GLOBAL
Insight
WEEKLY

Wealth Management

Perspectives from the Global Portfolio Advisory Committee
April 15, 2021

Have we seen the top for yields?

Thomas Garretson, CFA – Minneapolis

The economic data through April has only been good news on top of good news, but the puzzling drop in global yields seemingly suggests the opposite, leaving investors to wonder if we've already seen the top.

After a blistering start to the year, Treasury yields have retreated from one-year highs to one-month lows even as the incoming economic data had a blistering start to April.

First there was the ISM Manufacturing Purchasing Managers' Index (PMI) on Apr. 1 that showed the largest uptick in activity since 1983. That was then followed by the jobs report that showed nearly one million jobs added in March. Not to be outdone, the Service Sector PMI, on Apr. 5, showed activity running at the strongest level on record, dating back to 1997. Then this week we saw the headline Consumer Price Index pop to 2.6 percent year over year, and though largely fueled by weak prices this time last year, this is another sign that continues to point toward building inflationary pressures, in our opinion. Finally, stimulus-fueled retail sales data this week was off the charts, up nearly 10 percent month over month.

So, since reaching 1.75 percent at the end of March, the benchmark U.S. 10-year Treasury yield has slipped back to nearly 1.50 percent, seemingly putting the "rising rate" narrative firmly on the back burner, at least for the time being.

So what gives?

Surveying the landscape of traders and analysts this week looking for explanations, we think one thing is clear—no one really has any.

The easiest explanation might just be that after the torrid start to the year, yields were inevitably due for a period of consolidation. Foreign demand for U.S. bonds has also picked up notably in recent months, while the start of earnings season typically brings a glut of new corporate bond issuance—which tends to drive demand for Treasuries and hedging. The Fed continues to push back against the idea that rate hikes are anywhere on the horizon, with Fed Chair Jerome Powell stating this week that the conditions necessary for liftoff are highly unlikely before the end of 2022, let alone this year.

On top of Powell pushing back against the market's recent expectations regarding rate hikes, he also continues to signal that near-term inflationary pressures will only be transitory, and that downside risks over the long term remain. As the chart on the following page shows, the spike in the Consumer Price Index this week to 2.6 percent is expected by RBC Economics to crescendo near

For perspectives on the week from our regional analysts, please see pages 3–4.

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3.6 percent this quarter before falling sharply back to more stable levels.

But maybe it just comes down to the classic explanation that markets—being forward-looking as they are—had already priced in a lot, if not all, of the good news and stimulus that we have seen of late, with traders now awaiting any catalyst that might be cause to take yields to the next leg higher.

Not all rising rate environments are the same

While global yields are moving lower this week, the fear around rising rates continues to be front of mind for investors and portfolios, with this recent pullback only likely to amplify the issue should yields resume their march higher.

And higher yields remain the base case, in our view. This month, RBC Economics upgraded its economic and rate forecasts, as did most analysts, with our colleagues now seeing the 10-year Treasury yield rising to 2.05 percent, up from 1.85 percent previously, by this time next year.

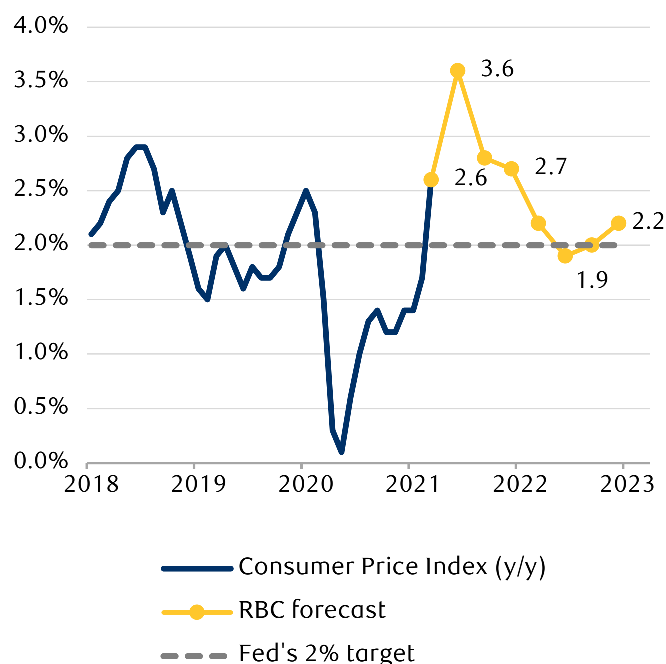
But what does this actually mean for bond prices and portfolio performance? With all of the moving parts in fixed income securities, things can get pretty murky, pretty quickly. At a high level, higher yields mean lower bond prices, but by how much, and how much coupon income is needed to offset declines in bond prices?

The table shows how bonds are likely to perform over the next year based on RBC Economics forecasts for the 2-year, 10-year, and 30-year Treasury yields. But higher Treasury yields don't necessarily translate exactly to other sectors. Muni bond yields are likely to remain less sensitive to movements in Treasury yields as investor demand is likely to remain elevated amid the risk of higher tax rates. Corporate bond yields will also rise in sympathy with Treasury yields, but to a lesser extent.

And, for the most part, the damage is actually minimal. Outside of Treasuries, the decline in bond prices due to higher market yields is more than offset by the interest earned from coupons over that one-year period. For example, if the 10-year Treasury yield rises to 2.05 percent, the price falls by $31, which isn't offset by the $11 in coupons. A comparable 10-year corporate would see its price fall by $27, nearly fully covered by $26 in coupons, and it's a similar story for municipals. And longer-dated securities may actually offer investors attractive value around current levels.

So the outlook may not be as bleak as feared by many fixed income investors, particularly as we believe any further rise in yields is likely to be more gradual than we have seen in recent months.

Jump in consumer prices still seen as temporary



Source - RBC Wealth Management, RBC Economics, Bloomberg; data as of 4/14/21

Scenario analysis: What impact does "rising rates" have on bond prices and portfolio performance?

Security type	Maturity	Coupon	Current yield	Current price	Q2 2022 forecast yield	Q2 2022 forecast price	Yield change	Price change	Coupon income	One-year total return
Treasuries	2Y	0.1%	0.16%	$999	**0.90%**	$994	0.74%	-$5	$1	-0.4%
	10Y	1.1%	1.61%	$962	**2.05%**	$931	0.44%	-$31	$11	-2.1%
	30Y	1.9%	2.30%	$926	**2.60%**	$861	0.30%	-$65	$19	-5.0%
Investment-grade corporates	2Y	0.8%	0.61%	$1,004	**1.30%**	$993	0.69%	-$11	$8	-0.3%
	10Y	2.6%	2.46%	$1,011	**2.85%**	$984	0.39%	-$27	$26	-0.1%
	30Y	3.6%	3.41%	$1,028	**3.60%**	$1,001	0.19%	-$27	$36	0.8%
Municipals	2Y	5.0%	0.08%	$1,121	**0.45%**	$1,071	0.37%	-$50	$50	0.0%
	10Y	4.0%	0.94%	$1,177	**1.19%**	$1,139	0.25%	-$38	$40	0.2%
	30Y	4.0%	1.87%	$1,178	**2.12%**	$1,145	0.25%	-$33	$40	0.6%

Source - RBC Wealth Management, RBC Economics; data through 4/14/21

UNITED STATES

Alan Robinson – Seattle

- **U.S. stocks were biased to the upside during the week. However, trading volumes were relatively light** as investors prepared for the onslaught of Q1 2021 earnings season, which started in earnest on Apr. 14 with positive announcements by the major U.S. banks. Banks' profits were boosted by the release of loan-loss reserves that had been built up in 2020 as a precaution against bad debts, which ultimately proved much less impactful than originally feared.

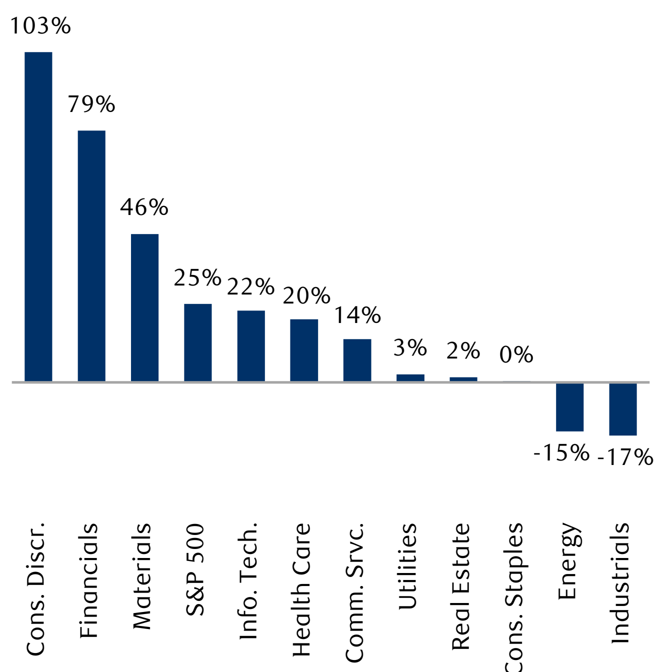
- Consensus forecasts prior to the start of earnings season expected overall earnings growth for the S&P 500 of nearly 25% relative to Q4 2020, as the U.S. economy turned the COVID corner, and as global growth picked up speed. **The Consumer Discretionary, Financials, and Materials sectors are projected to post the strongest growth**, while the Energy and Industrials sectors are likely to fall short of the solid results they posted in Q4 2020 (see chart).

- The Technology sector, which had lagged the market in March, continued its rebound during the week. **Shares of market bellwether Apple** (AAPL), which accounts for 5.7% of the S&P 500 Index, **reacted positively to news the firm plans a new product announcement on Apr. 20**. Apple shares had been flat in 2021 after a strong close to 2020, due partly to a global microchip shortage. Investors cheered the prospect of new products coming out to meet pent-up post-COVID demand from global consumers.

- U.S. economic data came in surprisingly strongly during the week. **March retail sales were up 9.8%** compared to February, and beat expectations of a 5.5% gain. Sales of motor vehicles, gasoline, and food all posted outsized increases. Gains were more dramatic on a year-over-year basis, with sales up nearly 28% compared to the lockdown low of March 2020. **Initial claims for unemployment benefits fell sharply** to 576,000 during the week. This was the first sub-600,000 print since the start of the pandemic. April **manufacturing and homebuilder surveys also beat** elevated forecasts.

Q1 2021 earnings season shaping up to be strong

Forecast Q1 2021 earnings growth by sector; q/q, annualized



Source - RBC Wealth Management, FactSet consensus estimates; data through 4/11/21

CANADA

Luis Castillo – Toronto

- **The Canadian economy added an impressive 303,000 jobs in March**, as reported by Statistics Canada, triple what economists were expecting. The unemployment rate has now dropped to the lowest level since the pandemic started, despite an encouraging increase in the participation rate. The March report came after another very strong print in February, bringing the labour market to just 296,000 jobs below the pre-pandemic level. However, following strong back-to-back monthly job gains, a renewed stay-at-home order in Ontario is likely to halt momentum in April. **Markets will be looking forward to the Bank of Canada's (BoC) Apr. 21 meeting, where updated guidance should be provided**. For months, the data has shown an economy gaining strength, and market participants are expecting the BoC to announce that it will reduce the pace of its purchases of Government of Canada bonds, currently at around CA$4 billion per week.

- **The release of the BoC's spring issue of the Business Outlook Survey follows in the footsteps of a strong employment print and adds fuel to the market's already optimistic view of the post-pandemic future**. The survey showed that business sentiment has continued to improve across most segments, with weakness still present in those related to tourism and non-essential retail. More than 50% of firms expect to see inflationary pressures on their input prices, with many anticipating this price increase to be commodity-driven. These firms also intend to pass the rising costs on to their consumers. **More than 50% of firms expect inflation to be above the BoC's midpoint target over the next two years**, supported by both fiscal and monetary policy as well as a surge in consumer spending once restrictions are lifted. Although the survey was conducted prior to the most recent round of lockdowns, it reinforces the view of a strong economic recovery post-pandemic with brewing inflationary pressures.

EUROPE

Thomas McGarrity, CFA – London

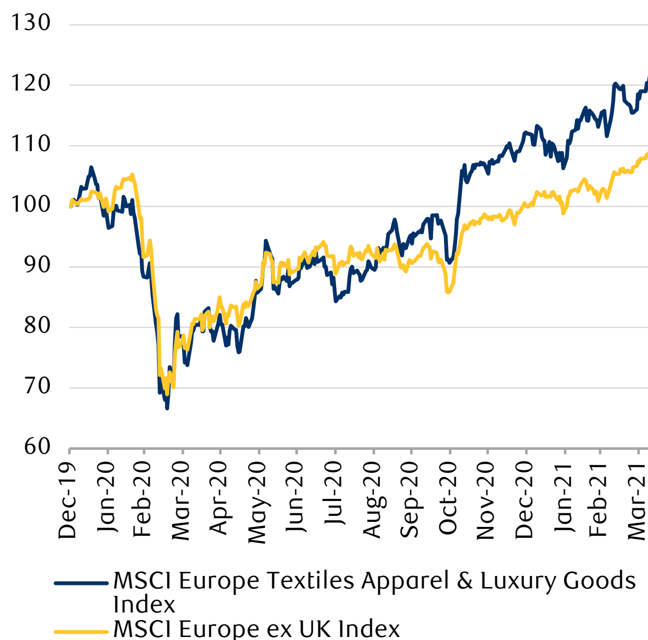
- As we enter the Q1 reporting season, we believe **company results should generally be a supportive factor for Pan-European equities in the weeks ahead**, given global economic activity indicators, such as purchasing managers' indexes, are robust and continuing to improve on the whole. Consensus is projecting earnings per share for the STOXX Europe 600 Index to be up almost 35% y/y, though this is clearly against a depressed comparative base period as we lap the onset of the pandemic. Notably, European earnings upgrades are outpacing downgrades by the most on record, according to a report from Bloomberg.

- **Luxury goods giant LVMH got the region's earnings season off to a good start**, reporting organic sales growth of 30% y/y, considerably ahead of consensus expectations for 19%, and growth of 8% over Q1 2019 levels. The group's Fashion & Leather Goods division delivered the standout performance, with 52% y/y organic revenue growth (consensus: 30%) and 37% growth versus Q1 2019. From a regional perspective, LVMH stated that the U.S. and Asia "enjoyed strong growth"; however, its European operations were still hampered by the pandemic due to store closures across several countries and the suspension of tourism. LVMH's market capitalisation has increased to over €300 billion, making it the biggest company in Europe by market value.

- **LVMH's results have a positive read-across for the broader luxury goods space**, indicating demand for luxury goods remains very healthy. The pandemic has seemingly only had a transitory impact on such demand, with it rebounding strongly post the first virus wave, particularly in Asia and the U.S. **We believe equity investors should continue to own exposure to this space**. Beyond consumer appetite for luxury goods remaining robust, the prospect of a pickup in inflation will likely shine a light on those companies that possess pricing power, a quality luxury goods companies tend to enjoy, in our view.

European luxury goods stocks have outperformed as demand has bounced back strongly

MSCI Europe Textiles Apparel & Luxury Goods Index vs. MSCI Europe ex UK Index



Source - RBC Wealth Management, Bloomberg, MSCI; data through 4/13/21

ASIA PACIFIC

Jasmine Duan – Hong Kong & Nicholas Gwee, CFA – Singapore

- **China's State Administration for Market Regulation (SAMR) imposed a US$2.8 billion (RMB 18.2 billion) fine on Alibaba** (9988 HK) **after an anti-trust investigation**. The fine is based on 4% of Alibaba's RMB 456 billion of domestic sales in 2019. An additional 34 tech companies, including Tencent (700 HK), JD.com (9618 HK), and Meituan (3690 HK), were ordered by the regulator to rectify their anti-competitive practices within the next month.

- **China Huarong Asset Management Co. (Huarong), a state-owned manager of non-performing loans, is preparing to get rid of non-core and loss-making units as part of a broad plan to revive profitability**. The company had delayed its 2020 earnings announcement due to audit issues. Global rating agencies placed the company on negative watch and review for downgrade. Huarong's dollar bond selloff has spread to other China investment-grade bonds this week.

- **Taiwan Semiconductor Manufacturing Co.** (2330 TT) **announced stronger-than-expected Q1 2021 net profit**, up 19% y/y, thanks to robust chip demand. In addition, it warned that the global chip shortage may last into 2022. The company expects to invest about US$30 billion on capacity expansions and upgrades in 2021 compared to the previous forecast of as much as US$28 billion.

- According to an unconfirmed Bloomberg report, **private equity firm KKR & Co. is weighing a bid for Toshiba Corp.** (6502 JP), which could value the company above the US$21 billion offered by CVC Capital Partners. Canadian investment giant Brookfield Asset Management Inc. is also said to be in the preliminarily stages of exploring an offer, according to the same article. Separately, **Toshiba said Chief Executive Officer Nobuaki Kurumatani has been replaced by Chairman Satoshi Tsunakawa**, effective April 15, 2021. The decision came as there is increasing resistance to the offer from CVC Capital Partners—where Kurumatani previously worked. Some senior management think the offer undervalued Toshiba, which still holds valuable energy and semiconductor assets.

MARKET Scorecard

Data as of April 15, 2021

Equities (local currency)	Level	MTD	YTD	1 yr	2 yr
S&P 500	4,170.42	5.0%	11.0%	49.8%	43.5%
Dow Industrials (DJIA)	34,035.99	3.2%	11.2%	44.8%	29.0%
Nasdaq	14,038.76	6.0%	8.9%	67.3%	76.0%
Russell 2000	2,257.07	1.6%	14.3%	90.6%	42.9%
S&P/TSX Comp	19,321.92	3.3%	10.8%	38.4%	17.0%
FTSE All-Share	3,988.72	4.1%	8.6%	29.2%	-2.1%
STOXX Europe 600	438.55	2.1%	9.9%	35.7%	13.0%
EURO STOXX 50	3,993.43	1.9%	12.4%	42.2%	15.7%
Hang Seng	28,793.14	1.5%	5.7%	19.2%	-3.4%
Shanghai Comp	3,398.99	-1.2%	-2.1%	20.9%	7.0%
Nikkei 225	29,642.69	1.6%	8.0%	51.6%	33.7%
India Sensex	48,803.68	-1.4%	2.2%	60.6%	25.4%
Singapore Straits Times	3,184.77	0.6%	12.0%	22.2%	-4.2%
Brazil Ibovespa	120,700.70	3.5%	1.4%	53.1%	29.7%
Mexican Bolsa IPC	48,514.10	2.7%	10.1%	43.3%	8.7%
Gov't bonds (bps change)	**Yield**	**MTD**	**YTD**	**1 yr**	**2 yr**
U.S. 10-Yr Treasury	1.567%	-17.3	65.4	93.6	-98.7
Canada 10-Yr	1.471%	-8.7	79.4	82.9	-28.4
UK 10-Yr	0.737%	-10.8	54.0	43.5	-48.3
Germany 10-Yr	-0.290%	0.2	27.9	17.5	-34.6
Fixed income (returns)	**Yield**	**MTD**	**YTD**	**1 yr**	**2 yr**
U.S. Aggregate	1.53%	0.7%	-2.7%	-0.2%	16.7%
U.S. Investment-Grade Corp	2.19%	1.0%	-3.7%	4.7%	22.3%
U.S. High-Yield Corp	4.07%	0.7%	1.5%	18.3%	19.2%
Commodities (USD)	**Price**	**MTD**	**YTD**	**1 yr**	**2 yr**
Gold (spot $/oz)	1,764.26	3.3%	-7.1%	2.8%	37.0%
Silver (spot $/oz)	25.87	5.9%	-2.0%	67.3%	72.4%
Copper ($/metric ton)	9,080.50	3.3%	17.2%	78.7%	40.7%
Oil (WTI spot/bbl)	63.46	7.3%	30.8%	219.4%	0.1%
Oil (Brent spot/bbl)	66.85	5.2%	29.1%	141.4%	-6.1%
Natural Gas ($/mmBtu)	2.66	2.1%	4.9%	66.6%	2.8%
Currencies	**Rate**	**MTD**	**YTD**	**1 yr**	**2 yr**
U.S. Dollar Index	91.6580	-1.7%	1.9%	-7.8%	-5.5%
CAD/USD	0.7970	0.1%	1.5%	12.5%	6.5%
USD/CAD	1.2547	-0.1%	-1.4%	-11.1%	-6.1%
EUR/USD	1.1970	2.0%	-2.0%	9.7%	5.9%
GBP/USD	1.3785	0.0%	0.8%	10.1%	5.2%
AUD/USD	0.7754	2.1%	0.8%	22.7%	8.1%
USD/JPY	108.7200	-1.8%	5.3%	1.2%	-3.0%
EUR/JPY	130.1300	0.2%	3.1%	11.0%	2.7%
EUR/GBP	0.8683	2.0%	-2.8%	-0.3%	0.6%
EUR/CHF	1.1035	-0.3%	2.1%	4.8%	-2.8%
USD/SGD	1.3344	-0.8%	0.9%	-6.3%	-1.4%
USD/CNY	6.5226	-0.5%	-0.1%	-6.0%	-2.8%
USD/MXN	19.9408	-2.4%	0.1%	-16.9%	5.8%
USD/BRL	5.6228	-0.2%	8.2%	48.8%	45.2%

Equity returns do not include dividends, except for the Brazilian Ibovespa. Bond yields in local currencies. Copper Index data and U.S. fixed income returns as of Wednesday's close. 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 0.79 means 1 Canadian dollar will buy 0.79 U.S. dollar. CAD/USD 1.5% return means the Canadian dollar rose 1.5% vs. the U.S. dollar year to date. USD/JPY 108.72 means 1 U.S. dollar will buy 108.72 yen. USD/JPY 5.3% return means the U.S. dollar rose 5.3% vs. the yen year to date.

Source - Bloomberg; data as of 4:35 pm ET 4/15/21

Authors

Thomas Garretson, CFA – Minneapolis, United States
tom.garretson@rbc.com; RBC Capital Markets, LLC

Alan Robinson – Seattle, United States
alan.robinson@rbc.com; RBC Capital Markets, LLC

Luis Castillo – Toronto, Canada
luis.castillo@rbccm.com; RBC Dominion Securities Inc.

Thomas McGarrity, CFA – London, United Kingdom
thomas.mcgarrity@rbc.com; RBC Europe Limited

Jasmine Duan – Hong Kong, China
jasmine.duan@rbc.com; RBC Investment Services (Asia) Limited

Nicholas Gwee, CFA – Singapore
nicholas.gwee@rbc.com; Royal Bank of Canada, Singapore Branch

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As of March 31, 2021

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Hold [Sector Perform]	559	40.68	179	32.02
Sell [Underperform]	53	3.86	4	7.55

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