RBC Global Asset Management

Economic outlook

SUMMER 2026

The bottleneck and the breakthrough

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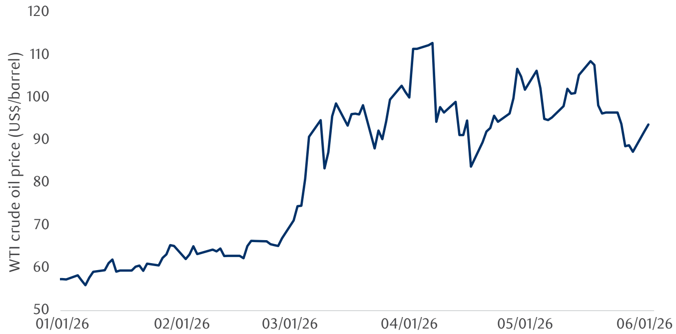
Two major forces are presently dominating the macroeconomic debate: the perils associated with the ongoing global energy shock (Exhibit 1) versus the rapid advancement and great promise of artificial intelligence (AI).

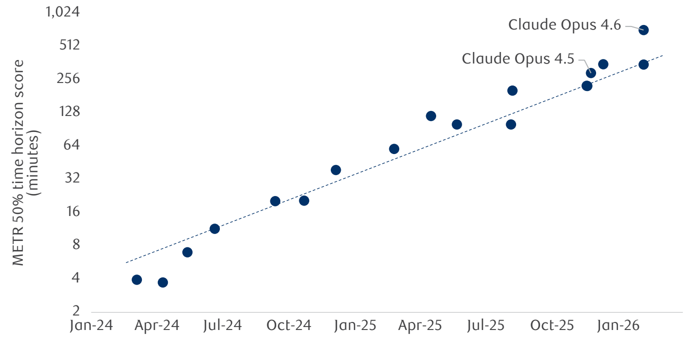
On the back of surging capital expenditures, large language models (LLMs) continue to improve at an exponential pace (Exhibit 2), with tentative evidence of AI-related productivity gains starting to manifest. The stock market has been highly enthused by this progress.

Exhibit 1: Crude oil prices surge in the wake of the Iran War



Note: As at June 2, 2026. Source: Bloomberg, Macrobond, RBC GAM

Exhibit 2: AI models are becoming expontentially more capable



Note: As at March 20, 2026. Source: METR, RBC GAM

Conversely, the energy shock resulting from the war with Iran has caused the prices of oil, natural gas and its distillates to surge, palpably increasing inflation (Exhibit 3) and theoretically damaging growth. But, in practice, economies have so far proven surprisingly resilient in the face of this shock (even if we do continue to budget for some damage eventually bubbling to the surface). Fortunately, this energy shock should prove temporary and may be resolved relatively shortly.

Alongside these factors, the pace of economic growth has been solid, with manufacturing purchasing managers' indexes (PMIs) broadly accelerating over the past several months (Exhibit 4). The risk of recession is low.

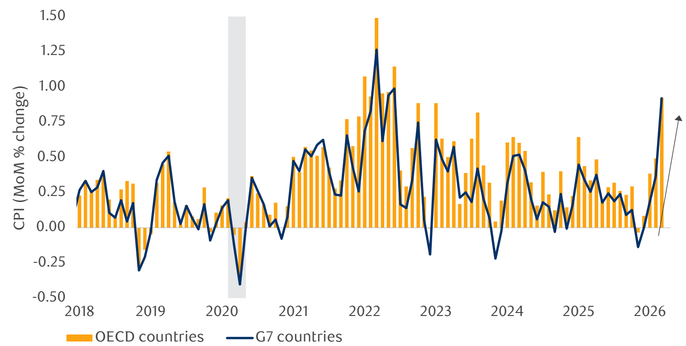
Our recommended asset mix added slightly to fixed income (out of cash) this quarter now that bond yields have risen to more attractive levels. Equities remain a slight overweight relative to fixed income due to the prospect of further economic and earnings growth and anticipated support from AI-related forces. Already-full valuations discourage a bolder stance. Regionally, the allocation to U.S. equities rose versus an incremental reduction from Europe, where the energy shock hurts more, geopolitical risks are higher and AI is less of a support for growth. We also slightly reduced the allocation to emerging markets, where memory chip makers have gone on quite a run and may now be vulnerable.

Temporary energy bottleneck

The war with Iran is now three months old, and while oil prices are not quite as astronomically high as feared and the stock market is showing a stiff upper lip, the fact remains that – at the time of writing – the war is not yet resolved.

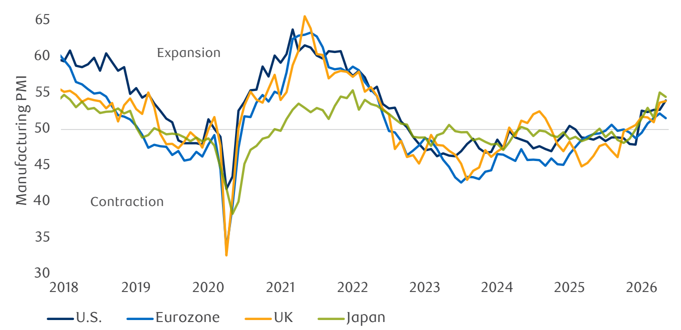
The fighting has substantially subsided, which for most wars would be the end of the story. But in this instance, the fact that the Strait of Hormuz – a narrow shipping channel through which about 20% of the world's oil and liquid natural gas would normally flow – is still closed means that the central economic problem created by the war has not yet been solved (Exhibit 5).

Exhibit 3: Global inflation has risen sharply since the start of Iran War



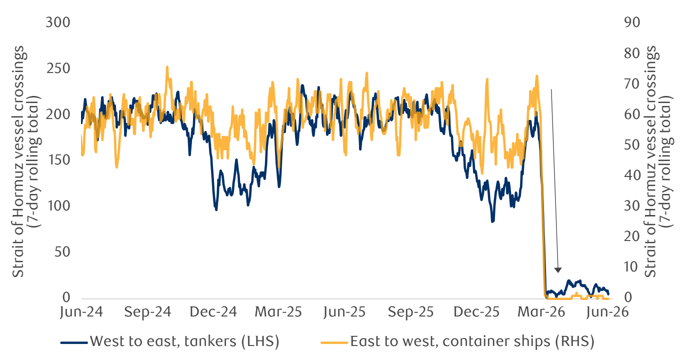
Note: As of March 2026. Shaded area represents U.S. recession. Source: OECD, Macrobond, RBC GAM

Exhibit 4: Manufacturing activity shows surprising strength



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

Exhibit 5: Strait of Hormuz remains largely closed despite ceasefire



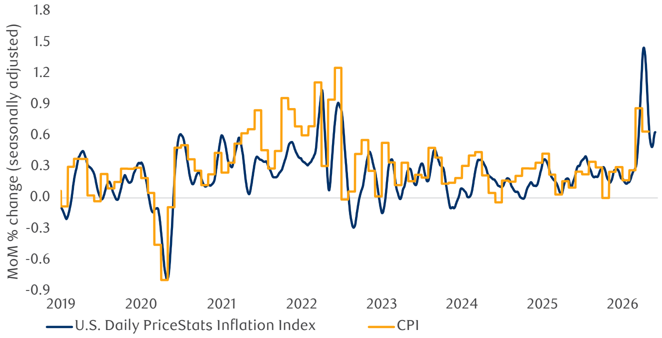
Note: As of June 02, 2026. Source: Bloomberg, RBC GAM

This lingering bottleneck means global oil prices and regional natural gas prices are still elevated, and the supply of refined products has been especially pinched in some markets. Inflation has accordingly accelerated over the past several months (Exhibit 6).

The economic consequences of the war are theoretically greatest for Asia and Europe, which are the primary consumers of the energy that would normally flow from the Middle East (Exhibit 7). Conversely, North America is much less affected for two reasons: it consumes far less energy from the region, and the U.S. and Canada are both net energy exporters, meaning that significant subsets of their economies actually profit from the energy shock.

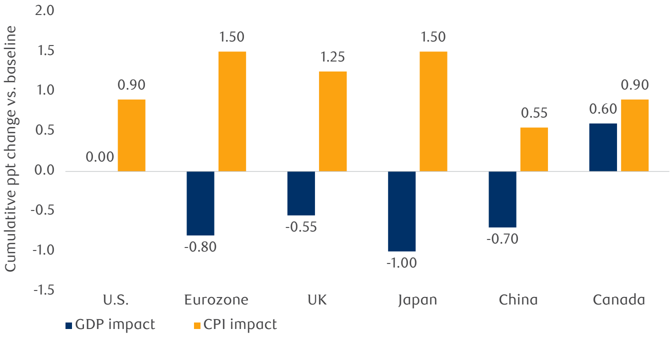
U.S. economic data in particular has largely shrugged off the effects of the war, with weekly jobless claims still quite low – a doubly impressive accomplishment given parallel concerns about AI-related job destruction (Exhibit 8).

Exhibit 6: U.S. inflation has accelerated due to oil spike



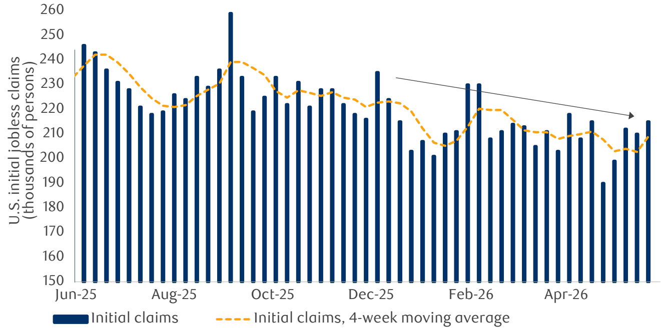
Note: PriceStats Inflation Index as of May 30, 2026, CPI as of April 2026. Source: State Street Global Markets Research, RBC GAM

Exhibit 7: Economic impacts of an energy shock vary by region



Note: As at March 9, 2026. Assumes a permanent $40/bbl increase in oil prices and 50% increase in natural gas prices. Source: Bloomberg Economics, OECD, RBC GAM

Exhibit 8: U.S. jobless claims are low and steady



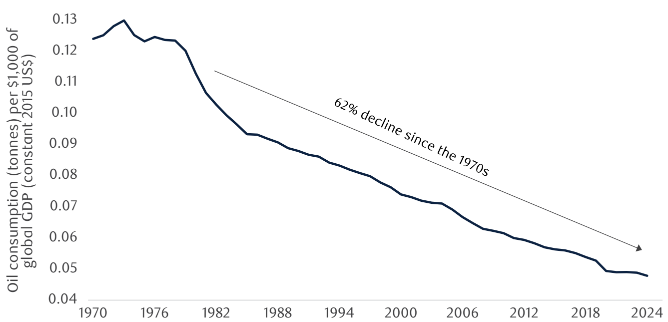
Note: As of the week ending May 23, 2026. Source: DOL, Macrobond, RBC GAM

The damage to Asia and Europe has also been less acute than feared. This is in part because the global economy is much less energy-intensive than in decades past – energy consumption per unit of economic output has declined by a remarkable 62% since the energy shocks that plagued the 1970s (Exhibit 9). Developed Asia and Europe are particularly light users of the affected energy products (Exhibit 10). Many national governments have also chosen to subsidize the cost of energy in their markets, partially transferring what would have been an economic and inflation irritant onto the fiscal ledger.

The U.S. has been quite transparent in desiring a resolution to the war, and this makes sense given the domestic political backlash the White House is suffering over the rising cost of living (Exhibit 11). Iran has taken a harder line, but also surely desires a resolution: it has been struck more than 25,000 times by the U.S. and Israel, its supply of munitions is greatly diminished, the Iranian economy is in shambles, China is exerting pressure on its ally, and Iranian leadership likely fear being targeted.

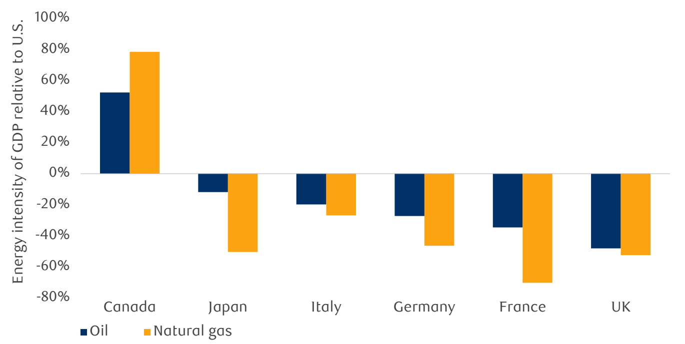
We and financial markets alike anticipate a near-term resolution to the war and reopening of the Strait of Hormuz. Consistent with this, both parties are attempting to hash out a deal. In turn, a widespread recession is unlikely, and recession probability markets have accordingly fully unwound their initial trepidations (Exhibit 12).

Exhibit 9: The global economy has become much less oil intensive over the past 50 years



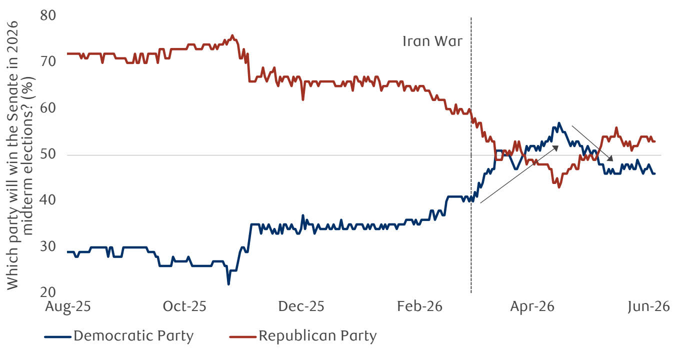
Note: As of March 18, 2026. Source: BP Statistical Review of World Energy, UN Trade and Development, Macrobond, RBC GAM

Exhibit 10: G7 oil and gas intensity relative to the U.S.



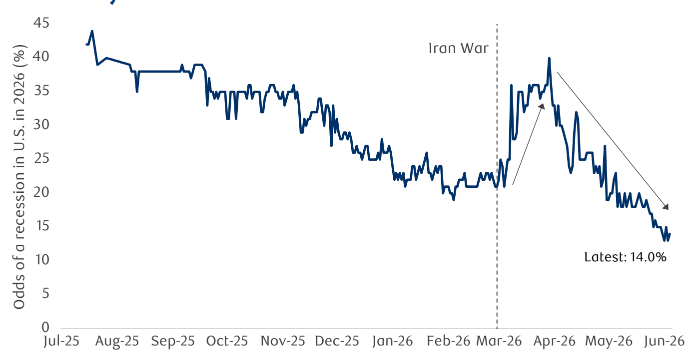
Note: As at May 24, 2026. Data is for 2024. Energy intensity measured as MJ of oil and natural gas consumption per dollar of constant 2015 US$ GDP. Source: BP Statistical Review of World Energy, UN Trade and Development, RBC GAM

Exhibit 11: Senate race has tightened since Iran War



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

Exhibit 12: Odds of U.S. falling into a recession in 2026 have fully reversed



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

Should the Strait of Hormuz instead be blocked for significantly longer, damage could begin to accelerate on a number of fronts, from second-round inflation effects that traditionally become stronger once energy shocks have persisted for more than three months, to acute shortages of particular products ranging from jet fuel to sulfur to helium. Supply chain pressures have already begun to mount (Exhibit 13).

This war also highlights several pre-existing themes. The prior rules-based order is in decline, and a power-based order in which the mightiest countries impose their will upon the world is now seemingly ascendant. It is therefore a more dangerous world, with military spending on the rise (Exhibit 14) and slightly larger investment risk premiums arguably justified across a range of assets.

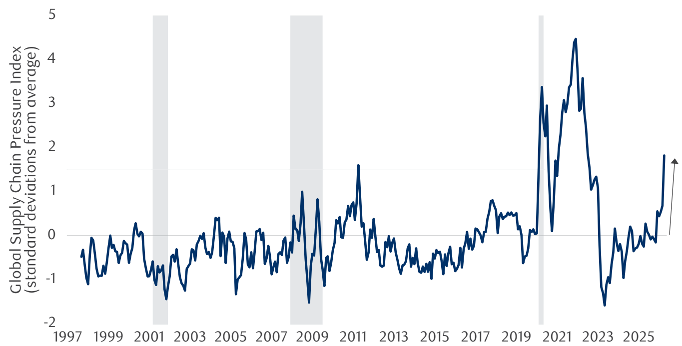
Artificial intelligence breakthrough

While the war with Iran will hopefully be resolved shortly, the rapid advancement of artificial intelligence is a theme that is unlikely to relinquish its grip anytime soon. The technological breakthrough appears destined to be the dominant economic and investment story of this era given the extent to which it promises to boost productivity, create corporate winners and losers, change how people work, and perhaps even alter society itself.

Concerns about AI have gained new prominence in 2026, with potentially disrupted software companies beaten down and anxiety about job losses taking centre stage. It must be emphasized that, so far, the overall U.S. labour market has held together as per a still-low unemployment rate. While there is some evidence that recent university graduates in AI-impacted fields are doing moderately worse, even this is not certain as other research argues that this trend actually began with the shift toward working from home after the pandemic, which has made it harder to train new hires.

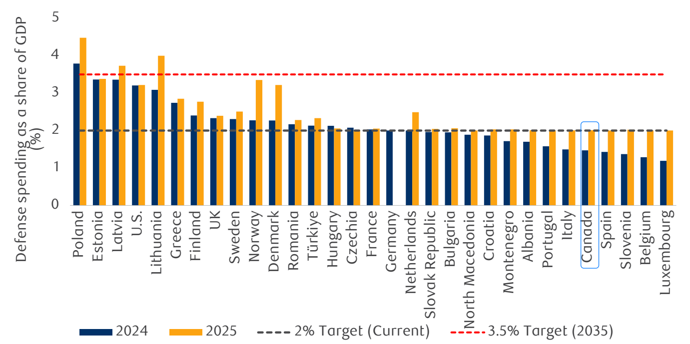
In the meantime, the most visible aspect of the AI revolution has been the incredible surge in capital expenditures undertaken by the corporate behemoths building out and scaling their new models (Exhibit 15). This spending continues to rise at a remarkable pace, contributing materially to U.S. economic growth in 2026 and with the prospect of further support in subsequent years. The many companies that provide the hardware and services necessary to expand data centres are naturally thriving.

Exhibit 13: Global supply chain pressure rising sharply



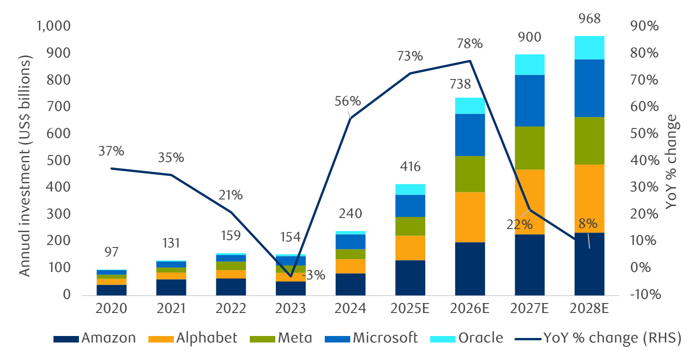
Note: As of April 2026. Shaded area represents U.S. recession. Source: Gianluca Benigno, Julian di Giovanni, Jan J. J. Groen, and Adam I.Noble, "A New Barometer of Global Supply Chain Pressures," Federal Reserve Bank of New York Liberty Street Economics; Macrobond, RBC GAM

Exhibit 14: Rising defense spending



Note: As at June 3, 2025. 2024 and 2025 expenditure are estimates. 2025 data not available for Germany. Source: NATO, RBC GAM

Exhibit 15: Hyperscalers are expected to continue ramping up CapEx

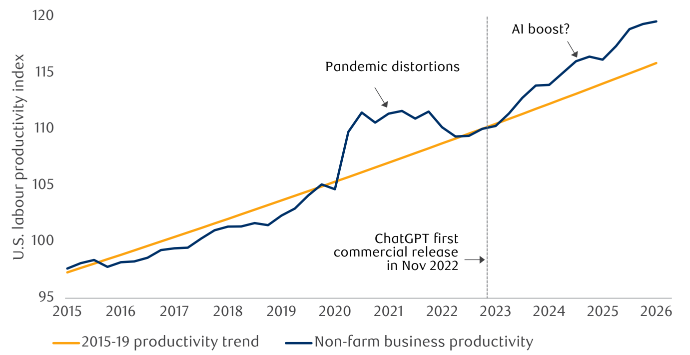


Note: As at June 03, 2026. Source: Bloomberg, RBC GAM

Memory chip makers have shone particularly brightly within this AI-supply ecosystem. While there is no evidence that the demand pressures or supply constraints that have enabled their outsized profit margins are about to reverse, the industry has a long history of boom-bust cycles and so investor risk in this segment is not trivial. This concern is particularly acute as hyperscalers express dissatisfaction with the fact that over half of the cost of an AI chip is now the memory embedded within it.

Of course, buying up computer hardware is just a means to an end. The goal of all this AI spending is to create a general artificial intelligence that greatly increases productivity. Promisingly, the large language models at the centre of this revolution have been improving by a remarkable 6.4-fold per year in recent years. We believe the recent visible acceleration in overall U.S. productivity growth means that the benefits of the new technology are starting to be realized (Exhibit 16).

Exhibit 16: U.S. labour productivity growth has accelerated since ChatGPT's release



Note: As of Q1 2026. Source: Macrobond, RBC GAM

Given the great uncertainties surrounding AI, we continue to think in terms of multiple scenarios (Exhibit 17).

There is a 25% chance that AI proves important but ultimately falls short of its seemingly infinite promise: it adds incrementally to productivity growth and proves useful across a range of tasks, but does not greatly change how businesses operate or lives are lived. If such a ho-hum outcome seems hard to fathom, just consider that video conferencing did not end business travel, nor did the internet and its nearly infinite information render schools redundant, narrow the gap between haves and have-nots, or end in-person shopping.

Exhibit 17: AI scenario road map

	General purpose technology		Unprecedented disruptor		
	1. Minor	2. Major	3A. Dystopia	3B. Utopia	3C. Mixed
Description	• AI improvement slows/stalls • Relatively narrow applications • Poor tech ROI	• AI continues to improve • Broad applications • Some labour market disruption, but new jobs created • Solid tech ROI	• Rapid improvement in AI capabilities • Broad and profound applications threaten to displace many workers		
			• Economic disaster • Widespread job losses, falling demand outweigh productivity gains	• Abundance! • Surging government revenues allow for broad income re-placement	• AI tax limits displacement • Labour partially compensated
Probability	25%	45%	3%	3%	24%
AI productivity shock	<0.25%	0.5-2.5%	5%+		

Note: As at June 02, 2026. Productivity shock is initial increase in annual productivity growth. Source: RBC GAM

The most probable scenario, with a 45% chance, is that AI proves to be the next major general-purpose technology, heralding a golden era of faster productivity growth akin to the 1990s through early 2000s. In this scenario, AI does displace significant numbers of workers in certain sectors – as prior such technologies have done – but, as with those other technologies, it doesn't ultimately impose a higher economy-wide unemployment rate because it creates enough wealth and new opportunities that workers are able to pivot elsewhere.

Also, do not underestimate the scope for rising demand – including for workers – in sectors that experience AI-related cost reductions. As an illustration, recall that computer spreadsheets were initially expected to sharply reduce the number of accountants since much of their job to that point was manually logging entries and calculating sums. And yet there are far more accountants today than before that revolution: the software greatly reduced the cost of providing accounting services, which in turn increased the demand for accounting.

On a similar note, 40 years ago it took a financial analyst several hours to produce a single chart tracking the price of a stock. Each data point had to be located in microfiche newspaper archives and strung together manually. By contrast, today that same chart can be created in a few seconds. This did not reduce the need for financial analysts by a thousand-fold; instead, the effective reduction in the cost of analysis meant that far, far more of the analysis was desired.

Finally, with a 30% chance, perhaps AI really is completely different than any technology that has come before – in the speed of its arrival, its capacity for self-improvement and its potential to displace high-skill jobs. This scenario could end happily if the unbelievable productivity growth enabled a world of abundance and leisure. Or it could end very badly, with companies laying off their workforces and economic demand subsequently crumbling. Helpfully, if there was evidence of the latter trajectory, policymakers would presumably step in and tax AI in a way that achieves some semblance of balance between the new technology and workers' needs, avoiding the worst-case version of this scenario.

Clearly, there are quite a number of paths this AI revolution could take. It promises to be a time of elevated uncertainty and creative destruction, with some companies winning and others losing. A common theme is that productivity growth picks up, and investors come out ahead in most (though not all) of the scenarios.

Resilient economic backdrop

The economic backdrop remains surprisingly resilient despite the energy shock, with economic data in both the U.S. and the G10 better than it was a year ago (Exhibit 18).

The year began with promising tailwinds blowing, and even as geopolitical events distract, it is important not to lose sight of them (Exhibit 19).

Exhibit 18: Economic growth improved globally

Note: As of June 03, 2026. Source: Citigroup, Bloomberg, RBC GAM

Exhibit 19: Growth tailwinds still exist for 2026

	U.S.	Canada	Rest of developed world
Monetary policy	+	+	+
Fiscal policy	++	++	++
Stock market wealth effect	++	++	++
AI CapEx	+	.	.
AI productivity	+	+	+
Overall	++	+	+

Note: As of June 03, 2026. Source: RBC GAM

While the benefit is fading and could yet reverse in the year ahead, the rate cutting delivered over the past two years still provides a slight boost to economic growth in 2026.

Meanwhile, the fiscal support for economic growth is only increasing. Alongside significant pre-existing stimulus from the U.S., Japan, Germany and Canada, geopolitical risks are prompting a further upgrade to already-bold military spending plans around the world. Widespread energy subsidies are now adding to the outlay. In the U.S., a court order to reimburse certain tariff payments is effectively adding another US$85 billion of unplanned fiscal support to the American economy.

Stock market strength continues to plump household balance sheets, with a fraction of those gains recycled via consumer spending into the economy. Indeed, after a brief Iran-related bump, financial conditions are easing and reasonably friendly toward economic growth (Exhibit 20).

As previously discussed in some detail, artificial intelligence also provides important support for near-term economic growth, both in the way that rising capital expenditures are mechanically adding to demand, and via the promise of additional productivity gains.

What about economic headwinds? Certainly, the energy shock is one, as already detailed. We anticipate at least a temporary dip in economic growth, but this should be fairly mild and partially reversed later.

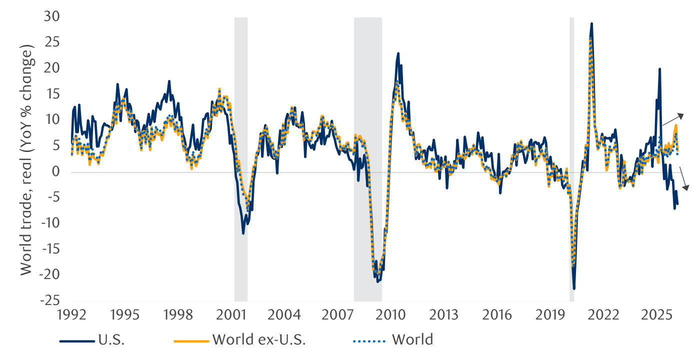
Consumer spending growth is nothing special, albeit understandably so given slow hiring plus higher energy costs and mortgage rates. The hiring constraint is arguably just a fact of life given the sluggish population growth on display in the vast majority of the world's developed nations. Fortunately, capital expenditures are carrying more than their usual share of economic growth.

Promisingly, the tariff headwind from 2025 has faded significantly this year, partly because much of the damage has already been significantly absorbed, partly because a significant subset of U.S. tariffs have been reversed via court action, and partly because the rest of the world took U.S. protectionism as a cue to engage more deeply with other trade partners, as evidenced by the remarkable acceleration in global trade excluding the U.S. over the past year (Exhibit 21).

Exhibit 20: Global financial conditions tightened amid Iran War, but have reversed

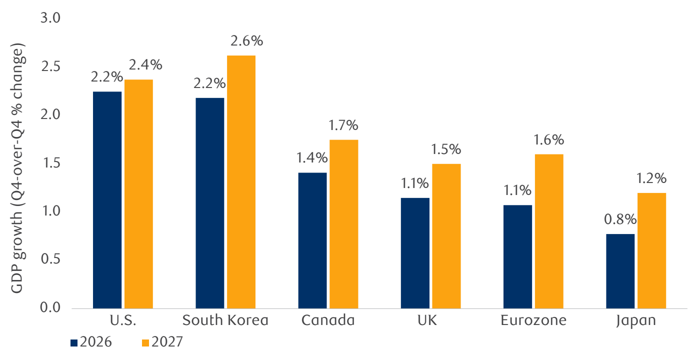
Note: As of June 03, 2026. Source: Goldman Sachs, Bloomberg, RBC GAM

Exhibit 21: Globalization continues outside of the U.S.



Note: As of March 2026. Shaded area represents U.S. recession. Source: CPB Netherlands Bureau for Economic Policy Analysis, Macrobond, RBC GAM

Exhibit 22: RBC GAM GDP forecast for developed markets



Note: As of June 01, 2026. Source: RBC GAM

Although several worrying viruses are now circulating, the risk of an economically consequential pandemic is still quite low. From a weather perspective, the year ahead is very likely to experience the El Niño phenomenon, and possibly quite a strong version of it, which creates the potential for a mild hit to global economic growth as agricultural output suffers.

Overall, despite having revised the outlook downward relative to a quarter ago on the presumption of an energy-related dip through the middle part of the year, we do anticipate an economic rebound over the second half of 2026 and a similarly solid outlook for 2027 (Exhibit 22). Our GDP forecasts are still primarily above the consensus (Exhibit 23).

The risk of recession is low according to our preferred year-ahead U.S. model (Exhibit 24). Our business cycle scorecard indicates that the cycle is probably in the “mid” or “late” phase (Exhibit 25). While the latter may sound ominous, it usually still permits a number of years of additional economic growth.

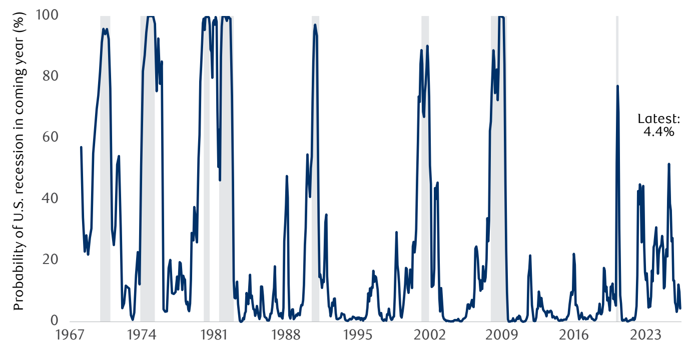
Our emerging market growth outlook similarly skews to above-consensus outcomes, and anticipates particularly speedy growth from India (Exhibit 26). China is discussed in more detail in a later section.

Exhibit 23: Growth outlook scorecard

Growth outlook scorecard							
Country/ Region	2026 GDP Forecast (Q4/Q4)	Forecast change vs. prior quarter	Level vs. potential	Momentum vs. prior year	Relative to other nations	Vs. consensus	Overall
U.S.	2.2	–	+	+	++	+	+
Canada	1.4	~	+	++	~	+	+
Eurozone	1.1	– –	~	~	–	++	~
UK	1.1	– –	–	~	–	+	–
Japan	0.8	– –	~	+	– –	~	–
South Korea	2.2	–	+	++	++	–	+

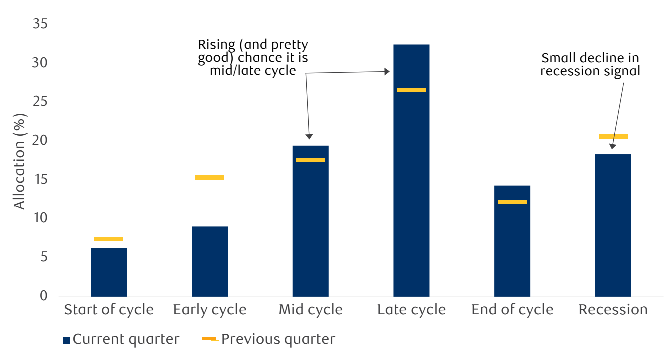
Note: As at June 01, 2026. Source: Bloomberg, RBC GAM

Exhibit 24: The probability of U.S. recession within a year is low



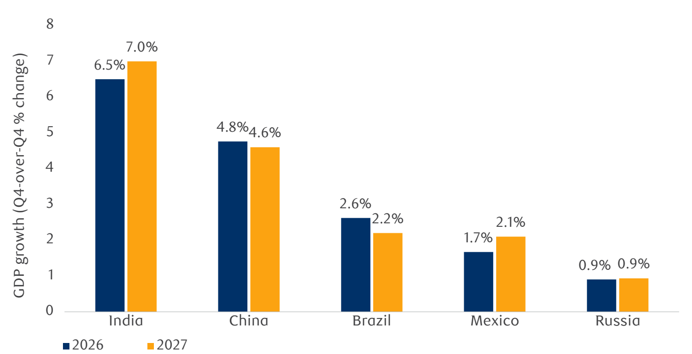
Note: As of May 2026. Based on RBC GAM model which includes financial and macro factors. Shaded area represents recession. Source: Haver Analytics, RBC GAM

Exhibit 25: U.S. business cycle score



Note: As at May 8, 2026. Calculated via scorecard technique by RBC GAM AM

Exhibit 26: RBC GAM GDP forecast for emerging markets



Note: As of June 01, 2026. Source: RBC GAM

Temporarily challenging inflation

The near-term inflation outlook has alas been upgraded due to the leap in energy prices, with some additional lingering pressure from the lagged effect of last year's tariff hikes.

The impact of the energy shock is starting to broaden, with our measure of inflation breadth revealing that consumer prices are now rising faster than normal across quite a range of product categories (Exhibit 27).

Although the war itself should soon be resolved, energy futures markets are pricing in some scarring in the form of energy prices that do not fully normalize post-conflict, and it is not clear that second-round price effects via higher transportation costs will fully reverse. In turn, inflation should be materially too high across 2026, and will likely remain elevated through the spring of 2027 before the mechanics of falling energy prices help pull inflation closer to target over the remainder of that year (Exhibit 28). These views are roughly consistent with the consensus.

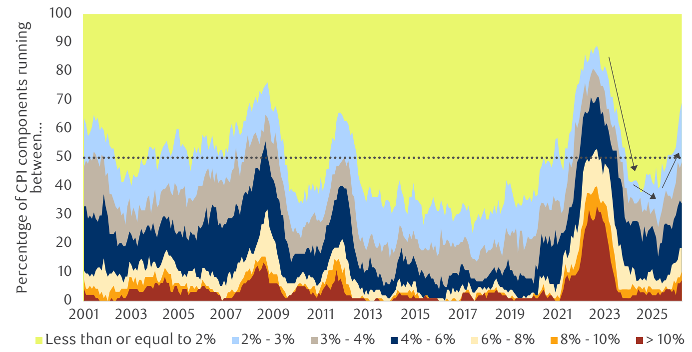
At the margin, El Niño should exert a mildly inflationary influence over the year ahead, while soft housing markets are deflationary. China should also continue to have a slightly deflationary influence on the world.

Over the longer run, our working assumption since the pandemic has been that inflation should average modestly above central banks' 2.0% targets. The ascent of artificial intelligence introduces a new twist. Its central impact on prices over a multi-decade time horizon should be deflationary: new technologies are not generally embraced unless they save money. But the open question is the extent to which this proves visible over the next few years, and critically whether it can outweigh the inflationary aspects of the AI arms race currently underway, including surging hardware prices.

Rotating monetary policy

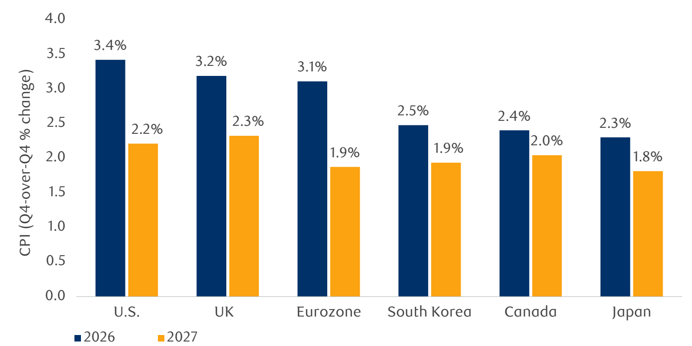
The era of monetary easing that marked the past several years is now seemingly coming to an end (Exhibit 29). That journey saw policy rates go from substantially restrictive levels to neutral or even slightly stimulative positioning for most major developed central banks. The U.S. was an exception, with a fed funds rate that is arguably still slightly restrictive, but with enough AI- and fiscal-related horsepower to permit the economy to continue growing adequately.

Exhibit 27: Inflation pressures broadening in U.S.



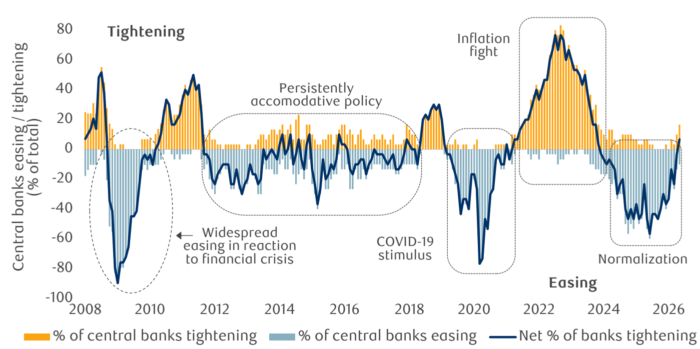
Note: As of April 2026. Share of CPI components with year-over-year % change falling within the ranges specified. Source: Haver Analytics, RBC GAM

Exhibit 28: RBC GAM CPI forecast for developed markets



Note: As of June 01, 2026. Source: RBC GAM

Exhibit 29: Monetary policy shifting from easing to hiking



Note: As of May 29, 2026. Based on policy rates for 30 countries. Source: Haver Analytics, RBC GAM

As they look to the future, central banks are now thinking more about rate hikes than cuts (Exhibit 30). This is an important changing of the monetary guard. Their motivation is the combination of still-resilient economic growth paired not just with higher energy prices, but some broadening of inflation pressures.

Certain developed-world central banks have already begun their tightening cycles, including the Reserve Bank of Australia and Norway's Norges Bank, but for most developed-world central banks there isn't any great urgency to act. The outlook is broadly for a few 25bps rate increases later this year or into next year, rather than urgent contractions.

The U.S. has a new Fed Chair with a slightly dovish inclination relative to his predecessor, and this, along with the slightly restrictive starting point for the U.S., points to an unchanged fed funds rate over the next year, in our view. That is nevertheless a pivot from the rate-cut expectations that prevailed a quarter ago.

Risk assets traditionally perform quite strongly during periods of economic growth that are paired with rate cuts, as demonstrated by the stock market strength in recent years. Periods of economic expansion that are combined with rate hikes tend to also be supportive but to a lesser extent.

China's long-run promise

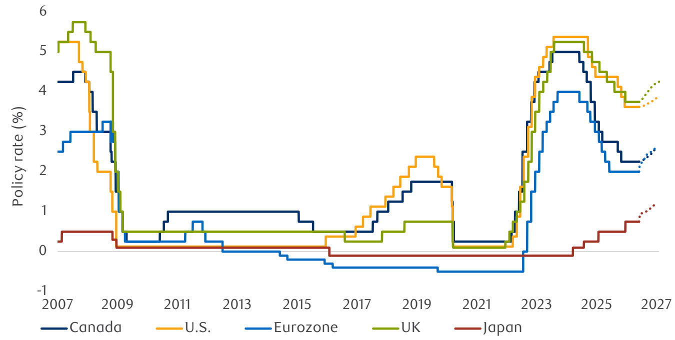
China's economy continues to be challenged by poor demographics, a soft housing market, reluctant consumers and the Middle Eastern energy shock. Still, it is notable that the country's economy still manages to grow at nearly 5% per year even without several traditional economic drivers. We forecast 4.8% Q4 over Q4 GDP growth for 2026, and 4.6% for 2027.

There is no near-term solution to China's demographic challenges (though, fascinatingly, policymakers there are trying harder than most countries to address this, not just via the abandonment of the one-child policy, but by recently ending a tax exemption on contraceptives and strengthening advertising restrictions for such products).

But there is a chance that the country's home prices could be bottoming out as per a recent increase in the value of big city home prices – often a leading indicator for the broader housing market (Exhibit 31). Any stabilization here could encourage more consumer spending.

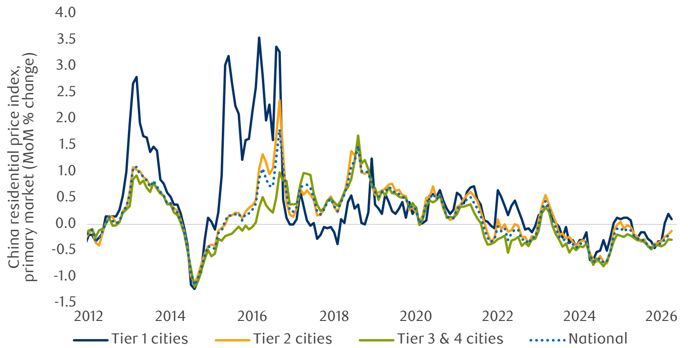
While China does not relish the energy shock, it is probably experiencing less damage than the raw statistics showing China as the single largest importer of Strait of Hormuz energy suggest. Tempering factors include the fact that China's enormous economy renders those imports less critical than they would be to almost any other country; the country has a large reserve of coal power plants and a rising number of nuclear power plants to fill in the electricity gap; and much of the fossil fuels that China imports are normally then refined and re-exported. To the extent that China has instead opted to keep some of this product, the energy

Exhibit 30: G7 central bank policy rates are expected to rise



Note: As of June 03, 2026. Dotted lines indicate futures pricing.
Source: Bloomberg, RBC GAM

Exhibit 31: Home prices rise in major cities



Note: As of April 2026. Source: CNBS, Macrobond, RBC GAM shock has been buffered for China itself, though exacerbated for developing Asian peers. China's oil reserves are also substantial and barely tapped at this point.

Where the Chinese economic story becomes exciting is over the long run. The country appears to have successfully made the leap from imitating developed nations to outright innovating at the technological frontier. China has emerged as the world leader in such technologies as electric cars, batteries, solar panels, robotics and drones, and is advancing rapidly in computer chips, artificial intelligence and pharmaceuticals.

Promisingly for future innovation, China now spends more on research and development than the U.S. (Exhibit 32). The disconnect between China's relatively low level of productivity and the incredible technologies it is building argue for a long runway of robust productivity growth ahead, and suggest that the Chinese economy has plenty of growth left in it.

Risks to the base-case view

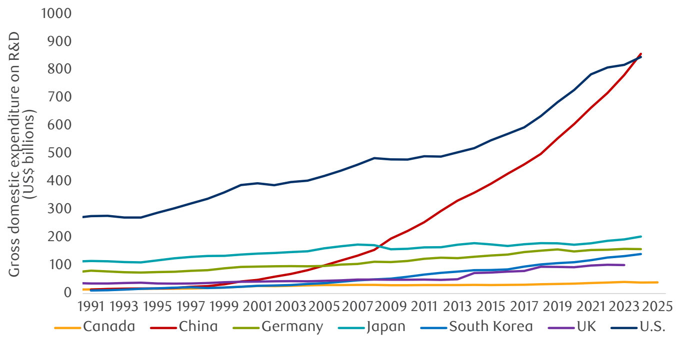
Economic forecasting is an imprecise science, making it important to contemplate events and forces that could deviate from our base-case view.

There are several negative risks. In the geopolitical space, there is of course the chance that the energy shock persists for longer, raising inflation further, making it stickier and thus harder to reverse, and doing additional economic damage to Asia and Europe in particular. Other geopolitical risks include the possibility that the U.S.-NATO fracture deepens, Russia expands its military efforts in Eastern Europe, or China militarily pursues Taiwan.

From an American political perspective, this has been a time of bold and unconventional economic policies, with the deployment of tariffs a prime example. Possible downside risks include the U.S. Federal Reserve becoming significantly politicized, or a divided post-midterms Congress becoming gridlocked and struggling to pass budgets or increase the debt ceiling.

In the artificial intelligence space, downside risks include the manifestation of large-scale job destruction, evidence of further major sector disruption beyond software, any sign that the pace of CapEx is slowing, evidence that the

Exhibit 32: China has surpassed U.S. in R&D spending

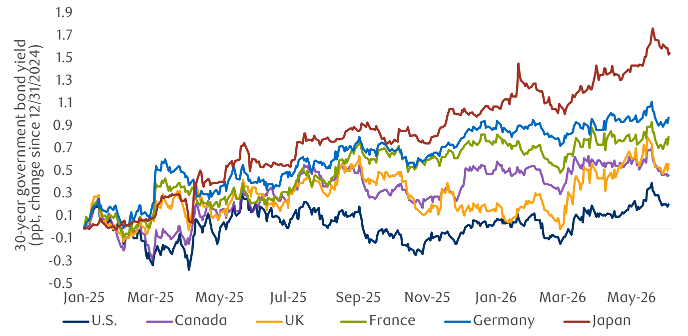


Note: As of 2025 for Canada, 2023 for UK, 2024 for all other countries. R&D expenditure in PPP-based constant prices using 2020 as base year.
Source: OECD, Macrobond, RBC GAM

pace of improvement in the quality of the AI itself is slowing, or signals that investors are beginning to question the valuations or monetization strategies of the key AI players.

Lastly, there are some financial market-related risks. The key among these is that bond yields continue to rise (Exhibit 33) due to some combination of fiscal excesses (Exhibit 34), inflation concerns, political dysfunction, and/or an opaque future as AI shakes the snow globe. More granularly, while private credit concerns have abated somewhat, risks in the space still exist and it is not impossible that these spill over into the banking sector. The yen carry trade is also worth watching given its enormous size as the Japanese central bank defends its currency.

Exhibit 33: Long-term government bond yields have increased



Note: As of June 03, 2026. Source: Macrobond, RBC GAM

Exhibit 34: Fiscal health scorecard

Country	Fiscal Health Index (1 - 5)	Debt (% of GDP)	Deficit (% of GDP)	Fiscal adjustment (ppt)	Interest payments (% of GDP)	GDP growth (%)	Current account (% of GDP)	Foreign-held debt (% share)	Committed spending share (%)	Currency control
U.S.	3.7	124	7.2	2.1	4.0	1.8	-3.6	26	70	Yes
France	3.5	116	5.0	1.6	2.1	1.1	-0.4	43	63	No
Belgium	3.5	106	5.4	2.0	2.3	1.3	-2.1	51	58	No
UK	3.4	102	4.9	1.6	2.8	1.4	-3.1	24	63	Yes
Italy	3.3	137	3.1	-0.6	3.9	0.7	1.2	30	61	No
Brazil	3.3	93	8.6	2.0	8.3	2.5	-3.0	10	66	Yes
Greece	3.1	146	-0.6	-4.8	3.5	1.6	-5.7	n.a.	61	No
South Africa	3.1	79	5.7	1.7	5.3	1.8	-0.5	24	39	Yes
Spain	3.0	100	2.7	-1.0	2.4	1.7	2.9	41	64	No
Japan	2.9	207	1.2	-4.0	1.5	0.6	4.8	12	67	Yes
Canada	2.8	114	1.4	-2.4	3.5	1.8	-0.9	22	63	Yes
Mexico	2.8	62	4.7	1.2	6.5	2.0	-0.4	20	n.a.	Yes
Norway	2.8	45	12.1	11.4	1.1	1.1	14.1	67	61	Yes
India	2.8	84	8.2	-0.2	5.1	6.5	-0.9	5	n.a.	Yes
China	2.7	127	7.5	-0.9	1.0	3.3	3.7	2	44	Yes
Finland	2.6	89	2.7	-0.9	1.6	1.2	1.3	49	64	No
Portugal	2.4	90	0.0	-2.8	2.1	1.6	1.2	45	62	No
Australia	2.4	51	3.7	1.4	1.7	2.3	-2.6	29	57	Yes
Germany	2.4	63	2.1	0.0	1.1	0.6	4.4	40	60	No
Russia	2.2	17	4.9	3.5	1.2	1.0	1.6	4	46	Yes
Turkey	2.0	23	2.8	-2.2	3.0	4.0	-1.9	37	56	Yes
Netherlands	1.9	43	2.1	0.6	0.7	1.2	8.8	36	59	No
Indonesia	1.8	41	2.9	-0.4	2.2	5.2	-0.1	35	32	Yes
South Korea	1.7	52	1.2	-1.3	1.0	1.9	6.6	17	n.a.	Yes
Ireland	1.5	33	-1.0	-2.0	0.6	2.3	8.2	47	62	No
Denmark	1.5	28	-2.3	-3.3	0.8	1.5	12.5	40	64	Yes
Sweden	1.4	35	0.8	-0.7	0.7	1.8	6.1	17	58	Yes

Legend	Extremely poor	Very poor	Poor	Fair	Good

Note: 2025 data for all indicators except interest payments (2024) and GDP growth (IMF forecast for 2031 used as proxy for “normal”). Fiscal adjustment refers to the necessary reduction in fiscal deficit to stabilize debt-to-GDP ratio. Source: IMF, Macrobond, RBC GAM

What about upside risks?

AI could boom even more remarkably than it has so far, creating additional wealth and delivering giant productivity and profit gains. Any such productivity boost could be substantially deflationary, removing inflation concerns and allowing central banks to cut rates – further boosting economic growth.

A global capital expenditure surge could occur, not just for AI-related reasons, but also as countries boost their military spending and resource security.

Related to this, nascent structural reforms in long-slumbering economies like the UK, the Eurozone, Japan and Canada could unleash additional investment and a sustained period of faster economic growth in those markets.

China's economy could accelerate if its housing market actually does stabilize, which would encourage the country's famously high private savings rate to fall and allow its consumer spending growth to become a globally relevant macro force.

Canadian wobbles

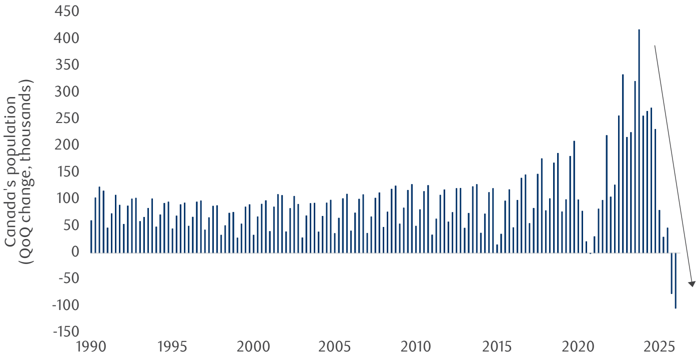
The Canadian economy recorded a disappointing second consecutive quarter of economic contraction in the first quarter of 2026, though this wasn't quite as bad as it looked given the truly minuscule decline, the counterpoint that the industry-based GDP estimate still rose, and the fact that Canada's population is temporarily contracting (Exhibit 35). GDP per capita also rose over the quarter, which means that the average Canadian was not retrenching.

Still, it is certainly fair to concede that the Canadian economy has been underwhelming in recent quarters. The housing market has been a notable source of weakness for several years, and despite significant regional variation, is unlikely to become a national-level economic driver in the year ahead.

Trade policy uncertainty continues to weigh on growth, and while it is hard to gauge the outlook for this with much accuracy, we think a revised USMCA trade deal may not come until 2027 – extending the uncertainty. On the other hand, we believe any deal will likely either cement existing tariffs in place or incrementally reduce them. The risk of a significant deterioration is lower, though there will likely be moments during the negotiation when such outcomes seem probable.

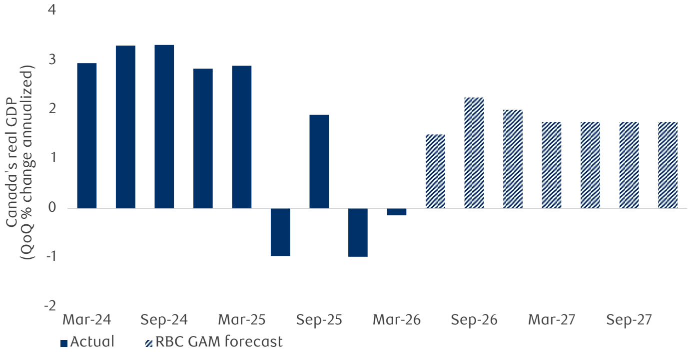
We continue to anticipate some improvement to the Canadian economy over the second half of 2026 and beyond (Exhibit 36). Canada is hurt less than almost any other country by the current energy shock, has stimulative monetary policy in place, and has enjoyed a rollicking stock market. Fiscal policy is also supportive due to a mix of tax cuts and pro-growth regulatory reforms, and the recent shift from a minority to majority government increases the prospective stability of this supportive policy environment. Businesses are not unaware of this support, with capital

Exhibit 35: Canada's population shrinks as federal government cuts immigration



Note: As of January 01, 2026. Source: Statistics Canada, Macrobond, RBC GAM

Exhibit 36: Canadian economy to improve

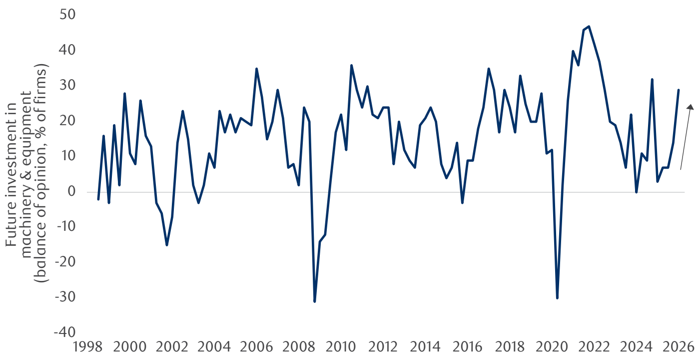


Note: Actual as of Q1 2026, RBC GAM forecast as of June 01, 2026.
Source: Statistics Canada, Macrobond, RBC GAM

expenditure plans recently reviving (Exhibit 37). As with a variety of its peers, the Bank of Canada could eventually raise interest rates incrementally over the year ahead.

In a world that is increasingly prioritizing reliable access to resources, Canada has a distinct advantage as a relatively stable resource superpower (Exhibit 38). This could prove a long-term engine of growth for the country after a lengthy period of actively constraining the sector.

Exhibit 37: Canadian business investment intentions are improving



Note: As of Q1 2026. Source: Bank of Canada Business Outlook Survey, Macrobond, RBC GAM

Exhibit 38: Canadian resource wealth is significant and increasingly valued globally

Canada's global resource ranking

Resource	Production	Reserves
Potash	1	1
Uranium	2	3
Diamonds	3	-
Aluminum	4	-
Crude oil	4	4
Platinum metals	4	5
Gold	4	8
Nickel	4	8
Natural gas	5	10
Wheat	5	-
Lithium	7	6
Cobalt	7	7
Iron ore	8	6
Corn	8	-

Note: As of 2024; crude oil reserves as of 2023. Crude oil production includes crude oil, shale oil, oil sands, condensates and NGLs. Source: Canadian Centre for Energy Information, Natural Resources Canada, Energy Institute Statistical Review of World Energy 2025, FAO, Our World in Data, RBC GAM

Bottom line

In summary, the global economic outlook for the quarters ahead is characterized by two competing forces that will shape outcomes: a temporary but significant energy shock stemming from the Iran conflict, and a potentially transformative artificial intelligence revolution that promises lasting productivity gains. While elevated oil and gas prices have stoked near-term inflation pressures and created short-term headwinds for growth – particularly in Asia and Europe – the anticipated reopening of the Strait of Hormuz should provide relief in the months ahead.

Economies have demonstrated remarkable resilience thus far, supported by accommodative financial conditions, robust fiscal stimulus and surging AI-related capital expenditures. Central banks are pivoting from their multi-year easing cycle toward a more neutral or mildly restrictive stance, reflecting the growth backdrop and inflation concerns. Recession risks remain low, and we expect a rebound in economic momentum through the second half of 2026 as energy pressures fade.

From an investment perspective, our cautiously optimistic stance continues to favour equities, with a renewed tilt toward U.S. markets given their technological leadership, energy independence and robust earnings growth. While valuations are not compelling enough to warrant aggressive positioning, the combination of solid economic fundamentals, accelerating productivity, and the long runway for AI-driven gains supports maintaining modest equity overweights. Fixed income has become somewhat more attractive following the recent backup in yields, prompting a tactical shift from cash.

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