RBC WEALTH MANAGEMENT

Global Insight Weekly

The way back

Kelly Bogdanova – San Francisco, Frédérique Carrier – London, & Jim Allworth – Vancouver

As we come to the end of a year unlike any other in memory, 2021 should bring a change in the narrative. Challenges and concerns certainly remain, but with the start of a new economic and investment era before us, we look at what investors can expect in the year ahead.

The passing of challenge-ridden 2020 can't come soon enough. It's time to look ahead.

As economies and corporate profits recover further, we believe ultralow interest rates should make equities the asset class of choice in 2021 while making fixed income investing more challenging.

Our team of specialists and strategists in the U.S., Canada, Europe, and Asia recently published the Global Insight 2021 Outlook, which sets forth RBC Wealth Management's views on the economy, equities, and fixed income, as well as forecasts for currencies and commodities.

Importantly, the report addresses common concerns we often hear from investors, even more so since the onset of the COVID-19 pandemic:

- Governments are now awash in debt, and there are no signs borrowing will let up anytime soon. Is more debt sustainable, and what are the risks for economies and taxpayers?
- With the U.S. economy still in the process of reopening, where is inflation going from here and what can investors watch to gauge how price pressures may be building?
- With interest rates near or below zero percent in many countries, it's becoming more evident that what worked for fixed income investing in the past may not work in the future.

Following are highlights from the 2021 Outlook and links to each individual article.

Market pulse

Click here for authors' contact information. Priced (in USD) as of 12/3/20 market close, ET (unless otherwise stated). **For important disclosures and required non-U.S. analyst disclosures, see page 6.**
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The shape of things to come

The COVID-19 economic damage should diminish greatly through 2021, while confidence in a return to a recognizable social and business landscape will likely grow. As GDP climbs back toward its pre-pandemic peak, corporate earnings, already recovering, could perform better than expected through 2021 and 2022.

Stocks in the major markets have priced in some of this better earnings trajectory but not all. We expect equities could provide attractive all-in returns in 2021, and probably for 2022.

Beyond this period, we expect slower economic growth to restrain the overall growth of earnings and business values, resulting in an intensely competitive business environment. Slowing birth rates and protectionism will likely play a role. Investors should also consider the interplay of China.

In terms of long-term positioning, we think equity portfolios should be largely populated with the shares of those businesses for which there is high conviction that sales, earnings, and dividends can grow faster than the economy.

The debt dilemma

Public debt has ballooned since the COVID-19 pandemic began. For advanced economies, it now sits beyond what was reached after World War II, at greater than 120 percent of GDP. The debt picture is even more acute when off-balance sheet social promises are taken into account.

We believe higher debt loads are manageable in the near and intermediate term. Ultralow interest rates have actually pushed debt service costs down, including in the U.S., and this trend should persist in the next couple of years.

But as debt costs start to rise in the out-years, this will eventually restrict government budgets and services, and is likely to result in higher tax rates, in our view.

High debt loads will probably be a powerful incentive for policymakers to further suppress interest rates over the long term. Investors should consider strategies for a low rate environment that may linger for much longer than one may think is reasonable.

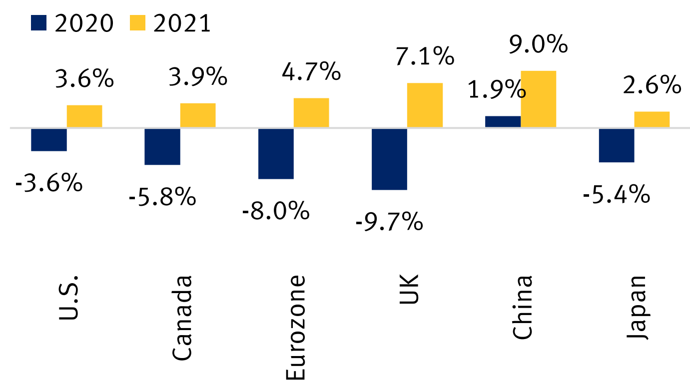
Inflation: To be, or not to be?

Inflation is bouncing back from weaker readings in the spring. Governments shut economies down and turned them back on. Inflation is responding to the "turning back on" part.

Before we see any potential for inflation to trend higher on a sustained basis we want to see the economy open more. That's especially true now that we are dealing with cross-currents of "second wave" shutdowns and vaccine optimism.

In this article, RBC Capital Markets, LLC Chief U.S. Economist Tom Porcelli addresses a wide range of issues that could impact inflation both over the near and longer term.

RBC's annual real GDP growth forecasts (y/y)



Source - RBC Global Asset Management; November 2020

Fixed income: Not dead, just different

Yields are set to start 2021 much lower than at the beginning of 2020, which is remarkable given that yields were already rather low a year ago. This makes the environment for reinvestment even more challenging.

We suggest splitting the roles of capital preservation and income generation in fixed income portfolios.

High-quality bonds and cash-equivalent securities can add ballast to portfolios and act as a potential source of funds during periods of market volatility. These lower-yielding positions can be offset by lower-rated and subordinated securities that provide higher yields in an attempt to maintain overall income.

2021 investment stance

All major economies seem set to reach their previous peak output levels much faster than they did following the global financial crisis.

Major central banks will likely keep the stimulus pedal to the metal in 2021. But amid concerns policy tools are already nearing speed limits, we look for policymakers to fine-tune current programs in order to deliver the most efficient and focused aid to support the economic recovery.

For 12–18 months following the end of a recession there is usually very rapid catch-up corporate earnings growth. The persistence of ultralow interest rates should support above-average equity valuations. We recommend holding an Overweight position in equities.

This article includes our outlook for the equity and fixed income markets in the U.S., Canada, UK, Europe, and Asia, while also providing forecasts for currencies and commodities.

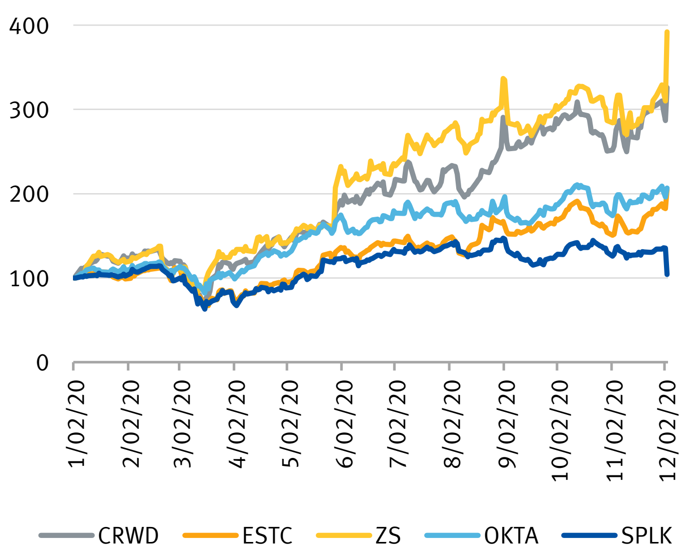
United States

Alan Robinson – Seattle

- **U.S. stock indexes posted new highs again during the week.** Concerns regarding increasing COVID-19 cases over the holiday season and stalled fiscal stimulus talks were outweighed by vaccine optimism, solid earnings reports, a tailwind from persistently low interest rates, and a fear of missing out on this quarter's stock rally.
- **With Q3 2020 earnings season largely in the rear view mirror, investor focus turned to a handful of typically later-reporting software companies** that announced results during the week. This sector has benefitted from strong growth as a result of accelerating secular trends related to changing business practices due to COVID-19. Analysts had voiced concerns about the rapid rise in share prices of these companies during the year, and whether results could meet relatively high consensus expectations. The answer was generally "Yes," with the prices of four out of five bellwether stocks posting double-digit percentage gains after reporting (see chart).
- **However, 2021 may present a challenge for software companies in a post-COVID-19 world** if their rapid sales growth starts to moderate, and if Value overtakes Growth as a stock investing theme. RBC Capital Markets, LLC software analyst Alex Zukin suggests investors focus on the fastest-growing names, where valuation seems at least relatively reasonable and there is lower downside risk if near-term fundamentals slightly underperform high expectations.

Software stocks round out a solid year, with exceptions

Performance of select U.S. software stocks that reported this week



Year-to-date performance of Crowdstrike (CRWD), Elastic (ESTC), Zscaler (ZS), Okta (OKTA), and Splunk (SPLK)
Source - RBC Wealth Management, Thomson One Refinitiv; data through 12/3/20, normalized with 1/2/20 = 100

- **Several merger deals were announced during the week**. S&P Global (SPGI) plans to buy IHS Markit (INFO) for $44 billion, salesforce.com (CRM) will acquire Slack Technologies (WORK) for $27.7 billion, and Australia's Macquarie Group is buying U.S. wealth manager Waddell & Reed (WDR) for $1.7 billion. While global M&A volume this year is running 12% lower than last, activity has seen a strong rebound since late summer as CEOs look beyond the current recession to acquire growth for the long term.
- **The OPEC+ meeting began** on Thursday, Dec. 3, with analysts **expecting the cartel to extend oil production cuts for another two or three months**. This sentiment pushed oil prices to nine-month highs and buoyed Energy stocks, providing some relief for this beleaguered sector.

Canada

Luis Castillo – Toronto

- **Canada's GDP growth for the month of September came in at 0.8% as reported by Statistics Canada**. Even though this marks the fifth consecutive monthly increase, total economic activity is still 5% below its pre-pandemic level. On an annualized basis, **GDP was up 40.5% in Q3, falling short of expectations, but representing a significant bounce back in economic activity** as businesses were given the green light to emerge from their COVID-19 lockdowns. On a year-over-year basis, Canada saw growth in consumer spending on goods and in residential investment, thanks in large part to the enormous support from the government and central bank in the form of transfer payments to consumers and low interest rates. However, the reintroduction of containment measures in recent weeks suggests that further growth from here will be difficult to attain. Statistics Canada notes that a full recovery to pre-pandemic levels may take longer than the previous trend suggests.
- **Chrystia Freeland, deputy prime minister and minister of finance, released the highly anticipated Fall Economic Statement 2020**, almost 18 months after the last formal budget update. The government announced an additional CA$70–$100 billion of post-pandemic spending and expects to run **a record deficit of roughly CA$382 billion this year, CA$39 billion higher than what was previously expected**. The release highlighted that nearly 80% of the jobs lost during the crisis have now been recovered and bankruptcies remain below pre-pandemic levels. However, the Statement noted, pandemic risks persist and **fiscal support will continue to be needed** as we head into 2021. Some of the most notable measures proposed include healthcare investment to prevent

the spread of COVID-19, an increase and extension of the Canada Emergency Wage Subsidy, extension of the Canada Emergency Rent Subsidy and Lockdown Support programs, and temporary support for families with young children entitled to the Canada Child Benefit.

Europe

Frédérique Carrier & Thomas McGarrity, CFA – London

- **UK approval of the Pfizer/BioNTech COVID-19 vaccine and its imminent rollout give hope the UK economy will reopen more fully in 2021**. After a harrowing GDP contraction this year the news is welcome.

- Still, **Brexit remains a challenge** as negotiations have been inconclusive until now. Progress is difficult to gauge at this stage as the UK and EU remain far apart relative to the sticking points of fishing, level playing field, and governance. A deal hangs in the balance. **The Dec. 10 European Council meeting could provide the necessary catalyst to advance negotiations**. With little time left for the European Parliament to ratify a deal before year end, any potential deal agreed upon could be applied on a provisional basis on Jan. 1 and be subject to a ratification process in the EU and member state parliaments after.

- **In Europe, the lockdowns imposed in the autumn have helped to reduce the number of daily COVID-19 infections, though at the cost of a significant contraction in Services activity**. The Markit Eurozone Services Purchasing Managers' Index (PMI) contracted further to a meagre 41.7 in November. The Manufacturing sector, having remained open despite the lockdowns, posted a more solid 53.8 result, slightly ahead of October's number.

- Faced with an economy in difficulty and inflation remaining stable at -0.3% y/y in November, **the European Central Bank will increase its Pandemic Emergency Purchase Programme** by some €500 billion next week, in our opinion.

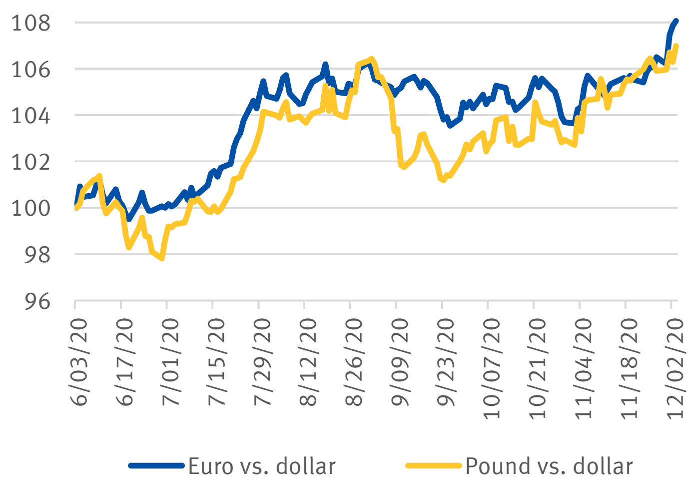
Asia Pacific

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

- **In the China and Hong Kong markets, sentiment for cyclical and "old economy" stocks continues to be stronger than that for "new economy" stocks** this week. With many companies' share prices reaching new highs, we are seeing some capital raising activities from big companies, including Xiaomi (1810 HK), BYD (1211 HK), and Longfor (960 HK).

As Brexit talks close in on the deadline, the euro appears to be gaining steam

Relative performance against the U.S. dollar



Source - RBC Wealth Management, Thomson One Refinitiv; data through 12/2/20; normalized with 6/3/20 = 100

- **Chinese smartphone maker Xiaomi (1810 HK) finalized a US$3.91 billion capital raising** on Dec. 2, which was the largest top-up placement in Hong Kong to date. The equity portion of the deal raised US$3.06 billion and a convertible bond deal raised a further US$855 million. The company said one billion shares were sold at HK$23.70 each as part of the top-up deal. The final price was a 9.4% discount to Xiaomi's closing price of HK$26.15 on Dec. 1.

- **JD Health (6618 HK), the online health care platform of Chinese e-commerce giant JD.com (9618 HK), raised HK$27 billion (US$3.5 billion) from its IPO**. The company is due to start trading in Hong Kong on Dec. 8. According to data compiled by Bloomberg, the IPO is also the largest of this year's first-time share sales in Hong Kong, excluding the second listing by JD.com in June.

- **Chinese food delivery giant Meituan (3690 HK) reported solid Q3 2020 results** with revenue up 29% y/y at RMB 35.4 billion, and ahead of consensus estimates. However, **the company said it will invest heavily in the online grocery business**, including bolstering its warehouse network and logistics capabilities as it expands to more than 1,000 cities and counties before the end of the year. The online grocery business is still at an early stage, and management said **investment may hurt the bottom line in the short term**.

MARKET SCORECARD

Data as of December 3, 2020

Equities (local currency)	Level	MTD	YTD	1 yr	2 yr
S&P 500	3,666.72	1.2%	13.5%	18.5%	31.4%
Dow Industrials (DJIA)	29,969.52	1.1%	5.0%	9.0%	16.0%
Nasdaq	12,377.18	1.5%	37.9%	45.3%	66.3%
Russell 2000	1,848.70	1.6%	10.8%	15.4%	19.4%
S&P/TSX Comp	17,398.02	1.2%	2.0%	3.0%	13.9%
FTSE All-Share	3,672.88	3.7%	-12.5%	-7.5%	-4.9%
STOXX Europe 600	391.72	0.6%	-5.8%	-1.7%	8.5%
EURO STOXX 50	3,517.10	0.7%	-6.1%	-2.6%	9.4%
Hang Seng	26,728.50	1.5%	-5.2%	1.3%	-1.7%
Shanghai Comp	3,442.14	1.5%	12.9%	19.3%	29.7%
Nikkei 225	26,809.37	1.4%	13.3%	14.7%	18.8%
India Sensex	44,632.65	1.1%	8.2%	9.7%	23.2%
Singapore Straits Times	2,822.34	0.6%	-12.4%	-11.1%	-11.5%
Brazil Ibovespa	112,291.60	3.1%	-2.9%	3.1%	25.0%
Mexican Bolsa IPC	43,934.21	5.2%	0.9%	3.9%	4.4%

Commodities (USD)	Price	MTD	YTD	1 yr	2 yr
Gold (spot $/oz)	1,841.05	3.6%	21.3%	24.6%	49.6%
Silver (spot $/oz)	24.09	6.4%	34.9%	40.3%	67.4%
Copper ($/metric ton)	7,666.50	1.3%	24.7%	32.4%	21.4%
Oil (WTI spot/bbl)	45.64	0.7%	-25.3%	-18.6%	-13.8%
Oil (Brent spot/bbl)	48.75	2.4%	-26.1%	-19.8%	-21.0%
Natural Gas ($/mmBtu)	2.52	-12.7%	14.9%	3.0%	-42.0%

Govt bonds (bps chg)	Yield	MTD	YTD	1 yr	2 yr
U.S. 10-Yr Tsy	0.911%	7.2	-100.6	-80.5	-205.9
Canada 10-Yr	0.740%	6.9	-96.2	-70.7	-149.5
U.K. 10-Yr	0.322%	1.7	-50.0	-34.8	-99.1
Germany 10-Yr	-0.556%	1.5	-37.1	-20.8	-86.2

Fixed Income (returns)	Yield	MTD	YTD	1 yr	2 yr
U.S. Aggregate	1.21%	-0.4%	6.9%	6.5%	19.2%
U.S. Invest Grade Corp	1.84%	-0.5%	8.9%	8.9%	25.9%
U.S. High Yield Corp	4.56%	0.3%	5.5%	7.8%	15.6%

Currencies	Rate	MTD	YTD	1 yr	2 yr
U.S. Dollar Index	90.6730	-1.3%	-5.9%	-7.2%	-6.6%
CAD/USD	0.7775	1.1%	1.0%	3.4%	2.6%
USD/CAD	1.2861	-1.1%	-1.0%	-3.3%	-2.5%
EUR/USD	1.2148	1.9%	8.3%	9.6%	7.0%
GBP/USD	1.3460	1.0%	1.5%	3.6%	5.8%
AUD/USD	0.7442	1.3%	6.0%	8.7%	1.1%
USD/JPY	103.8500	-0.4%	-4.4%	-4.4%	-8.6%
EUR/JPY	126.1600	1.4%	3.6%	4.8%	-2.2%
EUR/GBP	0.9025	0.8%	6.7%	5.8%	1.1%
EUR/CHF	1.0822	-0.2%	-0.3%	-1.1%	-4.5%
USD/SGD	1.3334	-0.6%	-0.9%	-2.3%	-2.5%
USD/CNY	6.5429	-0.5%	-6.0%	-7.3%	-4.9%
USD/MXN	19.8961	-1.4%	5.1%	1.7%	-2.3%
USD/BRL	5.1577	-3.8%	28.0%	36.5%	34.2%

Source - Bloomberg. Note: 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. Data as of 16:35 pm ET 12/3/20.

Examples of how to interpret currency data: CAD/USD 0.77 means 1 Canadian dollar will buy 0.77 U.S. dollar. CAD/USD 1.0% return means the Canadian dollar rose 1.0% vs. the U.S. dollar year to date. USD/JPY 103.85 means 1 U.S. dollar will buy 103.85 yen. USD/JPY -4.4% return means the U.S. dollar fell 4.4% vs. the yen year to date.

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As of September 30, 2020

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Buy [Outperform]	788	52.96	248	31.47
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Sell [Underperform]	81	5.44	11	13.58

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