Global Asset Management

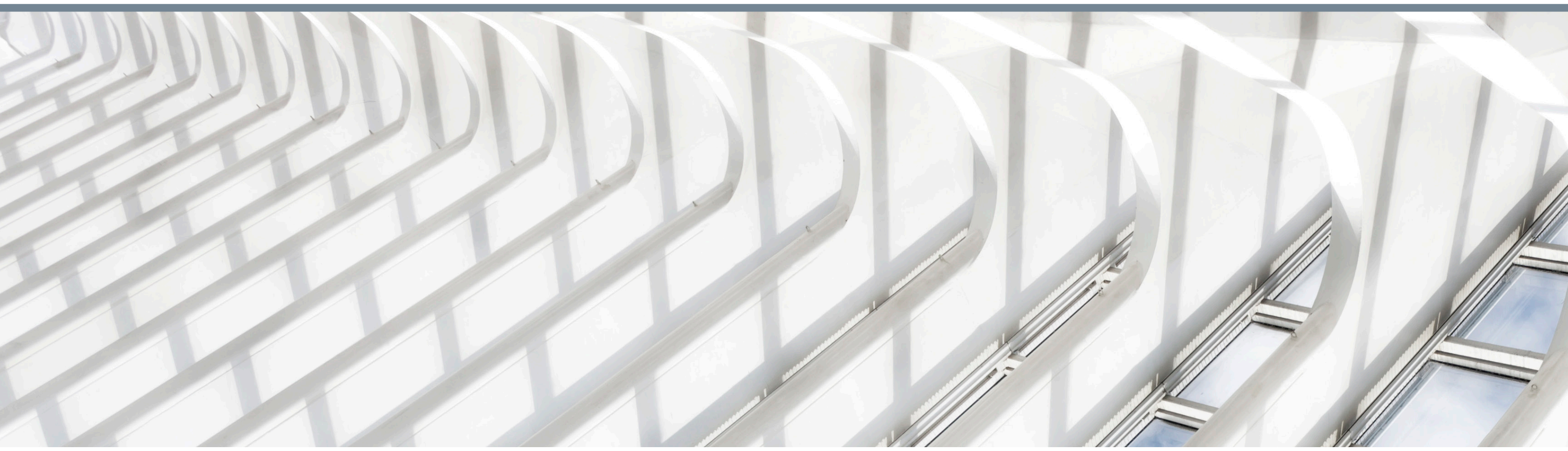

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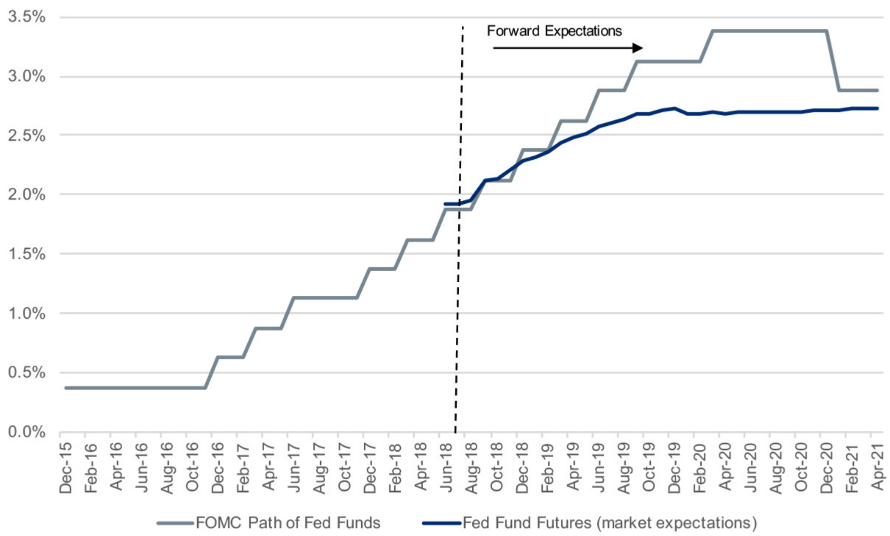
Exhibit 1
Expected Path of Fed Funds



Source: RBC GAM, Bloomberg as of June 13, 2018

The Fed Continues to Enact the Year of the Dots

The Federal Open Market Committee (FOMC) continues to fulfill the path of their 'dot plot' and has voted to raise the Fed Funds Rate 25 basis points (bps) to 1.75-2.00%. The FOMC stated that it "expects that further gradual increases in the target range for the federal funds rate will be consistent with sustained expansion of economic activity, strong labor market conditions, and inflation near the committee's symmetric 2% objective over the near term."

Current economic and geopolitical conditions support our expectation that the Fed will hike two more times this year. The Fed's plan to continue to raise interest rates gradually depends on a number of supporting economic fundamentals: a strong labor market, federal tax cuts and spending polices, high household and business confidence, stable financial conditions, and adequate global growth.

We expect GDP to be 3% in 2018, with tail winds from fiscal stimulus and tax reform providing an immediate boost to growth. However, the benefits of this stimulus will fade beyond 2018 and the Fed will have to contend with a flattening yield curve and slowing growth. We are skeptical that the Fed will be able to achieve its current long-term target for Fed Funds by 2020.

The Fed has indicated labor market conditions will continue to strengthen as GDP rises at a moderate rate, thus supporting a strong consumption outlook in the coming quarters. The FOMC expects consumer inflation to reach its 2% objective in the near future. However, a key consideration for the Fed as they move along their tightening path will be how much higher inflation will move. Additionally, global events continue to drive market volatility, as recently seen during political uncertainty in Italy. Looking forward, potential trade wars are a concern, giving the FOMC little room for error in their policy decisions.

Looking beyond 2018, we are uncertain if the Fed will continue to fulfill the path of their current projections. We are seeing a flatter yield curve, increased tensions from protectionism, ongoing geopolitical concerns, and market volatility from tighter financial conditions. As these issues and other uncertainties build into 2019, we think the Fed's dot trajectory will become harder and harder to achieve. 2018 may prove to be first and last time the Fed was able to carry out the "Year of the Dots."

Exhibit 2
Key Indicators Influencing Future Fed Policy

	Near Term (1 yr)	Long Term
Employment	🟢	🟡
Global Growth	🟢	🟡
Business Cycle	🟢	🟡
Inflation	🟢	🟡
Protectionism	🟡	🔴
Italy – Europe	🟡	🟡
Trade Wars	🟡	🔴
US Domestic Policy Events	🟢	🟡
Recession Risk (Inverted Curve?)	🟢	🔴

Source: RBC GAM

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