RBC Global Asset Management

Economic outlook

Resilient growth defies headwinds and risks

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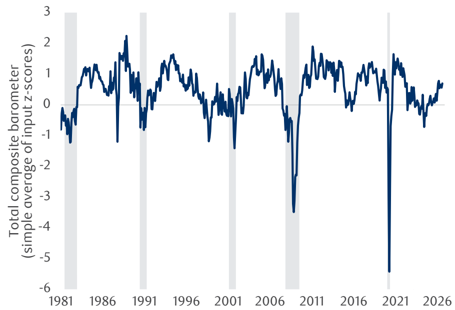
Key takeaways

- The global economy continues to grow solidly despite a barrage of headwinds.
- AI-related investment and productivity gains are an important growth engine.
- The energy shock, rising yields and new tariffs are real but manageable challenges.
- Inflation remains too high but should partially ease in 2027.
- Developed-world central banks are pivoting toward tightening.
- We maintain a slight equity overweight tilted to the U.S., Canada and Asia.

Overview

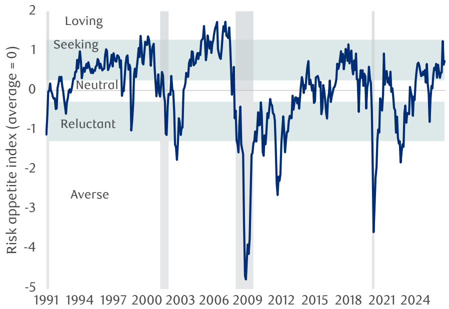
There continues to be a steady barrage of new macroeconomic headwinds and risks, but the global economy (Exhibit 1) and its constituent stock markets (Exhibit 2) continue to largely slough these off, instead muscling their way higher.

Exhibit 1: RBC GAM composite macro barometer for U.S. looks good



Note: As of September 2026. Shaded area represents recession. Source: RBC GAM

Exhibit 2: Investor risk appetite in risk-seeking mode



Note: As of August 2026. Measures risk appetite based on 45 normalized inputs. Grey area represents recession. Source: Bloomberg, BofA ML, Consensus Economics, UBS, Federal Reserve Bank of Philadelphia, NedDavis, Haver Analytics, RBC GAM

The latest concerns include the effect of the still-obstructed Strait of Hormuz on the global availability of energy, creeping bond market pressures, questions about the sustainability of the AI boom, another round of U.S. tariffs, and the ramifications of still-elevated inflation.

Despite this, and thanks in significant part to enormous AI-related capital expenditures, a burgeoning AI-related productivity acceleration and international fiscal support, the global economy continues to move forward at a solid rate, as conveyed by a host of manufacturing purchasing manager indices (Exhibit 3). The AI boom is even more central for corporate revenues and earnings, which are soaring – and some broadening out beyond the sector is also becoming visible.

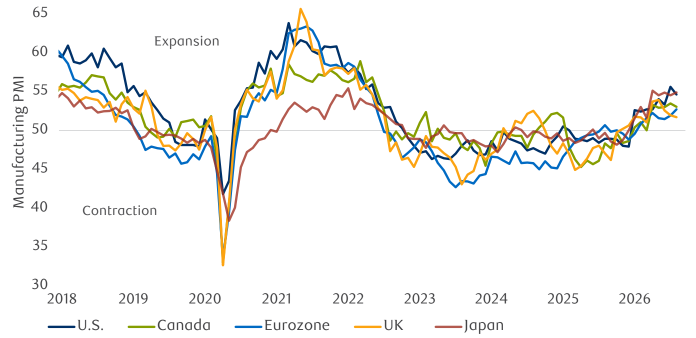
In turn, with a fairly supportive macro backdrop and relatively elevated bond yields, we maintain a slight equity overweight and – after sifting through the many pros and cons that can be affixed to the U.S. market – maintain a regional overweight to U.S. equities, alongside similar overweight positions in Canada and Asia.

Artificial intelligence to power growth

Artificial intelligence-related forces remain powerfully supportive for the U.S. economy. The vast sums U.S. hyperscalers are investing in data centres and the technology more generally continue to mount, and are contributing between 0.5% and 0.75% to the country's GDP 2026 growth rate (Exhibit 4). While the rate of capital expenditure growth is expected to slow in 2027 and beyond, the consensus forecast has been persistently too cautious relative to reality in this regard in recent years, and for that matter the dollar figures have become so large that even a markedly slower percentage growth rate in the years ahead can continue to represent a large absolute support for the economy.

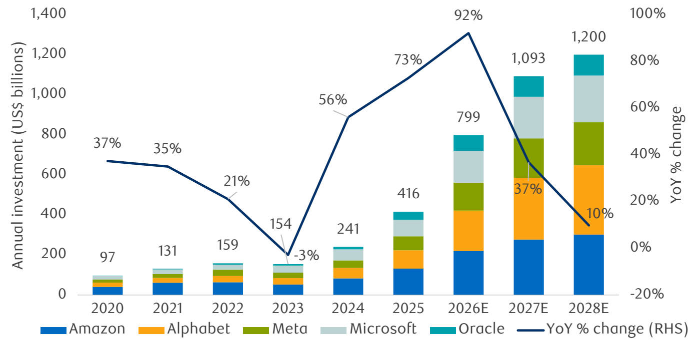
Simultaneously, and ultimately of far greater relevance to the long-term growth outlook, productivity growth appears to be accelerating (Exhibit 5). We believe a significant fraction of this represents the initial benefits from AI-related efficiencies, and that these gains should become an enduring – and increasingly international – tailwind over time. The developed world may be shifting from a low- to high-productivity growth regime. This would be enormously helpful, and quite a useful offset against long-standing structural headwinds including adverse demographics, high public debt loads and climate change.

Exhibit 3: Manufacturing activity shows surprising strength



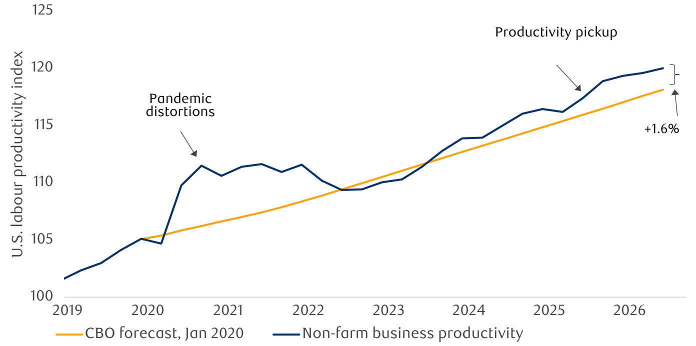
Note: As of August 2026. PMI refers to Purchasing Managers Index for manufacturing sector, a measure for economic activity. Source: Haver Analytics, RBC GAM

Exhibit 4: Hyperscalers are expected to continue ramping up CapEx



Note: As at September 01, 2026. Source: Bloomberg, RBC GAM

Exhibit 5: U.S. labour productivity growth has outperformed expectations



Note: Labour productivity index as of Q2 2026. CBO forecast is re-indexed to Q4 2019 actual. Source: Congressional Budget Office (CBO), U.S. Bureau of Labor Statistics, Macrobond, RBC GAM

Of course, few technological revolutions are entirely tidy. The question of whether AI will be substantially job-destroying is not presently clear. It certainly seems that AI will be capable of performing many of the tasks that white-collar workers do today. But that doesn't mean that net job losses must occur. New technologies also lower costs, create new markets and increase aggregate demand.

Another critical question is whether the AI race will continue at its torrid pace. Much is riding on this, not just because earnings forecasts are baking in further optimism, but because many companies in the AI space are increasingly weaving a web of interconnected promises and contractual obligations reliant on it.

There is a clear risk for the prominent frontier model makers, given the strong performance of cheaper fast-following open models (Exhibit 6). We suspect there will be room for both types of inference in a mature AI ecosystem, but a competitive market could limit the margins of the most advanced models, which might in turn slow the pace at which the frontier model makers are able to continue innovating.

Another risk for the sector is simply whether it is logistically possible to bring additional compute online fast enough given memory chip shortages and the time it takes to build new data centres.

But for all of that, we are generally optimistic on the AI technology itself and many hyperscalers seem well positioned to thrive. Even more importantly, the myriad companies that will deploy AI into their businesses are also well positioned to benefit.

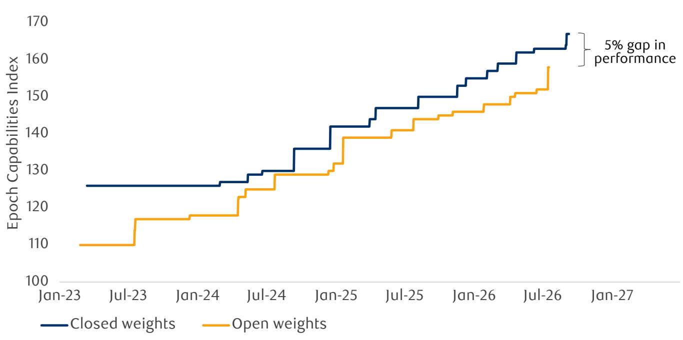
Solid growth outlook

The current year is delivering solid economic growth, supported prominently by fiscal stimulus, the lagged effect of earlier rate cuts, stock market wealth effects, and the duo of AI-related CapEx growth plus an AI-driven incremental addition to productivity growth.

Looking ahead, the economic environment is likely to remain reasonably supportive (Exhibit 7). Rising bond yields and the prospect of central bank tightening argue that the rate environment will no longer be as helpful. But fiscal policy should remain somewhat supportive, the energy shock is presumed to ease somewhat in 2027, and we look for even stronger AI-driven productivity growth as the technology matures.

U.S.-based capital investment is proving an unusually strong economic support. This is mainly an AI story, but may be broadening into other sectors. This isn't to say that the consumer is unimportant – the bulk of economic demand still originates with the consumer, and fortunately spending growth is acquitting itself well despite the challenge of high energy prices and rising borrowing costs.

Exhibit 6: Open models only lag modestly in performance but cost much less



Note: As at September 9, 2026. Source: Epoch AI, RBC GAM

Exhibit 7: Growth impulses: the transition from 2026 to 2027

	U.S.	Canada	Rest ofdeveloped world
Monetary policy / rates	+ → –	+ → •	+ → •
Fiscal policy	++ → +	++ → ++	++ → ++
Energy shock	– → •	• → •	– – → +
Stock market wealth effect	++ → +	++ → +	++ → +
AI CapEx	+ → +	• → •	• → •
AI productivity	+ → ++	+ → +	+ → +
Overall	+ → +	+ → +	+ → +

Note: As of August 3, 2026. Source: RBC GAM

While the U.S. economy has slowed slightly in recent months, this is arguably a good thing. Risk assets had become concerned about the economy overheating (with adverse implications for inflation and thus monetary policy), and to that end have recently celebrated some softer economic figures. The sweet spot is obviously avoiding both weakness and strength; decent growth is the goal, and we think likely to be achieved.

Our business cycle scorecard argues this is a mid-to-late cycle moment (Exhibit 8). That's not as attractive as being at the start of a brand new cycle with all of the stock market upside and economic runway associated with it, but neither is it a bad place to be. Our suite of recession models is also constructive, making the claim that the risk of a contraction over the next year is unusually low.

In turn, our economic growth forecasts mostly land ahead of the consensus for 2027 (Exhibit 9). Aside from fellow AI-supercharged South Korea, the U.S. is again expected to be the fastest growing developed-world economy in the coming year.

We continue to believe that structural reforms underway in the Eurozone, UK, Japan and Canada will gradually unlock additional growth in those jurisdictions, though patience is necessary as such initiatives are still in their early phases.

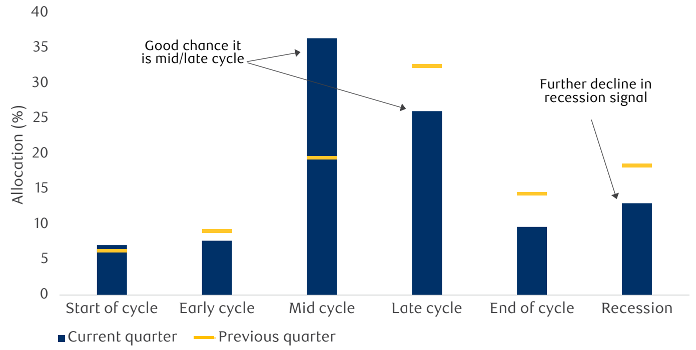
Real challenges, but seemingly manageable

Nipping at the heels of the positive economic growth environment are a number of pesky headwinds and risks, including the ongoing Middle East energy shock, rising bond yields and additional tariffs.

Energy shock lingers, but not as bad as feared

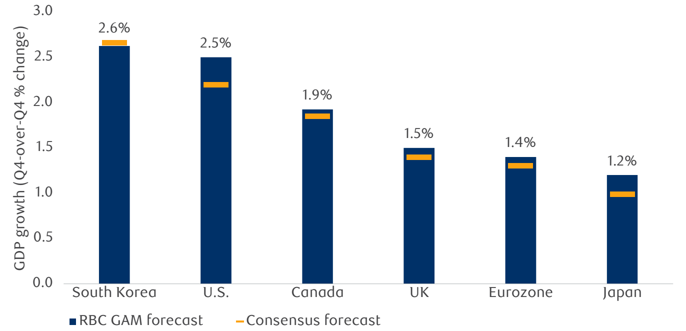
With the U.S.-Iran conflict now six months old, it is nothing short of remarkable that oil prices – while indisputably elevated versus pre-war levels – remain no worse than approximately US$100 per barrel (Exhibit 10).

Exhibit 8: U.S. business cycle score



Note: As at August 7, 2026. Calculated via scorecard technique by RBC GAM. Source: RBC GAM

Exhibit 9: RBC GAM GDP forecast for 2027: developed markets



Note: RBC GAM forecast as of August 25, 2026, consensus forecast as of September 4, 2026. Source: Bloomberg, RBC GAM

Exhibit 10: Crude oil prices rebound partially as conflict resumes in the Middle East

Note: As of September 4, 2026. Source: Bloomberg, RBC GAM

The initial consensus had been that the energy market would be catastrophically squeezed within just a few months. In practice, that hasn't happened. A series of cobbled-together supply and transportation solutions have eased much of the constraint, minimizing the demand destruction necessary to match oil supply with demand (Exhibit 11). In turn, oil prices haven't had to rise quite so far.

To be sure, the energy shock is still adding to inflation, and while we assume some easing of Hormuz restrictions in the months ahead, there is a clear alternative scenario in which the Strait instead remains mostly closed and certain temporary remedies such as inventory drawdowns become less viable, making the situation incrementally more painful.

A possible "super" El Niño weather pattern spanning the remainder of 2026 into 2027 could also slightly dim global growth and slightly add to global inflation, primarily via food prices.

Rising yields concerns

Global bond yields have been trending upward since 2020, marking an end to the previous low-rate era. There has been another leg higher in recent months, particularly at the longer end of the yield curve (Exhibit 12).

This movement is broadly logical. Many countries continue to run large fiscal deficits, and have accordingly accumulated large public debt loads. The U.S. national debt now exceeds an eye-watering US$40 trillion. Inflation also remains broadly too high. Further, there is now some crowding occurring in the bond market, not just as countries compete with one another for bond buyers, but as tech giants wade into the fray with large bond issuances of their own. Meanwhile, with the era of quantitative easing over and major sovereign reserve managers including China and Japan shifting their appetites, the burden has fallen upon rate-sensitive private investors to absorb much of the rising public debt. They are demanding a premium to do so.

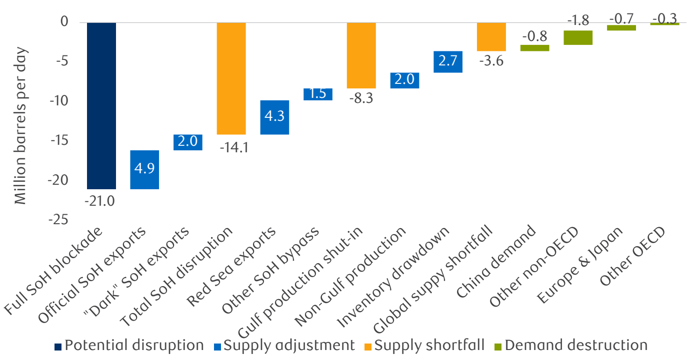
For U.S. bonds specifically, the "declining exceptionalism" theme – with the quality and predictability of public policy decisions being a particular source of concern – is a further theoretical catalyst.

The U.S. Treasury Department is attempting to counter upward pressure on yields with an expanded bond buyback program. But the program is small and with limited ability to upsize, so we expect yields to remain high though not to rise substantially beyond present levels.

More tariffs

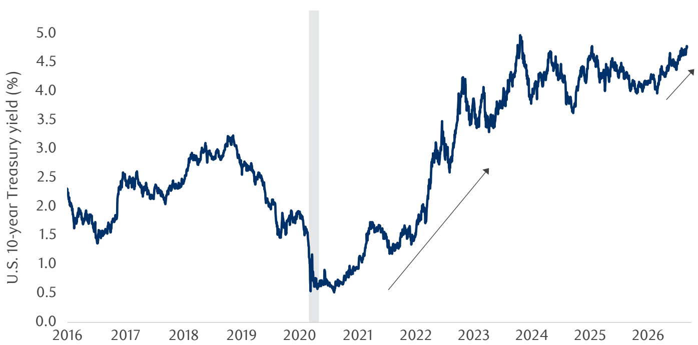
After courts knocked down the average U.S. tariff rate earlier in the year, the White House has been gradually reconstructing its desired tariff regime – in line with our expectations.

Exhibit 11: Both supply and demand have adjusted to Strait of Hormuz disruptions



Note: As at August 19, 2026. Source: U.S. Energy Information Administration (EIA), International Energy Agency (IEA), RBC GAM

Exhibit 12: Rising bond yield environment



Note: As of September 03, 2026. Shaded area represents recession. Source: U.S. Department of Treasury, Macrobond, RBC GAM

However, the recent U.S. imposition of a large 50% tariff on 5% of Canadian exports came as a surprise. Canada is now responding in tit-for-tat fashion, with the implication that both countries' economic and inflation trajectories are slightly worsened. But the blow to the U.S. is sufficiently small as to not require a significant forecast revamp, and for Canada it also amounts to just a few tenths subtracted from growth – discussed later in the Canada section of this report.

A key lesson from 2025 remains valid today – tariffs are certainly negative, but the scale of the damage is somewhat less than popularly imagined.

Upside risks should not be neglected

Much as there are downside risks, there are also upside risks that deserve mention. In fact, if anything, a key upside risk from the past few years has repeatedly come true: the AI boom keeps exceeding expectations.

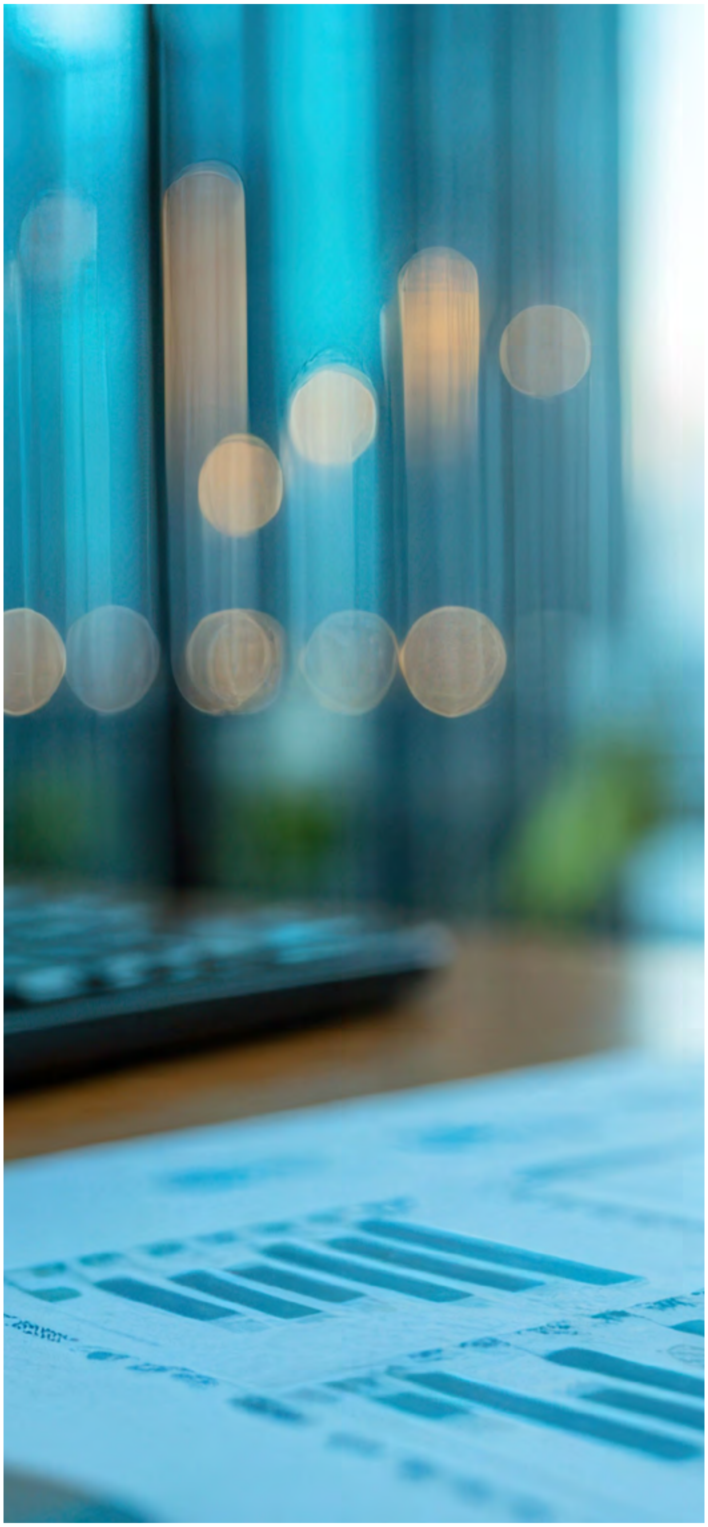
What could go surprisingly well from here?

The AI sector may continue to positively surprise: hyperscalers' CapEx plans could continue to be revised higher, and the tentative productivity gains visible in the data could strengthen. The many companies theoretically set to benefit from AI – in the form of cost savings and/or faster revenue growth – could see that benefit accrue more quickly. Over time, if the cost savings are significant, AI could become substantially deflationary, helping to counter some of the upward pressure on bond yields.

Elsewhere, growth unrelated to AI could accelerate. There is tentative evidence of non-AI CapEx starting to pick up in the U.S., and clear evidence of corporate profits unconnected to AI surging globally.

Just as the war with Iran could stretch on, it might instead resolve quickly, lowering oil prices for the benefit of global growth and global inflation. Although that may feel like an unlikely prospect, continuing the war is painful for both sides.

China's stubbornly high private savings rate could start to fall, perhaps as the country's beleaguered housing market stabilizes, or as another wave of rumoured stimulus is delivered. This would unleash a large source of demand upon the world.



Finally, perhaps the structural reforms underway in long-economically stagnant regions including much of Europe, the UK, Japan and Canada will start to pay their hoped-for dividends.

Inflation pressures to partially ease

Inflation remains too high, repeatedly buffeted by an unfortunate series of inflation shocks over the past six years: pandemic-related effects, then post-pandemic recovery distortions, then tariffs, and most recently the war with Iran. Our research also argues that while AI should eventually prove deflationary, it is for the moment moderately inflationary as computer chip prices and construction costs surge.

Unhelpfully, inflation pressures are fairly broad, meaning it is not just energy prices that are rising too quickly (Exhibit 13). El Niño could have food inflation running hot over the year ahead.

After so many shocks, we assume some scarring has built up beneath the surface. In turn, the current natural state for developed-world inflation likely remains modestly above 2% – a departure from the pre-pandemic norm, when getting up to 2% was the challenge.

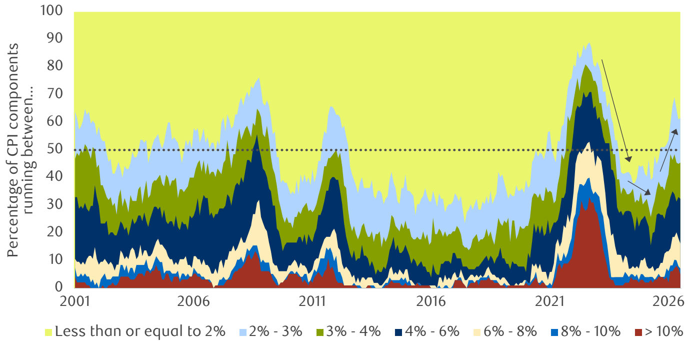
Still, there should be room for some moderate decline in inflation in 2027, if not all the way back to 2% (Exhibit 14). We budget for a diminishment of oil constraints through some combination of the Strait of Hormuz re-opening and additional supply from the rest of the world. Housing is set to remain a disinflationary force in a number of markets, including the U.S. and Canada. Modest rate hiking should also help cap more generalized inflation pressures.

Policymaker support diminishing

The net economic support from policymakers is set to diminish somewhat in the future.

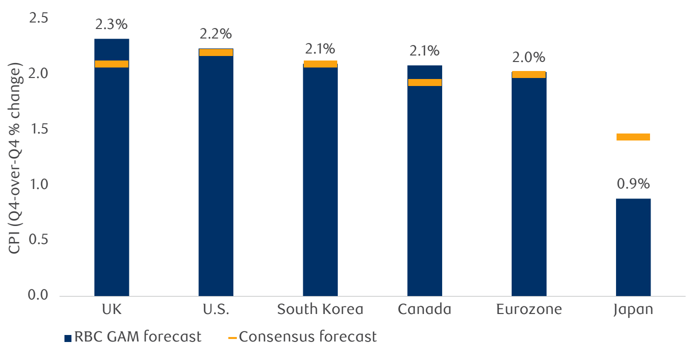
On the monetary policy side of the ledger, the era of monetary easing is transitioning toward tightening (Exhibit 15). The European Central Bank and Bank of Japan have already started raising rates, and markets expect a Fed rate hike this fall.

Exhibit 13: Inflation broadened in U.S.



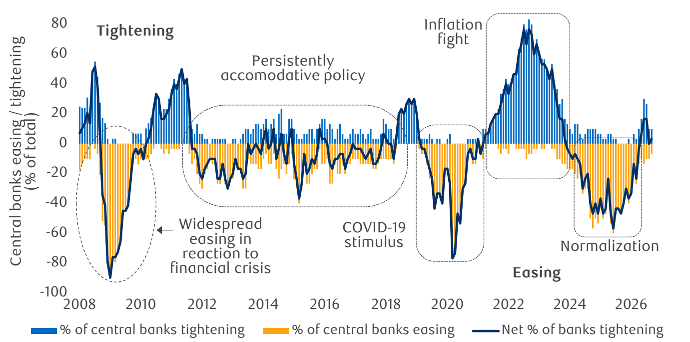
Note: As of July 2026. Share of CPI components with year-over-year % change falling within the ranges specified. Source: Haver Analytics, RBC GAM

Exhibit 14: RBC GAM CPI forecast for 2027: developed markets



Note: RBC GAM forecast as of August 25, 2026, consensus forecast as of September 4, 2026. Source: Bloomberg, RBC GAM

Exhibit 15: Monetary policy shifting from easing to tightening



Note: As of September 04, 2026. Based on policy rates for 30 countries. Source: Haver Analytics, RBC GAM

Monetary tightening in the developed world makes sense given still-elevated inflation readings paired with low unemployment rates and decent economic growth prospects.

The language being used by the U.S. Federal Reserve has clearly been hawkish, and this type of communication generally precedes rate hikes (Exhibit 16). New Fed Chair Warsh has lately conveyed particular dissatisfaction with elevated inflation.

Turning to fiscal policy, large deficits remain likely across a significant fraction of the developed world, providing some measure of economic support. There is evidence that Germany's military and infrastructure push is starting to gain traction, and Japan is similarly in motion.

However, the scale of U.S.-specific fiscal stimulus could fade in the coming years. Part of this is simply because so much has already been delivered, including prominent tax cuts and deregulation. But the upcoming midterm elections are also likely to result in the division of power between Republicans and Democrats, which could limit further fiscal stimulus and translate into fewer business-friendly initiatives. On balance, the election may be marginally negative for both growth and inflation.

Chinese weakness is only temporary

China's economy has slowed over the past year, notably including weaker retail sales and industrial production growth.

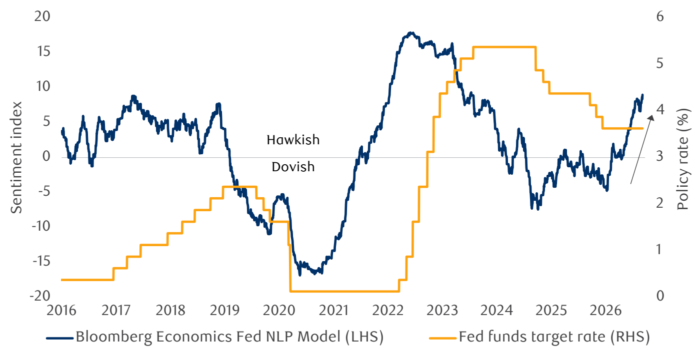
But we nevertheless remain optimistic about China's medium-term outlook.

The country's exports are successfully pivoting to new markets after U.S. tariffs were raised (Exhibit 17).

The housing market might be starting to bottom, as per a tentative increase in Tier 1 home prices (Exhibit 18). Our assumption is that further healing is necessary before a more enduring rebound can occur, but policymakers just extended the country's maximum mortgage term from 30 to 40 years, and so the process is already underway.

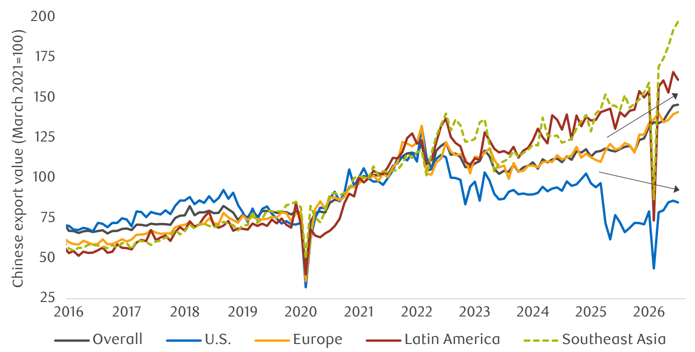
Chinese policymakers are also now discussing the potential for more government stimulus, which strongly argues for an improved economic growth trajectory ahead.

Exhibit 16: Natural language processing suggests Fed commentary has become more hawkish



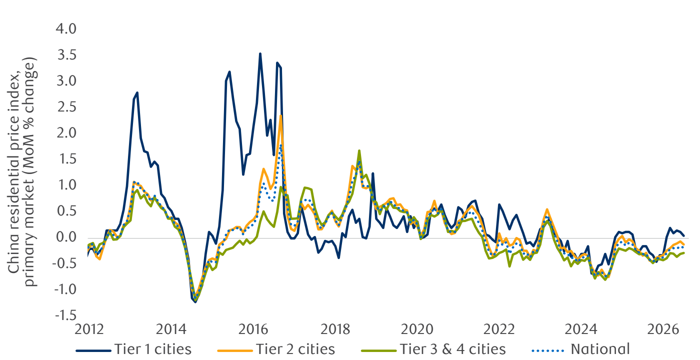
Note: As of September 04, 2026. Source: Federal Reserve Board, Macrobond, RBC GAM

Exhibit 17: Chinese exports diversifying away from U.S.



Note: As of July 2026. Source: China General Administration of Customs, Macrobond, RBC GAM

Exhibit 18: Home prices rise in major cities



Note: As of July 2026. Source: CNBS, Macrobond, RBC GAM

Fundamentally, the greatest cause for optimism relates to China's increasingly impressive track record of innovation. China now leads the world in such technologies as solar panels, batteries and robotics, is rapidly taking over the global auto market, and is moving quickly in AI, computer chips and pharmaceuticals. Promisingly, China now invests more in research and development each year than the U.S. (Exhibit 19).

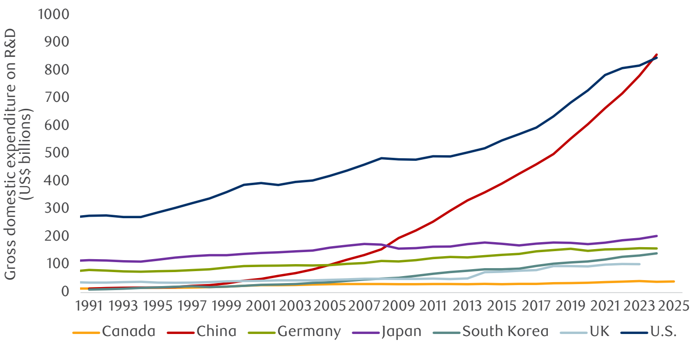
Examining the emerging-market outlook more broadly, our forecasts anticipate above-consensus growth in the two economic behemoths – China and India – versus on-consensus growth in Mexico and slightly below-consensus outcomes for Brazil and Russia (Exhibit 20).

Canada's latest challenge

The Canadian economy was just starting to find its feet, growing at a strong 3.2% annualized pace in the second quarter and quashing concerns that the country might be in a recession (happily, the prior quarter's slight decline was also revised away). Regional unemployment rates across the country have enjoyed a gradual decline in recent quarters (Exhibit 21).

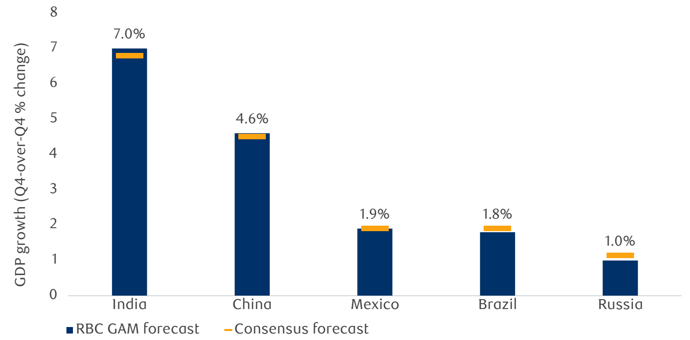
But a new threat emerged in mid-August when the U.S. levied significant additional tariffs that raise the average tariff rate on Canadian products from 5.9% to 8.4% (Exhibit 22).

Exhibit 19: China has surpassed U.S. in R&D spending



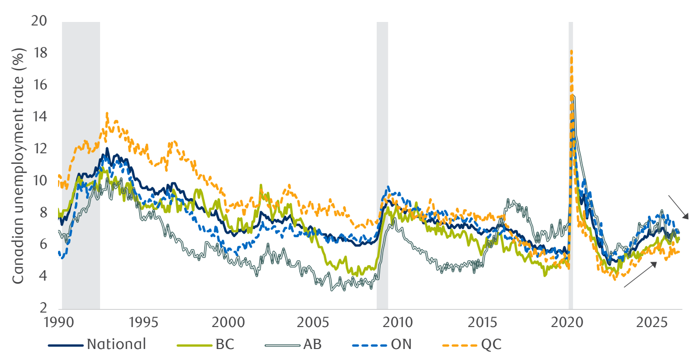
Note: As of 2025 for Canada, 2023 for UK, 2024 for all other countries. R&D expenditure in PPP-based constant prices using 2020 as base year. Source: OECD, Macrobond, RBC GAM

Exhibit 20: RBC GAM GDP forecast for 2027: emerging markets



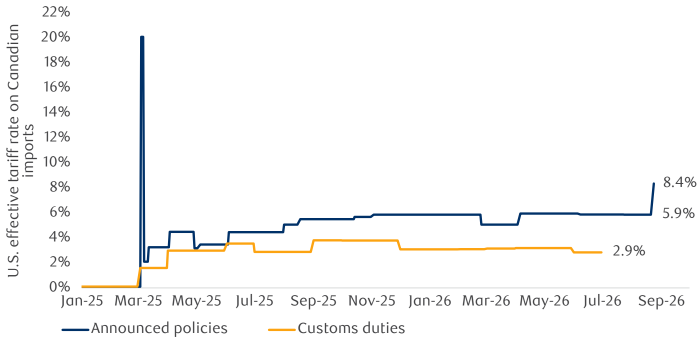
Note: RBC GAM forecast as of August 25, 2026, consensus forecast as of September 4, 2026. Source: Bloomberg, RBC GAM

Exhibit 21: Canadian unemployment rate by regions



Note: As of August 2026. Shaded area represents recession. Source: Statistics Canada, Haver Analytics, Macrobond, RBC GAM

Exhibit 22: New U.S. levies raise tariff rate on Canadian exports



Note: As at August 24, 2026. Source: Bloomberg, RBC GAM

Canada's tariff rate has now risen above Taiwan, the UK and Mexico. While the rate nevertheless remains below the global average, it is undeniably painful given Canada's close trade orientation toward the U.S.

Canada has responded in roughly proportionate fashion with tariffs of its own, and we estimate an approximate 0.2% hit to Canadian GDP after budgeting for government support, and an extra 0.1% to 0.2% added to Canadian inflation. These are unfortunate but manageable blows, and while they constrain the Canadian growth rate and serve as partial motivation for our view that Canada may fail to outpace the consensus expectations, they are not likely to prove recessionary. Of course, there is uncertainty around this assessment: the U.S. might back down as it has on several occasions over the past two years, or it might instead increase the tariffs further on January 1, as it has threatened to do.

The Bank of Canada should not be in a rush to tighten given Canada's unemployment rate remains slightly above target, tariffs present a new challenge, and Canadian inflation isn't as high as in the U.S. But based on the central bank's latest communication, there remains a clear bias toward tightening and market pricing assigns an over-90% likelihood of an initial 25-basis-point rate increase by year-end.

More generally, we remain hopeful that Canada's return to population growth in 2027, combined with the scope for more infrastructure spending and productivity growth, will unleash a period of good economic growth in the years ahead.

Bottom line

In sum, the global economy continues to demonstrate impressive resilience despite a formidable array of headwinds — the lingering Hormuz energy shock, rising bond yields, additional tariffs, and inflation that remains stubbornly above target. The AI-powered investment and productivity boom is proving a powerful counterweight, underpinning GDP growth and lifting corporate earnings, with some evidence of a broadening into other sectors and beyond U.S. shores.

With the earnings outlook strong, the recession risk unusually low, and the economic expansion appearing to have further room to run, we maintain a slight equity overweight with a continued tilt toward the U.S., Canada, and Asia — while remaining mindful that the range of outcomes, both upside and downside, is wider than usual.

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