Second, contrary to the usual rate-cutting experience, this cycle should be gradual. There isn't the traditional catalyst of a recession forcing central banks into emergency rate cuts, and inflation remains too high at the moment. Central banks are therefore likely to ease in limited 25-basis-point increments, and not at every meeting. It is possible that extended pauses could be interspersed across the cycle.

Amid this uncertainty and imprecision, it is worth keeping in mind that a "neutral" policy rate is likely considerably lower than current levels. Unavoidably, the exact level is also uncertain. In our view, a neutral North American policy rate might be as low as 2.00% or as high as 3.50%. But, either way, there should be scope for multiple percentage points of rate cutting from here. That should deliver relief for borrowers and a capital gain for bondholders.

It should be noted that very little of what has been written so far applies to Japan, which is on a very different trajectory. Inflation in Japan rose with a considerable lag, and interest rates are therefore still in the process of reviving from an exceedingly low starting point. That journey continues, with the country's 10-year bond yield only recently rising above 1.00% for the first time in more than a decade.

High uncertainty persists

It remains a time of high macroeconomic uncertainty. Part of this relates to the possibility that inflation and/or growth could simply follow a path that differs from our base case scenario, even absent an exogenous shock. Much of the remaining risk relates to geopolitical uncertainty – i.e. the possibility of an exogenous shock causing the economy to deviate from its trend.

On the pure forecasting uncertainty side, there remains the risk – thankfully diminishing – of a recession. Interest rates remain restrictive (Exhibit 21), and these impact the economy with long and variable lags. There is evidence of pain mounting in some quarters, with household-loan delinquencies in the U.S. rising significantly (Exhibit 22). Fortunately, a more holistic assessment of American consumers indicates that they are mostly fine, with few job losses (Exhibit 23), rising wages and rising wealth via the advancing stock market.

The fact that U.S. small-business owners are less optimistic about their prospects is a possible sign of trouble brewing (Exhibit 24). But a counterpoint is that small businesses have long expressed more pessimism than larger businesses, and from an investment standpoint it is large businesses that make up most of the stock market.

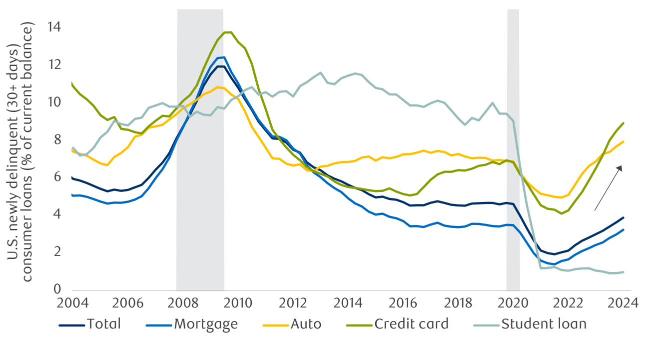
Certain recession signals continue to flash red, most prominently the fact that the U.S. yield curve remains inverted. But many other signals are no longer pointing to a recession, or now waffle on the subject. All told, we figure the risk of a U.S. recession over the coming year is down to about 35% – two to three times higher than normal, but nevertheless an unlikely outcome.

On the inflation front, there remains a risk that inflation gets stuck at an elevated level. We ultimately view this as unlikely given signs that inflation is declining again, and due to various favourable forces that were discussed earlier.

Exhibit 21: Bond yields rise on rate-cut delay as inflation proves to be sticky

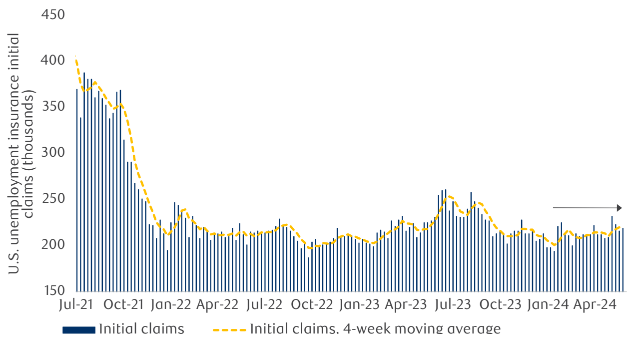
Note: As of 05/31/2024. Shaded area represents recession. Source: U.S. Treasury, Macrobond, RBC GAM

Exhibit 22: U.S. consumer-loan delinquency is now rising



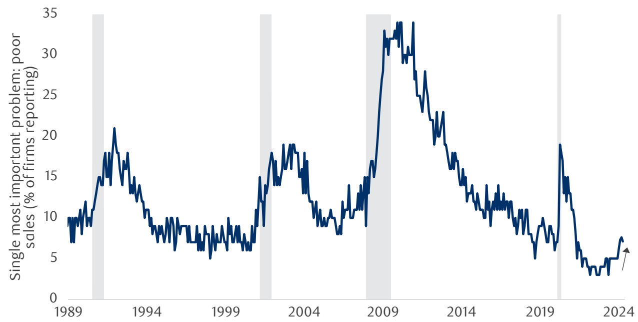
Note: As of Q1 2024. Shaded area represents recession. Source: FRBNY, Macrobond, RBC GAM

Exhibit 23: U.S. jobless claims remain low



Note: As of the week ending 05/25/2024. Source: DOL, Macrobond, RBC GAM

Exhibit 24: Poor sales have started to worry small businesses



Note: As of Apr 2024. Shaded area represents recession. Source: NFIB Small Business Economic Survey, Macrobond, RBC GAM

But there isn't much precision to the analysis, and it must be conceded that the first-quarter inflation revival wasn't entirely anticipated, either. There are thus scenarios in which inflation remains too high and interest rates must also remain elevated, with the possibility that the economy suffers for it.

Turning to geopolitical risks, we see a familiar set of issues:

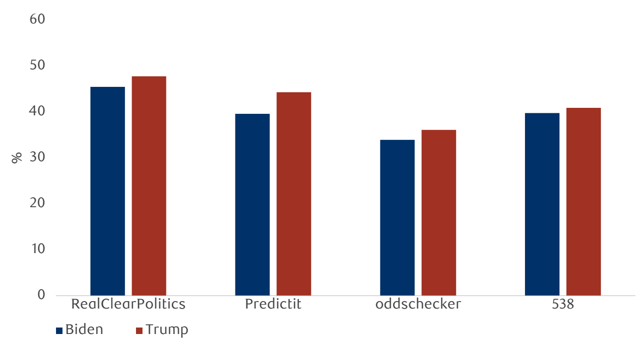
- The war in Ukraine is still unresolved and so grinds on. The fate of the global price of oil, natural gas and agricultural products lies partially in the balance.
- China-U.S. relations remain challenging, and probably will for years. The White House recently levied further tariffs on Chinese imports, with a particular focus on strategic green industries. We see no obvious end in sight to these economic frictions (and the possibility of a further deterioration depending on the outcome of the upcoming U.S. election), with the result that global growth may be incrementally dimmed and global inflation may be incrementally higher than otherwise.
- The Middle East remains conflict-ridden, with economic consequences that include a higher risk premium embedded within oil prices and trade-impeding missile strikes in the Red Sea, with the result that supply-chain problems have again mounted – with implications for inflation. A further escalation in tensions could increase these effects.
- Finally, the U.S. election contest between President Joe Biden and former President Donald Trump is fewer than five months away. The race remains a close one, according to polls and betting markets, with Trump leading slightly (Exhibit 25). We continue to think that a Trump win might be preferred by the stock market given a platform that includes corporate-tax cuts and deregulation. However, his proposal for major new tariffs and reduced immigration could have the opposite effect on the economy, with tariffs potentially increasing inflation as well.

Housing obscures Chinese recovery

The Chinese economy remains burdened by continued housing-market problems. After a period of overbuilding and excessive speculation, the property market is now very weak. Home sales are falling, home prices are in decline and many builders are technically insolvent.

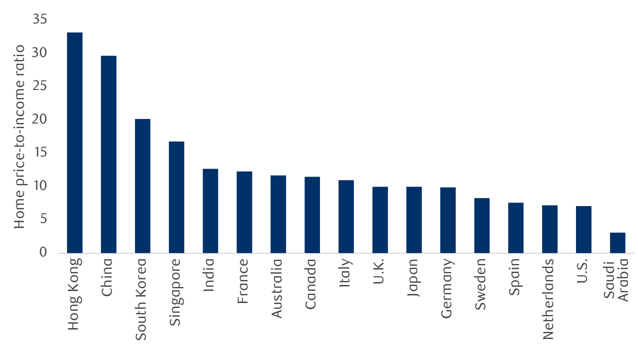
Chinese policymakers continue to grapple with the sector's woes. The latest initiative is a 500 billion renminbi (US$69 billion) program for local governments to absorb a fraction of the country's completed but unsold housing inventory. Even with this, it is unlikely that the Chinese property market will be rocking any time soon given projections for declining demand over the coming decade and still-poor housing affordability (Exhibit 26). But stabilization is a feasible goal.

Exhibit 25: 2024 U.S. presidential election: Biden vs. Trump



Note: RealClearPolitics (RCP) (06/03/2024) poll averages for Biden vs. Trump matchups only. Others acknowledge possibility of other candidates contesting the election. Predictit (06/03/2024) probability of winning derived from prediction markets data. oddschecker (06/03/2024) probability of winning derived from median daily betting odds. 538 (06/03/2024) weighted averages of national presidential polls. Source: ABC News, FiveThirtyEight, oddschecker, Predictit, RCP, Macrobond, RBC GAM

Exhibit 26: China's home price-to-income ratio is among the highest in the world



Note: As of 2024. Source: Numbeo, Macrobond, RBC GAM

Even with the real estate drag, the Chinese economy is set to expand more than 5% this year, as consumer spending rises moderately and capital investment and exports are advancing fairly quickly (Exhibit 27). Stories of China's economic demise are considerably exaggerated. The possibility of a trade war with the U.S. admittedly constitutes a downside risk to this view.

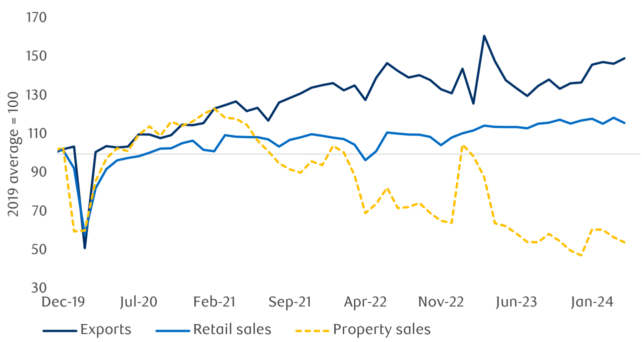
Looking further out, we continue to anticipate a general deceleration in Chinese GDP growth, to a trend of 3% to 4% per year. China's demographics are quite poor, with plummeting fertility rates increasingly making the case for the United Nation's low-fertility scenario in which China's population falls from 1.4 billion today to fewer than 500 million people at the end of the century (Exhibit 28). However, the country's productivity-growth rate, while slowing and set to continue slowing as the country becomes wealthier, is still moving deceptively quickly and can drive further prosperity gains (Exhibit 29).

Canadian distortions to fade

Consistent with most of its peers, the Canadian economy struggled in 2023. This was despite a theoretical tailwind from rapid population growth. Fortunately, and in line with those same peers, Canada now appears to be righting itself in 2024.

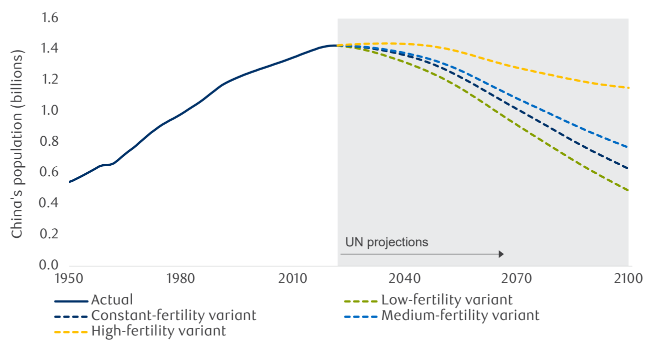
First-quarter economic growth was the best quarterly advance in a year, if not especially impressive in the context of still-strong population growth. Canada's real-time business conditions index continues to trend higher, confirming that growth continues into the middle of the year (Exhibit 30).

Exhibit 27: China's economic recovery is weighed down by housing



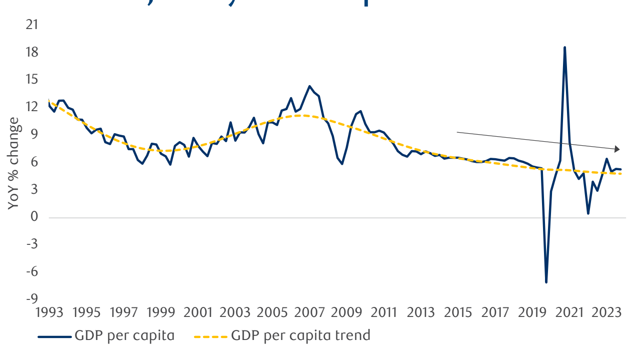
Note: As of Apr 2024. Average of 2019 levels indexed to 100. Source: Haver Analytics, RBC GAM

Exhibit 28: China's population to shrink under different scenarios



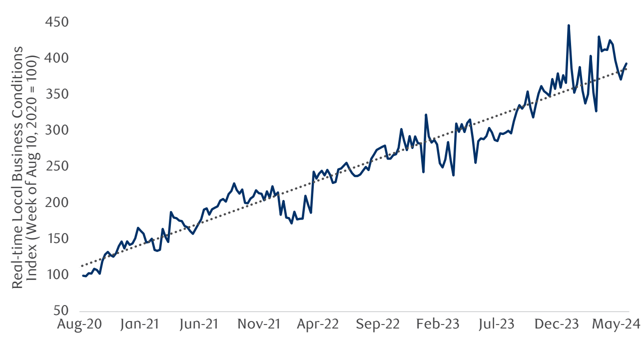
Note: Data based on World Population Prospects 2022. Source: United Nations, Macrobond, RBC GAM

Exhibit 29: China's productivity has been on a downward trajectory over the past decade



Note: As of Q1 2024. Trend estimated using Hodrick-Prescott filter. Source: China National Bureau of Statistics, Macrobond, RBC GAM

Exhibit 30: Business conditions in Canada look fine



Note: As of the week of 05/27/2024. Equal-weighted average of Business Conditions Index of Calgary, Edmonton, Montreal, Ottawa-Gatineau, Toronto, Vancouver and Winnipeg. Source: Statistics Canada, Macrobond, RBC GAM

The Canadian economy is especially sensitive to interest rates due to high household debt levels, poor housing affordability and the short-term orientation of mortgages themselves. Even so, the increase in household loan-delinquency rates has been surprisingly tame (Exhibit 31) and is actually below comparable U.S. levels. We posit that mortgage stress-testing regulations paired with deep client-bank relationships have combined to limit the pain in Canada. But household debt distress should nevertheless continue to mount for some time, with a large fraction of the country's mortgages resetting at higher rates over the next few years. In turn, the pressure is on the Bank of Canada to continue easing rates, threading the needle between minimizing economic pain and achieving its inflation target.

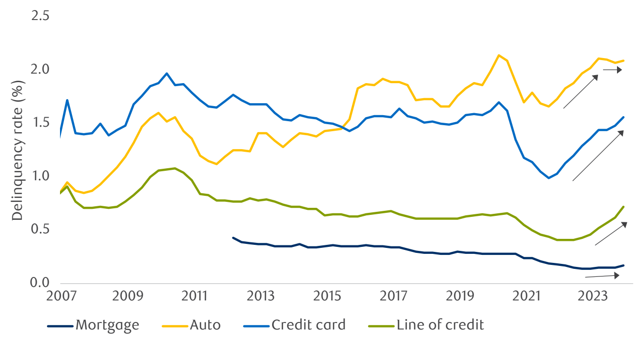
We forecast modest but acceptable economic growth for Canada over the next year, followed by a slight acceleration in the latter half of 2025 as the effect of lower interest rates starts to permeate the economy.

Canada's population leapt again in the first quarter of 2024, signaling that the explosive gains of 2023 are not quite complete (Exhibit 32). Still, we expect population growth in 2024 to be somewhat less extreme than in 2023 as the government has targeted a materially reduced inflow of temporary residents. The influx in subsequent years should moderate further as the restrictions bite. This period of faster-than-normal population growth should help to support Canada's rate of economic growth.

But the population does not increase in a vacuum. The incredibly rapid clip at which people have entered the country and the focus on low-skilled temporary labour have conspired to reduce Canada's level of productivity (Exhibit 33). This concern should ease as the rate of population growth slows and the recent influx of new residents are integrated into the economy. But even setting this force aside, Canada's longer-term productivity growth has been uninspiring, with more fundamental issues including insufficient capital expenditures and intellectual-property development.

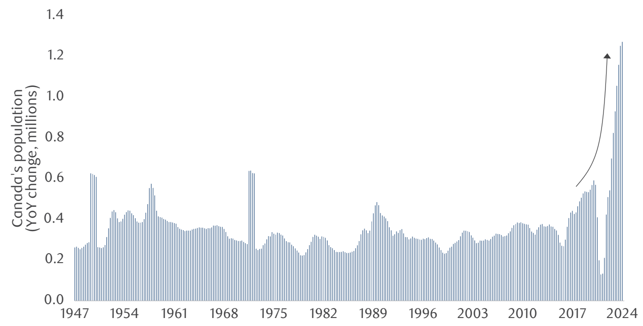
The Canadian housing market is buffeted by opposing forces. From a price perspective, booming population growth argues for higher prices, whereas poor affordability and the process of mortgage holders rolling into higher rates

Exhibit 31: Financial stress for Canadians is up, but only moderately



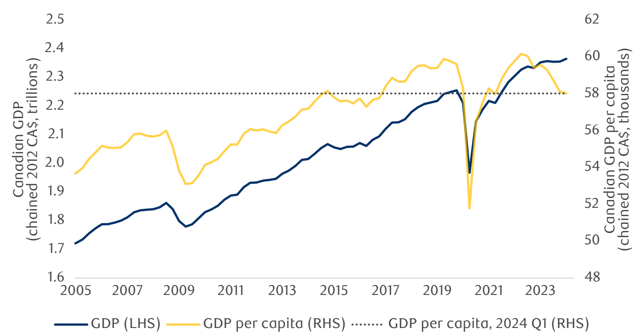
Note: As of Q4 2023. Share of the number of accounts 90 days or more past due over the previous three months. Source: Equifax, CMHC, RBC GAM

Exhibit 32: Canada's record population growth fueled by immigration



Note: As of Q1 2024. Source: Statistics Canada, Macrobond, RBC GAM

Exhibit 33: Canadian GDP per capita has been shrinking



Note: As of Q1 2024. Source: Statistics Canada, Macrobond, RBC GAM act as a depressant on home prices. We split the difference, anticipating a period of home-price stagnation over the next few years – similar to the experience of Canada's last housing bust in the early 1990s.

The story is somewhat different from a construction standpoint. Canada has a housing shortage, and this is set to get worse. But builders are not in a position to respond given the elevated cost of financing new projects, a skilled-labour shortage and uncertainty over the ability of households to afford new properties. We believe it will take a few years for these challenges to fade, and for government supply-side restrictions to ease, at which point construction can properly ramp up.

Longer-term forces

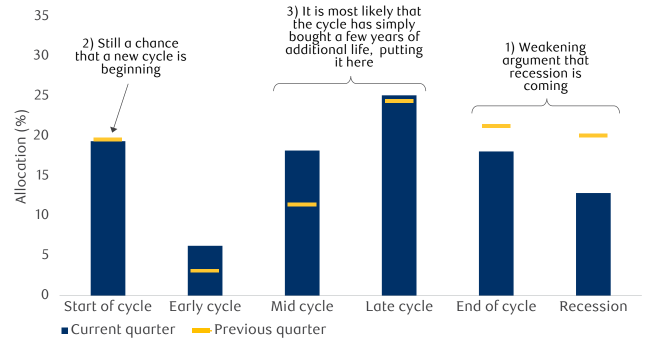
If economies do manage to continue growing over the coming years, it will mark the continuation of the existing cycle as opposed to the beginning of something new. Accordingly, our business-cycle scorecard argues that this is probably a mid-cycle or late-cycle moment (Exhibit 34). Traditionally, stock-market returns are moderate during this part of the cycle.

Don't be too alarmed by inclusion of the word "late" in the cycle assessment. That doesn't mean the cycle is destined to end in the near future. Instead, we think the expansion can run another two to five years.

Looking out over those next several years, we continue to bang the drum about fiscal excesses. Many countries continue to operate enormous fiscal deficits that will increasingly demand remedies as government debt resets at today's higher interest rates (Exhibit 35). This backdrop suggests a period of more constrained economic growth as the necessary fiscal austerity plays out. While the U.S. is among the more egregious offenders, it is concerning that neither presidential candidate has much time for the issue. The U.S. is likely to be given more rope than most other countries given its status as the world's reserve currency, but that could simply spell more pain later.

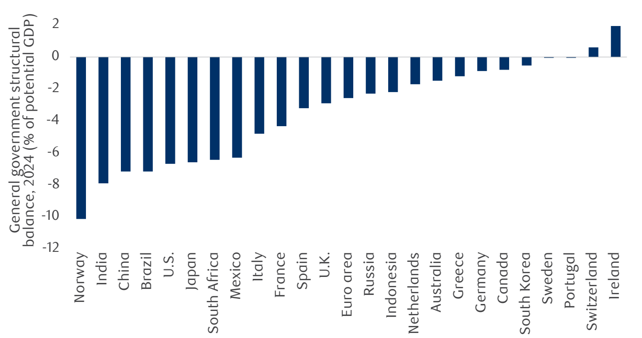
Gazing further into the future, there remain a number of long-term headwinds, including challenging global demographics, the effects of climate change (both the direct consequences and the economic drag associated with remedying it) and the impact of de-globalization (Exhibit 36).

Exhibit 34: U.S. business-cycle score



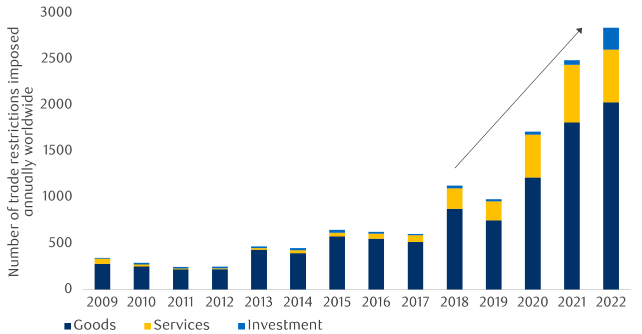
Note: As at 05/03/2024. Calculated via scorecard technique by RBC GAM. Source: RBC GAM

Exhibit 35: Significant structural fiscal deficits persist



Note: IMF projections for year 2024. Source: IMF WEO, April 2024, Macrobond, RBC GAM

Exhibit 36: Global trade restrictions ballooned in recent years

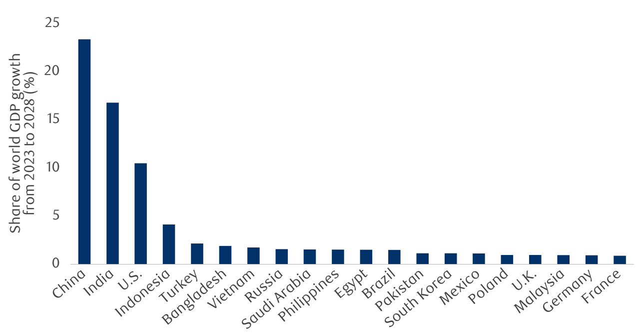


Note: As of 2022. Source: Global Trade Alert, IMF, fDi Intelligence, RBC GAM

The question is whether these adverse forces can be offset by some potentially positive long-term trends. The first is the promise of superior emerging-market growth as a driver of global demand (Exhibit 37). Even as China slows, its economy has become so large that it can still generate around a quarter of global growth each year. India's economy has now achieved sufficient scale and moreover continues to grow rapidly, representing another major positive force. Indonesia is not as large, but it is also set to contribute importantly to global growth. All told, emerging-market economies are in a position to deliver more than four-fifths of economic growth over the coming five years. This should prove quite helpful, even if developed-world economies are advancing more slowly.

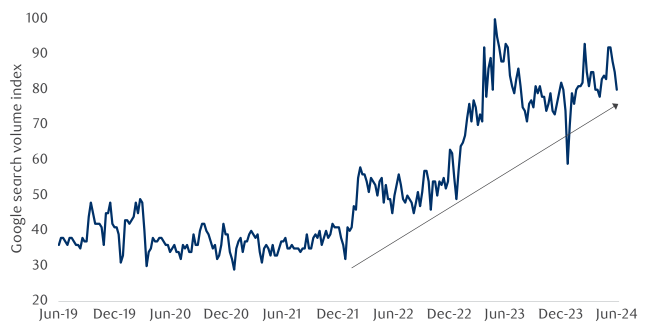
Finally, we remain optimists on the promise of new technologies (Exhibit 38). Generative artificial intelligence may indeed prove to be the next general-purpose technology that sends economy-wide productivity catapulting forward over a period of a decade or longer. Among a range of other potentially important developments, there is the chance that the new generation of weight-loss drugs prove not just successful in reducing obesity, but in reducing weight-associated ailments, unleashing a healthier and more productive populace. While we have already upgraded our long-term productivity-growth assumptions modestly, there is an upside scenario in which productivity growth surges well beyond our expectations in the years ahead.

Exhibit 37: China to remain the top driver of world growth



Note: Based on IMF forecast from 2024 to 2028. Source: IMF World Economic Outlook, Apr 2024, Macrobond, RBC GAM

Exhibit 38: Excitement about artificial intelligence swells



Note: As of the week ending 06/08/2024 (partial data used for the week). The weekly number of Google web searches for the topic relative to the total number of searches on Google over time is scaled and normalized to arrive at the search interest over time. Source: Google Trends, RBC GAM

Bottom line

In conclusion, the short-term economic outlook remains reasonably favourable, with a soft landing more likely than a hard landing. Inflation has shown inclinations to be sticky, but it is again descending gradually. In turn, central banks are well placed to undertake exploratory interest-rate cuts, reducing the degree of rate-related pain the economy is subjected to. This is not the perfect time to be an investor, but neither is it at a bad one with moderate returns likely available in the stock market and decent coupons offered by the bond market.

Disclosure

This document is 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 GAM or its affiliated entities listed herein. This document does not constitute an offer or a solicitation to buy or to sell any security, product or service in any jurisdiction; nor is it intended to provide investment, financial, legal, accounting, tax, or other advice and such information should not be relied or acted upon for providing such advice. This document is not available for distribution to investors in jurisdictions where such distribution would be prohibited.

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

In Canada, this document is provided by RBC Global Asset Management Inc. (including PH&N Institutional) and/or RBC Indigo Asset Management Inc. which is regulated by each provincial and territorial securities commission with which it is registered. 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, which is registered with the Securities and Futures Commission (SFC) in Hong Kong.

Additional information about RBC GAM may be found at www.rbcgam.com.

This document has not been reviewed by, and is not registered with, any securities or other regulatory authority, and may, where appropriate and permissible, be distributed by the above-listed entities in their respective jurisdictions.

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 such errors or omissions.

Opinions contained herein reflect the judgment and thought leadership of RBC GAM and are subject to change at any time. Such opinions are for informational purposes only and are not intended to be investment or financial advice and should not be relied or acted upon for providing such advice. RBC GAM does not undertake any obligation or responsibility to update such opinions.

RBC GAM reserves the right at any time and without notice to change, amend or cease publication of this information.

Past performance is not indicative of future results. With all investments there is a risk of loss of all or a portion of the amount invested. Where return estimates are shown, these are provided for illustrative purposes only and should not be construed as a prediction of returns; actual returns may be higher or lower than those shown and may vary substantially, especially over shorter time periods. It is not possible to invest directly in an index.

Some of the statements contained in this document may be considered forward-looking statements which provide current expectations or forecasts of future results or events. Forward-looking statements are not guarantees of future performance or events and involve risks and uncertainties. Do not place undue reliance on these statements because actual results or events may differ materially from those described in such forward-looking statements as a result of various factors. Before making any investment decisions, we encourage you to consider all relevant factors carefully.

Publication date: June 15, 2024

(6/2024)
ECONOMIC OUTLOOK-SUMMER-E 06/17/2024