

The Weekly Bottom Line

April 16, 2021

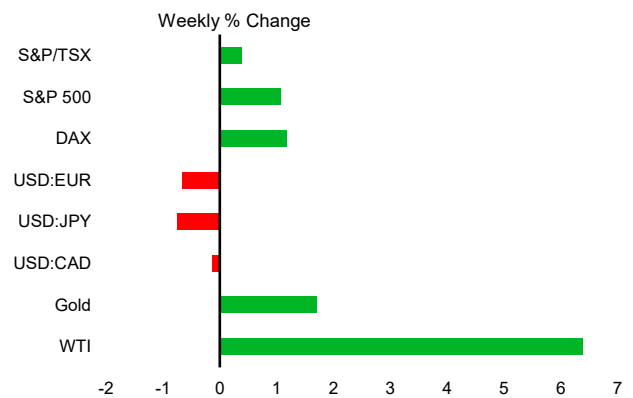
Highlights

- Headline inflation jumped in March, but it's too soon to sound the alarm. Economic slack is still high, inflation expectations benign, and the Fed unlikely to sit on the sidelines if they drift up persistently.
- Retail sales surged in March, thanks to massive income supports, accelerated vaccine rollouts and loosening restrictions.
- The issue of corporate taxation is back in the spotlight. President Biden has proposed an increase to the US corporate tax rate and Treasury Secretary Janet Yellen has recommended a global minimum rate of corporate tax.
- These proposals appear to be initiating a sea change. For decades, there has been a race to the bottom, where governments consistently reduced corporate taxes in an effort to attract investment. The race appears to be over.

This Week in the Markets				
	Current*	Week Ago	52-Week High	52-Week Low
Stock Market Indexes				
S&P 500	4173	4129	4173	2737
S&P/TSX Comp.	19312	19228	19322	13899
DAX	15412	15234	15412	10250
FTSE 100	7011	6916	7011	5577
Nikkei	29683	29768	30468	19138
Fixed Income Yields				
U.S. 10-yr Treasury	1.58	1.66	1.74	0.51
Canada 10-yr Bond	1.51	1.50	1.61	0.43
Germany 10-yr Bund	-0.27	-0.30	-0.23	-0.64
UK 10-yr Gilt	0.77	0.77	0.88	0.08
Japan 10-yr Bond	0.09	0.11	0.16	-0.04
Foreign Exchange Cross Rates				
C\$ (USD per CAD)	0.80	0.80	0.81	0.70
Euro (USD per EUR)	1.20	1.19	1.23	1.08
Pound (USD per GBP)	1.38	1.37	1.41	1.21
Yen (JPY per USD)	108.8	109.7	110.7	102.7
Commodity Spot Prices**				
Crude Oil (\$US/bbl)	63.6	59.3	66.1	-37.6
Natural Gas (\$US/MMBtu)	2.57	2.42	16.35	1.33
Copper (\$US/met. tonne)	9297.3	8935.3	9456.3	5000.5
Gold (\$US/troy oz.)	1775.4	1743.9	2063.5	1682.8

*As of 9:55 AM on Friday. **Oil-WTI, Cushing, Nat. Gas-Henry Hub, LA (Thursday close price). Copper-LME Grade A. Gold-London Gold Bullion. Source: Bloomberg.

Inventory Draws and Stronger Demand Boosts Oil Prices



Note: Data as of 10:00 AM ET, Friday, April 16, 2021.
Source: Bloomberg, TD Economics

Global Official Policy Rate Targets	
Central Banks	Current Target
Federal Reserve (Fed Funds Rate)	0.00 - 0.25%
Bank of Canada (Overnight Rate)	0.25%
European Central Bank (Refi Rate)	0.00%
Bank of England (Repo Rate)	0.10%
Bank of Japan (Overnight Rate)	-0.10%

Source: Bloomberg.

TD Economics Key Financial Forecasts													
	Current Rate	2020				2021				2022			
	4/16/21	Q1	Q2	Q3	Q4	Q1	Q2F	Q3F	Q4F	Q1F	Q2F	Q3F	Q4F
Fed Funds Target Rate	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
2-yr Govt. Bond Yield	0.16	0.23	0.16	0.13	0.13	0.16	0.18	0.20	0.25	0.30	0.35	0.45	0.55
10-yr Govt. Bond Yield	1.58	0.70	0.66	0.69	0.93	1.74	1.60	1.65	1.70	1.75	1.80	1.85	1.90
30-yr Govt. Bond Yield	2.27	1.35	1.41	1.46	1.65	2.41	2.30	2.35	2.40	2.45	2.50	2.50	2.50

Forecast by TD Economics as of March 2021; all forecasts are end-of-period. Source: Bloomberg, Federal Reserve Board, TD Economics.

Much to Cheer About

Who said the stock market rally was over? After a slow start to the week, the S&P 500 hit another all time high. As of writing, the index is up 1.3% compared to last week's close. Equities were helped by strong earnings and better than expected economic data. But interestingly, bond yields dropped on the news. At the time of writing, the 10-year Treasury yield was down nine basis points compared to last week. Usually, bond yields rise in response to strong data. The fact that yields drifted lower might seem like an anomaly but is likely due to the market already having priced in the economic recovery and inflation expectations. Meanwhile, growth stocks behaved as expected. Lower yields tend to increase future earnings of growth-oriented companies. So, tech stock rebounded as yields dropped.

On to one of economists' favorite topic these days, inflation! Consumer prices jumped in March (Chart 1). Inflation rose 0.6% month-on-month (m/m), pushing headline inflation to 2.6% year-on-year (y/y). Meanwhile, core inflation (ex. food and energy) was up 0.3% compared to the previous month and 1.6% higher compared to a year ago. The rise in inflation was mostly due to energy prices which went up 5.0% on the month. Energy prices will continue to keep the headline inflation number elevated over the next few months. In fact, year-on-year inflation numbers are likely to push through the 3% mark given the drop in prices in the second quarter of 2020.

Chart 1: Energy Prices Push Headline Inflation over 2% but Core Inflation Remains Subdued

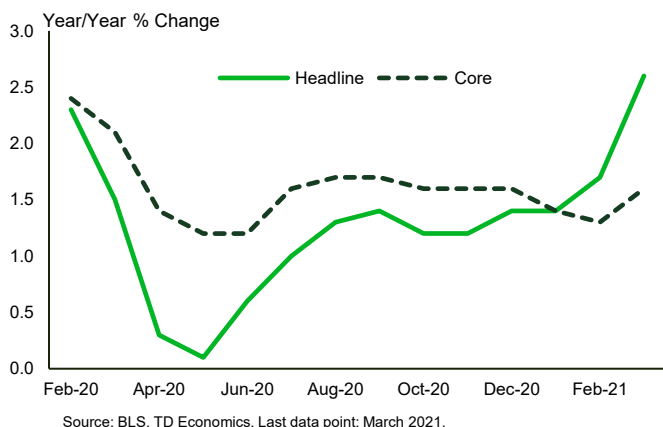
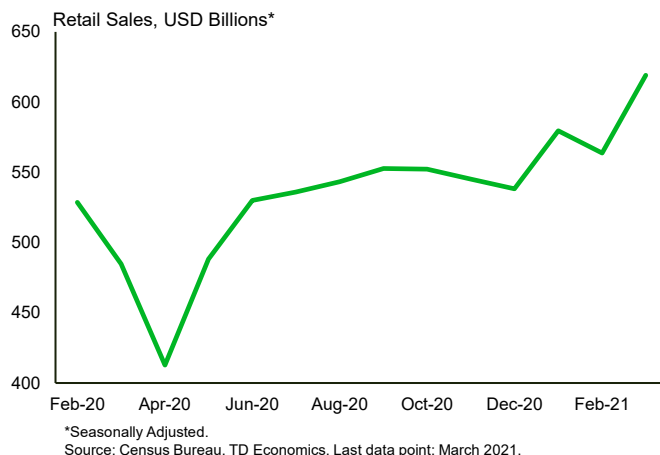


Chart 2: Retail Sales Are Swooshing Up



Still, it's too soon to sound the inflation alarm. The unemployment rate is still 2.5 percentage points (ppts) higher than its pre-recession level and there are roughly eight million fewer jobs. The 5-year U.S. breakeven – a measure of inflation expectations based on the spread between nominal and inflation adjusted Treasury yields – has cooled since hitting its highest point since 2008 in March. Rest assured the Federal Reserve is watching this and other measures of inflation expectations closely. In fact, Fed Vice Chair Richard Clarida said that if inflation expectations were to “drift up persistently [...] that would indicate to me that policy would need to be adjusted.” Clarida also added that the Fed’s “metrics of success” on inflation is keeping inflation expectations anchored at 2%. According to the Vice Chair, inflation expectations most recently stood at 1.96%.

Meanwhile, income supports, accelerated vaccine rollouts and loosening restrictions helped retail sales end the first quarter on a high note (Chart 2). Retail sales surged by 9.8% month-on-month in March, almost four ppts more than market expectations. The level of retail sales was a whopping 17.1% higher than February 2020, just before pandemic-induced restrictions took hold. Going forward, spending is likely remain robust as the job market strengthens and Americans tap into accumulated savings.

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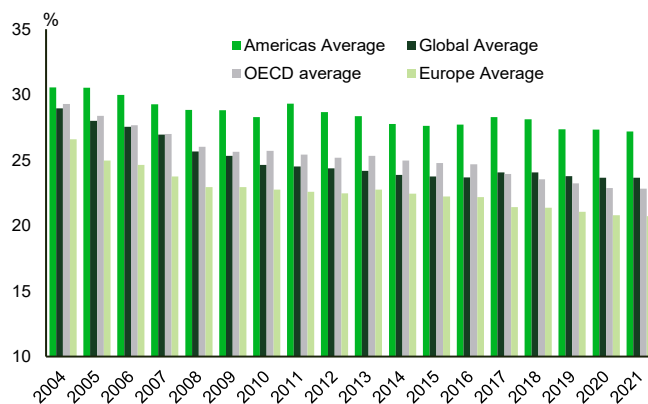
Financial - U.S. Corporate Taxes, Under the Microscope

Corporate taxation has been the topic du jour for policy makers in recent weeks. In addition to President Biden's push to raise the U.S. corporate tax rate to 28%, Treasury Secretary Janet Yellen recently proposed a global minimum tax for larger multinational corporations, in order to "level the playing field" and avoid tax leakage.

This push comes after years of governments around the world actively reducing tax rates in order to attract corporate investment. Since 2004, the average global corporate tax rate has declined from 29%, to 23.7% in 2021 (Chart 1). For the U.S., it was only four years ago that the Trump administration passed one of the largest corporate tax cuts in modern history. The Tax Cuts and Jobs Act (TCJA) of 2017 reduced the U.S. corporate tax rate from 35% to 21%, with the intent of triggering a corporate investment boom. Corporate investment has disappointed, but the policy did result in a greater percentage of profits being retained by large corporations. To be exact, corporate earnings after tax and interest payments rose from 67% of total operating earnings at the end of 2017, to 75% by the end of 2018. Corporations retained a larger share of the pie, while investors in these companies saw a valuation adjustment and strong price appreciation.

The international story is also telling. U.S. companies have spent years setting up and investing in holding companies (non-bank) domiciled in lower taxed countries. Indeed, roughly half of U.S. foreign investment has been in holding companies, with the majority of this investment in Europe. The TCJA eased this trend by lowering the corporate tax rate to more competitive international levels. Conversely, the Biden administration is proposing a different approach by proposing to raise the tax on overseas profits from 10% to 21%. The new strategy will calculate the minimum tax on a country-by-country basis, which should help address the tax avoidance issue.

Chart 1: The Decline in Global Corporate Tax Rates



Source: KPMG, TD Economics.

Policy analysts know that U.S. corporate taxes are both controversial and convoluted. From an economic perspective, it is imperative the Biden administration strikes the right balance to ensure that corporate incentives to invest remain in place. Assuming the administration is successful in unwinding a large portion of the Trump administration's corporate tax cut, it must also make sure it does not erode U.S. competitiveness. Hence the focus on rewriting the rules globally. Thus far, we have seen supportive voices from Europe, stating that an agreement on corporate taxation could bring about stability. While there is a big difference between voicing support for ending tax avoidance and actually signing onto a U.S.-led agreement, this is a step in the right direction.

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Recent Key Economic Indicators: Apr 12 - 16, 2021					
Release Date	Economic Indicator/Event	Data for Period	Units	Current	Prior
United States					
Apr 13	NFIB Small Business Optimism	Mar	Index	98.2	95.8
Apr 13	Consumer Price Index	Mar	M/M % Chg.	0.6	0.4
Apr 13	Consumer Price Index	Mar	Y/Y % Chg.	2.6	1.7
Apr 13	Consumer Price Index Ex Food and Energy	Mar	M/M % Chg.	0.3	0.1
Apr 13	Consumer Price Index Ex Food and Energy	Mar	Y/Y % Chg.	1.6	1.3
Apr 15	Empire Manufacturing	Apr	Index	26.3	17.4
Apr 15	Initial Jobless Claims	Apr 10	Thsd	576.0	769.0
Apr 15	Retail Sales Advance	Mar	M/M % Chg.	9.8	-2.7
Apr 15	Retail Sales Ex Auto and Gas	Mar	M/M % Chg.	8.2	-3.1
Apr 15	Capacity Utilization	Mar	%	74.4	73.4
Apr 15	Industrial Production	Mar	M/M % Chg.	1.4	-2.6
Apr 15	Manufacturing (SIC) Production	Mar	M/M % Chg.	2.7	-3.7
Apr 15	Business Inventories	Feb	M/M % Chg.	0.5	0.4
Apr 15	NAHB Housing Market Index	Apr	Index	83.0	82.0
Apr 16	Building Permits	Mar	Thsd	1766.0	1720.0
Apr 16	Housing Starts	Mar	Thsd	1739.0	1457.0
Canada					
Apr 12	BoC Business Outlook Future Sales	1Q	Q/Q % Chg.	52.0	48.0
Apr 15	Manufacturing Sales	Feb	M/M % Chg.	-1.6	3.1
Apr 15	Existing Home Sales	Mar	M/M % Chg.	5.2	6.6
Apr 16	Wholesale Trade Sales	Feb	M/M % Chg.	-0.7	4.0
International					
Apr 12	EZ Retail Sales	Feb	Y/Y % Chg.	-2.9	-5.2
Apr 13	UK Monthly Gross Domestic Product (3M/3M)	Feb	M/M % Chg.	-1.6	-1.4
Apr 15	CH Gross Domestic Product	1Q	Y/Y % Chg.	18.3	6.5
Apr 15	CH Retail Sales	Mar	Y/Y % Chg.	34.2	-
Apr 15	CH Surveyed Jobless Rate	Mar	%	5.3	5.5
Apr 16	EZ Consumer Price Index	Mar	Y/Y % Chg.	1.3	0.9

Source: Bloomberg, TD Economics.

Upcoming Economic Releases and Events: Apr 19 - 23, 2021						
Release Date	Time*	Economic Indicator/Event	Data for Period	Units	Consensus Forecast	Last Period
United States						
Apr 22	8:30	Initial Jobless Claims	Apr 17	Thsd	638.0	576.0
Apr 22	10:00	Existing Home Sales	Mar	Mlns	6.20	6.22
Apr 23	9:45	Markit US Manufacturing PMI	Apr	Index	60.0	59.1
Apr 23	9:45	Markit US Services PMI	Apr	Index	61.5	60.4
Apr 23	10:00	New Home Sales	Mar	Thsd	875.0	775.0
Canada						
Apr 19	8:30	Housing Starts	Mar	Thsd	255.0	245.9
Apr 20	8:30	Teranet/National Bank HPI	Mar	Y/Y % Chg.	-	9.8
Apr 21	8:30	Consumer Price Index	Mar	Y/Y % Chg.	-	1.1
Apr 21	8:30	Consumer Price Index NSA	Mar	M/M % Chg.	-	0.5
Apr 21	10:00	Bank of Canada Rate Decision	Apr 21	%	0.25	0.25
Apr 21	11:00	<i>Bank of Canada's Macklem Speaks to Press After Decision</i>				
International						
Apr 20	2:00	UK ILO Unemployment Rate 3Mths	Feb	%	5.1	5.0
Apr 21	2:00	UK Consumer Price Index	Mar	Y/Y % Chg.	0.8	0.4
Apr 22	7:45	EZ ECB Main Refinancing Rate	Apr 22	%	0.00	0.00
Apr 22	19:30	JN Natl Consumer Price Index	Mar	Y/Y % Chg.	-0.2	-0.4
Apr 22	20:30	JN Jibun Bank Japan PMI Mfg	Apr	Index	-	52.7
Apr 23	2:00	UK Retail Sales Ex Auto Fuel	Mar	Y/Y % Chg.	4.2	-1.1
Apr 23	4:00	EZ Markit Eurozone Manufacturing PMI	Apr	Index	62.0	62.5
Apr 23	4:30	UK Markit UK PMI Manufacturing SA	Apr	Index	59.0	58.9

Source: Bloomberg, TD Economics.

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