ECONOMIC AND FINANCIAL MARKET OUTLOOK

September 2014

U.S. economy slides into driver's seat with Canada going along for the ride

Geopolitical crises have complicated the outlook for the global economy with fighting in the Ukraine and Middle East, the vote on Scottish independence combined with sanctions by and against Russia creating downside risks to the forecast. The reaction to recent events in financial markets saw both equity and bond markets rallying with prices for energy commodities surprisingly little changed. This reaction highlights the dilemma faced by investors who are reaching for yield while at the same time harbour worries about how these geopolitical strains will affect the global economy. To-date, we view these developments as increasing the downside risks to the outlook rather than supporting a large-scale downgrading of our growth forecasts.

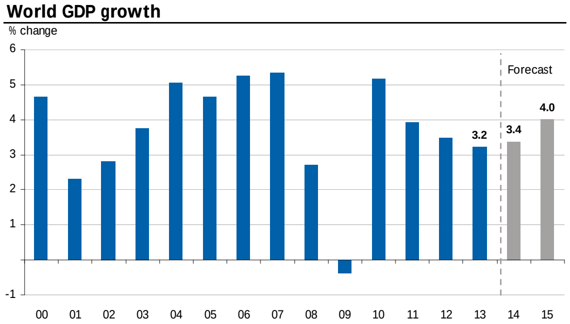
The world economy is likely to grow by 3.4% this year, slightly slower than was projected in June. The 0.2 ppt cut to 2014's growth forecast reflects a very poor start to the year in the US and a weak performance in some of the Emerging Market economies. That said, the sharp rebound in US growth in the second quarter and signs of an improvement in momentum in other developed market economies limited the magnitude of the forecast downgrade and support expectations that growth will accelerate to a 4.0% pace in 2015.

Despite all the volatility, the underpinnings of our view are little changed with interest rates forecast to remain historically low in 2014 and the weight from fiscal restraint continuing to recede. Official policy rates in Canada, the US and UK are expected to be held steady for the remainder of 2014. The European Central Bank reduced its key policy rates in June and September 2014 and implemented policies aimed at facilitating the transmission of the lower rates to the real economy. In 2015, we expect the ECB to continue to apply significant stimulus to the economy. The Bank of Canada, Federal Reserve and Bank of England conversely are expected to be in position to begin the process of removing policy stimulus with official interest rate increases expected in the first half of 2015.

US economy bounced back in second quarter

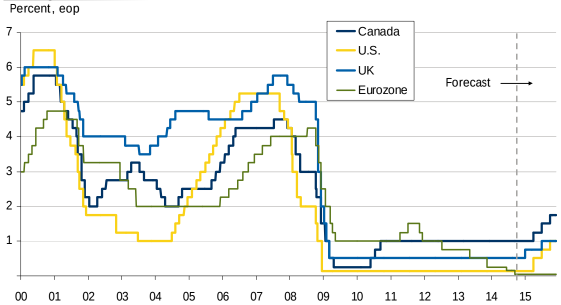
The US economy recorded a sharp 4.2% annualized gain in the second quarter more than reversing the 2.1% drop in the first quarter of 2014. The first quarter's decline reflected the impact of the unseasonably harsh winter that reduced business investment, housing activity and exports. Consumer spending rose in the quarter but the gain was small and insufficient to offset the declines in activity in other parts of the economy. With the return to more seasonal temperatures came a revival in spending by both businesses and consumers. July data indicate that the strong momentum continued early in the third quar-

World GDP growth



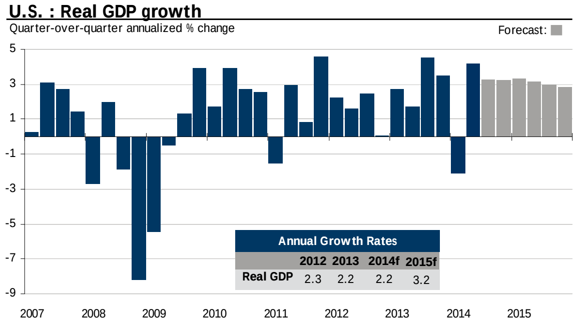
Source: International Monetary Fund, RBC Economics Research

Policy rates : International



Source: Bank of England, European Central Bank, Federal Reserve, Bank of Canada, RBC Economics Research

U.S. : Real GDP growth



Source: Bureau of Economics Analysis, RBC Economics Research

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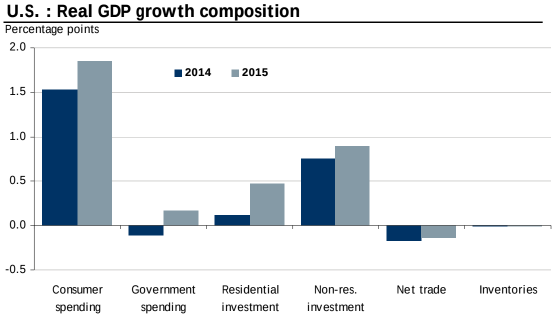
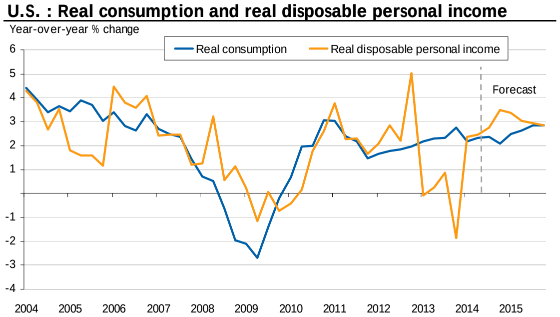
U.S. : Real GDP growth composition



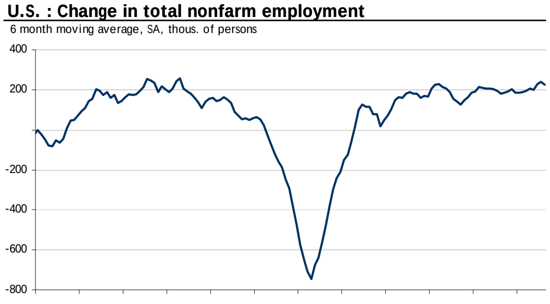
Source: Bureau of Economics Analysis, RBC Economics Research

U.S. : Real consumption and real disposable personal income



Source: Bureau of Economics Analysis, RBC Economics Research

U.S. : Change in total nonfarm employment



Source: Bureau of Labor Statistics, RBC Economics Research

ter, albeit at a slower pace relative to the second quarter with growth projected to increase at a 3.3% pace.

Despite the volatility in the first half of 2014, we are maintaining our view that US growth will be driven by a pickup in consumer spending and a modest increase in business investment. Trade activity is also expected to quicken though import growth is forecast to exceed the rise in export activity resulting in net exports trimming the annual growth rate. Favourable balance sheet conditions and improved confidence underpin our forecast for a strengthening in domestic demand. Housing market activity is also forecast to accelerate however given the slow start to the year, the sector's contribution to the economy's growth rate will be limited in 2014 with a much larger boost forecast for 2015. We expect the US economy to grow by 2.2% in 2014 and 3.2% in 2015.

Consumers got the cash

The health of household balance sheets continued to improve with another \$1.5 trillion earned in the first quarter for a total increase in net worth of \$8.8 trillion in the year to March 2014. Both financial and non-financial assets recorded strong gains with liabilities only inching higher. US households increased the amount of equity in their real estate holdings to 54%, a significant improvement from the low of 36.5% in the first quarter of 2009**.** That said, equity ownership is still less than the historical average of 64%. A pickup in the pace of personal income growth augmented this increase in wealth supporting not only a rise in consumption in the second quarter but a rise in the savings rate as well. Likely this improvement in the health of consumer balance sheets was in part responsible for the easing in lending standards reported by financial institutions in the July Senior Loans Officers Survey.

Easier lending conditions and low interest rates support turn in housing

After two consecutive quarters of tightening lending standards, US banks eased conditions for both mortgages and consumer credit according to the Fed's July survey. The sustained improvement in labour market conditions in 2014 likely played a role in boosting banks' willingness to lend. The average monthly pace of job creation so far this year was 215,000 supporting our forecast that 2014 will produce the strongest job growth in the post-recession period. The August unemployment rate, at 6.1%, is down sharply from the 6.7% recorded in December of last year to stand the closest to the Fed's estimated range of full-employment of 5.2% to 5.8% since before the recession. Looking beyond these two key measures of the labour market health, the Fed's Labour Market Conditions Index showed that as of April almost 80% of the drop in the index during the recession had been recovered although there is still room for further improvement in reducing the duration of unemployment and the number working part-time for economic reasons. The persistence of this slack is likely one of the factors holding back wages which are only increasing in line with the rate of inflation.

The easing in lending standards and declines in long-term mortgage rates augur well for US housing activity to continue to firm. Both existing home sales and housing starts began the third quarter at an elevated level setting up for a stronger second half of 2014 compared to the weather-related weak activity in the first half of the year. Builder sentiment improved and purchasers are facing historically favourable affordability conditions despite the increase in prices.

Business investment to get a boost as demand firms

US business investment slipped in 2013 as uncertainty about the fiscal backdrop and geopolitical events weighed on confidence. In 2014, businesses are expected to ramp up investment to take advantage of banks' improved appetite to lend and in reaction to the decline in commercial vacancy rates. Spending on capital goods will likely grind higher as businesses come up against capacity constraints due to rising demand. Similar to US households, business balance sheets are in good health with asset values at all-time highs and debt accumulation growing at a more modest pace.

The improvement in domestic activity driven by US consumers and businesses will also fuel increased demand for imports aided by an expected strengthening in the US dollar. At the same time, the gradual rise in global activity sets up for a firming in export growth although with the US economy leading the uptick in global growth, imports are likely to post stronger gains resulting in net exports acting as a drag on real GDP this year and next.

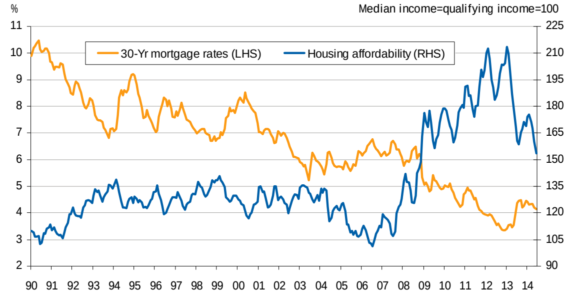
Accelerating growth limits downside to inflation outlook

As discussed, the US economy is operating with some degree of economic slack that has limited the pace of inflation. That said both the headline and core CPI measures started the third quarter close to the Fed's 2% objective. The Fed's preferred measure of inflation, the core PCE deflator, accelerated in the second quarter to average 1.5%, 20 bps higher than the average pace over the prior four quarters. While the persistence of spare capacity will likely curtail the speed of inflation in the near term, the quickening momentum in the pace of economic growth and stable inflation expectations will limit the downside to the inflation outlook.

Monetary policy – slow grind to unwind stimulus

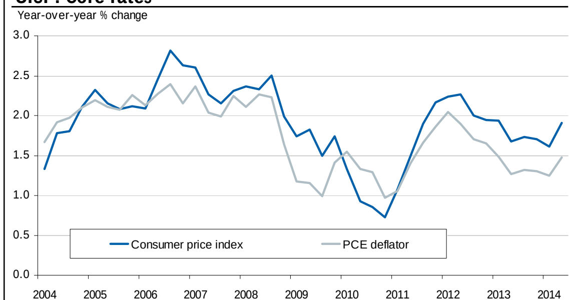
The Fed's decision to reduce the size of the quantitative easing program in recent months has had very limited effect on longer-term interest rates which slipped to the year's low in late-August. The unwavering bid for these securities reflected a revival in risk aversion due to the rise in geopolitical risks. At the same time, Chinese purchases of US Treasuries accelerated sharply with China accumulating bonds at a record clip during the first six months of 2014. We expect the Fed will conclude the quantitative easing program at the October meeting completing the first step toward policy normalization. Tightening action via higher interest rates will likely follow late in the second quarter of 2015 at which time both the unemployment rate and the core PCE measure of inflation will be closer to the Fed's mandated objectives. The most likely course is for the Fed to remove stimulus slowly with 25 basis point increases expected to be announced at every second meeting in the second half of 2015 meaning the funds target will be 1.0% by the end of next year. Even with these increases, there will still be sufficient monetary policy stimulus being applied to the economy to ensure growth continues at an above-potential pace and excess capacity is mopped up.

U.S. : Mortage rates & housing affordability index



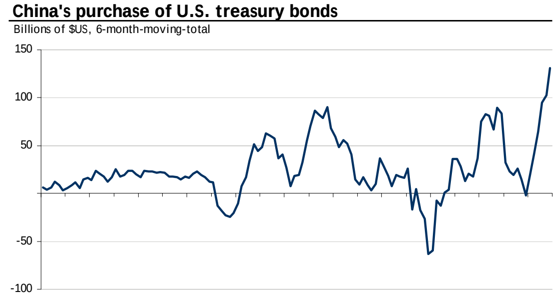
Source: National Association of Realtors, Federal Reserve, RBC Economics Research

U.S. : Core rates



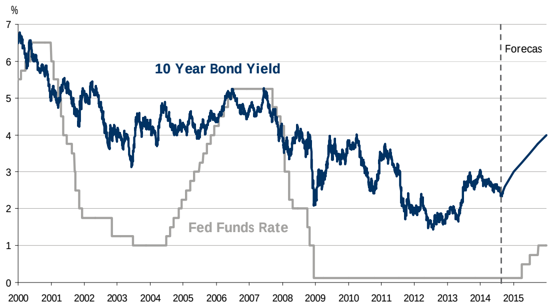
Source: Bureau of Labor Statistics, Federal Reserve Bank of San Francisco, RBC Economics Research

China's purchase of U.S. treasury bonds



Source: U.S. Treasury, RBC Economics Research

U.S. : Interest rates



Source: Federal Reserve Board, U.S. Treasury, RBC Economics Research

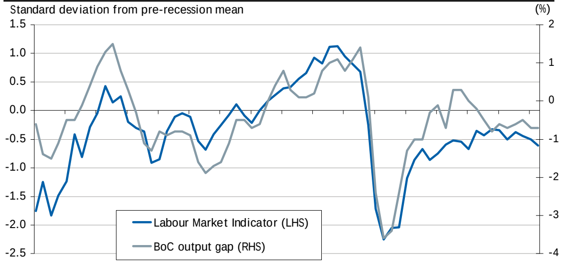
Canada : Final Domestic Demand

Quarter-over-quarter annualized % change

Source: Statistics Canada, RBC Economics Research

Canada : Labour Market Indicator

Standard deviation from pre-recession mean



Labour Market Indicator is made up of 7 indicators including discouraged workers, labour shortages, part-time for economic reasons, unemployment duration.
Source: Statistics Canada, RBC Economics Research

Interest rate increases to follow

Against this backdrop, we expect US Treasury bond yields will break out of the post-recession range with the 10-year yield expected to breach April 2010's high of 3.85% in the second half of 2015. Shorter-term yields will come under greater upward pressure with the 2-year US government bond yield projected to rise 190 basis points by the end of 2015 resulting in a flattening in the US yield curve. The more aggressive increase in short-term interest rates combined with the acceleration in the pace of US growth will underpin a strengthening in the US dollar which we expect to outperform against the Euro, yen, sterling and the Canadian dollar over the forecast horizon.

Canada's economy emerged from Q1's soft patch

Domestic demand contracted, albeit minimally, in early 2014 for the first time since the recession weighed down by falling business investment, declining housing market activity and very soft consumer spending – all of which were hurt by unseasonably harsh winter weather. The trade sector also weakened however with the drop in imports being larger than the dip in exports, net trade still managed to prop up real GDP in the quarter resulting in an overall increase in GDP of 0.9%. Similar to the US, Canada's economy managed to recover in the second quarter with GDP expanding at a 3.1% pace as more seasonal weather temperatures fuelled a rebound in consumer and business activity. More importantly, Canada's export sector saw a very sharp increase in demand that added 1.7 percentage points to Q2's real GDP growth rate even after accounting for a jump in imports.

July and August data signal that the economy continued along its firmer growth path early in the third quarter. Housing starts and sales, auto sales and the RBC/Markit manufacturing index remained elevated teeing up for another quarter of above-potential real GDP growth.

Labour market volatility obscures trend

The month-to-month volatility in the Canadian employment data yielded a very weak trend in job gains in the first half of the year. To start the third quarter, July's unexpected largely 42,000 job increase combined with August's 11,000 dip boosted the average monthly gain to 10,400 however this is still running slower than what would be consistent with the economy entering a period of above-potential growth. Also, worrying was the skew to part-time (6,000 per month) job gains over full-time (4,400 per month) over the period. This resulted in the proportion of full-time employed falling 0.2 ppt to 80.7% so far in 2014.

A broader measure of labour market conditions shows excess capacity existed in the first half of 2014 mirroring the persistent output gap as the economy failed to grow at an above-potential pace on a sustained basis. This also helps to explain the slow pace of wage growth. With the economy entering a period of above-potential growth in the second quarter, we expect both a narrowing in the output gap and tightening in labour market conditions. In turn, this tightening will result in a recovery in full-time employment and eventually exert upward pressure on wages. The unemployment rate, which has been significantly less volatile, remains in a range between 6.9% and 7.2% and is expected to breach the downside of this range to end 2015 at 6.5%.

As the world economy turns more quickly….

The long-awaited pick up in demand for Canada's exports potentially got underway in the second quarter of 2014. Following a period where gains were concentrated in energy exports, both non-natural resource goods and non-energy commodities posted sharp increases. Both of these sectors suffered larger declines during the recession and have taken much longer to recover than the energy sector where exports are 26% higher than at the pre-recession peak.

…so too will Canadian exports

In the second quarter, exports of industrial machinery, chemicals, electronic machinery and aircraft posted strong gains. Further, after a period of weakening, exports of autos and parts recorded a double-digit rise in the second quarter and continued to rise in July. We expect that exports, outside of energy, will maintain this improved momentum with sales of non-commodity products rising alongside a strengthening in US investment in equipment and software. The rotation toward external demand opens the door to the economy growing at an above-potential pace despite expectations that the high level of debt will limit growth in consumer spending while affordability strains slow housing market activity. On the upside, strengthening external demand is likely to incent Canadian businesses to increase the pace of investment as capacity limits are reached.

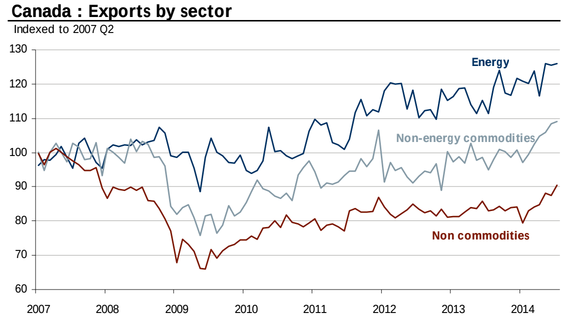
Canadian consumers to provide steady, if unspectacular, support

The Canadian consumer shook off the winter blues in the second quarter with spending rising at a 3.8% annualized pace, more than compensating for Q1's weather-related slowing. Looking forward, we expect consumption to grow at a trend rate of 2.3% with the support from a record level of net wealth tempered by the elevated level of household indebtedness. As discussed, labour market conditions weakened recently resulting in wage growth barely keeping up with the rate of inflation. We expect labour market conditions will improve resulting in a pickup in wages and incomes thereby limiting the slowing in consumption activity ahead. Further, interest rate increases are expected to be gradual and occur as income growth accelerates. This will allow consumers to absorb the increase in debt service costs without pulling back sharply on durable goods or services expenditures.

Can't keep the housing market down

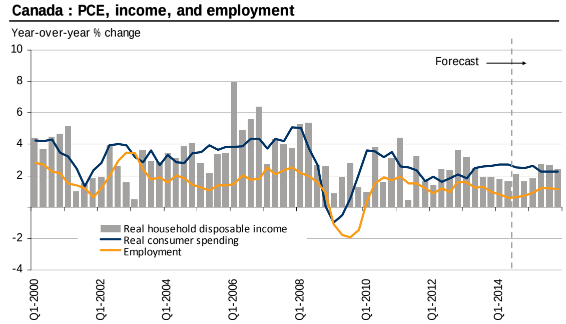
One area of the economy that has proven surprisingly resilient has been the housing market with sales not only fully recovering the winter-related dip but proceeding higher over the summer months. In part, the stronger performance was due to the lowering of mortgage rates in the late spring that tempered the deterioration in affordability. We expect home sales activity to gradually soften as affordability is increasingly strained. Our expectation that the strengthening in economic activity will lead the Bank of Canada to raise the policy rate in 2015 will add to pressures coming from the steady rise in prices.

Canada : Exports by sector



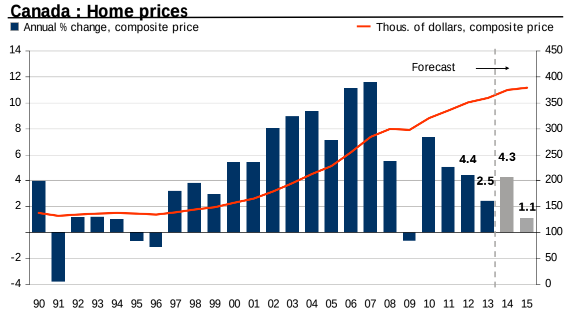
Source: Statistics Canada, RBC Economics Research

Canada : PCE, income, and employment



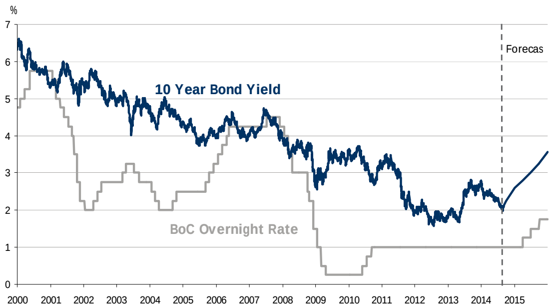
Source: Statistics Canada, RBC Economics Research

Canada : Home prices



Source: Royal LePage, RBC Economics Research

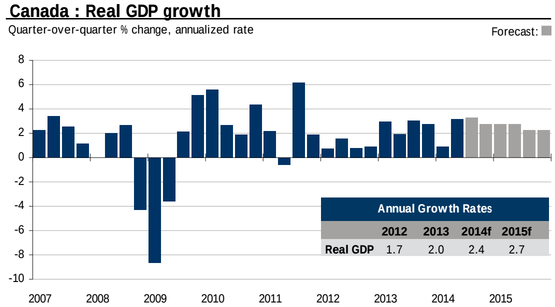
Canada : Interest rates



Source: Bank of Canada, RBC Economics Research Forecasts

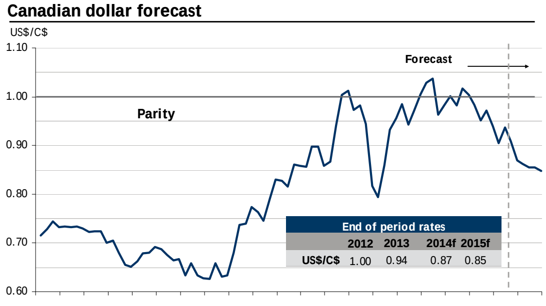
Canada : Real GDP growth

Quarter-over-quarter % change, annualized rate



Source: Statistics Canada, RBC Economics Research

Canadian dollar forecast



Source: Bank of Canada, RBC Economics Research Forecasts

Backed by the recent strength in sales activity, 2014 is likely to see re-sales increase by 2.1% with prices posting a hefty 4.3% gain. However as pressures on affordability intensify in 2015, sales are likely to ease with price gains slowing to 1.1%. That said supports for housing will remain in place including demand from immigration that will result in activity cooling though not collapsing.

Stronger growth to prompt Bank of Canada to change policy bias

The Bank of Canada maintained their neutral policy bias in early September although acknowledged that both exports and housing activity were strong in the second quarter. The run of stronger-than-expected increases in Canada's headline and core inflation rates that pushed them closer to the 2% target continued to dampen concern that the inflation rate would gravitate back to the lower bound of the 1% to 3% target band. That said, the Bank still expects the inflation rates to ease due to one-off factors.

Our forecast for real GDP growth in 2014 is higher than the Bank's 2.2% at 2.4% and we expect the economy to expand more aggressively at a 2.7% pace in 2015, above the Bank's 2.4% projection. Our forecast highlights a broadening out in the drivers of growth resulting in a strengthening in the economy's momentum that supports job creation and keeps inflation at the 2% target. The recovery in second quarter export growth indicates that this process is underway. However until there is evidence that the rotation in the drivers of demand is sustainable, the central bank is likely to maintain its policy stance with the overnight rate at 1.0% and the neutral bias intact. Our assessment that demand for exports will accelerate supporting a period of above-potential growth will likely induce the Bank to shift policy slightly and we expect policymakers to reestablish a tightening bias before year-end. We still see the Bank as likely to hold the overnight rate at 1.0% in 2014 with the first rate hike most likely to be announced in the second quarter of 2015.

Canadian dollar weakness a by-product of US dollar appreciation

After three months of steady appreciation, the Canadian dollar reversed course in August. The loonie's decline was more a function of US dollar strength than any made-in-Canada factor. That said, at the margin, Canada/US short-term interest rate spreads narrowed, commodity prices eased and foreign net purchases of Canadian securities continued to grow at a pace that was much slower than the rapid gains of 2011-2012. The prospect of a further appreciation in the US dollar reflecting a strengthening in economic growth and prospective Federal Reserve interest rate hikes will translate into another round of Canadian dollar weakening with the currency forecast to end 2014 at 0.87 US cents and 2015 at 0.85 US cents.

Economic forecast detail — Canada

Real growth in the economy

Quarter-over-quarter annualized % change unless otherwise indicated

	Actual						Forecast						Actual		Forecast	
	2013				2014				2015				year-over-year % change			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2012	2013	2014	2015
Household Consumption	1.4	3.8	3.0	2.4	1.7	3.8	2.2	2.3	2.3	2.2	2.2	2.2	1.9	2.4	2.6	2.3
Durables	2.2	14.0	0.3	-3.7	1.6	14.7	5.4	-2.0	1.4	2.6	2.5	2.5	2.6	3.4	3.7	2.4
Semi-Durables	1.8	1.8	11.0	6.5	-5.6	9.9	2.8	3.0	2.5	2.6	2.5	2.5	2.1	3.3	3.5	3.1
Non-durables	-0.3	2.1	4.9	5.5	4.4	-0.6	1.5	3.5	2.5	2.3	2.3	2.3	0.7	2.4	3.1	2.3
Services	1.9	2.7	1.9	1.9	1.4	2.8	1.8	2.6	2.3	2.1	2.1	2.1	2.2	2.1	2.0	2.2
NPISH consumption	3.7	-1.8	0.1	0.4	1.8	-1.1	2.2	2.3	2.3	2.2	2.2	2.2	1.2	2.2	0.6	2.0
Government expenditures	0.1	1.0	-0.4	0.3	-0.2	1.4	0.4	0.4	0.8	0.8	1.0	1.0	1.1	0.6	0.4	0.7
Government fixed investment	-2.4	-6.1	-0.6	-8.8	-3.6	-0.1	0.6	1.0	1.2	1.2	1.5	1.5	0.5	-1.0	-3.0	1.1
Residential investment	-4.5	6.1	0.4	-1.7	-5.6	11.9	2.0	-2.4	-1.2	-1.0	-0.7	-0.8	6.1	-0.3	0.9	-0.1
Non-residential investment	0.9	-1.2	0.5	-0.8	-3.0	0.9	6.9	5.5	4.6	5.0	4.7	4.3	6.2	1.3	0.4	4.9
Non-residential structures	2.5	-1.0	3.1	-2.4	-0.7	0.6	6.9	5.8	4.5	5.1	4.8	4.4	6.9	2.2	1.0	4.9
Machinery & equipment	-1.6	-1.6	-3.4	1.7	-6.6	1.5	7.0	4.9	4.7	4.9	4.4	4.2	5.2	-0.2	-0.5	4.8
Intellectual property	-4.9	-12.8	10.5	0.5	-11.2	-10.8	5.2	5.4	4.6	5.0	4.6	4.3	-1.5	-3.2	-3.6	3.8
Final domestic demand	0.4	2.0	1.8	0.8	-0.2	3.0	2.3	1.9	2.0	2.0	2.0	2.0	2.3	1.4	1.4	2.1
Exports	5.4	4.9	0.7	3.9	-0.7	17.8	10.0	4.8	7.7	6.8	6.0	6.1	1.5	2.2	5.7	7.5
Imports	2.7	2.4	-0.7	1.5	-5.5	11.1	3.5	6.2	5.4	4.1	4.1	4.9	3.1	1.1	1.7	5.2
Inventories (change in $b)	11.8	7.7	11.5	16.8	14.5	7.1	2.3	8.0	8.2	7.7	5.9	5.4	6.8	11.9	8.0	6.8
Real gross domestic product	**3.0**	**1.9**	**3.0**	**2.7**	**0.9**	**3.1**	**3.3**	**2.7**	**2.7**	**2.7**	**2.2**	**2.2**	**1.7**	**2.0**	**2.4**	**2.7**

Other indicators

Year-over-year % change unless otherwise indicated

	2013 Q1	2013 Q2	2013 Q3	2013 Q4	2014 Q1	2014 Q2	2014 Q3	2014 Q4	2015 Q1	2015 Q2	2015 Q3	2015 Q4	2012	2013	2014	2015
Business and labour																
Productivity	-0.2	0.9	1.5	2.1	1.8	2.7	2.3	1.7	2.0	0.9	1.2	1.3	0.0	1.1	2.1	1.3
Pre-tax corporate profits	-8.2	-4.3	2.4	4.3	7.0	12.1	7.1	8.1	3.2	2.9	3.5	3.6	-4.9	-1.7	8.5	3.3
Unemployment rate (%)*	7.1	7.1	7.1	7.0	7.0	7.0	7.0	6.8	6.7	6.6	6.5	6.5	7.2	7.1	6.9	6.6
Inflation																
Headline CPI	0.9	0.8	1.1	0.9	1.4	2.2	2.1	2.2	1.8	1.4	1.5	2.0	1.5	0.9	2.0	1.7
Core CPI	1.3	1.2	1.3	1.2	1.3	1.7	1.8	1.9	1.9	1.9	2.0	2.0	1.7	1.3	1.7	2.0
External trade																
Current account balance ($b)	-60.3	-61.5	-56.8	-62.6	-48.1	-47.5	-43.4	-44.0	-43.0	-41.9	-41.0	-40.4	-62.2	-60.3	-45.7	-41.6
% of GDP	-3.2	-3.3	-3.0	-3.3	-2.5	-2.4	-2.2	-2.2	-2.1	-2.1	-2.0	-1.9	-3.4	-3.2	-2.3	-2.0
Housing starts (000s)*	172	190	194	194	175	196	194	186	180	179	175	173	215	188	188	177
Motor vehicle sales (mill., saar)*	1.72	1.78	1.80	1.79	1.73	1.85	1.92	1.84	1.81	1.82	1.83	1.83	1.72	1.77	1.83	1.82

*Period average

Source: Statistics Canada, RBC Economics Research forecasts

Economic forecast detail — United States

Real growth in the economy

Quarter-over-quarter annualized % change unless otherwise indicated

	Actual						Forecast						Actual		Forecast	
	2013				2014				2015				year-over-year % change			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2012	2013	2014	2015
Consumer spending	3.6	1.8	2.0	3.7	1.2	2.5	2.0	2.7	2.9	3.0	2.9	2.7	1.8	2.4	2.2	2.7
Durables	8.4	4.5	4.9	5.7	3.2	14.3	4.5	5.7	6.3	6.5	6.4	6.1	7.3	6.7	6.3	6.5
Non-durables	4.8	-0.2	2.8	2.7	0.0	1.9	3.4	2.5	2.8	3.1	2.8	2.5	0.7	1.9	1.8	2.8
Services	2.4	2.0	1.3	3.7	1.3	0.8	1.2	2.2	2.3	2.4	2.3	2.2	1.3	1.9	1.7	2.1
Government spending	-3.9	0.2	0.2	-3.8	-0.8	1.4	0.4	0.4	1.0	1.0	1.3	1.5	-1.4	-2.0	-0.6	0.9
Residential investment	7.8	19.0	11.2	-8.5	-5.3	7.2	17.6	16.5	17.0	13.6	12.3	10.5	13.5	11.9	3.8	14.7
Non-residential investment	1.5	1.6	5.5	10.4	1.6	8.4	7.6	8.6	8.4	8.4	7.9	7.9	7.2	3.0	6.2	8.2
Non-residential structures	-11.5	7.3	11.1	12.8	2.9	9.5	5.8	7.0	6.5	6.5	6.0	6.8	13.1	-0.5	7.8	6.6
Equipment & software	4.8	1.5	4.7	14.1	-1.0	10.7	8.5	9.5	9.4	9.3	8.8	8.4	6.8	4.6	6.6	9.2
Intellectual property	6.4	-1.9	2.8	3.6	4.7	4.5	4.6	4.6	4.0	4.0	4.1	4.3	3.9	3.4	3.8	4.2
Final domestic demand	2.0	1.9	2.3	2.7	0.7	3.1	2.8	3.3	3.5	3.5	3.3	3.2	2.1	1.9	2.2	3.3
Exports	-0.8	6.3	5.1	10.0	-9.2	10.1	9.5	5.5	6.5	7.4	7.4	7.2	3.3	3.0	3.7	7.2
Imports	-0.2	8.5	0.6	1.3	2.2	11.0	2.0	5.9	6.8	7.9	7.9	7.5	2.3	1.1	4.0	6.7
Inventories (change in $b)	33.4	43.4	95.6	81.8	35.2	83.9	62.5	68.5	68.5	65.0	60.0	53.4	57.1	63.6	62.5	61.7
Real gross domestic product	**2.7**	**1.8**	**4.5**	**3.5**	**-2.1**	**4.2**	**3.3**	**3.3**	**3.3**	**3.1**	**3.0**	**2.9**	**2.3**	**2.2**	**2.2**	**3.2**

Other indicators

Year-over-year % change unless otherwise indicated

	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2012	2013	2014	2015
Business and labour																
Productivity	0.8	0.5	1.1	2.4	0.5	0.9	0.6	0.2	2.0	1.8	1.6	1.6	0.9	1.2	0.6	1.8
Pre-tax corporate profits	3.1	3.9	4.9	4.7	-4.8	-0.3	-0.6	0.4	12.2	5.2	4.8	4.7	11.4	4.2	-1.3	6.6
Unemployment rate (%)*	7.7	7.5	7.2	7.0	6.7	6.2	6.1	6.0	6.0	5.9	5.8	5.7	8.1	7.4	6.3	5.9
Inflation																
Headline CPI	1.7	1.4	1.6	1.2	1.4	2.1	2.0	2.1	2.1	1.9	1.8	2.0	2.1	1.5	1.9	1.9
Core CPI	1.9	1.7	1.7	1.7	1.6	1.9	1.9	2.0	2.0	1.9	1.9	2.0	2.1	1.8	1.9	1.9
External trade																
Current account balance ($b)	-422	-425	-405	-349	-445	-459	-425	-426	-437	-449	-462	-472	-461	-400	-439	-455
% of GDP	-2.6	-2.6	-2.4	-2.0	-2.6	-2.7	-2.4	-2.4	-2.4	-2.5	-2.5	-2.5	-2.9	-2.4	-2.5	-2.5
Housing starts (000s)*	947	865	882	1025	925	997	1050	1161	1256	1340	1413	1473	784	930	1033	1370
Motor vehicle sales (millions, saar)*	15.3	15.5	15.6	15.6	15.7	16.5	16.6	16.4	16.4	16.6	16.7	16.9	14.4	15.5	16.3	16.6

*Period average

Source: Bureau of Economic Analysis, RBC Economics Research forecasts

Financial market forecast detail

Interest rates—North America

%, end of period

	Actual						Forecast						Actual		Forecast	
	13Q1	13Q2	13Q3	13Q4	14Q1	14Q2	14Q3	14Q4	15Q1	15Q2	15Q3	15Q4	2012	2013	2014	2015
Canada																
Overnight	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.25	1.50	1.75	1.00	1.00	1.00	1.75
Three-month	0.98	1.02	0.98	0.91	0.90	0.94	1.10	1.10	1.10	1.35	1.60	1.85	1.05	0.91	1.10	1.85
Two-year	1.00	1.22	1.19	1.13	1.07	1.10	1.15	1.40	1.75	2.00	2.30	2.50	1.05	1.13	1.40	2.50
Five-year	1.30	1.80	1.86	1.95	1.71	1.53	1.70	2.15	2.35	2.50	2.75	3.00	1.30	1.95	2.15	3.00
10-year	1.88	2.44	2.55	2.77	2.46	2.24	2.25	2.60	2.80	3.00	3.25	3.55	1.75	2.77	2.60	3.55
30-year	2.50	2.90	3.07	3.24	2.96	2.78	2.80	3.10	3.25	3.40	3.60	3.85	2.40	3.24	3.10	3.85
Yield curve (10s-2s)	88	122	136	164	139	114	110	120	105	100	95	105	70	164	120	105
United States																
Fed funds	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.50	0.75	1.00	0.25	0.25	0.25	1.00
Three-month	0.07	0.04	0.02	0.07	0.05	0.04	0.05	0.05	0.25	0.65	0.90	1.30	0.09	0.07	0.05	1.30
Two-year	0.25	0.36	0.33	0.38	0.45	0.47	0.60	0.95	1.45	1.75	2.20	2.50	0.25	0.38	0.95	2.50
Five-year	0.77	1.41	1.39	1.75	1.74	1.62	1.85	2.30	2.65	2.90	3.20	3.45	0.70	1.75	2.30	3.45
10-year	1.87	2.52	2.64	3.04	2.73	2.53	2.60	3.00	3.25	3.50	3.75	4.00	1.70	3.04	3.00	4.00
30-year	3.10	3.52	3.69	3.96	3.55	3.34	3.35	3.80	3.95	4.15	4.35	4.55	2.90	3.96	3.80	4.55
Yield curve (10s-2s)	162	216	231	266	228	206	200	205	180	175	155	150	145	266	205	150
Yield spreads																
Three-month T-bills	0.91	0.98	0.96	0.84	0.85	0.90	1.05	1.05	0.85	0.70	0.70	0.55	0.96	0.84	1.05	0.55
Two-year	0.75	0.86	0.86	0.75	0.62	0.63	0.55	0.45	0.30	0.25	0.10	0.00	0.80	0.75	0.45	0.00
Five-year	0.53	0.39	0.47	0.20	-0.03	-0.09	-0.15	-0.15	-0.30	-0.40	-0.45	-0.45	0.60	0.20	-0.15	-0.45
10-year	0.01	-0.08	-0.09	-0.27	-0.27	-0.29	-0.35	-0.40	-0.45	-0.50	-0.50	-0.45	0.05	-0.27	-0.40	-0.45
30-year	-0.60	-0.62	-0.62	-0.72	-0.59	-0.56	-0.55	-0.70	-0.70	-0.75	-0.75	-0.70	-0.50	-0.72	-0.70	-0.70

Interest rates—International

%, end of period

	Actual						Forecast						Actual		Forecast	
	13Q1	13Q2	13Q3	13Q4	14Q1	14Q2	14Q3	14Q4	15Q1	15Q2	15Q3	15Q4	2012	2013	2014	2015
United Kingdom																
Repo	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.75	0.75	1.00	1.00	0.50	0.50	0.50	1.00
Two-year	0.21	0.41	0.30	0.57	0.71	0.87	0.90	1.20	1.60	1.90	2.20	2.40	0.20	0.57	1.20	2.40
10-year	1.78	2.46	2.50	3.04	2.73	2.68	2.65	3.10	3.40	3.60	3.80	4.10	1.70	3.04	3.10	4.10
Euro Area																
Refinancing rate	0.75	0.50	0.50	0.25	0.25	0.15	0.05	0.05	0.05	0.05	0.05	0.05	0.75	0.25	0.05	0.05
Two-year	-0.02	0.20	0.15	0.24	0.17	0.03	0.00	0.00	0.10	0.10	0.10	0.10	0.00	0.24	0.00	0.10
10-year	1.29	1.73	1.70	2.11	1.57	1.25	1.10	1.30	1.50	1.75	2.00	2.25	1.50	2.11	1.30	2.25
Australia																
Cash target rate	3.00	2.75	2.50	2.50	2.50	2.50	2.50	2.50	2.50	2.50	2.50	2.75	3.00	2.50	2.50	2.75
Two-year swap	2.83	2.58	2.45	2.68	2.78	2.80	2.70	2.85	3.00	3.25	3.50	3.75	2.75	2.68	2.85	3.75
10-year swap	3.42	3.76	3.81	4.23	4.08	4.00	3.60	3.90	4.05	4.30	4.55	4.80	3.00	4.23	3.90	4.80
New Zealand																
Cash target rate	2.50	2.50	2.50	2.50	2.75	3.25	3.50	3.50	3.75	4.00	4.00	4.00	2.50	2.50	3.50	4.00
Two-year	2.85	2.85	3.42	3.81	4.01	3.90	4.20	4.30	4.50	4.60	4.60	4.70	2.60	3.81	4.30	4.70
10-year	3.96	4.16	4.86	5.23	4.62	5.00	5.20	5.40	5.70	5.90	6.00	6.20	3.80	5.23	5.40	6.20

Growth outlook
% change, quarter-over-quarter in real GDP

	13Q1	13Q2	13Q3	13Q4	14Q1	14Q2	14Q3	14Q4	15Q1	15Q2	15Q3	15Q4	2012A	2013A	2014F	2015F
Canada*	3.0	1.9	3.0	2.7	0.9	3.1	3.3	2.7	2.7	2.7	2.2	2.2	1.7	2.0	2.4	2.7
United States*	1.1	2.5	4.1	2.6	-2.1	4.2	3.3	3.3	3.3	3.1	3.0	2.9	2.3	2.2	2.2	3.2
United Kingdom	0.4	0.7	0.8	0.7	0.8	0.8	0.7	0.6	0.6	0.6	0.6	0.6	0.2	1.9	3.0	2.7
Euro Area	-0.2	0.3	0.1	0.3	0.2	0.0	0.3	0.3	0.3	0.3	0.3	0.3	-0.6	-0.4	0.8	1.1
Australia	0.5	0.8	0.6	0.8	1.1	0.5	0.5	0.6	0.9	0.9	0.9	0.9	3.6	2.4	3.2	3.1
New Zealand	0.5	0.1	1.0	0.7	1.3	0.6	0.6	0.6	0.6	0.6	0.6	0.6	2.8	2.4	3.0	2.4

*Seasonally adjusted annualized rates

Inflation outlook
% change, year-over-year

	13Q1	13Q2	13Q3	13Q4	14Q1	14Q2	14Q3	14Q4	15Q1	15Q2	15Q3	15Q4	2012A	2013A	2014F	2015F
Canada	0.9	0.8	1.1	0.9	1.4	2.2	2.1	2.2	1.8	1.4	1.5	2.0	1.5	0.9	2.0	1.7
United States	1.7	1.4	1.6	1.2	1.4	2.1	2.0	2.1	2.1	1.9	1.8	2.0	2.1	1.5	1.9	1.9
United Kingdom	2.8	2.7	2.7	2.0	1.8	1.6	1.6	1.7	1.5	1.7	1.7	1.5	2.8	2.6	1.7	1.6
Eurozone	1.8	1.4	1.3	0.8	0.7	0.6	0.3	0.5	0.6	0.7	0.8	0.8	2.5	1.3	0.5	0.8
Australia	2.5	2.4	2.2	2.6	2.9	3.0	2.2	2.1	2.2	2.4	2.7	2.8	1.8	2.4	2.5	2.8
New Zealand	0.9	0.7	1.4	1.6	1.5	1.6	1.8	2.0	2.2	2.3	2.3	2.4	1.1	1.1	1.7	2.3

Exchange rates
%, end of period

	Actual						Forecast						Actual		Forecast	
	13Q1	**13Q2**	**13Q3**	**13Q4**	**14Q1**	**14Q2**	**14Q3**	**14Q4**	**15Q1**	**15Q2**	**15Q3**	**15Q4**	**2012**	**2013**	**2014**	**2015**
AUD/USD	1.04	0.91	0.93	0.89	0.93	0.94	0.94	0.95	0.93	0.92	0.91	0.90	1.04	0.89	0.95	0.90
USD/CAD	1.02	1.05	1.03	1.06	1.11	1.07	1.10	1.15	1.16	1.17	1.17	1.18	0.99	1.06	1.15	1.18
EUR/USD	1.28	1.30	1.35	1.38	1.38	1.37	1.30	1.30	1.28	1.27	1.26	1.25	1.32	1.38	1.30	1.25
USD/JPY	94.2	99.1	98.3	105.3	103.2	101.3	104.0	103.0	103.0	105.0	107.0	110.0	86.8	105.3	103.0	110.0
NZD/USD	0.84	0.77	0.83	0.82	0.87	0.88	0.85	0.86	0.86	0.85	0.84	0.82	0.83	0.82	0.86	0.82
USD/CHF	0.95	0.95	0.90	0.89	0.89	0.89	0.93	0.94	0.96	0.97	0.98	0.99	0.92	0.89	0.94	0.99
GBP/USD	1.52	1.52	1.62	1.66	1.67	1.71	1.65	1.69	1.71	1.65	1.59	1.56	1.62	1.66	1.69	1.56

Note: Exchange rates are expressed in units per USD, with the exception of the Euro, GBP, AUD, and NZD, which are expressed in USD per local currency unit.
Source: Reuters, RBC Economics Research forecasts