# July 2021 market update

## All eyes are on Canadian's pocketbooks as the recovery continues.

August 9, 2021

**Introduction**

Global economic conditions continued to improve in July, but a rise in cases of the COVID-19 Delta variant in some areas of the world raised concerns that another wave of the virus could derail the economic recovery. Global service sector activity expanded further during the month as ongoing reopenings led to increased spending within the sector. Meanwhile, the U.S. Federal Reserve Board ("Fed") and European Central Bank ("ECB") both cautioned that policy tightening might occur well into the future, and suggested they are considering ongoing supportive conditions to help bolster the economic recovery.

Global equity markets experienced some volatility in July, mainly in response to concern about the Delta variant, along with rising inflation and the potential impact that inflation could have on the recovery. In Canada, the S&P/TSX Composite Index closed the period slightly higher, and was led by the Consumer Staples sector. U.S. equities advanced, with the S&P 500 Index, NASDAQ Composite Index and Dow Jones Industrial Average all reaching new record highs during the month. Global equities, as measured by the MSCI ACWI Index, posted a small gain. Yields on 10-year government bonds in both Canada and the U.S. fell in July. Oil prices posted a small gain, while gold prices finished the month higher.

**Concern over high household debt**

In its most recent Consumer Debt Index, MNP found some concerning trends involving Canadian household debt levels. Just under half of MNP's respondents were concerned about their ability to afford all their living expenses without using credit over the next year. Meanwhile, three in 10 respondents claimed to be insolvent, or unable to pay their monthly expenses, which is the highest level since inception of the index. Many cited the pandemic as part of the reason for their higher debt, including employment uncertainty and taking on more debt amid lower interest rates. In the same survey, many respondents claimed a rise in interest rates could make their financial positions even more precarious. If more Canadians are forced to scale back spending in response to debt uncertainty, this could eventually hinder economic conditions, including the labour market and trade. Still, the impact of this debt on the overall economy might be minimal in the short term. The survey found that 32% of respondents will increase spending as the economy reopens. The Bank of Canada will certainly be watching household debt levels closely, and will consider these debt levels in its policy decisions based on the understanding that higher interest rates could negatively impact many Canadians.

### Labour shortage

Where are all the employees? That is the question being asked by many U.S. businesses. A shortage of labour is developing in the U.S. and is being reflected in some key economic indicators. Initial jobless claims were relatively elevated in July, with the four-week moving average number of claims ticking higher. Meanwhile, the unemployment rate moved slightly higher in June as the number of unemployed individuals increased, while the labour force participation rate remained steady. And this isn't a result of a lack of available jobs. According to the U.S. Bureau of Labor Statistics, there were 9.2 million job openings at the end of May, the highest number ever recorded. Reasons cited for the lack of labour are ongoing concerns about the pandemic, uncertainty over childcare and enhanced government benefits. However, the labour market shortage may be largely temporary. With ongoing vaccination efforts, concerns about the spread of the virus could begin to ease. Additionally, children returning to school in the fall could alleviate concerns over childcare, while government benefits in many states are scheduled to expire at the end of September. Getting more people back to work should have a positive impact on the economic recovery.

### Easing expectations for early tightening

While expectations are rising for global central banks to start tightening their policies in response to the economic recovery, two major central banks indicated that financial markets should modify those expectations. After hinting that its federal funds rate could be increased earlier than previously expected and that its bond purchases could be scaled back in the very near future, Fed Chairman Jerome Powell indicated that these steps might not be imminent in his semi-annual Monetary Policy Report to Congress. Chairman Powell noted the economic recovery has not progressed enough to warrant a pullback in the Fed's support. At its meeting late in the month, however, the Fed did acknowledge progress has been made and that the Fed will monitor that economic progress before scaling back support.

Similarly, the ECB sent a strong message to market participants that an increase to its benchmark interest rate is still some time away. Early in July, the ECB announced a new inflation target of 2% over the medium term. The ECB's previous inflation target was just under 2%. At its meeting in late July, the ECB noted that it will hold its key interest rate steady until inflation is sustained at 2% over its projected horizon. With expectations of 1.4% consumer price growth in 2023, the ECB suggested that interest rate increases are likely far down.

These major central banks calmed financial markets and reassured investors that their accommodative policies should remain in place for some time to support full economic recoveries, as well as to sustainably push inflation and employment to these central banks' targets.

**Many signs point to a balanced recovery**

China's gross domestic product expanded by 7.9% year-over-year in the second quarter of 2021, but trailed the 18.3% growth posted during the first quarter. This economic growth has been driven by a strong manufacturing sector, along with robust trade activity. Despite the slowdown in the second quarter, China's economy was still relatively strong and remained on track to meet the government's 6% target over 2021. With economies around the world reopening and lockdown restrictions easing, spending at service-type businesses could rise substantially, while spending on manufactured goods could ease. This could negatively impact China's key manufacturing sector and the country's exports, which could weigh on the country's economic growth in the second half of 2021.

Data released in July, however, appeared to point to a pickup in other areas of the economy, which could lead to a more balanced recovery for China's economy. Strong domestic demand could bolster economic growth. Retail sales in China rose 12.1% in June over the same month in the previous year. This meant that China's year-to-date retail sales figure was 23.0% higher than during the same period in 2020. Meanwhile, the real estate market has been a key contributor to growth, and that trend could continue. From January to June 2021, property sales increased by 38.9% over the same period in 2020. Despite ongoing concern about the continued threat posed by the spread of the virus, it appears China's economy could experience a fairly well-balanced recovery over the remainder of the year.

## Market performance - as at July 31, 2021

| Equity Markets | Level | Month to date | Year to date | One year |
|---|---|---|---|---|
| S&P/TSX Composite Index C$ | 20,287.80 | 0.61% | 16.37% | 24.47% |
| S&P 500 Index US$ | 4,395.26 | 2.27% | 17.02% | 35.40% |
| Dow Jones Industrial Average US$ | 34,935.47 | 1.25% | 14.14% | 32.77% |
| MSCI EAFE Index US$ | 2,321.09 | 0.70% | 8.08% | 27.52% |
| MSCI Emerging Markets Index US$ | 1,277.81 | -7.04% | -1.04% | 18.43% |

| Fixed Income Markets | Level | Month to date | Year to date | One year |
|---|---|---|---|---|
| FTSE Canada Universe Bond Index C$ | 1,191.05 | 1.03% | -2.47% | -2.66% |
| FTSE World Investment Grade Bond Index US$ | 252.28 | 1.34% | -2.22% | -0.11% |

| Currencies | Level | Month to date | Year to date | One year |
|---|---|---|---|---|
| CAD/USD | 0.8019 | -0.39% | 2.23% | 7.84% |

| Commodities | Level | Month to date | Year to date | One year |
|---|---|---|---|---|
| West Texas Intermediate (US$/bbl) | 73.95 | 0.65% | 52.41% | 85.25% |
| Gold (US$/oz) | 1,814.19 | 2.49% | -4.43% | -7.28% |

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