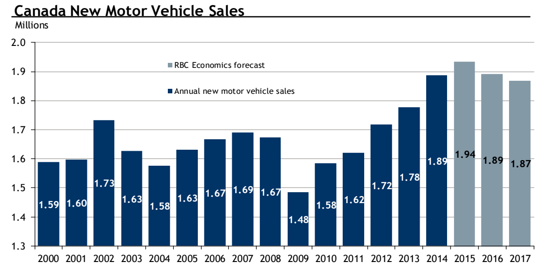
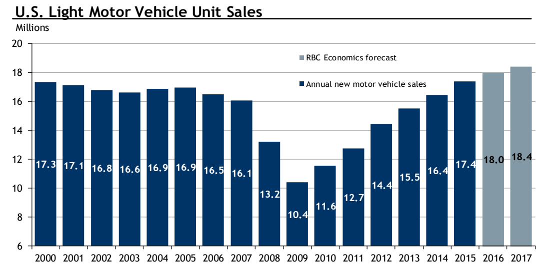
CANADA AND U.S. DECEMBER 2015 AUTO SALES

January 2016



Source: Statistics Canada, RBC Economics Research



Source: Bureau of Economic Analysis, RBC Economics Research

Canada New Motor Vehicle Sales

Canadian auto sales polished off a record sales year with a solid month of sales in December. Sales were down 1.9% from a year ago according to the Global Automakers of Canada (GAC); however, that more reflects the strength of year ago sales than any sign of weakness in the last month of 2015. Our estimates suggest that, on a seasonally adjusted annualized basis, sales of new vehicles (including heavy vehicles) inched up to a 2.01 million unit pace in December from 1.98 million in November and 2.01 and 2.04 million unit readings in October and September, respectively. Annual sales in 2015 totaled an estimated 1.94 million units marking a third consecutive record sales year and up solidly from the 1.89 million units sold in 2014 and 1.78 million in 2013. The strong pace of auto sales last year stands in sharp contrast to weakness in overall GDP growth as a sharp downturn in oil prices weighed heavily on investment in the oil & gas sector. Auto sales have been supported by a combination of resilient labour markets, low interest rates and lower gasoline prices that have provided a boost to household purchasing power. Longer-term interest rates are expected to begin to drift modestly higher going forward and unusually warm weather may also have provided some support to spending in recent months which could result in some 'payback' when temperatures return closer to seasonal normals; however, our base case assumes only a modest slowing in auto sales to a 1.89 million unit pace in 2016.

U.S. Light Vehicle Sales

U.S. light vehicle sales declined to a 17.2 million unit seasonally adjusted annualized rate in December (according to the U.S. Bureau of Economic Analysis) from the 18.1 million unit rate posted in each of the three prior months. Sales still totaled 17.4 million units in 2015 as a whole to match (and, with more decimal places, slightly exceed) an annual sales record previously set in the year 2000. Although we expect interest rates to drift higher, the pace is likely to be gradual and, in terms of household spending, offset by continued improvement in labour markets and consumer confidence. We assume that oil prices will begin to rise in 2016 but remain low which means still low gasoline prices that will continue to free up household incomes for the purchase of other goods and services while remaining pent-up demand left over from the 2008/09 recession will continue to provide some near-terms support to auto sales. Our forecast assumes that auto sales will increase to 18.0 million units on an annual basis in 2016 followed by a further rise to 18.4 million units in 2017.

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RBC Economics Forecasts

Growth outlook	15Q1	15Q2	15Q3	15Q4	16Q1	16Q2	16Q3	16Q4	2014	2015F	2016F	2017F
Canada												
Real GDP growth[1]	-0.7	-0.3	2.3	0.0	2.2	2.4	2.4	2.5	2.5	1.2	1.8	2.6
Unemployment rate[2]	6.7	6.8	7.0	7.1	6.9	6.8	6.7	6.6	6.9	6.9	6.8	6.5
New motor vehicle sales[3]	1.82	1.92	2.00	2.00	1.95	1.88	1.87	1.87	1.89	1.94	1.89	1.87
United States												
Real GDP growth[1]	0.6	3.9	2.0	1.4	2.5	2.9	2.8	2.7	2.4	2.4	2.5	2.7
Unemployment rate[2]	5.6	5.4	5.2	5.0	5.0	4.9	4.9	4.8	6.2	5.3	4.9	4.7
Light vehicle sales[3]	16.7	17.1	17.8	17.8	17.8	17.9	18.1	18.2	16.4	17.4	18.0	18.4
Interest rates												
Canada	*percent, end-of-period*											
Overnight rate	0.75	0.75	0.50	0.50	0.50	0.50	0.50	0.50	1.00	0.50	0.50	1.75
3-month	0.55	0.58	0.43	0.51	0.50	0.55	0.60	0.60	0.91	0.51	0.60	1.80
2-year	0.50	0.48	0.52	0.48	0.55	0.80	1.00	1.10	1.01	0.48	1.10	2.45
5-year	0.77	0.82	0.80	0.73	0.85	1.25	1.50	1.70	1.34	0.73	1.70	2.80
10-year	1.36	1.69	1.43	1.40	1.60	1.90	2.20	2.30	1.79	1.40	2.30	3.15
United States	*percent, end-of-period*											
Fed funds target	0.25	0.25	0.25	0.50	0.75	1.00	1.25	1.50	0.25	0.50	1.50	3.50
3-month	0.04	0.03	0.00	0.17	0.45	0.65	0.70	0.95	0.04	0.17	0.95	3.20
2-year	0.56	0.64	0.64	1.05	1.30	1.50	1.70	2.00	0.67	1.05	2.00	3.80
5-year	1.37	1.64	1.37	1.76	2.05	2.15	2.30	2.55	1.65	1.76	2.55	4.00
10-year	1.93	2.35	2.04	2.27	2.60	2.70	2.85	3.05	2.17	2.27	3.05	4.15
Currency	*end-of-period*											
Canadian dollar (USD/CAD)	1.27	1.25	1.33	1.38	1.45	1.40	1.36	1.33	1.16	1.38	1.33	1.25
Euro (EUR/USD)	1.07	1.11	1.12	1.09	1.03	1.00	1.00	1.02	1.21	1.09	1.02	1.06
U.K. pound sterling (GBP/USD)	1.48	1.57	1.51	1.47	1.51	1.47	1.45	1.48	1.56	1.47	1.48	1.63
Japanese yen (USD/JPY)	120.1	122.5	119.9	120.2	128.0	132.0	130.0	128.0	119.8	120.2	128.0	120.0

1. quarterly numbers are quarter-over-quarter annualized rate, annual is the annual percent change
2. percent
3. millions, annual rate

Sources: Statistics Canada, Global Automakers of Canada, U.S. Bureau of Economic Analysis, RBC Economics Research

Financial Markets Summary:

A renewed downturn in oil prices put additional downward pressure on the Canadian dollar in the latter part of 2015, with the Fed's December rate hike adding fuel to the depreciating trend. In mid-December, the price of oil (West Texas Intermediate or WTI) slipped below $35/barrel for the first time since the financial crisis and has been sitting close to that mark to date in 2016. We continue to expect oil prices to drift modestly higher this year but now assume that the average WTI price will remain below $50/barrel for the first half of 2016. The impact of lower oil prices is expected to keep the Bank of Canada firmly on the sidelines with our forecast assuming that the Canadian overnight rate will hold steady at 0.5% through 2016 while a strengthening U.S. economy (which on net benefits from lower oil prices) contributes to further expected rate hikes by the Fed. The combination of low oil prices and divergent monetary policy is expected to push the Canadian dollar as low as US$0.69 by the end of the first quarter, with only a modest recovery to US$0.71 by mid-year. The depreciating trend is expected to reverse somewhat in the second half of 2016, as oil prices recover and the effect of monetary policy divergence begins to lessen.