RBC Global Asset Management

The Global Investment Outlook

RBC GAM Investment Strategy Committee

FALL 2023

The RBC GAM Investment Strategy Committee

The RBC GAM Investment Strategy Committee consists of senior investment professionals drawn from all areas of RBC Global Asset Management. The Committee regularly receives economic and capital markets related input from internal and external sources. Important guidance is provided by the Committee's regional equity advisors (North America, Europe, Asia, Emerging Markets) and from the Global Fixed Income & Currencies sub-committee. From this, the Committee builds a detailed global investment forecast looking one year forward.

The Committee's view includes an assessment of global fiscal and monetary conditions, projected economic growth and inflation, as well as the expected course of interest rates, major currencies, corporate profits and stock prices.

From this global forecast, the RBC GAM Investment Strategy Committee develops specific guidelines that can be used to manage portfolios.

These include:

The recommended mix of cash, fixed income instruments, and equities.

The recommended global exposure of fixed income and equity portfolios.

The optimal term structure for fixed income investments.

The suggested sector and geographic make-up within equity portfolios.

The preferred exposure to major currencies.

Results of the Committee's deliberations are published quarterly in *The Global Investment Outlook*.

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Executive summary

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The global economy has been resilient and a variety of challenges stemming from the pandemic have become less severe. But the lagged impact of aggressive monetary tightening, in our view, is still likely to eventually push the economy into recession and, in an environment of heightened macroeconomic uncertainty, substantial risk taking is unwarranted and patience is critical.

Growth remains positive for now, but headwinds are likely to dominate

Most major economies have continued to expand so far this year and some of the key risks to growth have diminished. Inflation has moderated from an extreme, stress in the U.S. regional-banking system has eased, risk assets have rallied and North America's housing market rebounded in the spring. But offsetting this long list of positives is the fact that the most critical headwinds have intensified. China's economic rebound from late last year is fizzling as the world's second-largest economy struggles despite attempts by policymakers to stimulate growth. Moreover, short-term interest rates have risen even further than previously anticipated in the developed world and are now at decidedly restrictive levels not experienced in over two decades. The full effect of tightening monetary conditions typically slows the economy with a significant lag, with the implication that the window for a recession may just now be starting to open. As a result, we continue to expect a recession in most of the developed world over the year ahead, though its contours should be mild in depth and short in duration. Our GDP growth forecasts have mostly been raised for 2023 and lowered for 2024, reflecting better-than-expected economic data during the summer and the deferral of the start of the anticipated recession from the third quarter of 2023 to the fourth quarter. Our 2024 growth forecasts remain below the consensus.

Inflation trend remains favourable

U.S. consumer inflation peaked at 9% in mid-2022 and has since cooled toward 3% as the four main drivers of high inflation have all turned. The commodity-price surge following Russia's invasion of Ukraine has reversed, supply-chain problems have mostly been resolved, monetary policy has moved from extreme accommodation to a restrictive stance and fiscal policy has become far less stimulative. While inflation has declined relatively quickly during the past year, further material improvements toward the 2.0% target will prove more difficult in the near term as gasoline prices have rebounded in recent months and base effects will be less favourable. Nevertheless, we remain optimistic with regard to the medium-term inflation outlook and believe that inflation can fall faster than the consensus expectation, aided in part by weaker economic conditions, to just above 2.0% by next year.

Dollar detour: how short-term factors have interrupted the cyclical decline

The U.S.-dollar downtrend remains intact and we continue to expect significant U.S.-dollar weakness over the coming years. However, the long-term cyclical decline embedded in our outlook has run into a few shorter-term roadblocks, and so its progress has been slower than we had anticipated. While the dollar sits roughly 7% below its September 2022 peak, the currency is unchanged since the start of 2023. Higher U.S. interest rates and disappointing economic growth abroad have interrupted the dollar's slide in 2023. Still, emerging-market currencies as a whole have fared impressively – a few even managing double-digit returns so far this year – and the euro, Canadian dollar and British pound have also outperformed the U.S. dollar. We remain optimistic on most emerging- and developed-market currencies over the next 12 months, as we expect the U.S. dollar to decline broadly.

Rate-hiking cycle is drawing to a close, and cuts are likely over the year ahead

Central banks are now near or already across the finish line in their monetary-tightening journeys. Emerging-market central banks have been leading the way, raising rates before the developed world during this cycle, and some have now pivoted to delivering rate cuts. It is not unreasonable to think that central banks in the developed world may follow suit within the next year. Our model suggests the neutral U.S. fed funds rate is currently 3.4%, but if inflation continues to decline in line with our forecast, that neutral reading falls to around 2% in 12 months. As a result, and in combination with our recession forecast, it seems unlikely that the fed funds rate will remain at an elevated 5.5% for an extended period. This view is in line with pricing in the futures market, which flags the possibility of one more 25-basis-point hike by the end of this year, followed by the start of an interest-rate cutting cycle beginning in early 2024.

Sovereign bonds offer attractive return potential, minimal valuation risk

Government-bond yields have climbed to their highest levels since just before the 2008/2009 global financial crisis and at this point represent attractive value. According to our models, much of the acute valuation risk that so worried us in 2020 and 2021 has dissipated with last year's painful bond sell-off. With bond yields now at a much higher starting point, the economy likely to weaken and inflation pressures capable of moderating further over the coming year, we believe the risk of capital losses in sovereign bonds is minimal and forecast lower bond yields and thus higher bond prices ahead. As a result, sovereign fixed-income assets are the most appealing they have been in many years and we expect that government bonds will deliver returns in the mid to high single digits over the year ahead, with some regions even capable of low double-digit returns.

Equity-market gains have been dominated by U.S. mega-cap technology

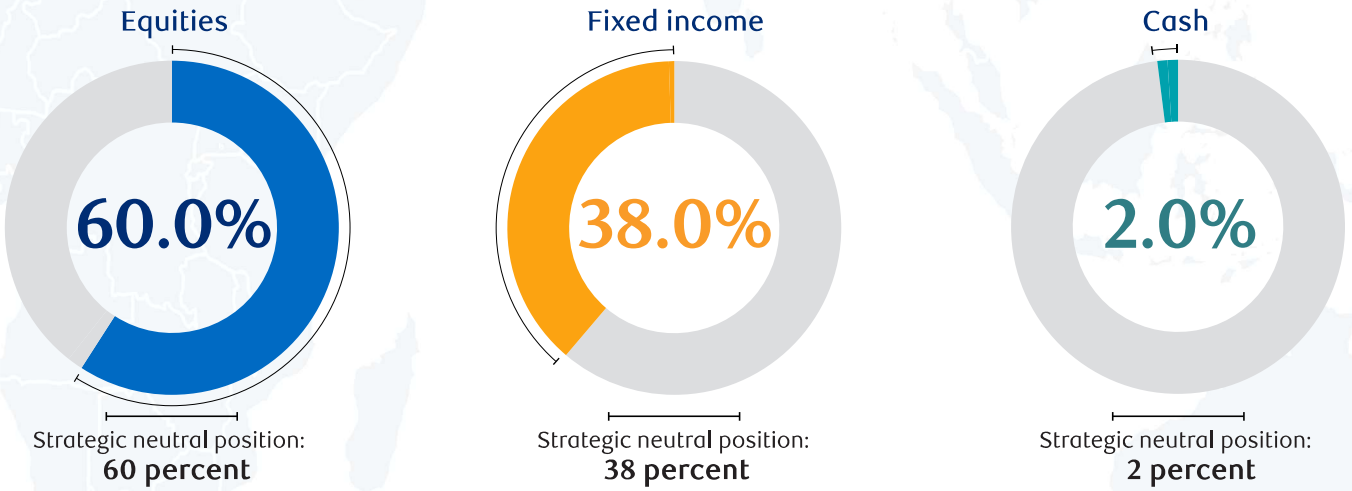
Global stocks extended their gains in the past quarter, but their performance so far this year has been increasingly concentrated to just a handful of names. The "Magnificent 7" – the largest U.S. publicly listed companies – have benefited tremendously from emerging trends in artificial intelligence (AI), which have propelled valuations of these stocks to especially demanding levels. The group now makes up over a quarter of the S&P 500 Index's market capitalization and has delivered outsized gains of 70% so far this year, contributing to almost three quarters of the S&P 500's 17% gain over that period. Returns offered by the rest of the market, however, pale in comparison. The equal-weighted S&P 500, a better representation of how the average stock has performed, is up just 5.8%. As a result, the performance of the S&P 500 is masking the fact that underlying market breadth has been relatively poor – often an indication that the economy is struggling or set to weaken. Although global equity-market valuations are not unreasonable, earnings are vulnerable to a contraction in economic activity, which limits the potential upside in stocks. In this late-cycle environment, we are looking for low-to-mid-single-digit returns for stocks, with relatively worse outcomes from U.S. equities due to their higher valuations and the influence of expensive mega-cap technology names that could falter if the economy entered a downturn.

Asset mix – maintaining neutral allocation

Assuming we are correct in our view that the economy is likely to enter recession over the next 12 months, interest rates, bond yields and stock prices could all be closing in on near-term peaks. While there are pathways to a positive outcome for the economy and markets if an economic soft landing is achieved, we think the reward for taking substantial risk in this environment is not as appealing as it would have been at earlier points in the cycle. Further supporting this view is the fact that the premium offered on stocks versus bonds is at its lowest level in nearly two decades. As a result, we have been gradually dialing down the equity overweight position in our asset mix over the past 18 months, balancing these near-term risks with the asset class's long-term upside potential. We have used those proceeds to narrow our prior underweight in fixed income as rising yields boosted the appeal of sovereign bonds, whose current elevated yields should provide a better ballast against any downturn in equities. Last quarter, we completed the process of fully closing our tactical risk exposures. This quarter, we maintain that neutral stance relative to our benchmark weights. For a balanced global investor, we currently recommend an asset mix of 60% equities (strategic neutral position: 60%) and 38% fixed income (strategic neutral position: 38%), with the balance in cash. Actual fund or client portfolio positioning may differ depending on individual investment policies.

Recommended asset mix

RBC GAM Investment Strategy Committee



Note: as of August 31, 2023. Source: RBC GAM

Economic & capital markets forecasts

Economic forecast (RBC GAM Investment Strategy Committee)

	United States		Canada		Europe		United Kingdom		Japan		China		Emerging markets*	
	Fall 2023	Change from Summer 2023	Fall 2023	Change from Summer 2023	Fall 2023	Change from Summer 2023	Fall 2023	Change from Summer 2023	Fall 2023	Change from Summer 2023	Fall 2023	Change from Summer 2023	Fall 2023	Change from Summer 2023
Real GDP														
2022A	2.06%		3.44%		3.41%		4.10%		1.01%		3.17%		3.49%	
2023E	1.90%	0.90	1.30%	0.70	0.50%	0.40	0.30%	0.50	2.00%	1.40	4.90%	(0.90)	4.70%	0.60
2024E	0.30%	(0.30)	0.20%	(0.50)	0.20%	(0.50)	0.20%	(0.40)	0.70%	(0.40)	4.40%	0.10	4.00%	(0.20)
CPI														
2022A	8.00%		6.80%		8.38%		9.07%		2.50%		1.87%		4.86%	
2023E	4.00%	0.10	3.70%	0.50	5.40%	(0.20)	7.40%	1.20	3.10%	0.60	0.50%	(0.20)	2.80%	(2.60)
2024E	2.20%	(0.20)	2.30%	0.10	2.10%	(0.40)	2.40%	N/C	1.50%	0.10	1.60%	(0.50)	3.10%	(2.50)

A = Actual E = Estimate *GDP Weighted Average of China, India, South Korea, Brazil, Mexico and Russia.

Targets (RBC GAM Investment Strategy Committee)

	August 2023	Forecast August 2024	Change from Summer 2023	1-year total return estimate* (%)
Currency markets against USD				
CAD (USD–CAD)	1.35	1.24	(0.02)	9.0
EUR (EUR–USD)	1.08	1.21	0.01	10.0
JPY (USD–JPY)	145.54	120.00	4.00	15.0
GBP (GBP–USD)	1.27	1.33	0.03	4.1
Fixed income markets				
U.S. Fed Funds Rate (upper bound)	5.50	4.50	(0.25)	0.0
U.S. 10-Year Bond	4.11	3.50	0.25	9.2
Canada Overnight Rate	5.00	4.25	0.25	0.0
Canada 10-Year Bond	3.56	3.00	0.25	8.4
Eurozone Deposit Facility Rate	3.75	3.25	(0.25)	0.0
Germany 10-Year Bund	2.47	2.60	0.35	1.3
U.K. Base Rate	5.25	5.25	0.50	0.0
U.K. 10-Year Gilt	4.36	4.25	0.50	5.3
Japan Overnight Call Rate	(0.06)	0.10	0.10	0.0
Japan 10-Year Bond	0.65	0.75	N/C	(0.3)
Equity markets				
S&P 500	4508	4400	275	(0.8)
S&P/TSX Composite	20293	20700	700	5.6
MSCI Europe	154	154	(6)	3.7
FTSE 100	7439	7500	(200)	5.0
Nikkei	32619	33100	600	3.4
MSCI Emerging Markets	980	1000	(10)	5.0

*Total returns are expressed in local currencies with the exception of MSCI Emerging Markets whose return is expressed in USD. Source: RBC GAM

Recommended asset mix

Asset mix – the allocation within portfolios to stocks, bonds and cash – should include both strategic and tactical elements. Strategic asset mix addresses the blend of the major asset classes offering the risk/return tradeoff best suited to an investor's profile. It can be considered to be the benchmark investment plan that anchors a portfolio through many business and investment cycles, independent of a near-term view of the prospects for the economy and related expectations for capital markets. Tactical asset allocation refers to fine tuning around the strategic setting in an effort to add value by taking advantage of shorter-term fluctuations in markets.

Every individual has differing return expectations and tolerances for volatility, so there is no "one size fits all" strategic asset mix. Based on a 40-year study of historical returns[1] and the volatility[2] of returns (the range around the average return within which shorter-term results tend to fall), we have developed five broad profiles and assigned a benchmark strategic asset mix for each. These profiles range from very conservative through balanced to aggressive growth. It goes without saying that as investors accept increasing levels of volatility, and therefore greater risk that the actual experience will depart from the longer-term norm, the potential for returns rises. The five profiles presented below may assist investors in selecting a strategic asset mix best aligned to their investment goals.

Each quarter, the RBC GAM Investment Strategy Committee publishes a recommended asset mix based on our current view of the economy and return expectations for the major asset classes. These weights are further divided into recommended exposures to the variety of global fixed income and equity markets. Our recommendation is targeted at the Balanced profile where the benchmark (strategic neutral) setting is 60% equities, 38% fixed income, and 2% cash.

A tactical range of +/- 15% around the benchmark position allows us to raise or lower exposure to specific asset classes with a goal of tilting portfolios toward those markets that offer comparatively attractive near-term prospects.

This tactical recommendation for the Balanced profile can serve as a guide for movement within the ranges allowed for all other profiles.

The value-added of tactical strategies is, of course, dependent on the degree to which the expected scenario unfolds.

Regular reviews of portfolio weights are essential to the ultimate success of an investment plan as they ensure current exposures are aligned with levels of long-term returns and risk tolerances best suited to individual investors.

Anchoring portfolios with a suitable strategic asset mix, and placing boundaries defining the allowed range for tactical positioning, imposes discipline that can limit damage caused by swings in emotion that inevitably accompany both bull and bear markets.

[1]**Average return**: The average total return produced by the asset class over the period 1983 – 2023, based on monthly results.
[2]**Volatility**: The standard deviation of returns. Standard deviation is a statistical measure that indicates the range around the average return within which 2/3 of results will fall into, assuming a normal distribution around the long-term average.

Global asset mix

	Benchmark policy	Allowable range	Fall 2022	New Year 2023	Spring 2023	Summer 2023	Fall 2023
Cash	**2.0%**	0.0% – 15.0%	1.0%	1.0%	1.5%	2.0%	**2.0%**
Bonds	**38.0%**	23.0% – 53.0%	37.5%	37.0%	37.5%	38.0%	**38.0%**
Stocks	**60.0%**	45.0% – 75.0%	61.5%	62.0%	61.0%	60.0%	**60.0%**

Note: Effective June 1, 2020, we reset our strategic neutral positions to reflect long-lasting changes in economy and capital markets' dynamics. Boosting strategic neutral equity exposure by 5% and reducing fixed income by same amount in our reference balanced portfolio.

Regional allocation

Global bonds	WGBI* August 2023	Allowable range	Fall 2022	New Year 2023	Spring 2023	Summer 2023	Fall 2023
North America	**45.2%**	35.2% – 55.2%	45.2%	51.8%	49.0%	42.7%	**40.3%**
Europe	**34.8%**	24.8% – 44.8%	40.2%	30.7%	31.2%	37.1%	**39.8%**
Asia	**20.0%**	10.0% – 30.0%	14.6%	17.6%	19.8%	20.3%	**20.0%**

Global equities	MSCI** August 2023	Allowable range	Fall 2022	New Year 2023	Spring 2023	Summer 2023	Fall 2023
North America	**69.8%**	59.8% – 79.8%	70.0%	71.0%	68.0%	67.7%	**69.3%**
Europe	**14.5%**	4.5% – 24.5%	14.0%	13.6%	15.5%	15.8%	**14.5%**
Asia	**7.4%**	0.0% – 17.4%	8.1%	7.4%	8.2%	8.4%	**8.2%**
Emerging markets	**8.3%**	0.0% – 18.3%	7.9%	8.1%	8.4%	8.1%	**8.1%**

Our asset mix is reported as at the end of each quarter. The mix is fluid and may be adjusted within each quarter, although we do not always report on shifts as they occur. The weights in the table should be considered a snapshot of our asset mix at the date of release of the Global Investment Outlook.

Global equity sector allocation

	MSCI** August 2023	RBC GAM ISC Summer 2023	RBC GAM ISC Fall 2023	Change from Summer 2023	Weight vs. benchmark
Energy	4.62%	5.09%	5.12%	0.03	110.8%
Materials	4.17%	4.33%	5.17%	0.85	124.0%
Industrials	10.97%	10.54%	12.97%	2.43	118.2%
Consumer discretionary	11.02%	10.64%	11.02%	0.38	100.0%
Consumer staples	7.33%	8.78%	7.33%	(1.45)	100.0%
Health care	12.58%	15.59%	12.58%	(3.01)	100.0%
Financials	14.88%	12.19%	13.58%	1.39	91.3%
Information technology	22.09%	23.02%	23.89%	0.86	108.1%
Communication services	7.21%	7.01%	7.21%	0.20	100.0%
Utilities	2.74%	1.31%	0.74%	(0.57)	27.0%
Real estate	2.40%	1.50%	0.40%	(1.10)	16.7%

*FTSE World Government Bond Index. **MSCI World Index. Source: RBC GAM Investment Strategy Committee

At RBC GAM, we have a team dedicated to setting and reviewing the strategic asset mix for all of our multi-asset solutions. With an emphasis on consistency of returns, risk management and capital preservation, we have developed a strategic asset allocation framework for five client risk profiles that correspond to broad investor objectives and risk preferences. These five profiles range from Very Conservative through Balanced to Aggressive Growth.

Very Conservative

Asset class	Bench-mark	Range	Last quarter	Current recommendation
Cash & Cash Equivalents	2%	0-15%	2.0%	2.0%
Fixed Income	73%	68-88%	73.0%	73.0%
Total Cash & Fixed Income	75%	60-90%	75.0%	75.0%
Canadian Equities	10%	0-20%	9.9%	9.9%
U.S. Equities	8%	0-18%	7.9%	7.9%
International Equities	7%	0-17%	7.2%	7.2%
Emerging Markets	0%	0%	0.0%	0.0%
Total Equities	25%	10-40%	25.0%	25.0%

	Return	Volatility
40-year average	7.5%	4.8%
Last 12 months	4.3%	6.8%

Very Conservative investors will seek income with maximum capital preservation and the potential for modest capital growth, and be comfortable with small fluctuations in the value of their investments. This portfolio will invest primarily in fixed-income securities, and a small amount of equities, to generate income while providing some protection against inflation. Investors who fit this profile generally plan to hold their investment for the medium to long term.

Conservative

Asset class	Bench-mark	Range	Last quarter	Current recommendation
Cash & Cash Equivalents	2%	0-15%	2.0%	2.0%
Fixed Income	58%	43-83%	58.0%	58.0%
Total Cash & Fixed Income	60%	45-75%	60.0%	60.0%
Canadian Equities	13%	3-23%	12.9%	12.9%
U.S. Equities	15%	5-25%	14.9%	14.9%
International Equities	12%	2-22%	12.2%	12.2%
Emerging Markets	0%	0%	0.0%	0.0%
Total Equities	40%	25-55%	40.0%	40.0%

	Return	Volatility
40-year average	8.0%	6.1%
Last 12 months	6.7%	7.7%

Conservative investors will pursue modest income and capital growth with reasonable capital preservation, and be comfortable with moderate fluctuations in the value of their investments. The portfolio will invest primarily in fixed-income securities, with some equities, to achieve more consistent performance and provide a reasonable amount of safety. The profile is suitable for investors who plan to hold their investment over the medium to long term.

Balanced

Asset class	Bench-mark	Range	Last quarter	Current recommendation
Cash & Cash Equivalents	2%	0-15%	2.0%	2.0%
Fixed Income	38%	23-53%	38.0%	38.0%
Total Cash & Fixed Income	40%	25-55%	40.0%	40.0%
Canadian Equities	15%	5-25%	14.8%	14.8%
U.S. Equities	25%	15-35%	24.8%	24.8%
International Equities	15%	5-25%	15.5%	15.5%
Emerging Markets	5%	0-15%	4.9%	4.9%
Total Equities	60%	45-75%	60.0%	60.0%

	Return	Volatility
40-year average	8.4%	7.7%
Last 12 months	9.5%	9.1%

The **Balanced** portfolio is appropriate for investors seeking balance between long-term capital growth and capital preservation, with a secondary focus on modest income, and who are comfortable with moderate fluctuations in the value of their investments. More than half the portfolio will usually be invested in a diversified mix of Canadian, U.S. and global equities. This profile is suitable for investors who plan to hold their investment for the medium to long term.

Growth

Asset class	Bench-mark	Range	Last quarter	Current recommendation
Cash & Cash Equivalents	2%	0-15%	2.0%	2.0%
Fixed Income	23%	8-38%	23.0%	23.0%
Total Cash & Fixed Income	25%	10-40%	25.0%	25.0%
Canadian Equities	18%	8-28%	17.8%	17.8%
U.S. Equities	30%	20-40%	29.8%	29.8%
International Equities	19%	9-29%	19.6%	19.6%
Emerging Markets	8%	0-18%	7.8%	7.8%
Total Equities	75%	60-90%	75.0%	75.0%

	Return	Volatility
40-year average	8.6%	9.5%
Last 12 months	11.6%	10.4%

Investors who fit the **Growth** profile will seek long-term growth over capital preservation and regular income, and be comfortable with considerable fluctuations in the value of their investments. This portfolio primarily holds a diversified mix of Canadian, U.S. and global equities and is suitable for investors who plan to invest for the long term.

Aggressive Growth

Asset class	Bench-mark	Range	Last quarter	Current recommendation
Cash & Cash Equivalents	2%	0-15%	2.0%	2.0%
Fixed Income	0%	0-15%	0.0%	0.0%
Total Cash & Fixed Income	2%	0-17%	2.0%	2.0%
Canadian Equities	29%	19-39%	28.8%	28.8%
U.S. Equities	38%	28-48%	37.8%	37.8%
International Equities	20%	10-30%	20.7%	20.7%
Emerging Markets	11%	1-21%	10.7%	10.7%
Total Equities	98%	83-100%	98.0%	98.0%

	Return	Volatility
40-year average	8.9%	12.0%
Last 12 months	14.3%	12.3%

Aggressive Growth investors seek maximum long-term growth over capital preservation and regular income, and are comfortable with significant fluctuations in the value of their investments. The portfolio is almost entirely invested in stocks and emphasizes exposure to global equities. This investment profile is suitable only for investors with a high risk tolerance and who plan to hold their investments for the long term.