RBC WEALTH MANAGEMENT

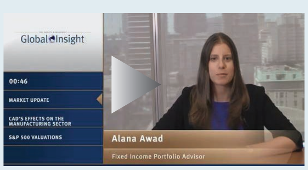
Global Insight

Perspectives from the Global Portfolio Advisory Committee

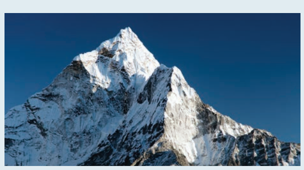
Loonie letdown

An adjustment in altitude could be in store for the loonie as it appears vulnerable to some gathering headwinds.

Rajan Bansi | Page 4



Video
September edition highlights



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RBC Wealth Management

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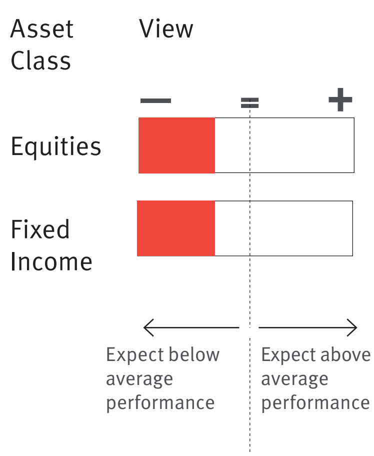

See "Views explanation" below for details

Source - RBC Wealth Management

Equities

- The nearly 10% post-Brexit rally in the MSCI World Index is losing momentum as we head into September, typically a slow month for equities. Greater market, sector, and stock selectivity seem warranted.
- We continue to favor North America. U.S. earnings trends suggest improved growth over the next two quarters and in 2017 as the Energy sector stabilizes/recovers. If oil prices work their way higher, as we anticipate, Canada's TSX should also benefit. Furthermore, select Asian markets still offer attractive relative value.
- We maintain Underweight positions in Continental Europe and the U.K. partly due to Brexit negotiation risks. Europe also remains vulnerable to earnings missteps, negative interest rate pressures on banks, and political crosscurrents. Our modest Underweight recommendation for global equities overall stems from concerns in this region.

Fixed Income

- Volatility could pick up this month as high-profile central bank meetings set the near-term direction for the market. While some Federal Reserve officials recently indicated a September rate hike is possible, the futures market is pointing toward December, and we believe 2017 is more likely. Whether the European Central Bank and Bank of Japan layer on additional quantitative easing could end up having a greater impact on the global fixed income market's next move.
- Corporate credit remains our favorite sector; however, the pool of attractively valued securities has diminished meaningfully. We would continue to exercise caution in putting new money to work. At this stage, we recommend investors consider shifting out of overvalued corporate securities by swapping into those that offer better relative value or into cash for future opportunities.

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.

= In-line 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

Loonie letdown

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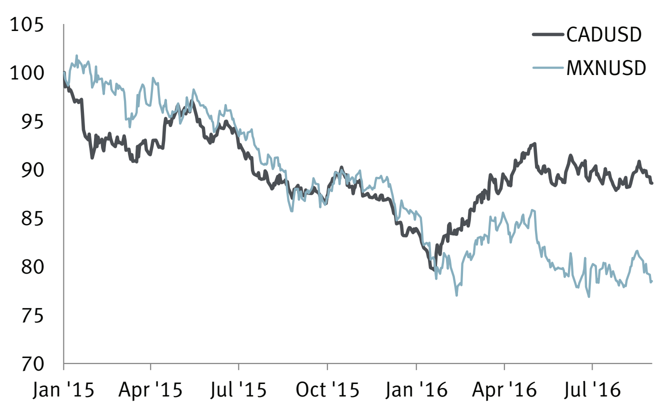
Investors hoping for a Bank of Canada interest rate hike to help boost loonie value are likely to be disappointed as the BoC's focus shifts to the need for non-energy sector growth. However, we believe additional obstacles to increased loonie strength may be on the horizon and not necessarily from within the Canadian border.

The Canadian dollar has traded within a relatively narrow range after an ominous dip below US$0.69 early in the year. By the middle of March it had rallied sharply to US$0.76 and has stayed within US$0.03 of that level. We believe any further strength in the Canadian dollar for the balance of 2016 will be limited as the Bank of Canada (BoC) maintains its accommodative policy stance amidst what it sees as a complex transition towards non-energy sector-led growth through 2017. In fact, the risks for the Canadian dollar may be tilted to the downside as uneven activity out of the manufacturing sector may prolong the BoC's current accommodative policy stance even as the Federal Reserve moves closer to a rate hike in 2017. Should a backdrop of sputtering growth in Canada develop concurrent with rising U.S. rates, we believe a retreat by the loonie toward the mid-to-low US$0.70s is likely.

The non-energy economy is not yet carrying the load

Exports are notoriously volatile, and data released as of this writing has provided a mixed picture. Helpfully, manufacturing sales grew at a faster-than-expected pace in June with a rebound in machinery and transportation equipment a particularly welcome sign. Against this, sales in the auto sector improved less than expected. The BoC was clear in its July *Monetary Policy Report* that firmer activity from the non-energy sector of the economy was necessary if its H2 2016 (+3.2%) and full year 2017 (+2.2%) growth forecasts are to be met. It conceded that monthly data on

Loonie exhibiting relative strength



The loonie's relative strength versus the peso has been a headwind for manufacturers.

Source - RBC Wealth Management, Bloomberg; data through 8/31/16

All values in this article in Canadian dollars, unless otherwise stated.

goods exports to date had been disappointing, with resulting business investment and employment opportunities "progressing, albeit unevenly." If growth from the sector continues to sputter in the coming months, the BoC may have to downgrade its outlook for growth and inflation.

Financial markets are pricing in *zero* chance of a BoC interest rate hike this year.

Questions about the health of the non-energy export market in Canada are partly behind the reason RBC Capital Markets believes the Canadian dollar could dip to US$0.73 by the end of September and finish the year near US$0.75.

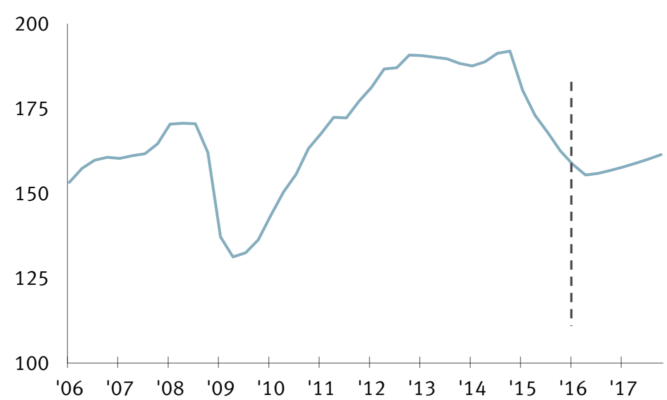
BoC on hold as business investment remains lethargic

Financial markets are pricing in *zero* chance of an interest rate hike by the BoC in 2016 and only a 10% chance of a rate hike by the end of 2017. In fact, we believe there are greater prospects for an interest rate cut in 2017 (18% probability) as the growth and inflation picture remain muddled.

Aside from concerns regarding exports, we think there is another important reason the BoC may stay on hold for longer than markets are expecting—the slow recovery of business investment. The chart below shows how investment in Canada will likely finish 2016 essentially flat with where it was 10 years ago, with only a modest uptick expected in 2017. The contraction of investment in the energy sector has no doubt contributed in large part to this, as capital spending could finish 2016 at a level 60% below what the sector posted in 2014. The decline, which has been breathtaking as much for its speed as its magnitude, will leave investment in the Energy sector as a percentage of nominal GDP at a decade low of just 1.5%.

Canada: Investment in non-residential structures, machinery, and equipment

Chained 2007 ($ in billions)



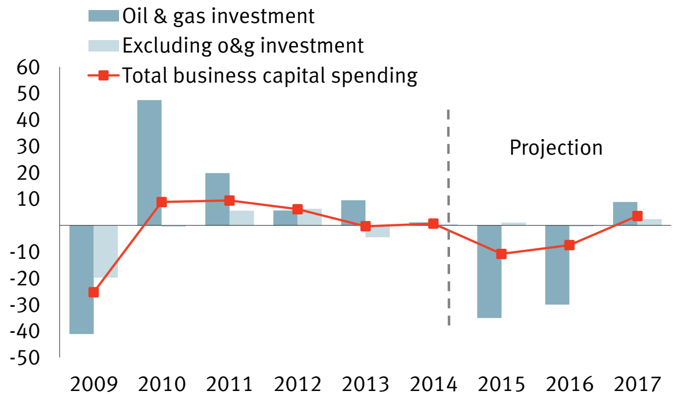
Total business investment is subdued, essentially flat with 10 years ago.

Source - Statistics Canada, RBC Economics Research

Yet, the non-energy sector has picked up very little of the slack. The chart on the following page shows how RBC Economics expects business investment to be restrained outside the oil and gas industry through 2017, a trend already in place for several years.

Canada business investment by industry

Annual percent change



Source - Statistics Canada, RBC Economics Research

Non-energy sector has yet to fill the business investment void.

Canada's share of North American auto sector production is only 16% versus Mexico's 20%.

Much of this disappointing growth in non-energy capital spending can be traced to the important auto sector where capital outlays have been more or less flat for 4.5 years despite the fact North American unit sales are at all-time highs and Canadian auto, truck, and parts manufacturing sales are approaching the prior cycle peak. Canada's competitive challenge comes into sharper focus when one considers the position of Mexico where exports have risen 1,000% since the advent of the North American Free Trade Agreement (NAFTA) in 1994. The country holds a 20% share of auto sector production in North America, up from 6% before NAFTA was signed and exceeding Canada's 16% share. Recently Mexico became more competitive vis-à-vis Canada as the peso has fallen 10% more than the Canadian dollar has versus the greenback since the beginning of 2015.

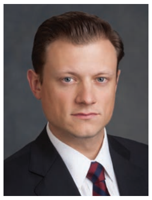
Could higher U.S. rates clip the loonie's wings?

The next leg lower for the Canadian dollar may be a function of higher U.S. interest rates. Minutes from the July Federal Open Market Committee (FOMC) meeting pointed to a Fed that recognized the robust health of the domestic labour market. The July employment report, which was released after the FOMC meeting had occurred, was much better than expected and included an upward revision of the June report. The Fed has continued to advocate patience in the face of global uncertainty and stubbornly low inflation in the U.S. But, a rate hike in 2017 seems increasingly likely should growth continue at its current pace. The futures market is placing a better than 50% chance the Fed will raise the Fed Funds target rate by 25 basis points by the middle of 2017 with a 25% chance of two interest rate hikes by the end of 2017

Ultimately, the most likely catalyst for Canadian dollar weakness in the rest of 2017 may be the rising likelihood of a rate hike south of the border as the Bank of Canada stays on hold.

Focus article

Peak perspective



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The stock market finally ascended to a new all-time high earlier this summer—more than a year since the last such milestone. The history of "dry spells" between new highs that last longer than a year strongly suggests the market will be up in the subsequent 12 months by about 12%.

If that were to happen, U.S. stocks would have moved from modestly overvalued, where they are today, to more extravagantly valued. This is not impossible, maybe even likely. But this would raise questions about the market's return potential for the following years and about the scale of risks facing investors were the economy to fall into recession.

The market spends a lot of time backing and filling

New all-time closing highs appear to be something of a rarity, occurring in roughly 7% of the trading days between September 22, 1954 and July 11, 2016.

There have been just 13 instances since September 22, 1954 in which it has taken the S&P 500 more than a calendar year to reach a new all-time closing high, i.e., a long-term dry spell.

Periods where the S&P 500 took more than one calendar year to reach a new all-time closing high

Prior all-time high	New all-time high	Calendar days between highs	Max drawdown between highs	Returns after new high		
				6 months	12 months	18 months
08/02/56	09/24/58	783	-22%	12%	14%	12%
08/03/59	01/27/61	543	-14%	9%	11%	-7%
12/12/61	09/03/63	630	-28%	8%	14%	20%
02/09/66	05/04/67	449	-22%	-3%	4%	9%
11/29/68	03/06/72	1,193	-36%	2%	5%	-3%
01/11/73	07/17/80	2,744	-48%	11%	8%	-5%
11/28/80	11/03/82	705	-27%	14%	14%	13%
10/10/83	01/21/85	469	-14%	11%	17%	35%
08/25/87	07/26/89	701	-34%	-4%	5%	-1%
02/02/94	02/14/95	377	-9%	16%	36%	37%
03/24/00	05/30/07	2,623	-49%	-3%	-8%	-47%
10/09/07	03/28/13	1,997	-57%	7%	18%	26%
05/21/15	07/11/16	417	-14%	TBD	TBD	TBD
	High	2,744	-9%	16%	36%	37%
	Average	1,049	-29%	7%	12%	8%
	Low	377	-57%	-4%	-8%	-47%

Source - RBC Wealth Management, Bloomberg, Standard & Poor's; data from 9/22/54 through 7/11/16

Following previous dry spells, the S&P 500 appreciated 12%, on average, over the next 12 months.

However, those 13 each lasted approximately three years (1,049 days) on average, which leads to a somewhat surprising observation that most of the past 62 years has been spent in such dry spells. Specifically, of the 22,573 calendar days from September 22, 1954 to July 11, 2016, long-term dry spells comprise 60% (13,631 days), leaving 40% (8,942 days) during which the market was tallying new all-time highs at least once a year.

So, while the S&P 500 has appreciated materially over time, this analysis shows that the market spends a lot of time backing and filling.

Finally, we note that the most recent dry spell, which lasted slightly more than a year and saw the market draw down 14% peak to trough, was less severe than the average three-year, 29% drawdown (see table on previous page).

Room to run?

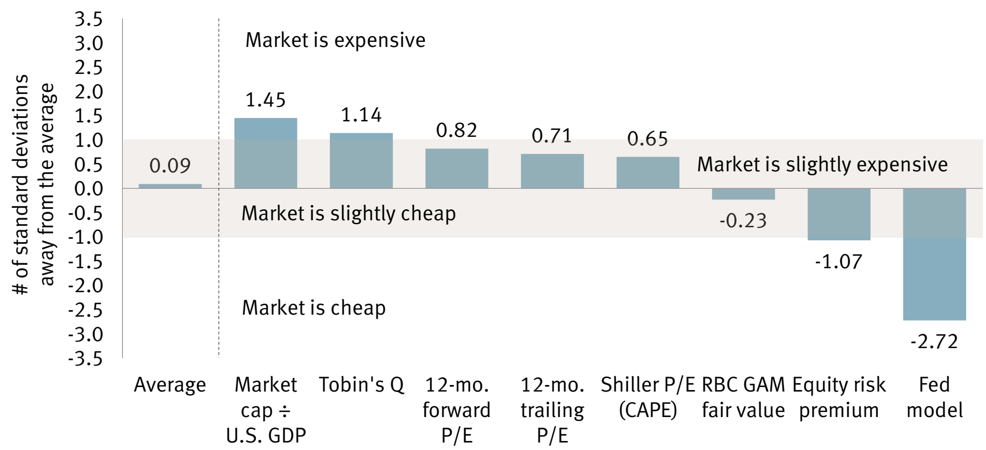
In the previous 12 instances in which it has taken the market more than a year to reach a new all-time closing high, the S&P 500 appreciated 7%, on average, over the next six months and 12% over 12 months.

How would such a gain, if it occurred, leave the market from a valuation perspective?

The chart below rates seven popular value metrics, as well as one proprietary to RBC Global Asset Management, as to whether the S&P 500 is expensive or cheap. They range from "expensive" (the so-called Buffett indicator—the market value of stocks compared to the size of the economy) all the way to "cheap" (the Fed model that relates the market's price-to-earnings, or P/E, ratio to the 10-year Treasury yield). A simple average of all eight valuation scores would suggest the market is modestly overvalued.

S&P 500 Index

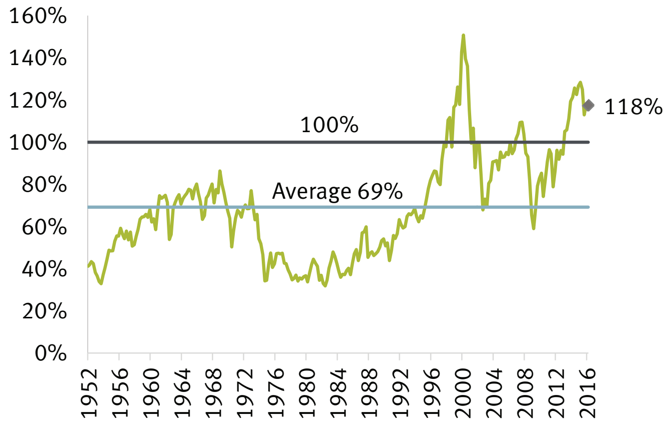
Normalized valuation metrics as of August 2016



Notes: Historical data from Jan 1956 for 12-mo. trailing P/E, 12-mo. forward P/E, Equity risk premium, Schiller P/E, and Fed model; from Mar 1956 for Market cap ÷ U.S. GDP; and from Jan 1960 for RBC GAM fair value.
Source - Haver Analytics, RBC Capital Markets, RBC Global Asset Management

If we roll forward to next summer and imagine the S&P 500 is at 2394, up 12% from the recent July 11 new peak of 2137, then some (but not all) of these valuation measures would have moved upward, more deeply into the expensive zone.

The Buffett Indicator



While currently above its long-term average, the Buffett Indicator suggests valuations are far from the excesses observed during the Tech bubble.

Source - RBC Wealth Management, Bloomberg, Federal Reserve, U.S. Bureau of Economic Analysis

It's not high valuation that turns the market down.

Certainly P/E ratios would be higher than today. RBC Capital Markets LLC Chief U.S. Equity Strategist Jonathan Golub forecasts S&P 500 earnings per share to be flat again at $118 this year for the third year running, rising by just 5% to $124 in 2017. If the market is up by 12%, then its P/E ratio would shift higher from 18.1x to 19.3x.

And the market value of stocks would rise from 118% of the level of GNP to an estimated 126%—still well short of the 151% posted at the peak of the tech bubble in 2000, but more deeply into expensive territory nonetheless.

On the other hand, both the Fed model and RBC's proprietary valuation model would still rate the market as inexpensive and below calculated "fair value."

Aside from brief moments at the bottom of sharp, often unsettling, market pullbacks, mouth-watering valuations haven't been available for some time. It's also worth remembering that there is no line in the sand beyond which valuation cannot go. And it's not high valuation that turns the market down. Rather it's changes in policy, usually credit policy, that turn the expected trajectory of the economy lower, and with it the market. When that day comes—and we think it is still quite some ways off—valuation at the market peak will tell the investor something about how far the market might have to retreat before attracting sustainable new buying.

Until credit conditions appear that would threaten the economic expansion, which, in our view, would require a Fed funds rate north of 1.50%, the market is likely to go on delivering worthwhile all-in returns—all the more so now the latest dry spell for new highs has ended.

Patience rewarded

It's been a good run. Since the February lows the MSCI World Index is up 17%. The S&P 500 is ahead by 20%, posting several new all-time highs since mid-July. These new highs hold positive implications for the year ahead, in our view (see *Peak perspective* on page 7). Most other markets turned in strong performances but remain below their own all-time highs.

So far, these gains have been mostly due to an expansion of price-to-earnings (P/E) multiples. With earnings flat year to date at $118 per share, the gains since February have been attributable to the market's P/E rising—from 15.3x to 18.3x. Investors have not been overly concerned about this big jump in valuation for two reasons:

- **Because P/Es usually go up when corporate borrowing costs are falling**, which they did. Moody's Baa yields fell from 5.55% all the way down to 4.15% in just seven months, one of the steepest declines on record.
- **Because much of the profit weakness was due to the collapse of earnings in just one sector—Energy**. And as oil prices rebounded, doubling off the February low of $26 per barrel, investors realised that Energy sector earnings could be contributing to growth, rather than subtracting, by Q3 or Q4.

On the simplistic assumption that such measures don't move in a straight line in the same direction forever, it might be prudent to expect that oil prices, bond prices, and stock prices might give back some of the gains racked up over the past half year.

For oil that is already happening. A few weeks ago oil was at $52 per barrel and appearing unstoppable on its way to $60 or higher. Now, however, oil is back below $45, oil stocks are weakening again, and confidence is wobbling. The bond market may also be vulnerable to over-optimism with respect to the scope for further interest rate declines in the short run.

To this, one could add we have just entered the seasonally weakest few weeks of the year—particularly relevant in a presidential year—and that there is a long list of other factors investors may choose to worry about, from Brexit, to Italian banks, to a weakening Chinese currency, to geopolitics. Our conclusion is that the next couple of months could see the market give back some of its gains, or at least experience a bout of volatility.

We remain committed to our long-held view that equities should be given the benefit of the doubt as long as no U.S. recession or global economic downturn is in sight—and in our view none is. We would approach any market weakness opportunistically.

Equity views

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

Source - RBC Wealth Management

Regional highlights

United States

- The S&P 500 is showing nascent signs of fatigue after rallying 8.5% from the Brexit low in late June and climbing to new all-time highs. If a typical

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seasonal pullback occurs this month or next month, we would use it as a buying opportunity.

- The U.S. economy seems well positioned to deliver above-trend growth in Q3 helped by strong consumer spending, a rebound in business investment, and inventory adjustments. Recession risks remain very low. S&P 500 earnings could climb back into positive territory in Q3 for the first time in more than a year as Energy sector losses diminish. The market should be supported by mid-single digit or better earnings growth in 2017, depending on the path of crude oil.
- The Technology sector remains our favorite due to attractive valuations, above-average growth prospects, and the competitive advantages of the sector's most innovative companies. Bank stocks are our preferred deep value plays. Bank capital positions are strong and balance sheets are sturdy at the same time price-to-book ratios are near historic lows. If the Fed raises interest rates by 25–50 basis points in the next year—a likely scenario—we believe bank stocks would perform well.

Canada

- We maintain our Overweight recommendation in Canadian equities where we believe the outlook for key sectors continues to look favourable.
- Q3 Canadian bank results generally exceeded expectations, driven by stronger-than-expected performance in capital markets units and lower-than-expected credit losses. Cost containment initiatives showed progress and should help banks generate earnings growth in spite of revenue headwinds. Should analyst expectations for credit losses prove to be overly conservative, there is scope for upward revisions to earnings estimates.
- Real estate investment trusts have outperformed year to date as long-term interest rates have declined. While RBC Capital Markets estimates that valuations relative to net asset value are no longer cheap, the cash flow yield premium relative to fixed income remains attractive.
- We believe rail stocks have upside potential due to considerable operating leverage should volumes move higher. In response to a year and a half of declining carloads, management teams have taken aggressive action to rationalize costs. The rate of decline in industry carloads has eased of late, with grain in particular showing signs of positive inflection. A pickup in volumes could result in meaningful earnings growth.
- The combination of geopolitical tensions, economic uncertainty, and accommodative monetary policy provides a favourable backdrop for gold exposure. We expect precious metal producer share prices to remain highly sensitive to the price of the underlying commodity and would be selective with our entry point for investors looking to add exposure.

Continental Europe & U.K.

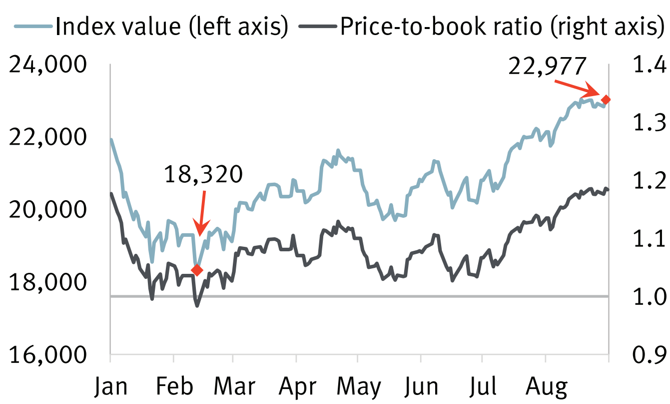
- We are Underweight European equities. A lacklustre earnings season and renewed euro strength are unlikely to lead to significant earnings upgrades in the short term. Upward revisions would be needed, in our view, for equities to break out from their recent trading range. The upcoming political cycle, with countries representing more than 50% of EU GDP going to the polls over the next 18 months, adds to our cautious view given rising levels of euro scepticism. We have adopted fairly defensive positioning with a preference for companies in the Health Care and Telecom sectors.

- We are Underweight U.K. equities as we are concerned the economic risks of Brexit are not fully reflected in valuations. The U.K.'s negotiation strategy to extricate itself from the EU is slowly emerging. More clarity would be welcome as uncertainty will likely start to erode economic prospects, despite the Bank of England's renewed quantitative easing efforts.
- In this lower-for-longer interest rate environment, we continue to have a bias towards dividend payers and growers and particularly prefer those that generate sales from a well-diversified international base. We favour Consumer Staples, Health Care, and selective Consumer Discretionary stocks. We would increase our exposure to domestic cyclicals once the economy and the pound stabilise and valuations become more attractive.

Asia

- Asian equities have continued to consolidate after the steep correction in the first quarter. Valuations in many parts of the region are now closer to fair value after reaching very inexpensive levels earlier in the year. In Hong Kong, the Hang Seng Index, which at one point was trading at book value, has rallied 25%. Consensus estimates for Asian equities' earnings growth, which have been subdued for 2016, are trending upwards for 2017 and could provide a fresh tailwind for stocks.
- Share price performance has recently been aided by stable economic data from China and an absence of headline events in the mainland equity market. The housing market in China has shown some notable strength that has led to tightening measures in certain locations.
- The Chinese currency has declined modestly against the USD in recent months but investors now seem comfortable with the trading profile of the renminbi. RBC Capital Markets forecasts further declines for the currency against the dollar on the horizon. Capital outflows from China, a concern earlier in the year, have become significantly smaller.
- Japan's TOPIX Index has also traded in a range, albeit fairly wide, since its February low. This is despite the strong appreciation of the yen against the dollar since then. The rally in the yen appears to have encountered resistance at the USDJPY100 level. The TOPIX trades at an undemanding valuation of 1.17x book value.

Hang Seng price levels and price-to-book ratio

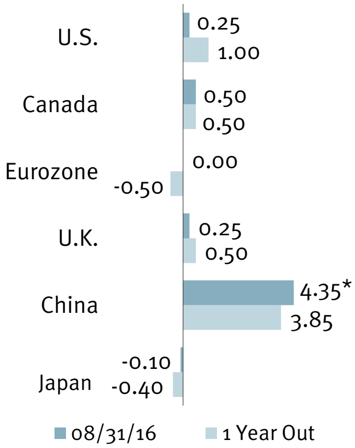


Hong Kong rallies 25%-plus off the low amid cheap P/B ratios.

Source - RBC Wealth Management, Bloomberg; data through 8/31/16

Preparing for the next step?

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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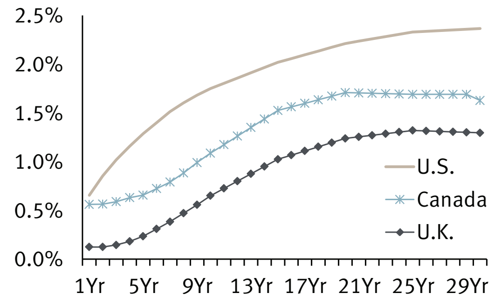
Summer vacation will end early for fixed income investors after Fed Chair Janet Yellen put the market on notice that an interest rate hike could be on the horizon. Speaking at the Jackson Hole Symposium in late August, Yellen said the sustained pace of job gains had left central bank officials confident the time had come for the next step in the current rate-hiking cycle. The futures market expects the Fed to wait until December of this year before raising rates another 25 basis points, although a strong employment report on September 2 could increase the odds of the central bank moving sooner. We continue to believe the Fed's next rate increase will be in 2017 despite the strength of recent economic data as this would be in the spirit of the patient and gradual approach to policy tightening Yellen has emphasized.

We continue to favor corporate credit but caution that investors must now be selective. Credit spreads have tightened materially over the course of the year, and opportunities now exist at the security level as opposed to the sector level. In instances where valuations are now full, investors should consider taking advantage of the liquidity in the marketplace and either raise some cash or switch into other issues that may be attractive from a relative value perspective

Sovereign yield curves



Source - Bloomberg

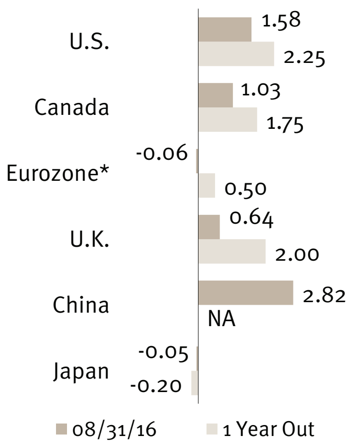
Regional highlights

United States

- Fed Chair Janet Yellen's Jackson Hole speech affirmed that policymakers will remain patient in raising rates and lacked any firm signal of an imminent rate hike. Every meeting is still "live," but concerns over inflation, low productivity growth, and global developments will likely keep the Fed grounded into 2017. Yellen emphasized that quantitative easing will remain the primary policy hammer in the Fed's toolkit, when needed, as it's seen as a more-effective option than negative rates.
- Yields on investment-grade and speculative-grade ex-energy corporates approached five-year lows in August with further declines in Treasuries. However, spreads—or compensation for credit risk—remain near five-year averages, suggesting to us that markets are fairly priced. As such, we see the most-attractive relative value for new money in $1K par fixed-to-float preferred shares.
- Municipals continue to benefit from strong demand led by bond fund inflows with the tally now at 47 consecutive weeks of positive inflows. We are expecting a significant increase in new issuance this month with estimates topping $14B, which could pressure yields higher. We would view any volatility, as the market absorbs the increased new issuance, as opportunities for investors amid muted expectations for any imminent Fed action.

Global fixed income

10-year rate (%)



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

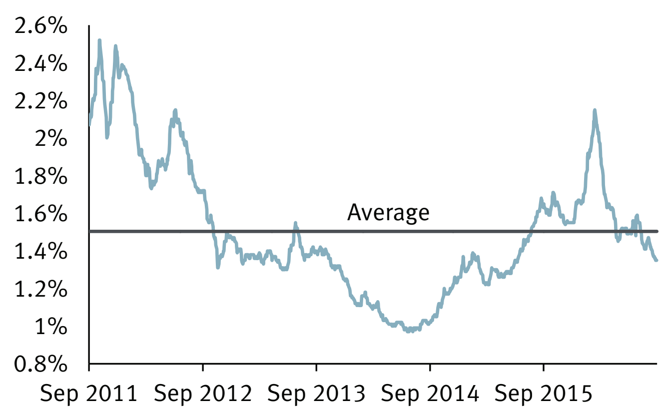
Canada

- Disappointing data in August has led to increased conjecture around the need for incremental fiscal and monetary stimulus in Canada. If the data continues to be weak through September, the Bank of Canada (BoC) will most likely have to revise down its growth and inflation forecasts in its next *Monetary Policy Report*, scheduled for release in October.
- If the BoC stands pat as the Federal Reserve moves closer to a rate hike, we believe the Canadian rates market will outperform. We recommend investors favor the 5- to-10-year portion of the Canadian yield curve as a result.
- Despite weakness following some issuance towards the end of the month, the preferred share market ended August 0.5% higher after reaching a new year-to-date high on August 9.

Continental Europe & U.K.

- Bond yields in the U.K. reached new lows as the Bank of England (BoE) delivered a raft of measures to combat the expected negative effects of the U.K.'s vote to leave the EU. The yield on the 10-year gilt reached 0.50%, a large differential of 100 basis points versus the equivalent issue by the U.S. Treasury. Although this sharp move has arguably been too quick, a further interest rate cut is expected which should keep gilt yields low.
- Recent data hints the eurozone may be less affected by the Brexit vote than feared, providing a boost to European fixed income markets. Core country yields have been range-bound and are expected to be anchored by the expectation of future central bank action while peripheral spreads could level out after narrowing in August.
- U.K. credit spreads have tightened significantly since the BoE's recent stimulus measures. Last month we noted that valuations were particularly attractive, but this has firmly reversed. We expect the policy to be supportive of credit spreads going forward; however, it is difficult to justify current valuations given the uncertainty ahead.

Investment-grade spreads



With credit spreads materially tighter year to date, investors should focus on selective opportunities at the security level rather than the broader sector level.

Source - RBC Wealth Management, Bloomberg; data through 8/29/16

Grainy days

Commodity forecasts

	2016E	2017E
Oil (WTI $/bbl)	45.00	59.00
Natural Gas ($/mmBtu)	2.40	3.00
Gold ($/oz)	1,325	1,500
Copper ($/lb)	2.10	2.25
Corn* ($/bu)	3.59	3.90
Wheat* ($/bu)	4.30	4.88

*Corn and wheat 2016 forecasts are for H2 2016 per Bloomberg consensus.

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

Corn & wheat

Wheat prices are at decade lows, while corn prices are barely better, as 2016 shapes up to be the fourth-straight year of bumper crops thanks to favorable weather conditions.

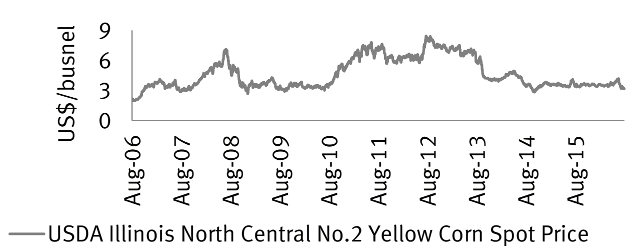
The August edition of the U.S. Department of Agriculture's *World Agricultural Supply and Demand Estimates* (WASDE) report is arguably the most important of the year given the robust data available as Northern Hemisphere crops enter the late stages of the growing season.

Global wheat production has been trending around 700 million–730 million tonnes since 2013, much higher than the 650 million–680 million tonne range for the prior five years. Global output for the 2015-2016 crop year is high in the context of these levels at 735 million tonnes according to the report. Positive growing conditions in Russia, Ukraine, Canada, and Australia have more than offset a damaged crop caused by excessive rain in France, Europe's biggest producer.

Like wheat, global corn production has also been elevated at around 950 million–1 billion tonnes since 2013, much higher than the 750 million–850 million tonne range for the prior five years. Global output for the 2015-2016 crop year remains robust at an estimated 960 million tonnes according to the report. Dry conditions in Brazil and eastern Canada have led to lower expected output. The U.S. Corn Belt, the world's dominant producer, has suffered somewhat from elevated summer temperatures but is expected to deliver a solid level of production this year with acreage sown at the third-highest level since 1944.

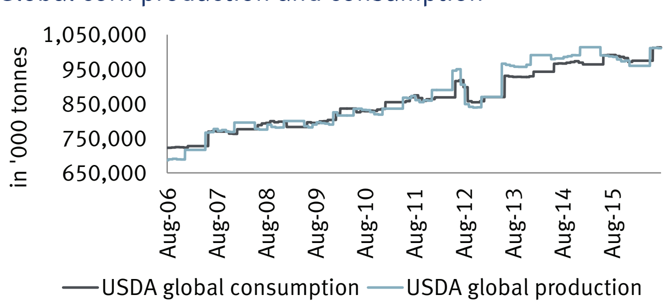
The bounty of recent years has accommodated the continued march forward in consumption as human population expands. High stock-to-use ratios may provide a temporary buffer for future production lulls; however, prices are likely at unsustainably low levels.

Historical corn prices



Steadily rising demand has been met with unusually good growing conditions in recent years keeping prices down.

Global corn production and consumption



Source - Bloomberg, U.S. Department of Agriculture (USDA)

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Currencies

Currency forecasts

Currency pair	Current rate	Forecast Sep 2017	Change*
Major currencies			
USD Index	96.02	100.59	5%
CAD/USD	0.76	0.77	1%
USD/CAD	1.31	1.30	-1%
EUR/USD	1.12	1.03	-8%
GBP/USD	1.31	1.20	-8%
USD/CHF	0.98	1.06	8%
USD/JPY	103.43	95.00	-8%
AUD/USD	0.75	0.67	-11%
NZD/USD	0.73	0.59	-19%
EUR/JPY	115.40	98.00	-15%
EUR/GBP	0.85	0.86	1%
EUR/CHF	1.10	1.09	-1%
Emerging currencies			
USD/CNY	6.68	7.40	11%
USD/INR	66.96	72.00	8%
USD/SGD	1.36	1.58	16%
USD/PLN	3.91	4.08	4%

* 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

We maintain our bullish outlook on the dollar and anticipate a necessary degree of patience for gains to materialise. The dollar reacted to mixed economic data in August as weak inflation and a miss in retail sales were offset by a strong nonfarm payroll report, the latest in a string of encouraging jobs reports, which could inch the Federal Reserve closer to its next interest rate hike. Anticipation of a Fed rate hike should be a tailwind for the greenback, given other major central banks remain highly accommodative.

Euro

The European Central Bank is scheduled to meet this month, the first time since July, when it decided against fresh stimulus until the post-Brexit landscape was clearer. Besides Brexit contagion effects, another concern for the eurozone is the upcoming political cycle, with many powerful nations within the single market holding votes in the coming year. We believe this only adds further uncertainty for the region looking ahead, and more headwinds for the single currency.

British pound

The Bank of England was one of the few central banks to meet in August, and it made the most of the spotlight by cutting rates to a historic low, increasing the quantitative easing program, and introducing a new lending measure to ensure lower interest rates are passed onto the economy. This was above and beyond what had been priced into the GBP, and, as a result, sterling weakened on the headline. In amongst slightly more mixed U.S. data, some of these losses have been regained, although our longer-term outlook remains for a weaker pound as Brexit-related uncertainties and economic headwinds continue.

Canadian dollar

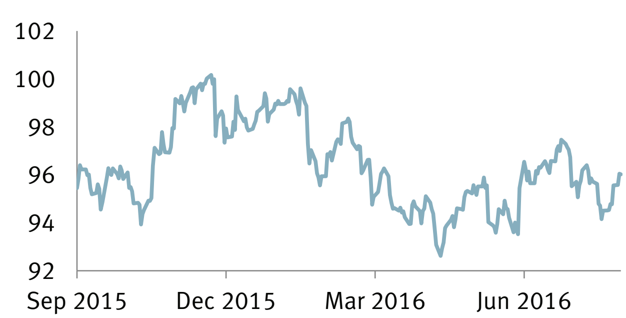
September will be an important month for the direction of the loonie for the next few months. While the Bank of Canada (BoC) is on hold for the foreseeable future, the Fed could very well signal it is nearing a decision to hike rates. If economic data continues to disappoint in September, as it did in August, the BoC could be forced to ratchet down its expectations for growth and inflation yet again. Calls for more fiscal and monetary stimulus, currently only a murmur, could reach a crescendo by October when the BoC is scheduled to release its next *Monetary Policy Report*.

Japanese yen

The USD/JPY has primarily stayed above the 100 level since further fiscal and monetary stimulus over the summer fell short of market expectations. With the likelihood of further policy changes in the near term significantly reduced, we see little to prevent a gradual appreciation of the yen.

Investors should remain patient for U.S. dollar gains

US Dollar Index



Despite recent pullback, USD positioned well for appreciation.

Source - RBC Wealth Management, Bloomberg; data as of 8:00 am GMT 8/31/16

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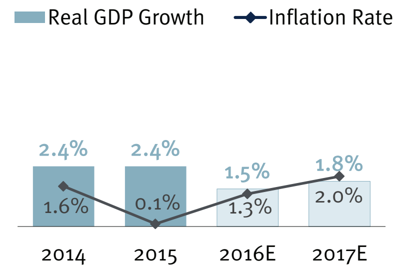
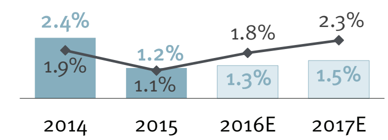
Key forecasts

United States — sustained, slow growth



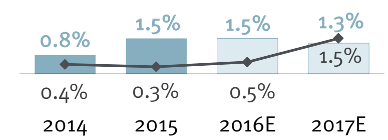
- Q2 GDP growth a disappointing 1.1% largely due to continued inventory liquidation. Mfg. PMI weaker than expected in August, new orders lower. Consumer balance sheets, income growth, employment, confidence all strong. Spending up 4.2% in Q2. Housing steady, permits higher. Capex soft, exports weak. Leading indicators, confidence point to sustained, albeit slow, domestic growth.

Canada — in transition



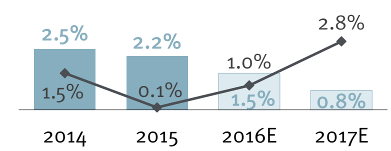
- Q1 growth improved to 2.5%. Q2 collapsed to -1.6%. Ex-Fort McMurray effect, data not bad. Q3 should deliver rebound. House construction firm, PMI off its high, but still positive. Energy capex weak. Mfg. sales ex-petroleum products softer recently due in part to one-time issues as were related exports. Tourism strong helped by weak loonie.

Eurozone — plateauing



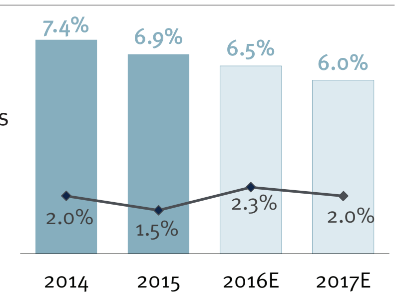
- Q2 growth slowed to 1.7% in Q2. Germany and Spain solid. France and Italy faded after a better Q1. Bank loans to private sector up year over year. PMIs slightly softer but still in expansion zone. Refugee crisis, fractious politics, Brexit weighing on consumer and business sentiment. Tourism bookings down sharply. Italian banks keeping ECB ultra loose, euro soft. Full-year GDP growth steady in 2016, slipping modestly in 2017.

United Kingdom — weakening



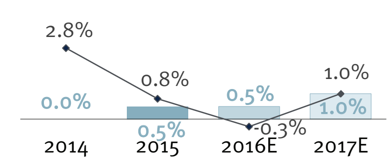
- PMIs, new orders slumped into contraction territory in July following Brexit vote, rebounded sharply in August as weak pound spurred exports. Construction weak as is business confidence. Important services sector also affected. Employment firmer prior to vote as were household earnings.
- Mild recession expected later in the year. Brexit drain more in evidence next year.

China — slowing



- Q2 firm, GDP now at +6.7% y/y. Domestic loan growth distorted by paydown of U.S. dollar debt, but still growing faster than GDP. PMIs improved in July and August, new orders eased. Services sector PMI off fractionally. Employment, wages, retail sales all growing, but somewhat more slowly. Exports, industrial production, mfg. output mixed in July.
- Fixed asset investment slowing. Currency weaker. House prices higher year over year in major centers.

Japan — conflicted, still weak



- GDP growth regained positive territory in Q1, but posted zero for Q2 leading indicators and mfg. Both Mfg. and Services PMIs somewhat improved. Corporate earnings solid, but business confidence weak.
- Wages growing, but household spending weak. Low oil prices, strong currency putting inflation targets in jeopardy. Planned sales tax increase has been put off until 2018, new fiscal package announced.

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	2,170.95	-0.1%	6.2%	10.1%
Dow Industrials (DJIA)	18,400.88	-0.2%	5.6%	11.3%
NASDAQ	5,213.22	1.0%	4.1%	9.1%
Russell 2000	1,239.91	1.6%	9.2%	6.9%
S&P/TSX Comp	14,597.95	0.1%	12.2%	5.3%
FTSE All-Share	3,697.19	1.2%	7.3%	7.6%
STOXX Europe 600	343.53	0.5%	-6.1%	-5.3%
German DAX	10,592.69	2.5%	-1.4%	3.2%
Hang Seng	22,976.88	5.0%	4.8%	6.0%
Shanghai Comp	3,085.49	3.6%	-12.8%	-3.8%
Nikkei 225	16,887.40	1.9%	-11.3%	-10.6%
India Sensex	28,452.17	1.4%	8.9%	8.3%
Singapore Straits Times	2,820.59	-1.7%	-2.2%	-3.5%
Brazil Ibovespa	57,901.11	1.0%	33.6%	24.2%
Mexican Bolsa IPC	47,541.32	1.9%	10.6%	8.7%
Bond Yields	**8/31/16**	**7/29/16**	**8/31/15**	**12 mo chg**
US 2-Yr Tsy	0.805%	0.655%	0.738%	0.07%
US 10-Yr Tsy	1.580%	1.453%	2.218%	-0.64%
Canada 2-Yr	0.576%	0.540%	0.439%	0.14%
Canada 10-Yr	1.024%	1.027%	1.493%	-0.47%
UK 2-Yr	0.144%	0.110%	0.687%	-0.54%
UK 10-Yr	0.642%	0.685%	1.962%	-1.32%
Germany 2-Yr	-0.618%	-0.625%	-0.203%	-0.42%
Germany 10-Yr	-0.065%	-0.119%	0.798%	-0.86%
Commodities (USD)	**Price**	**1 Month**	**YTD**	**12 Month**
Gold (spot $/oz)	1,308.97	-3.1%	23.3%	15.3%
Silver (spot $/oz)	18.66	-8.3%	34.6%	27.6%
Copper ($/metric ton)	4,605.75	-6.3%	-2.1%	-10.5%
Uranium ($/lb)	25.25	1.0%	-26.6%	-31.3%
Oil (WTI spot/bbl)	44.70	7.5%	20.7%	-9.1%
Oil (Brent spot/bbl)	47.04	10.8%	26.2%	-13.1%
Natural Gas ($/mmBtu)	2.89	0.4%	23.5%	7.4%
Agriculture Index	279.24	-3.8%	-1.5%	-0.3%
Currencies	**Rate**	**1 Month**	**YTD**	**12 Month**
US Dollar Index	96.02	0.5%	-2.6%	0.2%
CAD/USD	0.76	-0.5%	5.6%	0.3%
USD/CAD	1.31	0.6%	-5.3%	-0.3%
EUR/USD	1.12	-0.1%	2.7%	-0.5%
GBP/USD	1.31	-0.7%	-10.8%	-14.4%
AUD/USD	0.75	-1.0%	3.2%	5.7%
USD/CHF	0.98	1.5%	-1.8%	1.7%
USD/JPY	103.43	1.3%	-14.0%	-14.7%
EUR/JPY	115.40	1.2%	-11.7%	-15.1%
EUR/GBP	0.85	0.5%	15.2%	16.2%
EUR/CHF	1.10	1.3%	0.9%	1.2%
USD/SGD	1.36	1.7%	-4.0%	-3.5%
USD/CNY	6.68	0.7%	2.9%	4.7%
USD/BRL	3.23	-0.7%	-18.5%	-10.9%

Hong Kong and China markets led as the Chinese economy continued to stabilize.

Treasury yields rose as the Fed attempted to reset rate hike expectations.

Crude oil hung onto gains despite a late-month pullback.

The U.S. dollar barely budged amid the Fed's rate posturing.

Equity returns do not include dividends, except for the German DAX. 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 0.76 means 1 Canadian dollar will buy 0.76 U.S. dollar. CAD/USD 0.3% return means the Canadian dollar has risen 0.3% vs. the U.S. dollar during the past 12 months. USD/JPY 103.43 means 1 U.S. dollar will buy 103.43 yen. USD/JPY -14.7% return means the U.S. dollar has fallen 14.7% vs. the yen during the past 12 months.

Source - RBC Wealth Management, RBC Capital Markets, Bloomberg; data through 8/31/16.

Research resources

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			Investment Banking Services Provided During Past 12 Months	
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Hold [Sector Perform]	741	42.64	129	17.41
Sell [Underperform]	119	6.85	10	8.40

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