

Executive summary



FALL 2025



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Our base case is for modest economic growth and inflation calm enough to allow for a resumption of interest-rate cuts. In this environment, we expect decent returns from bonds and even better performance from stocks, especially in regions outside North America where valuations are relatively appealing.

Economies prove resilient in the face of tariff headwinds

U.S. public policy remains the dominant macroeconomic theme, with tariffs and tax cuts both attracting close attention. The average U.S. tariff rate has risen over the past quarter, increasing economic headwinds and adding slightly to inflationary pressures. The good news is that the global economy has been resilient in the face of this protectionism, likely reflecting a combination of economic buoyancy and

lags that may only reveal additional damage later. Some areas of the economy have begun to soften modestly, including the labour market. We believe a U.S. recession remains unlikely, and our global growth forecasts are flat to slightly higher than a quarter ago. Recent U.S. tax cuts provide a partial offset to 2025 headwinds and support an economic acceleration in 2026.

Tariff-induced inflation is less concerning than initially feared

Inflation resulting from President Trump's tariffs is becoming visible, most prominently in the cost of core U.S. consumer goods and reflects the fact that most tariffs focus on this subset of products. We anticipate further price increases given that U.S. inflation has risen by only a fraction of the 1.1 percentage point increase that our models indicate is likely, and real-time data is signaling the arrival of additional price pressures.

That said, the net effect of tariffs on inflation may be somewhat smaller than initially expected. The reasons for this surprise include the fact that many manufacturers have so far held off on passing all of the current inflationary pressures to consumers, the disinflationary impact of declining prices for shelter and oil, and the reality that inflation is not affecting most other countries and regions as much as the U.S.

Longer-term U.S.-dollar bear market still intact

The U.S. dollar fell 10% in the first half of 2025, its largest six-month decline since 2009, followed by a rally in July. The greenback resumed its decline after weak jobs data and as concerns mounted about the integrity and independence of U.S. institutions including the Federal Reserve (Fed).

Our longer-term outlook remains firmly bearish on the U.S. dollar and is reinforced by persistent structural negatives.

We believe the greenback is in the beginning stages of a multi-year downtrend, and that the bulk of the decline will materialize within the first three years of the cycle. Investors will need to be quick to call the dollar's peak if they are to capitalize on this move. In our view, the Japanese yen, the euro and emerging-market currencies stand to benefit the most from U.S.-dollar weakness.

U.S. Fed rate cuts set to resume after long pause

The Fed is on the cusp of resuming interest-rate cuts even as inflation remains slightly above target. In late August, Fed Chair Jerome Powell indicated that the U.S. central bank would place greater weight on the weakening labour market than above-target inflation. Slowing job gains and only slightly elevated inflation should allow Powell's Fed to loosen monetary conditions in support of employment and the economy.

Investors agree and are pricing with near-certainty a rate cut of at least 25 basis points at the September 17 meeting of the Fed's rate-setting committee, with further easing to follow in late 2025 and into 2026. As of August, the market was pricing in between 100 and 125 basis points of cuts over the year ahead. These market-based projections align well with our own thinking in that we expect four rate cuts over the next year.

Sovereign bonds offer coupon-like returns and insurance if the economy stumbles

The U.S. 10-year yield at 4.2% is attractive and situated above modelled equilibrium if inflation does not return with force. Most of the recent increase in bond yields has been driven by rising real interest rates as investors worried about heightened debt levels exacerbated by the One Big Beautiful Bill which promises to boost fiscal spending. Our model indicates that the current real yield is about 70 basis points above normal given structural factors such as aging populations, slowing longer-term economic growth and

increased preference for saving versus spending. We can expect 10-year Treasury bonds to deliver returns in the mid single digits over the year ahead, with minimal valuation risk. Fixed income is also appealing across most of the developed world, except for Japan, where inflation pressures are elevated. In addition to offering decent return potential, bonds at today's higher yields provide critical ballast against equity-market volatility in the context of a balanced portfolio.

Equities soared to records but value remains outside of U.S. mega-cap stocks

Global equities have extended their impressive rebound from earlier this year, with most major markets rallying to record levels. While returns were initially led by mega-cap technology stocks amid excitement around artificial intelligence, the rally has ultimately featured broad participation from international stocks. We should also note that U.S.-dollar returns were bolstered by the weakening greenback. U.S. large-cap stocks, Canadian equities and Japanese equities are fully valued, but stocks in Europe, the UK and emerging markets appear to be attractively priced.

Although valuations are elevated in the highly concentrated U.S. large-cap equity market, the ultimate driver of a

sustained advance in stocks is corporate-profit growth, and earnings have been much better than expected. The resilience of U.S. large-cap companies to deliver strong profit growth even in the face of a challenging macroeconomic backdrop has led analysts to raise their forecasts. The consensus estimate is now for healthy 10.5% earnings growth this year, followed by an even faster 13.7% clip in 2026. If profits continue to meet or even exceed analysts' expectations, the rally could have further room to go. That said, we recognize that heightened valuations will likely limit the magnitude of any future gains.

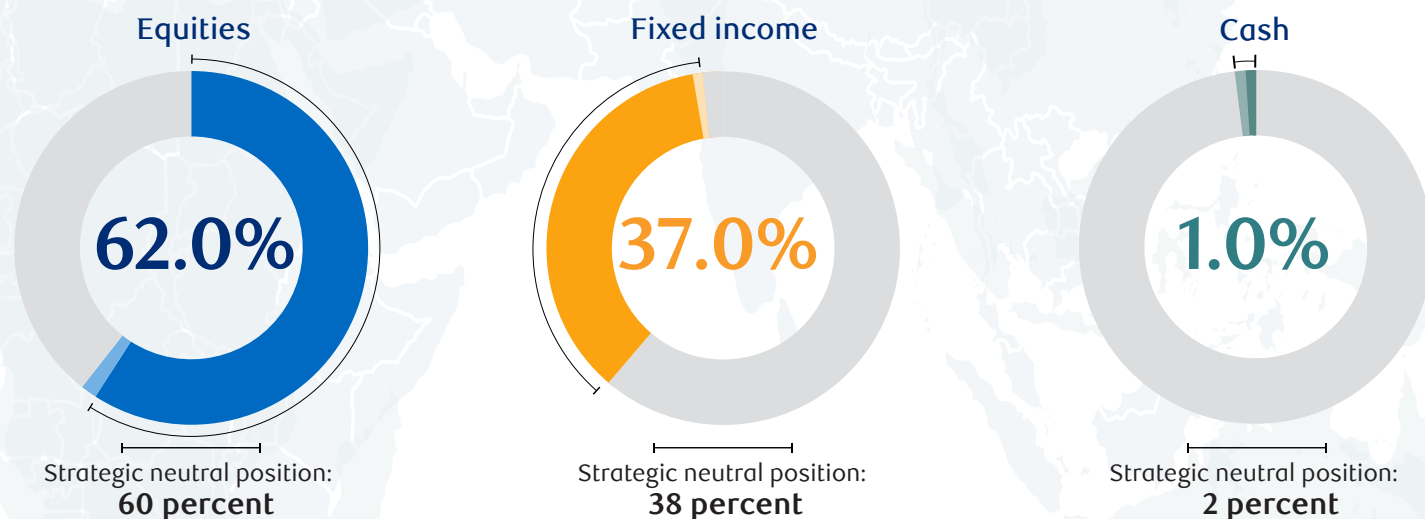
Asset mix – adding to equity allocation, favouring non-U.S. regions

In our base case, the economy continues to grow at a modest pace and inflation remains calm enough to allow the Fed to resume interest-rate cuts soon. We recognize that risks remain with tariffs and trade policy, geopolitical tensions and highly indebted governments. In this environment, we expect bonds to deliver mid single digit returns if inflation doesn't rise drastically. In equities, valuations are more compelling in most of Europe and Asia's developed markets as well as emerging markets,

and these areas therefore offer the potential for superior returns versus North America. As a result, we added one percentage point to our equity allocation, sourced from fixed income, and have directed our equity overweight toward Europe, Asia and emerging markets. For a balanced global investor, our current recommended asset mix is 62.0% equities (strategic "neutral": 60.0%), 37.0% bonds (strategic "neutral": 38.0%) and 1.0% cash.

Recommended asset mix

RBC GAM Investment Strategy Committee



Note: As of September 3, 2025. Source: RBC GAM

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