TD Economics

The Weekly Bottom Line

September 24, 2021

Highlights

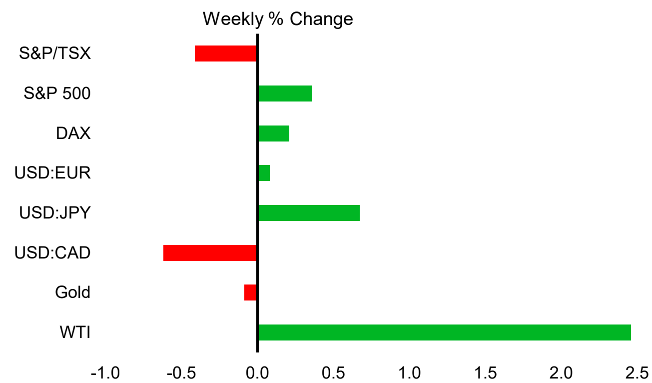
- Housing starts surprised to the upside in August (rising 3.9%), powered by gains in the multifamily segment.
- Solid data out of the housing sector and reassuring words from the FOMC confirm that the economic recovery is well under way. However, notable risks remain, primarily the ongoing standoff over the debt ceiling.
- The stand-off in Washington continues, with two issues becoming evermore pressing. The government's spending power needs to be renewed and the debt ceiling needs to be raised to avoid a default on U.S. Treasury debt.
- The deadlines are approaching quickly. Though a deal should get done, the closer we get to the dropdead date, the greater the risk that this gridlock turns into financial market stress.

This Week in the Markets

	Current*	Week Ago	52-Week High	52-Week Low
Stock Market Indexes				
S&P 500	4443	4433	4537	3247
S&P/TSX Comp.	20395	20490	20821	15581
DAX	15532	15490	15977	11556
FTSE 100	7055	6964	7220	5577
Nikkei	30249	30500	30670	22977
Fixed Income Yields				
U.S. 10-yr Treasury	1.45	1.36	1.74	0.65
Canada 10-yr Bond	1.37	1.28	1.61	0.54
Germany 10-yr Bund	-0.23	-0.28	-0.10	-0.64
UK 10-yr Gilt	0.93	0.85	0.93	0.17
Japan 10-yr Bond	0.06	0.05	0.16	0.01
Foreign Exchange Cross Rates				
C$ (USD per CAD)	0.79	0.78	0.83	0.75
Euro (USD per EUR)	1.17	1.17	1.23	1.16
Pound (USD per GBP)	1.37	1.37	1.42	1.27
Yen (JPY per USD)	110.7	109.9	111.5	102.7
Commodity Spot Prices**				
Crude Oil ($US/bbl)	73.1	72.0	75.3	35.8
Natural Gas ($US/MMBtu)	4.90	5.26	15.83	1.38
Copper ($US/met. tonne)	9284.5	9307.3	10448.5	6374.8
Gold ($US/troy oz.)	1752.4	1754.3	1951.4	1683.5

*As of 11:38 AM on Friday. **Oil-WTI, Cushing, Nat. Gas-Henry Hub, LA (Thursday close price). Copper-LME Grade A. Gold-London Gold Bullion. Source: Bloomberg.

Oil Prices Rise as Demand Picks up and Hurricanes Hinder Production



Note: Data as of 11:10 AM ET, Friday, September 24, 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	2021				2022				2023			
	9/24/21	Q1	Q2	Q3F	Q4F	Q1F	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	0.50	0.75	1.00	1.25	1.50
2-yr Govt. Bond Yield	0.27	0.16	0.25	0.20	0.50	0.80	1.00	1.20	1.40	1.55	1.70	1.80	1.90
10-yr Govt. Bond Yield	1.45	1.74	1.45	1.35	1.85	2.00	2.10	2.20	2.30	2.35	2.35	2.30	2.25
30-yr Govt. Bond Yield	1.97	2.41	2.06	1.90	2.15	2.30	2.40	2.50	2.60	2.65	2.65	2.60	2.55

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

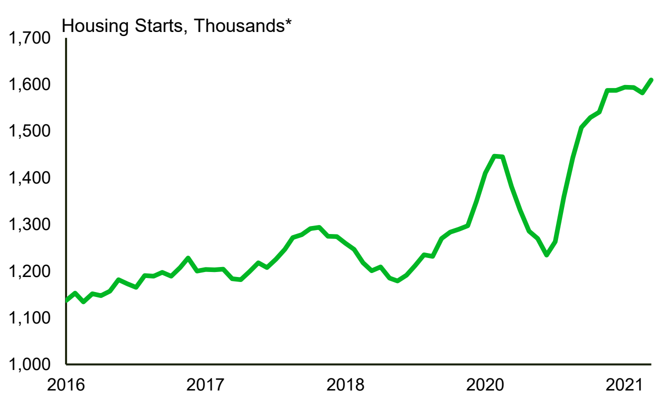
Recovery Continues, But Debt Ceiling Looms

The week kicked off with market jitters over the prospects of contagion from the ongoing deleveraging in the Chinese property sector. Yet, positive data from the U.S. housing market and a reassuring message from the FOMC reinforced the notion that, with each passing week, the American economy is leaving the pandemic recession in the rear-view mirror. As of the time of writing the S&P 500 is back up 2.1% over last Monday's close.

After declining in July, housing starts recovered on the month – rising 3.9% and outstripping the 1.9% gain the analyst consensus was expecting. Smoothing out some of the near-term volatility, the six-month moving average of housing starts now stands at 1.61 million units (annualized), well above the pre-pandemic high of 1.45 million units (Chart 1). The strong reading was entirely supported by strength in the multifamily segment, which was up over 20% month-on-month. Single family starts pulled back modestly on the month, though remain at a very healthy level of 1.08 million – slightly above their pre-pandemic level of 1.06 million units. With permitting also up in August, it appears that residential construction will continue to be a net positive for economic growth over the coming months.

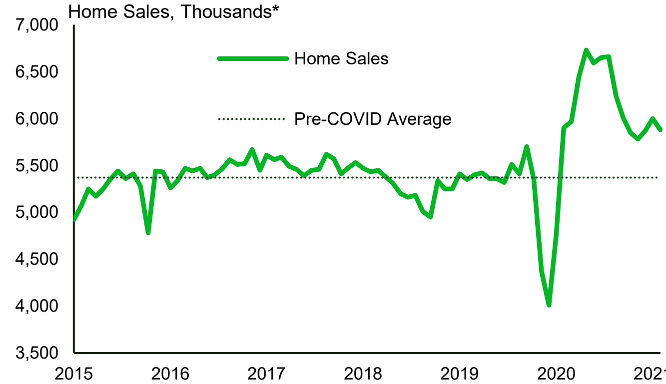
On the demand side of the equation, a small contraction in existing home sales (-2.0%) fell right in line with consensus expectations. After the frenzy in the market between the summer of 2020 and early 2021 some give-back in sales was expected. The ongoing reversion to pre-pandemic trends reflects a return to a more sustainable pace of activity (Chart 2). In fact, the 5.88 million (annualized) sales in August were still 8.5% higher than in the same month in 2019. Over two years that amounts to an average growth rate of roughly 4.2%, still well above trend.

Chart 1: Housing Starts Remain Well Above Pre-Pandemic Levels



*Seasonally adjusted annual rate. Six-month moving average.
Source: Census Bureau, TD Economics. Last observation: August 2021.

Chart 2: Home Sales Are Returning to Pre-COVID Levels



*Seasonally adjusted annual rate.
Source: National Association of Realtors, TD Economics. Last observation: August 2021.

Further evidence that the economic recovery remains on track came from the Fed on Wednesday. In its statement, FOMC members strengthened the language around the economic recovery and hinted that some "moderation" in its asset purchase program "may soon be warranted".

In the accompanying projections, FOMC members shaved their growth forecast for 2021 (now expecting 5.9% for the year, from 7.0% in June), but lifted it for 2022 and 2023. Risks to the inflation forecast continue to be described as "transitory" with PCE inflation expected to moderate from 4.2% this year to 2.2% in 2022. A more stable inflation path and the steady return to full employment have officials now projecting rate hikes to commence in 2022, with three more coming in 2023.

Altogether, we've received a reassuring message of an economy on the mend. There are certainly risks to the outlook – the standoff over the debt ceiling (discussed in the financial section below) being top of mind – but the broader picture is one of healthy domestic demand and gradually receding supply side stresses. The pandemic isn't over yet, but the light at the end of the tunnel is getting brighter.

Andrew Hencic, Senior Economist

Another Debt Ceiling Debacle

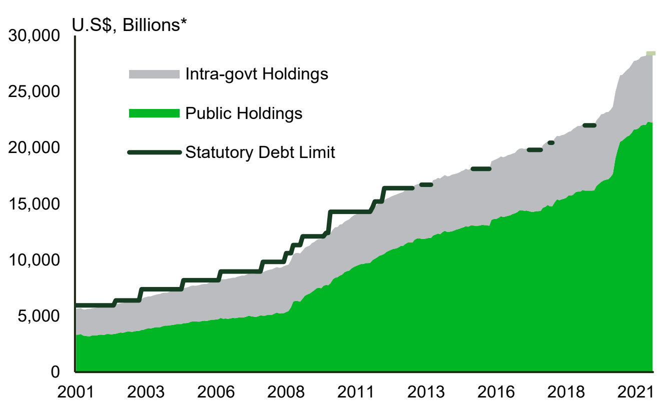
President Biden continues to push his legislative agenda, which centers around two major proposals: a plan to spend $3.5 trillion on education, health, childcare, and to combat climate change and $1 trillion on the nation's aging infrastructure. Given the current state of bipartisan politics, getting agreement on these plans is no easy task and is sparking a lot of debate. In the meantime, the White House faces a pressing September 30th deadline to renew the government's spending power. If Congress does not act, the government will be forced to shut down.

At the same time, Congress must lift the ever-precarious debt ceiling. Recall that the debt ceiling was reinstated on August 1st after a COVID-induced pause. The limit imposed by legislation means that the U.S. Treasury is not currently permitted to issue debt to pay its bills and has been running down its cash assets to make ends meet (Chart 1). It's estimated that around mid-to late-October, it will run out of cash for all needed payments. Last week, Treasury Secretary, Janet Yellen, warned that if swift resolution didn't occur, this impasse could turn into a financial market stress.

But You Already Promised!

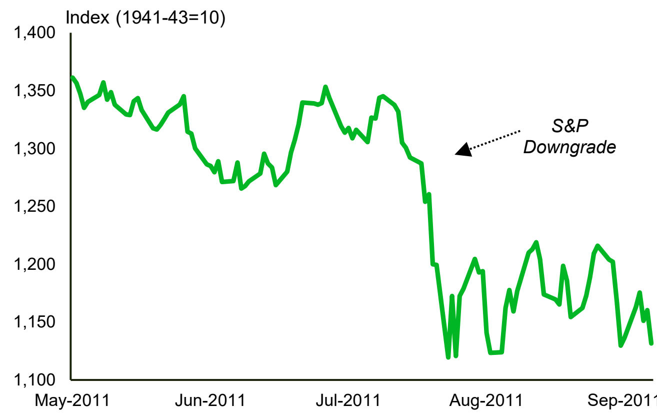
The U.S. government has committed to spending a lot of money over fiscal 2022. But, for the government to continue its deficit spending, Congress needs to renew its spending authority. Logically we expect the government to pay its bills, but this isn't the first time it's dangled against the precipice.

Chart 1: The U.S. Debt Limit Has Been Reached



*End of period.
Source: TD Economics. Last observation: August 2021.

Chart 2: The 2011 Debt Ceiling Stress



Source: Standard & Poor's, TD Economics. Last observation: September 30, 2011.

The most recent incident happened in late-2018/early-2019 during the Trump presidency. The historic 35-day shutdown over the funding of the U.S.-Mexico border wall resulted in about $11 billion in lost output, with a disproportionate impact on government workers. Though it was impactful on those who were furloughed (or ended up temporarily working for free during that time), the overall impact on the economy was small (0.1% on GDP). And that has also been the case in prior episodes. However, the tension in getting a deal done so the government can keep working can keep markets on edge, at a time when global events are already causing angst. Then there's the debt ceiling issue, that poses much more economic and financial risk.

As American as Baseball and Apple Pie

The debate over the debt ceiling is a unique American past-time. This cap on the amount of government debt was established during World War I so that the U.S. Treasury could issue bonds and bills without the approval of Congress (particularly important given large/uncertain wartime spending). Though the spirit of the law was to make debt issuance easier, the ceiling has evolved to act as a blunt tool for political fiscal restraint.

As the size of the American economy expands, the capacity for the government to take on new debt increases as well. This means that the debt ceiling needs to be raised at regular intervals. And indeed, it has – nearly 80 times since 1960. However, the debt ceiling debate has become more acrimonious and brinkmanship more common over the past several decades. Congress has, on several occasions waited until the very last minute to increase or suspend the limit. The most infamous incident occurred during the Obama presidency in 2011. While a deal was struck days before default would have occurred, the uncertainty caused by the quarrel spurred Standard & Poor's to downgrade the credit rating on U.S. sovereign debt. The stock market dropped around 12% in its wake (Chart 2).

Bottom Line

The news out of Washington will be closely watched over the coming days and weeks. Although financial markets have become more accustomed to legislative battles, the chance of this turning into a tail-risk rises by the day. From our perspective, the odds of a government shutdown will be high as the September 30th deadline approaches, though it should have a minimal impact on our economic outlook if history holds true.

On the other hand, if the debt ceiling battle extends and causes investors to get panicky about the government's ability to meet its debt payments, this would pose a bigger risk to markets. The worst-case scenario would be a missed Treasury payment, which would almost certainly result in a significant decline in equity prices, a large jump higher in yields, and a depreciation of the USD. Although the government would go to all lengths to avoid a missed Treasury payment, it only takes one misstep to set a new precedent. Our base assumption is that this unthinkable mistake will be avoided, but we will be intently watching negotiations as the clock ticks down.

James Orlando, Senior Economist | (416) 413-3180

Recent Key Economic Indicators: Sep 20 - 24, 2021						
Release Date		Economic Indicator/Event	Data for Period	Units	Current	Prior
United States						
Sep 20		NAHB Housing Market Index	Sep	Index	76.0	75.0
Sep 21		Building Permits	Aug	Thsd	1728.0	1630.0
Sep 21		Housing Starts	Aug	Thsd	1615.0	1554.0
Sep 22		Existing Home Sales	Aug	Mlns	5.9	6.0
Sep 22		FOMC Rate Decision (Upper Bound)	Sep 22	%	0.25	0.25
Sep 23		Initial Jobless Claims	Sep 18	Thsd	351.0	335.0
Sep 23		Markit US Manufacturing PMI	Sep	Index	60.5	61.1
Sep 23		Markit US Services PMI	Sep	Index	54.4	55.1
Sep 24		New Home Sales	Aug	Thsd	740.0	729.0
Canada						
Sep 20		Teranet/National Bank HPI	Aug	Y/Y % Chg.	18.4	17.8
Sep 23		Retail Sales	Jul	M/M % Chg.	-0.6	4.2
Sep 23		Retail Sales Ex Auto	Jul	M/M % Chg.	-1.0	4.7
International						
Sep 22	JN	BOJ Policy Balance Rate	Sep 22	%	-0.10	-0.10
Sep 23	EZ	Markit Eurozone Manufacturing PMI	Sep	Index	58.7	61.4
Sep 23	UK	Markit UK PMI Manufacturing SA	Sep	Index	56.3	60.3
Sep 23	UK	Bank of England Bank Rate	Sep 23	%	0.10	0.10
Sep 23	JN	Natl Consumer Price Index	Aug	Y/Y % Chg.	-0.4	-0.3
Sep 23	JN	Jibun Bank Japan PMI Mfg	Sep	Index	51.2	52.7

Source: Bloomberg, TD Economics.

Release Date	Time*	Economic Indicator/Event	Data for Period	Units	Consensus Forecast	Last Period
		Upcoming Economic Releases and Events: Sep 27 - Oct 1, 2021				
		United States				
Sep 27	8:00	*Fed's Evans Speaks at Annual NABE Conference*				
Sep 27	8:30	Cap Goods Orders Nondef Ex Air	Aug	M/M % Chg.	0.3	0.1
Sep 27	8:30	Durable Goods Orders	Aug	M/M % Chg.	0.7	-0.1
Sep 27	9:00	*Fed's Williams Makes Opening Remarks at Conference on Culture*				
Sep 27	12:00	*Fed's Williams Discusses the Economic Outlook*				
Sep 27	12:15	*Fed's Brainard Speaks at Annual NABE Conference*				
Sep 28	8:30	Advance Goods Trade Balance	Aug	Blns	-87.3	-86.4
Sep 28	9:00	*Fed's Evans Makes Welcome Remarks at Payments Conference*				
Sep 28	9:00	S&P CoreLogic CS US HPI NSA	Jul	Y/Y % Chg.	-	18.6
Sep 28	10:00	Conf. Board Consumer Confidence	Sep	Index	115.0	113.8
Sep 28	10:00	*Powell and Yellen Appear Before Senate Banking Panel*				
Sep 28	15:00	*Fed's Bostic Discusses the Economic Outlook*				
Sep 28	19:00	*Fed's Bullard Discusses U.S. Economy and Monetary Policy*				
Sep 29	10:00	Pending Home Sales	Aug	M/M % Chg.	1.3	-1.8
Sep 29	14:00	*Fed's Bostic Gives Remarks at Chicago Fed About Inclusive Payments*				
Sep 30	8:30	Core Personal Consumption Expenditure	2Q	Q/Q % Chg.	-	6.1
Sep 30	8:30	Gross Domestic Product Annualized	2Q	Q/Q % Chg.	6.6	6.6
Sep 30	8:30	Initial Jobless Claims	Sep 25	Thsd	325.0	351.0
Sep 30	8:30	Personal Consumption	2Q	Q/Q % Chg.	11.9	11.9
Sep 30	10:00	*Fed's Williams Discusses the Fed's Pandemic Response*				
Sep 30	10:00	*House Panel Holds Hearing on Fed and Treasury's Covid Response*				
Sep 30	11:00	*Fed's Bostic Discusses Economic Mobility*				
Sep 30	12:30	*Fed's Evans Discusses Economic Outlook*				
Sep 30	13:05	*Fed's Bullard Makes Opening Remarks at Book Launch*				
Sep 30	15:30	*Fed's Harker Discusses Sustainable Assets and Financial Markets*				
Oct 1	8:30	Personal Consumption Expenditure Deflator	Aug	Y/Y % Chg.	4.1	4.2
Oct 1	8:30	Personal Income	Aug	M/M % Chg.	0.2	1.1
Oct 1	8:30	Real Personal Spending	Aug	M/M % Chg.	0.4	-0.1
Oct 1	9:45	Markit US Manufacturing PMI	Sep	Index	60.5	60.5
Oct 1	10:00	ISM Manufacturing	Sep	Index	59.5	59.9
Oct 1	11:00	*Fed's Harker Discusses the Economic Outlook*				
Oct 1	13:00	*Fed's Mester Discusses Inflation and Employment*				
Oct 1		Wards Total Vehicle Sales	Sep	Mlns	13.4	13.1
		Canada				
Sep 29	8:30	Industrial Product Price	Aug	M/M % Chg.	-	-0.4
Sep 30	6:00	CFIB Business Barometer	Sep	Index	-	67.1
Oct 1	8:30	Gross Domestic Product	Jul	M/M % Chg.	-	0.7
Oct 1	9:30	Markit Canada Manufacturing PMI	Sep	Index	-	57.2
		International				
Sep 29	19:50	JN Retail Sales	Aug	Y/Y % Chg.	-1.3	2.4
Sep 29	21:00	CH Manufacturing PMI	Sep	Index	50.2	50.1
Sep 29	21:45	CH Caixin China PMI Mfg	Sep	Index	49.5	49.2
Sep 30	2:00	UK Gross Domestic Product	2Q	Y/Y % Chg.	22.2	22.2
Sep 30	5:00	EZ Unemployment Rate	Aug	%	7.5	7.6
Sep 30	19:30	JN Jobless Rate	Aug	%	2.9	2.8
Sep 30	20:30	JN Jibun Bank Japan PMI Mfg	Sep	Index	-	51.2
Oct 1	4:00	EZ Markit Eurozone Manufacturing PMI	Sep	Index	58.7	58.7
Oct 1	4:30	UK Markit UK PMI Manufacturing SA	Sep	Index	56.3	56.3
Oct 1	5:00	EZ Consumer Price Index Estimate	Sep	Y/Y % Chg.	3.3	3.0

*Eastern Standard Time. Source: Bloomberg, TD Economics.