April 2017

RBC WEALTH MANAGEMENT

Global Insight

Perspectives from the Global Portfolio Advisory Committee

Global Britain?

The U.K. has recast its position on the world's stage. But the transformation has just begun and an arduous road lies ahead.

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RBC Wealth Management

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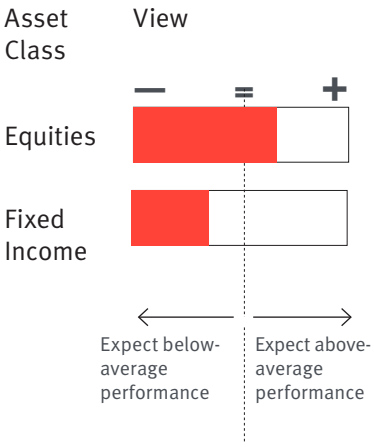

See "Views explanation" below for details

Source - RBC Wealth Management

Equities

- The MSCI World Index surged 5.9% in Q1 even though most markets came off the boil in March. It was the fourth straight quarter of gains and the strongest quarterly performance for developed markets in more than three years. Equities have been energized by improved earnings prospects worldwide and better economic data in the U.S., Europe, and China.
- Following such a strong run, periods of consolidation, or even a pullback, can't be ruled out. Nevertheless, we anticipate this bull market, which began in 2009, can persist so long as the U.S. and global economies avoid a recession. We recommend investors hold a moderate Overweight position in global equities. Among regions, we continue to favor the U.S. We have downgraded Canada to Market Weight from Overweight as the risk-reward balance has shifted.

Fixed Income

- Despite improved global economic trends and moderately higher Federal Reserve rate hike expectations, government bond yields in North America, the U.K., and Europe could be range-bound for the foreseeable future. Global GDP is unlikely to reach "breakout" speed in the near term, and we doubt U.S. fiscal policy, the French elections, and Brexit developments will jolt yields. Also, the upward pressure on yields brought about by higher inflation may have run its course for the time being.
- Corporate credit continues to be our favorite segment of the fixed income market, but investors should be patient regarding entry points as there are fewer opportunities currently. Yield spreads are very narrow, especially in North America. Investors would be best served by adhering to a "quality is king" strategy.

Views explanation

(+/=/–) represents the Global Portfolio Advisory Committee's (GPAC) view over a 12-month investment time horizon.

+ Overweight implies the potential for better-than-average performance for the asset class or for the region relative to other asset classes or regions.

= Market Weight implies the potential for average performance for the asset class or for the region relative to other asset classes or regions.

– Underweight implies the potential for below-average performance for the asset class or for the region relative to other asset classes or regions.

Focus article

Global Britain?

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The clock has started and it's time for the U.K. government to roll up its sleeves because the heavy lifting begins now. How it splits assets and liabilities with the EU and whether it can negotiate a trade deal to replace the current relationship with its most important trading partner within two years will be key. And while it's been so far, so good for the U.K. economy since the Brexit vote, will the consumer continue to drive growth? As this new era dawns we look at how investors should position portfolios.

Breaking up is hard to do

Prime Minister Theresa May's Brexit negotiations strategy is now clear. The U.K. will leave the EU's single market, the territory with over 500 million people with free movement of goods and services. By doing so, the U.K. will escape the restraints of EU regulations and reclaim control of immigration.

The U.K. will also have to withdraw from the EU customs union in order to form new trade links outside the Continent. No trade agreements with non-EU countries can be negotiated so long as the U.K. is a member of the customs union.

Having triggered Article 50 (the formal withdrawal mechanism), May will initiate the Brexit negotiations, which have a strict two-year deadline—i.e., whether any agreement has been reached or not the U.K. will be out of the EU two years from the trigger date. Much like a divorce settlement, these negotiations will focus exclusively on winding up the current relationship and discussing how to separate assets and liabilities, such as property and pensions.

Separately, the terms of a new relationship with the EU also need to be agreed upon. This process will also be difficult as the EU will focus on preserving the cohesion of its remaining members. Indeed, negotiations may not start until the divorce has been settled. Even so, they are likely to start slowly as Europe remains

A busy time for U.K. negotiators

Source - RBC Wealth Management

preoccupied by the French presidential elections in the spring and the German federal elections in September, where a real challenger to Chancellor Angela Merkel, Martin Shultz, has emerged.

Furthermore, Scotland's first minister, Nicola Sturgeon, plans to call a second independence referendum within the next two years. Given that more than 60% of Scots voted "Remain" in the Brexit referendum, she believes they feel usurped by May's pursuit of a hard Brexit. The U.K. government will do all it can to delay a second Scottish referendum as it could weaken the U.K.'s bargaining position with the EU. Trying to preserve the British union at the same time as complex negotiations with the EU take place would be a significant challenge.

Trading places

There is no deadline for agreeing to the new terms of the relationship with the EU, so if an agreement is not struck before Brexit's completion, by default the U.K./EU relationship will be governed by the regulations of the World Trade Organization (WTO). U.K. exports would not only face tariffs going into Europe, but also non-tariff barriers, such as product standards and regulations, would be erected. Imports could be held up at customs due to lengthy debates about rules of origin, disrupting supply chains.

Replicating the EU's trade deal with more than 50 third-party countries will likely be daunting.

Falling under the auspices of the WTO could be painful as U.K. exports to the EU are worth 12% of GDP (EU exports to the U.K. are a lesser 3%). We would rate the probability of this as low but not negligible. Certainly, the government seems to be bracing itself for this possibility, and May has stated she would rather have no deal than a bad deal. An interim or transitional trade agreement until the final relationship with European countries is agreed upon would be useful so as to avoid a "cliff edge" for businesses.

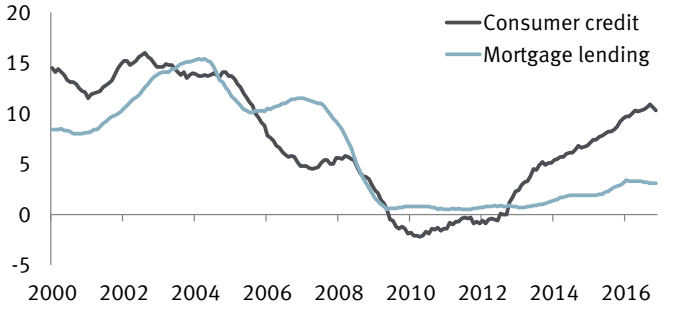
To replace the U.K.'s trade relationship with the EU, May plans to establish free trade agreements with other regions around the world. But with the EU receiving roughly half of U.K. exports, this is no small task. While it would be remiss to underestimate the resilience and ingenuity of the U.K., replicating the EU's trade deal with more than 50 third-party countries will likely be daunting.

So far, so good?

Despite the challenges ahead, the U.K. economy has held up well since the Brexit vote. Swift action by the Bank of England and a weaker pound underpinning exports are often cited as reasons for this. But the main driver has been consumption as households not only dipped into savings, but also increased debt levels, taking advantage of the cheap credit.

Spending has been fuelled by credit growth

Net consumer credit and net mortgage lending, % y/y



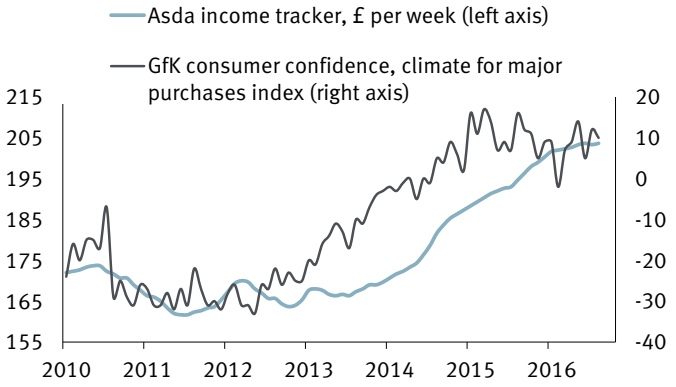
Growth in consumer credit doesn't look sustainable.

Source - Haver Analytics, RBC Capital Markets

Indeed, 85% of new loans were made at a low rate of 3% or lower. As the chart on the previous page shows, net consumer credit grew at a rate of over 10% y/y, a level which may prove difficult to sustain. With most loans on a variable rate basis, any increases in interest rates in the years ahead would pinch households' pockets.

And even though no interest rate increase is likely in the medium term, it may become more difficult for the consumer to prop up the economy going forward. Disposable incomes are already losing momentum just as consumer confidence has plateaued (see chart below).

Disposable incomes are losing momentum



It may become more difficult for the consumer to continue to prop up the economy.

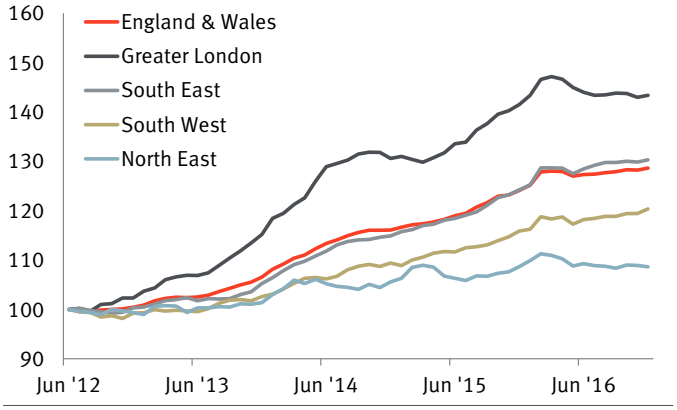
Note: Asda income tracker (measure of disposable incomes) and consumer confidence about "big ticket" purchases
Source - Haver Analytics, RBC Capital Markets

Inflation is picking up and could surpass economists' 3% consensus expectation over the next year, as the weak pound feeds through, squeezing disposable incomes. Moreover, overall house prices, which have underpinned the consumer for years, are rising more slowly and are actually coming down in London as heavier property taxes take their toll. Brexit uncertainty will likely deter buyers, though, at some point, the weaker pound may start to attract foreign buyers back to the London prime market.

Overall, whilst RBC Capital Markets' forecast of 1.6% for 2017 GDP growth sounds benign, the risk is skewed to the downside.

Housing prices are rising more slowly and declining in London

Normalised level of house prices for selected U.K. regions, 100 = May 2012



House price increases are easing.

Source - Haver Analytics, RBC Capital Markets

Portfolio positioning

The barometer for this Brexit uncertainty has been the currency. The pound is down 16% since the referendum and more than 20% since the vote was first promised in the run-up to the 2015 general election.

We expect GBP/USD could trade lower from here as factors which enabled the currency to remain within its recent trading range of 1.21–1.26 GBP/USD are likely to be challenged going forward.

For instance, rising growth expectations will likely eventually sow the seeds of their own demise and become unattainable. Second, export volumes are failing to respond to GBP weakness. RBC Capital Markets maintains a target of 1.15 in GBP/USD by the end of Q2. Though there is no sign of heading there at the moment, should a balance of payments crisis erupt in the medium term, given the U.K.'s sizable current account deficit of 5%, the pound could fall lower. We would suggest foreign currency-denominated clients to protect their portfolios against currency risk.

While investors should approach U.K. investing with caution, we see compelling selective opportunities.

We are modestly Underweight U.K. equities to signal greater uncertainty than in other regions. Moreover, with its comparatively high exposure to defensive industries, such as Utilities, Telecoms, Consumer Staples, and Health Care, the FTSE All-Share Index tends to lag relative to other regions at times of global economic expansion.

This said, we would expect U.K. equities to be reasonably underpinned by various factors. For one, the U.K. has the highest exposure to non-domestic sales in Europe, at some 70%. These revenues are likely to benefit from a weak pound and from the improved global economic environment. We reiterate our longstanding preference for U.K.-based international companies.

The equity market is also likely to be supported by merger and acquisition activity. With the pound now 25% cheaper than at its peak in USD terms, U.K. companies are more attractively priced for foreign buyers. A number of large deals have been suggested and some are taking place. Where deals fall through, the target is likely to take drastic steps to stay out of the crosshairs. We saw this with Unilever, targeted by Kraft Heinz, which has announced a comprehensive review of its strategy to appease shareholders.

Finally, the marked exposure to Financials, at some 20% of the index, is among the highest in the developed world and should also underpin equity performance. The Financials sector tends to perform well when interest rates move higher at this stage in the economic cycle. U.K. Financials exposed to U.S. interest rates should benefit the most, while enjoying the current low level of nonperforming loans.

In the fixed income world, we expect the EU divorce negotiations to feature heavily over the coming months. This, and the belief that the Bank of England may cut rates to prop up markets, will likely bring added volatility to the short end of the U.K. bond market. As a consequence, we prefer bonds in the 5- to 7-year range.

Overall, there is little visibility at the moment as to what the shape of the U.K. economy will be in two years' time. While investors should approach U.K. investing with caution, there continue to be compelling selective opportunities in the region.

Clear as mud

Policy uncertainty indexes are giving extreme readings. The surprising Brexit referendum result last June apparently kicked off a new interlude (or perhaps "era") in which the shifting priorities of voters disrupt traditional party allegiances and the electoral/policy equilibrium.

It was the surprise U.S. presidential upset which convinced many that the Brexit vote rejecting the status quo was not a "one-off." Observers are now looking ahead to French and German elections in the coming months with some trepidation. And, perhaps more importantly, the emerging policy ramifications of both Brexit (see the article on page 4) and the new administration in Washington remain murky and highly fluid.

Is this the "wall of worry" the major stock markets have been climbing? And would the arrival of some policy clarity spell the end of what has been an impressive rally? If so, then the markets probably have further to go because, in our view, it will be some time before actionable policies emerge.

It has taken Britain nine months just to get to formally asking for a "divorce" from the EU. That has triggered the start of a two-year negotiating period at the end of which the U.K. will be out of the EU regardless of whether any agreement on continuing a relationship has been reached; many believe the negotiations will drag on for much longer.

In the U.S. it's still comparatively "early days" for the new administration. Its policy preferences for fiscal stimulus, tax cuts, and deregulation remain in the formative stages. Once formally proposed they are unlikely to sail through Congress quickly or unaltered. President Trump's own party tends to be reluctant on infrastructure spending, especially if it is not accompanied by offsetting cuts elsewhere in the budget. Some deep spending cuts have been proposed but are getting pushback from legislators in both parties. And tax cuts, unless they are "revenue neutral" (i.e., largely offset by spending reductions or revenue increases), will need some significant Democratic support.

Equity views

Region	Prior	Current
Global	+	+
United States	+	+
Canada	+	↓ =
Continental Europe	=	=
United Kingdom	–	–
Asia (ex-Japan)	=	=
Japan	=	=

Source - RBC Wealth Management

Our view continues to be that any stimulative benefits to the economy from lower taxes and/or infrastructure spending are unlikely to arrive before late 2017 or more fully in 2018. That should provide a bump for GDP growth next year and a somewhat bigger lift for U.S. corporate profits.

In fact, rising economic activity indexes just about everywhere in the developed world suggest that earnings expectations for this year, and perhaps next, are likely to be met. In our view, it is this perception of a firmer footing for most developed economies that has been powering greater confidence in the earnings outlook and a willingness to pay up for equities.

At some point this unanimously constructive view will crumble in response to some uncooperative data

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or perhaps to the arrival of a policy clarity which turns out to be at odds with today's optimism. That would probably mark the end of the current dynamic uptrend and usher in a period of consolidation and perhaps correction. However, we do not think it would mark the end of the bull market.

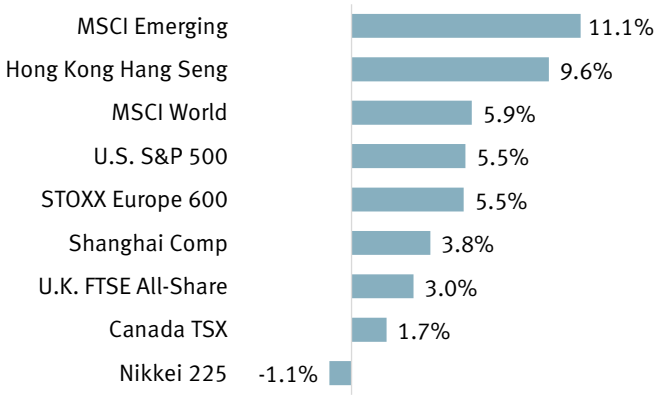
That, in our judgment, would require that a new global economic downturn, in particular a U.S. recession, was imminent. It is highly likely the next U.S. recession will be triggered, as recessions nearly always have been, by the arrival of restrictive monetary conditions—i.e., the combination of prohibitively high interest rates and an unwillingness of banks to extend credit. We don't think those conditions are likely to arrive before 2019. Until they do, we expect to recommend global portfolios remain committed to equities.

Regional highlights

United States

- U.S. equity market momentum began to slow in March as former leaders such as Financials and small-cap stocks lagged and the broader indexes struggled at times. While setbacks for the Trump administration's pro-growth agenda probably played a role, mostly it appeared to be normal churning following a strong run. After all, the S&P 500 has been on a tear, rising 10.4% since the election and 14.7% in the past year.
- We remain constructive on U.S. equities and would maintain a moderate Overweight position based on a 12-month time horizon. The economy is on solid footing, recession risks are rather low, and corporate earnings seem set to deliver the strongest growth since 2011, at 8% or more. Over the one-year horizon, periods of consolidation or retrenchment can't be ruled out. Economic and earnings data have higher hurdles to clear in coming months. The market's above-average valuation, while not eye-popping, leaves little room for disappointment. These factors, combined with tax policy uncertainty in Washington, may limit the market's fuel.
- Portfolio equity positions often become outsized following strong rallies. In our view, it is always the right time to manage risk by revisiting and, if necessary, adjusting equity weights back within target guidelines. Given how far the market has come on the strength of prospective economic and earnings growth, we recommend no more than a moderate Overweight.

Q1 performance in local currencies*



*MSCI Indexes in USD
Source - RBC Wealth Management, Bloomberg

Emerging markets led; the U.S. and Europe performed well among peers.

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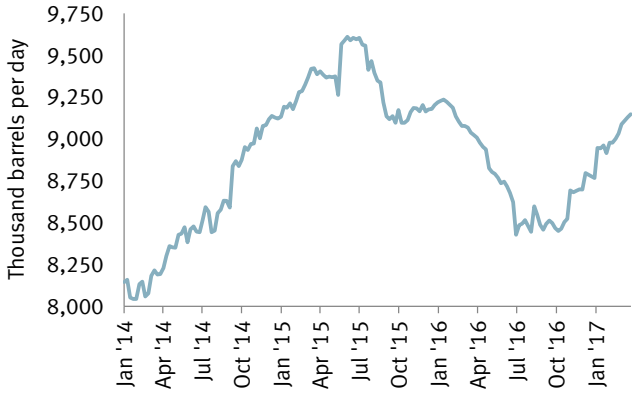
Canada

- We have downgraded Canadian equities to Market Weight from Overweight. Our outlook for key sectors of the domestic equity market has shifted to a point where the risk-reward opportunity appears more balanced.
- The Canadian banks continue to trade at a modest premium to the group's long-term average price-to-earnings multiple. First-quarter results were supportive of this premium as the group broadly displayed improving credit trends, positive operating leverage, and strong capital ratios. While we believe these trends can continue in the short term, we recognize that banks now face a backdrop of persistent revenue growth headwinds, including the housing market and energy prices.
- Elevated household leverage and the potential for further policy action to rein in house prices are headwinds to consumer and mortgage credit growth. National home price growth accelerated to 16% y/y in February with much of that upward momentum concentrated in pockets of Southern Ontario. While no national housing policy measures were introduced in the Federal Budget, stretched affordability in certain markets has given voice to calls for local policy action. We stress that elevated home prices in isolation pose a limited credit risk to banks absent a material employment or interest rate shock.
- The outlook for crude oil has become somewhat more clouded given the sharp rebound in U.S. shale production. Additional data is required to confirm the sustainability of recent production trends, and we believe elevated U.S. crude inventories should improve as the OPEC-led production curtailments wind their way through the global supply chain. However, there is now a more-elevated risk to our base-case outlook for higher crude oil prices in 2017, as the global cost curve has moved lower than previously anticipated.

Continental Europe & U.K.

- We hold a Market Weight position on Continental Europe. Macroeconomic surprises are reaching new six-year highs, deflationary fears have receded, and the region offers relatively good value.
- Politics, however, should not be entirely dismissed. A Marine Le Pen victory in the French presidential election would likely have a wide ranging effect, possibly akin to that of

U.S. production of crude oil



U.S. producers responded to US$50 crude oil with a significant increase in volumes off the summer 2016 lows.

Source - Energy Information Administration; weekly data through 3/24/17

the 2012 crisis, with effects including much higher bond spreads in France and the periphery, business and consumer confidence tumbling, and a currency looking to discount the prospects of a possible breakup of the eurozone.

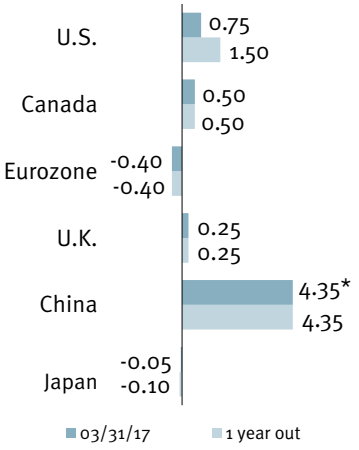
- Current polls suggest that while Le Pen may get through the first round on April 23, she will lose in the second round on May 7. Were this to occur, we would expect a relief rally in equities. Centrist candidate Emmanuel Macron, who currently leads in the polls, preconizes lower taxes, lower spending, and a strong European Union.
- German companies could prove a valuable hedge against a Le Pen victory, while the Financials sector, despite its re-rating in the second half of last year, still offers attractive value.

Asia

- Asian equities remain well supported by the strength in global leading economic indicators.
- Tightening measures in China's strongest property markets are having the desired effect. In the 70 largest cities, month-over-month price increases are close to zero and year-over-year gains may have peaked. However, we expect a soft landing for property prices (see the *Global Insight Weekly* from March 23, 2017).This is the fourth such cycle over the past decade. Outside China's largest cities, where the majority of the population lives, price appreciation has been far smaller. Housing inventories have come down meaningfully as a result of the leadership's focus on "destocking" since 2015.
- Chinese economic data are relatively steady. Gains in producer price inflation continue to help profits in the Industrials sector, which in turn reduce some of the concerns around nonperforming loans in the banking sector. China's capital outflows have moderated. China's foreign exchange reserves, the largest in the world at $3T, rose in February. The renminbi has been steady for several months and is down around 8% against the dollar since the mini-devaluation in summer 2015.
- In Hong Kong, Carrie Lam won the leadership contest to become the next chief executive of the region. We expect this to have minimal impact, if any, on the equity market.

No time to go "wobbly"

Central bank rate (%)



*1-yr base lending rate for working capital, PBoC
Source - RBC Investment Strategy Committee, RBC Capital Markets, Global Portfolio Advisory Committee, Consensus Economics

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Politics, central banks, and economic fundamentals have increased volatility for fixed income investors, leaving many to question current allocations to the sector. Paraphrasing former British Prime Minister Margaret Thatcher, we agree prompt attention should be devoted to portfolios, but it's not time to panic as there continue to be areas of opportunities in corporate credit across all geographies.

The "pedal to the metal" feel of market-moving events continues this month—U.S. fiscal policy pivots to tax reform, France commences its presidential election process, and the U.K. and Europe begin to deal with Brexit. One can't forget the central banks, but for now only the Federal Reserve is on a path toward normalizing interest rates and it is likely to move slowly. Despite these issues, rates in North America, the U.K., and Europe continue to be relatively well contained and could be range-bound for the foreseeable future.

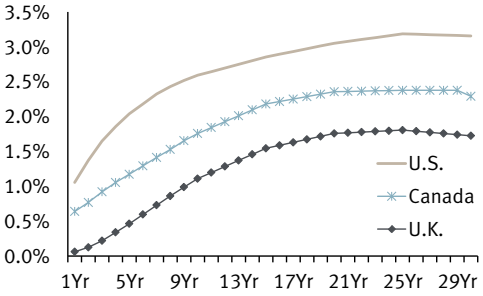
We continue to favor corporate credit for opportunities, but yield spreads are still historically tight even though we have seen the start to the long-awaited pullback in high-yield bonds. This suggests to us, for now, investors will be better served by not blindly chasing yield but adhering to a more-patient, "quality is king" focus. Global developments will likely generate additional volatility, and while we feel investors shouldn't go "wobbly" in the face of opportunities that arise, it is also not the time to radically change fixed income investment strategies.

Regional highlights

United States

- The Fed delivered its widely anticipated third rate hike in mid-March, but as was the case after the first two rate hikes, the long end of the Treasury yield curve has actually drifted lower in the weeks since. We continue to believe that political realities will push fiscal stimulus measures into 2018, which should keep the 10Y Treasury yield range-bound between 2.30% and 2.60%, and the 7–10 year part of the curve our preferred place to put money to work.
- The "risk-off" market sentiment into month end started to open up the first pockets of value in the high-yield market this year, but we remain patient. The average yield on the Bloomberg Barclays US Corporate High Yield Index pushed above 6% for the first time in 2017 after declining to just 5.5%. But with prospects for corporate tax reform this year, we think investors can afford to be patient and pick entry points.
- Municipals have tracked the bond market rally since the Fed meeting with benchmark 10-year and 30-year yields firmer by 20 basis points (bps) and 16 bps, respectively. We expect market fundamentals to remain strong, driven by solid demand, a light issuance calendar, and strong secondary market activity that should give the rally legs. We believe value on the yield curve can be found between 15 and 20 years, where muni/Treasury yield ratios of 110% remain attractive.

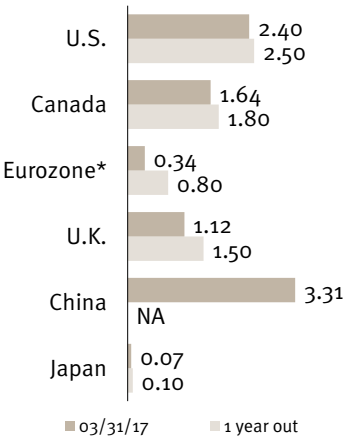
Sovereign yield curves



Source - Bloomberg

Global fixed income

10-year rate (%)



* Eurozone utilizes German Bunds
Source - RBC Investment Strategy Committee, RBC Capital Markets, Global Portfolio Advisory Committee

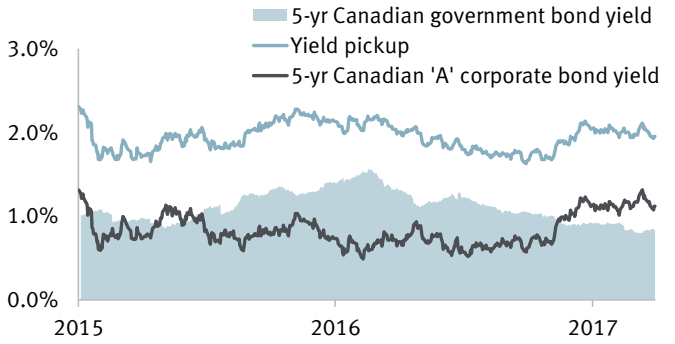
Canada

- Persistent slack in the economy combined with a lack of core inflationary pressure provides good reason to believe the Bank of Canada will remain cautious during its Monetary Policy Report meeting this month. We expect the shorter end of the yield curve to be relatively anchored and would treat any move higher in yields further out on the Government of Canada curve as an opportunity to invest bond ladder positions at higher rates.
- We see value in upgrading credit quality within portfolios given the low additional compensation for taking on credit risk; corporate credit spreads generally are among the tightest they've been in two-and-a-half years in Canada. High-yield investors should also consider upgrading quality given the lack of additional compensation currently available as well as the possibly unwanted high correlation to the Canadian equity market.
- We continue to see more attractive opportunities in the preferred share market versus corporate bonds although we advise investors to be selective given parts of the market look fairly valued. Buy-and-hold preferred share investors should stay the course, but we see value in tilting portfolios defensively against potential market weakness.

Continental Europe & U.K.

- U.K. Prime Minister May finally triggered Article 50, which enables the U.K. to begin formal proceedings to exit from the EU. We expect the negotiations to feature heavily in the news over the coming months, which is likely to bring added volatility to the U.K. bond market. As a consequence, we see little value in short-dated bonds due to the potential market swings resulting from the Brexit negotiations. In the U.K., we currently prefer bonds in the 5- to 7-year range.
- With the Dutch election result indicating a rejection of a populist party forming a government, the European bond market has turned its attention towards this month's French presidential election. The market is likely to be volatile as the election could be seen as a vote on eurozone confidence. Investors seem inclined to favour safe havens during this uncertain period, which may add even more volatility. Furthermore, the European Central Bank is likely to sit on the sidelines for now despite potential widening in yield spreads of French and peripheral debt versus German benchmarks.
- We prefer corporate bonds to government bonds as they are likely to be more-stable during this period. Across Europe, we currently favour large multinationals over domestic issuers in order to provide some protection against any forthcoming political or regulatory changes.

Canadian corporate credit spreads



Yield pickup on Canadian corporate bonds lowest in two-and-a-half years.

Source - RBC Wealth Management, Bloomberg; data through 3/31/17

Cornucopia

Commodity forecasts

	2017E	2018E
Oil (WTI $/bbl)	56.00	62.63
Natural Gas ($/mmBtu)	3.30	3.40
Gold ($/oz)	1,300	1,300
Copper ($/lb)	2.65	2.75
Corn ($/bu)	3.70	3.94
Wheat ($/bu)	4.46	5.06

Source - RBC Capital Markets forecasts (oil, natural gas, gold, and copper), Bloomberg consensus forecasts (corn and wheat)

Corn prices have fallen close to 60% since their peak in 2012. Reduced acreage and more normal weather should gradually reduce excess inventories.

Harvest volumes for corn have been unusually robust since 2013 on favorable weather conditions across major producing regions. Demand has increased modestly in response to lower prices, along with steady global population growth. However, overall, the market has tilted toward oversupply in recent years.

Production

Major exporting nations, such as Brazil and Argentina, are experiencing favorable weather conditions from La Niña, adding to the U.S.'s large 2016 fall harvest. The U.S. Department of Agriculture's (USDA) September 2016–August 2017 forecast for corn has global production increasing 8% y/y in the current crop year.

Prior-year prices are a strong indicator of next year's planted acreage. The USDA, given weak prices, is forecasting corn planting at 90 million acres for this coming season, down about 4%. Assuming normalized weather conditions, yields are expected to decline modestly, resulting in a harvest broadly in line with expected domestic consumption.

Politics

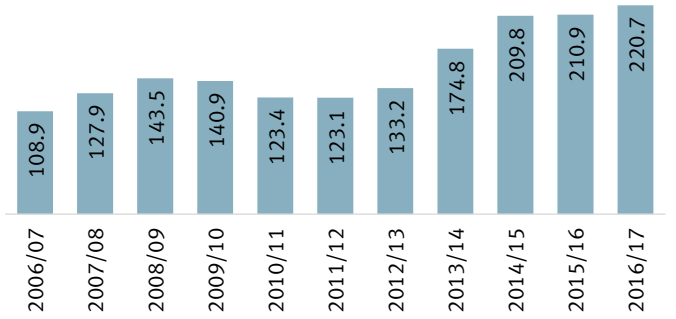
Ethanol consumes about 40% of corn produced in the U.S. It is not yet clear how the Trump administration and the Environmental Protection Agency (EPA) will approach the Renewable Fuel Standard (RFS) program. The program establishes quotas for renewable energy sources to be blended into gasoline motor fuels. Ethanol is important to the nation's energy independence, and the oil and farming industries represent powerful political lobbies. The Renewable Volume Obligation for 2017 has been set by the EPA, up 6% y/y.

Summary

High storage levels, recent strong production from South America, and political uncertainty have weighed on prices. However, high inventory levels can be reset by just one or two challenging crop years. Reduced acreage committed to corn should help bring available stocks down this year but, as usual, much depends on the vagaries of global weather patterns. We are constructive on corn and the agricultural sector over a multiyear horizon.

World corn ending stocks

Million tonnes



Source - USDA *World Agricultural Supply and Demand Estimates* report

The tight market conditions of 2012/13, with prices at the time more than double today's levels, were eviscerated in just two years. While depressed today, a normalization can play out in just one or two harvests.

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Currency forecasts

Currency pair	Current rate	Forecast Mar 2018	Change*
Major currencies			
USD Index	100.35	105.43	5%
CAD/USD	0.75	0.73	-3%
USD/CAD	1.33	1.37	3%
EUR/USD	1.07	0.98	-8%
GBP/USD	1.26	1.18	-6%
USD/CHF	1.00	1.12	12%
USD/JPY	111.39	100.00	-10%
AUD/USD	0.76	0.72	-6%
NZD/USD	0.70	0.74	6%
EUR/JPY	118.67	98.00	-17%
EUR/GBP	0.85	0.83	-2%
EUR/CHF	1.07	1.10	3%
Emerging currencies			
USD/CNY	6.89	7.60	10%
USD/INR	64.85	70.00	8%
USD/SGD	1.40	1.51	8%
USD/PLN	3.97	4.34	9%

* Defined as the implied appreciation or depreciation of the first currency in the pair quote.
Examples of how to interpret data found in the Market Scorecard.
Source - RBC Capital Markets, Bloomberg

U.S. dollar

The rate hike delivered at the Federal Reserve's March meeting was partnered with an outlook more dovish than the market expected, causing the dollar to weaken over 1% by the end of the month. Given rising inflation, a tight labour market, and the potential for a fiscal stimulus boost, we are still bullish on the dollar, and see this recent pullback as offering a better entry point for investors.

Euro

The eurozone recovery story continues, with preliminary readings of sentiment surveys for March showing fresh all-time highs. The Dutch elections also went against the populist vote, alleviating some pressure on the euro. However, low core inflation will keep the European Central Bank's accommodative monetary policy in place, and the main political risk for the euro—the French elections—is still to come. We hold our bearish outlook for now.

British pound

A weaker U.S. dollar and slightly more hawkish commentary from the Bank of England allowed the pound to rally from the lows. In our view, this is a correction not a trend reversal. Slowing wage growth and rising inflation will erode disposable income, holding back consumer spending. This will be a drag on the economy. Combined with the large uncertainty around the U.K.'s relationship with the EU, we expect further weakness in GBP.

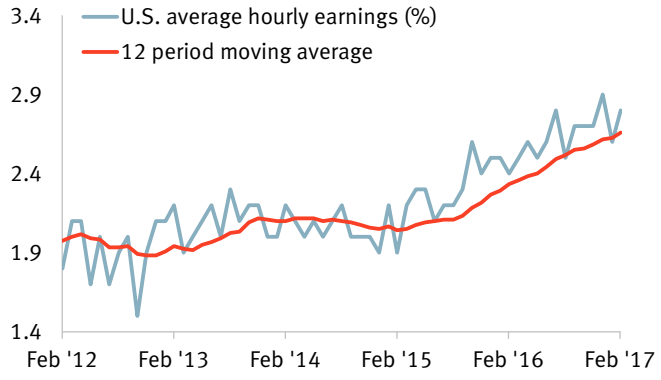
Canadian dollar

The Bank of Canada (BoC) remained dovish at its March meeting, citing slack in the domestic economy and weakness in the labour market, inflation, and exports. This was seen as an attempt from the BoC to prevent the market pricing in rate hikes too rapidly. Attention was also drawn to the many uncertainties the new U.S. administration brings to the Canadian economy's future, largely in regards to trade. Given this backdrop, we see a difficult road ahead for the Canadian dollar.

Japanese yen

While we expect rates rising faster in the U.S. than Japan to weaken the yen, this has largely been priced into markets. When considering that the record USD/JPY rally following the U.S. election was largely speculative, the lack of follow-through in real capital flows out of Japan opens up the potential for the yen to retrace these losses. Therefore, we are forecasting USD/JPY to grind lower to around the 100 level over the next 12 months.

U.S. wage growth consistently moving higher



Source - RBC Wealth Management, Bloomberg; data through 2/28/17

Short U.S. rates to rise as a tighter labour market drives inflation higher.

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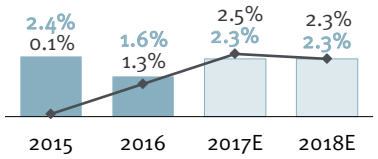
Key forecasts

Real GDP Growth — Inflation Rate

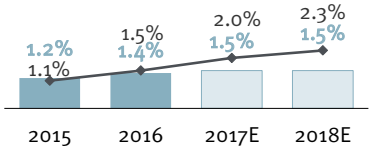
United States — sustained growth

- Q4 GDP growth revised up to 2.1% on stronger consumer. Mfg. PMI as well as new orders rose in December and January, then surged in February. Employment solid. Consumer and business confidence elevated. Housing steady. Capex perking up. Leading indicators, confidence point to sustained domestic growth.



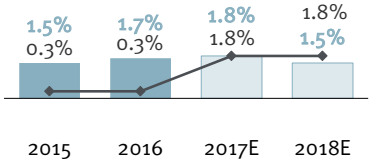
Canada — in transition

- Q4 growth solid at 2.4%. Disappointing full year of 1.4% due to Fort McMurray fire. House construction firm, PMI rose at fastest pace in 2 years in February, as did new orders. Energy capex weak. Employment strong, wage growth steady. Tourism very strong helped by undervalued loonie.



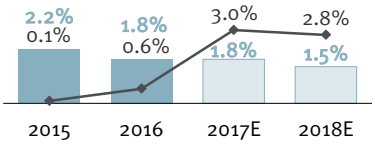
Eurozone — picking up

- Q4 GDP growth picked up to a 2% annualized rate on the back of a late surge in the French economy. Stronger PMIs suggesting momentum has carried into Q1. Refugee crisis, Brexit, and upcoming elections weighing on consumer sentiment. Italian banks keeping ECB ultraloose, euro soft. Full-year GDP growth steady in 2017.



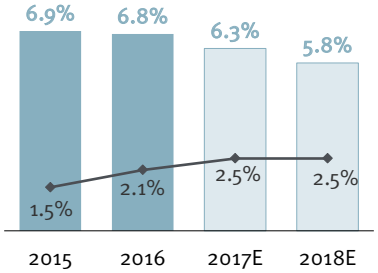
United Kingdom — period of adjustment

- PMIs, new orders weakened in January and February but still in solidly positive territory. Construction mixed. Unemployment steady, but real wages getting squeezed as inflation rising with weak pound. Q4 and full-year GDP growth revised lower. Growth should ease moderately in 2017 and again in 2018.



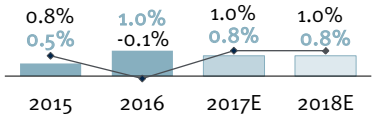
China — stabilizing

- Full-year growth +6.8% y/y. Loans still growing faster than GDP. PMIs improved in December, held their own in Q1. Employment, wages, retail sales, car registrations all growing. Recent export data distorted by Lunar New Year. Fixed asset investment slowing. House prices higher year over year in major centers, but restrictive policy is cooling the sector.



Japan — gradually improving growth

- GDP revised higher in Q4, positive for 4 quarters running. Longest such streak in 3 years. Corporate earnings solid, business confidence has perked up. Wages growing, consumer confidence improving. Firmer oil prices, weak currency putting inflation targets back within reach. BoJ looking for 1.5% GDP growth in 2017.



Source - RBC Investment Strategy Committee, RBC Capital Markets, Global Portfolio Advisory Committee

Market scorecard

Index (local currency)	Level	1 Month	YTD	12 Month
S&P 500	2,362.72	0.0%	5.5%	14.7%
Dow Industrials (DJIA)	20,663.22	-0.7%	4.6%	16.8%
NASDAQ	5,911.74	1.5%	9.8%	21.4%
Russell 2000	1,385.92	-0.1%	2.1%	24.4%
S&P/TSX Comp	15,547.75	1.0%	1.7%	15.2%
FTSE All-Share	3,990.00	0.9%	3.0%	17.5%
STOXX Europe 600	381.14	2.9%	5.5%	12.9%
German DAX	12,312.87	4.0%	7.2%	23.6%
Hang Seng	24,111.59	1.6%	9.6%	16.1%
Shanghai Comp	3,222.51	-0.6%	3.8%	7.3%
Nikkei 225	18,909.26	-1.1%	-1.1%	12.8%
India Sensex	29,620.50	3.1%	11.2%	16.9%
Singapore Straits Times	3,175.11	2.5%	10.2%	11.8%
Brazil Ibovespa	64,984.07	-2.5%	7.9%	29.8%
Mexican Bolsa IPC	48,541.56	3.6%	6.4%	5.8%
Bond yields	**3/31/17**	**2/28/17**	**3/31/16**	**12 mo chg**
US 2-Yr Tsy	1.254%	1.260%	0.721%	0.53%
US 10-Yr Tsy	2.387%	2.390%	1.769%	0.62%
Canada 2-Yr	0.748%	0.758%	0.542%	0.21%
Canada 10-Yr	1.625%	1.635%	1.227%	0.40%
UK 2-Yr	0.125%	0.100%	0.441%	-0.32%
UK 10-Yr	1.139%	1.151%	1.415%	-0.28%
Germany 2-Yr	-0.740%	-0.899%	-0.487%	-0.25%
Germany 10-Yr	0.328%	0.208%	0.153%	0.18%
Commodities (USD)	**Price**	**1 Month**	**YTD**	**12 Month**
Gold (spot $/oz)	1,249.35	0.1%	8.4%	1.4%
Silver (spot $/oz)	18.27	-0.3%	14.7%	18.3%
Copper ($/metric ton)	5,816.00	-2.5%	5.3%	19.2%
Uranium ($/lb)	23.25	-5.1%	14.1%	-17.3%
Oil (WTI spot/bbl)	50.60	-6.3%	-5.8%	32.0%
Oil (Brent spot/bbl)	52.83	-5.0%	-7.0%	33.4%
Natural Gas ($/mmBtu)	3.19	15.0%	-14.3%	62.8%
Agriculture Index	289.11	-5.2%	-0.6%	2.1%
Currencies	**Rate**	**1 Month**	**YTD**	**12 Month**
US Dollar Index	100.3500	-0.8%	-1.8%	6.1%
CAD/USD	0.7509	-0.1%	0.9%	-2.4%
USD/CAD	1.3318	0.1%	-0.9%	2.4%
EUR/USD	1.0652	0.7%	1.3%	-6.4%
GBP/USD	1.2550	1.4%	1.7%	-12.6%
AUD/USD	0.7629	-0.4%	5.8%	-0.4%
USD/CHF	1.0026	-0.3%	-1.6%	4.2%
USD/JPY	111.3900	-1.2%	-4.8%	-1.0%
EUR/JPY	118.6700	-0.5%	-3.5%	-7.4%
EUR/GBP	0.8485	-0.7%	-0.6%	7.1%
EUR/CHF	1.0690	0.5%	-0.3%	-2.3%
USD/SGD	1.3971	-0.4%	-3.4%	3.6%
USD/CNY	6.8872	0.3%	-0.8%	6.7%
USD/BRL	3.1220	0.4%	-4.1%	-13.1%

Germany and Hong Kong helped power a 5.9% rally in the MSCI World Index in Q1, the strongest quarterly gain in more than three years.

U.S. yields barely budged despite a Fed rate hike and improved economic data.

Crude oil recorded its biggest monthly loss since last summer.

The U.S. Dollar Index weakened in March and in Q1 despite heightened prospects for two more Fed rate hikes this year.

Equity returns do not include dividends, except for the German DAX and Brazilian Ibovespa. Equity performance and bond yields in local currencies. U.S. Dollar Index measures USD vs. six major currencies. Currency rates reflect market convention (CAD/USD is the exception). Currency returns quoted in terms of the first currency in each pairing. Examples of how to interpret currency data: CAD/USD 0.75 means 1 Canadian dollar will buy 0.75 U.S. dollar. CAD/USD -2.4% return means the Canadian dollar has fallen 2.4% vs. the U.S. dollar during the past 12 months. USD/JPY 111.39 means 1 U.S. dollar will buy 111.39 yen. USD/JPY -1.0% return means the U.S. dollar has fallen 1.0% vs. the yen during the past 12 months.

Source - RBC Wealth Management, RBC Capital Markets, Bloomberg; data through 3/31/17.

Research resources

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			Investment Banking Services Provided During Past 12 Months	
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Hold [Sector Perform]	679	41.84	149	21.94
Sell [Underperform]	101	6.22	8	7.92

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