RBC Global Asset Management

Asset class commentary

SUMMER 2025

Global economy

There remains substantial uncertainty in the global economy and financial markets, particularly regarding the precise contours of trade policy. Tariffs are set to exert a substantial drag on economic growth over the second half of 2025, but probably not to the extent of causing a global recession. Inflation has so far been tame but may become more of a concern in the U.S. as time progresses. Policy decisions such as U.S. tax cuts should be growth positive, but others such as reducing immigration and withholding resources from researchers may have a negative effect. Uncertainty remains considerable but is not quite as high as it was several months ago. U.S. exceptionalism is in retreat, with adverse implications for the dollar, term premiums and beyond. China and the EU have an opportunity to fill some of the void left by the U.S.

Fixed income

Investors are increasingly concerned about the sustainability of government finances and are demanding higher yields for longer lending terms. As a result, term premiums are at decade highs and yield curves are steep, offering incentive for investors to extend duration. The rise in bond yields since the beginning of April reflects a cloudy macroeconomic outlook with growth that is slower but not recessionary, inflation that is lower but not low enough, and central banks that are unlikely to respond with meaningful interest-rate cuts if governments continue running large fiscal deficits. Less sovereign bond demand from central banks and less Treasury demand from foreign investors because of trade wars also pushed yields higher. That said, bond yields have risen to what we consider to be attractive levels and would also offer important portfolio insurance should the economy fall into recession.

Canada

The S&P/TSX Composite Index recorded total returns of 3.9% in the three months ended May 31, 2025 and is now back near all-time highs, boosted by the strength in gold prices. Trade tensions with the U.S., a Canadian federal election and sharp moves in currencies and commodities have dampened domestic business activity and household spending. The current situation is an improvement from the worst-case scenario but consumer and business confidence is unlikely to improve this year unless trade tensions get dialed back.

Canada's economy is expected to expand at a below-trend rate of 1.2% in 2025, down from 1.5% in 2024, and that growth will slow even further to 1.0% in 2026 amid the ongoing trade policy uncertainty. S&P/TSX consensus profit estimates have stayed surprisingly consistent over the past three months, with earnings currently expected to expand 11% in both 2025 and 2026.

United States

U.S. stocks, measured by the S&P 500 Index, were essentially flat during the three months ended May 31, 2025, though the path was highly volatile. Stock prices fell 15% over the three trading days following Trump's "Liberation Day" tariff announcements but then rebounded ferociously when those reciprocal tariffs were delayed a week later.

The effective U.S. import-tariff rate, which was less than 3% a year ago, is about 12% today. Consensus S&P 500 earnings growth for 2025 is roughly 8% but is more likely to be 4% if tariffs persist. The 2026 profit growth estimates exceed 10%, which seems optimistic to us. Technology and interactive media stocks generated about 58% of the market's aggregate earnings, from 60% last year. To keep the bull market going, we need a relatively benign resolution to the trade war, the adoption of AI to continue and the promised increased productivity to materialize.

Europe

The negative impact of tariffs on European equity markets in recent months has masked the positive implications of planned increases in fiscal spending by Germany and, perhaps, France.

Germany's GDP growth is expected to rise to 1.9% in 2026 from the 0.3% forecast for this year, driven by the ambitious fiscal agenda. Overall eurozone growth is predicted to pick up to 1.3% in 2026. Higher government spending will stimulate consumption and investment across the EU.

Consensus expectations are for earnings growth in the Eurozone of 5% to 6% this year, but we now expect flat earnings growth amid uncertainty over the coming months. This lacklustre performance, we note, could be setting the stage for a profit rebound as the year progresses. We are more optimistic about European equity markets over the medium term even though the shorter-term outlook is muddied by the U.S. tariff situation.

Asia Pacific

Asian equities posted moderate gains over the past three months, slightly outperforming global equity markets. Within Asia, India and Hong Kong outperformed, while Taiwan and Thailand underperformed as trade tensions drove differences in relative performance.

Tariffs and weak global demand could slow Asia's exports and capital expenditures in the second half of 2025. Trade-dependent economies such as Thailand, Singapore, Taiwan and South Korea are most vulnerable, while India, Australia and the Philippines, which rely less on exports, are more insulated. Disinflation should continue due to lower oil prices, weak demand and a flood of Chinese exports resulting from the impact of U.S. tariffs. The soft backdrop for growth and inflation suggests that central banks will now be faster to cut interest rates and that the reductions will be deeper than had been forecast. Greater fiscal support in the region is also likely.

Emerging markets

The emerging-market equity benchmark had its biggest one-day decline in at least five years, falling 10%, after Trump introduced reciprocal tariffs. A week later, Trump announced delays to the implementation of those tariffs and emerging-market stocks more than recovered the losses sustained in early April. It appears Trump has begun to refocus the trade war to prioritize isolating China but US-China trade talks are underway.

Emerging markets have outperformed the U.S. so far this year and it is conceivable in our view that this trend continues. With slowing economic growth in the U.S., a weaker U.S. dollar and emerging-market valuations that are still half those in the U.S., there is strong potential for continued outperformance. Moreover, most emerging-market countries, with Mexico an important exception, have relatively low exposure to U.S. tariffs. Emerging-market stocks have historically provided returns of 7% to 13% when valuations are at current levels.

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