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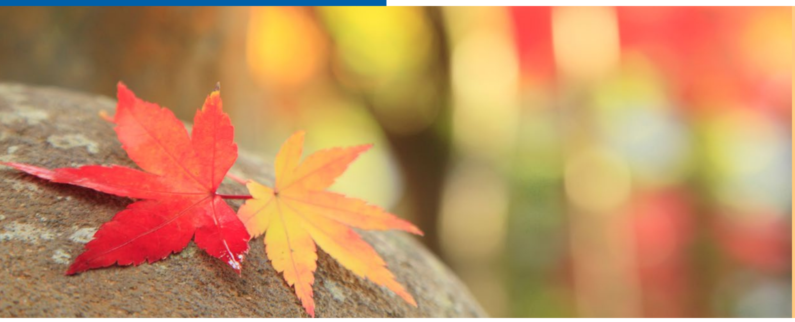
Investment UPDATE

Fall 2017 Edition



In this issue

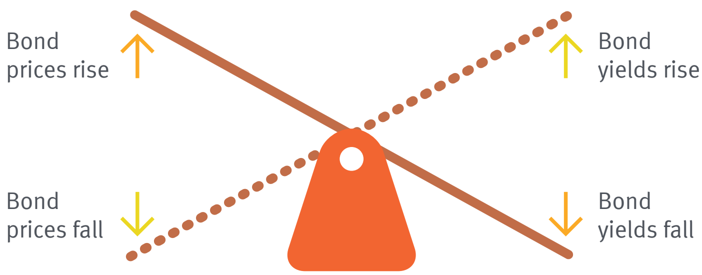
Falling leaves, rising rates

The Bank of Canada has increased interest rates twice this year, and you may be wondering what this means for your personal finances. Here's a look at how rising rates may impact your investments.

Central banks signal interest-rate policy change

Multiple signals over the last year indicate the global economy has turned a corner and is gradually improving. Thanks to this sustained economic growth, many central banks around the world have begun to raise interest rates from record lows. For the first time in seven years, the Bank of Canada raised interest rates by 0.25% in July, and then did so again by another 0.25% in September. The U.S. Federal Reserve has already raised rates three times in the last 12 months and is signaling more increases are likely on the way.

Bond prices and yields generally move in opposite directions



The ups and downs of the bond yield see-saw

These developments have led to a lot of talk in the financial press about the effects of rising interest rates on people's financial well-being – from borrowing to fixed-income investments.

Rising interest rates can have an impact on the price of your fixed-income holdings. When interest rates rise, bond yields normally do the same. A bond's yield and its price have an inverse relationship, meaning when bond yields rise, bond prices fall, and vice versa.

During periods when bond yields go up, the market value of bonds, and mutual funds that invest in them, can decline, which can be concerning for fixed-income investors. However, the positive side of rising yields is that investors can reinvest their principal, interest or coupon payments into new bonds at higher yields.

The benefits of bonds

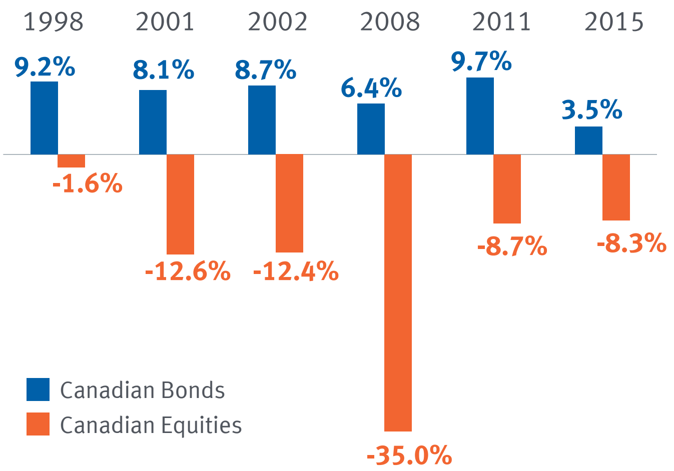
It's important to remember that despite the potential for higher rates, bonds play an important role for investors now and over the long term. These benefits include:

- A predictable source of income
- Capital preservation
- Diversification
- Can cushion against volatility and a long-term return generator

The bedrock of an investment portfolio: How owning bonds helps manage through market volatility

The chart below compares the performance of the Canadian bond market during years when equity markets were negative. You can see that since 1998, each year that equity market performance was negative, the bond market delivered positive returns, helping to offset this decline. With an actively managed portfolio that provides diversified exposure to all asset classes, including fixed income, investors can better weather periods of market stress.

Bond markets performed well during years when stocks were down*



*An investment cannot be made directly into an index. The graph does not reflect transaction costs, investment management fees or taxes. If such costs and fees were reflected, returns would be lower. Past performance is not a guarantee of future results.
Source: RBC GAM. Canadian bonds = FTSE TMX Canada Universe Bond Index; Canadian equities = S&P/TSX Composite Index.

RISING RATES CHECKLIST

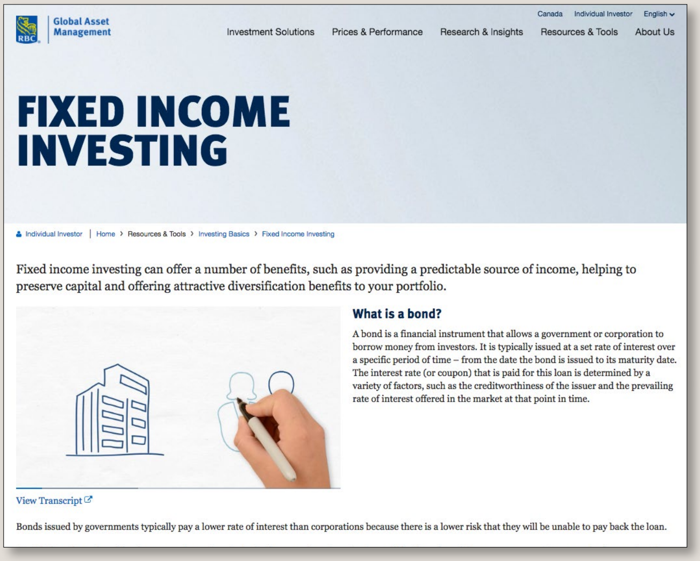
If you are worried about the impact of rising rates on your financial plan, here are a few things to consider:

- [ ] **Borrowing costs:** As interest rates rise, variable rates on loans, lines of credit and mortgages are likely to rise too. Talk to your RBC® advisor about any mortgage or loans you may have, as it could be the right time to lock in your rate.
- [ ] **Bonds:** If you own individual bonds, such as government or corporate bonds, and you intend or are likely to sell them prior to maturity, consider the impact of rising bond yields on the value of your holdings.
- [ ] **Fixed-income portfolios:** Have you reviewed your investment portfolio recently? Is your portfolio well diversified? This can help minimize losses from a rising-rate environment.

Your RBC advisor can help you determine the best course of action and offer the right investment solutions to ensure you stay on course to achieve your financial goals.

Learn more about fixed-income investing

The RBC Global Asset Management Learning Centre provides helpful insights and easy-to-understand videos that are designed to build your investing knowledge and complement the advice provided by your RBC advisor. To learn more about fixed-income investing and topics such as the impact of changes in interest rates on your portfolio, visit rbcgam.com/fixed-income-investing.



Staying the course – How your RBC advisor can help

In this changing rate environment, where news coverage and provocative headlines can sometimes be confusing, look to your RBC advisor for information and support. It's important to make sure the financial plan you put in place together prepares you for the ups and downs of interest rates, and the effects they may have on your portfolio.

Did you know?

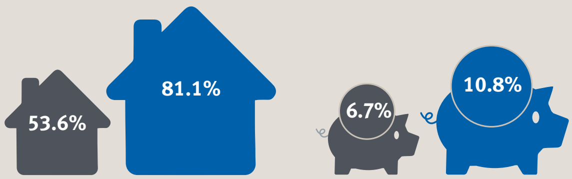
Advised clients have greater discipline through volatile markets

70%

of investors believe they **remain in financial markets despite volatility** because of their financial advisor.

Source: Strengthening Investor Protection in Ontario - Speaking with Ontarians, Ascentum 2013

Working with an advisor encourages savings and investing



Source: The Gamma Factor and the Value of Financial Advice, Claude Montmarquette, Natalie Viennot-Briot, 2016

A PLACE TO LEARN, GROW AND DISCOVER

The RBC Student Solutions site provides important resources for students and their parents

Autumn is the perfect time to get student finances on point. Whether you are a post-secondary student or the parent of one, find the resources you need for school and beyond at rbcroyalbank.com/student-solution.

ONE-MINUTE MARKET UPDATE

For the full Fall 2017 Global Investment Outlook, please visit rbcgam.com/gio.

ECONOMY

- Supported by stimulative financial conditions, soaring confidence and the lessening friction of secular stagnation, the global acceleration in economic growth that began in the middle of 2016 has largely been sustained.
- Risks have diminished with respect to European populism, Chinese growth and the potential of sharply higher interest rates, but protectionism represents a considerable threat to global growth and the risk surrounding international relations is arguably rising.
- We have moderately upgraded our growth forecasts for both this year and next in response to the strength of the recent economic trend, although we don't expect growth to accelerate further in 2018 versus 2017 because many economies are approaching their full potential.

FIXED INCOME

- The need for extreme monetary stimulus is fading and several central banks are gradually shifting toward tighter policy, with the U.S. Federal Reserve leading the global charge and the Bank of Canada following along more recently.
- A number of structural headwinds – deteriorating demographics, slower productivity growth and demand for safe-haven assets – are keeping real interest rates depressed.
- Our models continue to suggest the long-term direction for bond yields is higher, on a path that could span many years, which would weigh on total returns for bond holders.

EQUITY MARKETS

- Stocks continue to be supported by a global synchronized expansion and renewed corporate-profit growth around the world.
- The valuation tailwind from falling interest rates may be exhausted, so earnings growth will be critical for the continuity of the bull market.
- S&P 500 corporate profits have been recovering nicely following their two-year slump and stocks can still deliver decent gains if earnings come through as analysts expect. However, we are mindful that markets would be vulnerable to correction if earnings fail to come through.
- We continue to dial back the risk exposure in our recommended asset mix for balanced, global investors as the business cycle matures, trimming our equity overweight allocation again this quarter by one percentage point and moving the proceeds to fixed income.

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