

The Weekly Bottom Line

June 17, 2022

Highlights

United States

- Equity markets did not take kindly to the Fed cranking up the heat on rate increases this week, with the S&P falling 6.3% on the week.
- The FOMC hiked rates by 75 basis points on Wednesday, the largest increase since 1994. It also dramatically moved up the number of rate hikes it is expecting to do over the next year.
- Meanwhile, U.S. economic data in May is showing that momentum is slowing in both new home construction and retail sales. These sectors are contending with higher interest rates and a shift in consumer preferences away from goods and towards services.

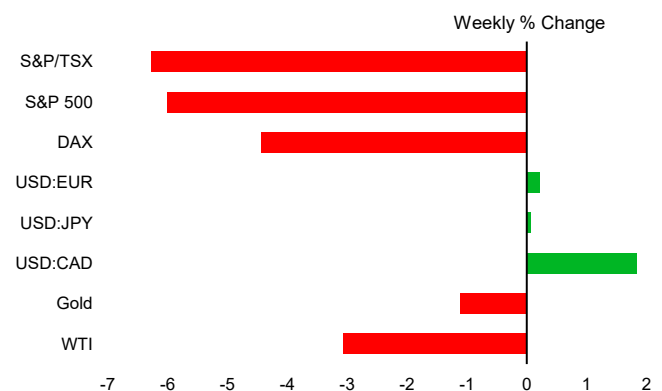
Canada

- Financial markets in Canada were volatile with equities declining on central bank repricing.
- The federal government laid out its plan to help Canadians most impacted by high inflation, though no net-new spending was tabled.
- Housing statistics showed a significant deterioration in demand, as sales and prices both dropped in May. This brought the sales-to-listing ratio further into a balanced market.

This Week in the Markets				
	Current*	Week Ago	52-Week High	52-Week Low
Stock Market Indexes				
S&P 500	3667	3901	4797	3667
S&P/TSX Comp.	19004	20275	22087	19004
DAX	13152	13762	16272	12832
FTSE 100	7105	7318	7672	6844
Nikkei	25963	27824	30670	24718
Fixed Income Yields				
U.S. 10-yr Treasury	3.21	3.16	3.47	1.17
Canada 10-yr Bond	3.38	3.35	3.62	1.12
Germany 10-yr Bund	1.67	1.52	1.76	-0.50
UK 10-yr Gilt	2.47	2.45	2.59	0.51
Japan 10-yr Bond	0.23	0.25	0.26	0.01
Foreign Exchange Cross Rates				
C\$ (USD per CAD)	0.77	0.78	0.81	0.77
Euro (USD per EUR)	1.05	1.05	1.19	1.04
Pound (USD per GBP)	1.23	1.23	1.40	1.20
Yen (JPY per USD)	134.5	134.4	135.5	109.0
Commodity Spot Prices**				
Crude Oil (\$US/bbl)	117.6	120.7	123.7	62.3
Natural Gas (\$US/MMBtu)	7.88	8.65	9.43	3.15
Copper (\$US/met. tonne)	9079.8	9447.3	11299.5	8894.0
Gold (\$US/troy oz.)	1850.9	1871.6	2050.8	1726.4

*As of 9:24 AM on Friday. **Oil-WTI, Cushing, Nat. Gas-Henry Hub, LA (Thursday close price). Copper-LME Grade A. Gold-London Gold Bullion. Source: Bloomberg.

Markets Volatile on Supersized Fed Hike



Note: Data as of 9:28 AM ET, Friday, June 17, 2022.
Source: Bloomberg, TD Economics.

Global Official Policy Rate Targets	
Central Banks	Current Target
Federal Reserve (Fed Funds Rate)	1.50 - 1.75%
Bank of Canada (Overnight Rate)	1.50%
European Central Bank (Refi Rate)	0.00%
Bank of England (Repo Rate)	1.25%
Bank of Japan (Overnight Rate)	-0.10%

Source: Bloomberg.

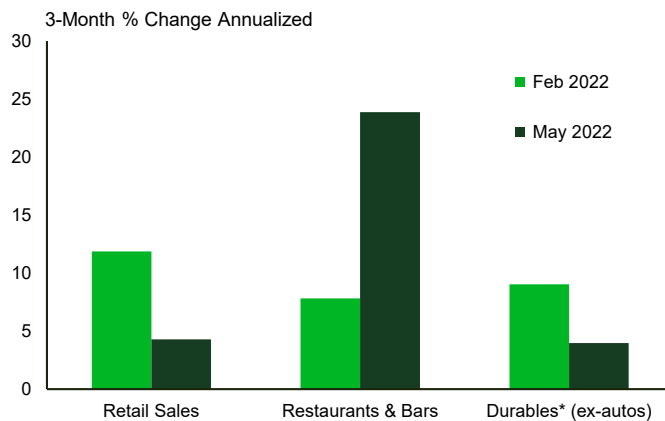
U.S. - FOMC Says Supersize Me

It has been a hectic week for financial markets with equities dropping 6.3% and bond yields rising as the Fed cranked up the heat on rate increases. At the same time, the latest data from housing and retailers showed evidence of cooling demand. And it's not just in the U.S. that central bankers are taking away the punchbowl. Central banks in England, Switzerland, New Zealand, and Hungary, also hiked rates this week. Meanwhile, the European Central Bank sought to stave off an emergent sovereign-debt crisis, by pledging to act to keep government bond yield spreads contained in highly indebted countries (Portugal, Italy, Greece & Spain) as interest rates rise.

The move up in U.S. yields was kicked off by a Wall Street Journal article on Monday that signaled that a 75-basis point hike was on the table for the FOMC after the sharp increase in May [CPI inflation](#) reported last Friday. The FOMC made good on those rumors with a supersized 75-basis point hike on Wednesday (see [details](#)). The median FOMC member expects the policy rate to reach 3.4% at the end of 2022, up from 1.9% at its March meeting, and 3.8% by the end of 2023 (up from 2.8%) (Chart 1). Approximately 50 bps of rate cuts are expected in 2024. The long-run neutral rate was assumed to be 2.5%, implying the Fed expects it will need to bring monetary policy a ways into restrictive territory to rein-in inflation from its 40-year highs.

The FOMC also downgraded its growth projections and expects the unemployment rate to start rising later this year as growth slows. The Fed's projections are truly the "goldilocks scenario" where they can engineer a perfectly

Chart 2: Spending on Retail Goods Cooling



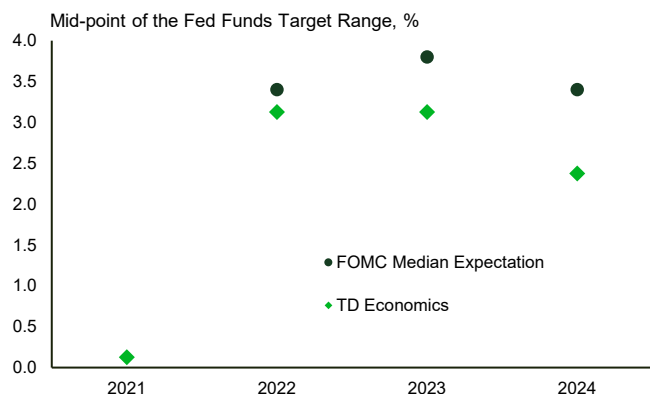
Source: TD Economics.

executed soft landing. The chances of this happening are very slim, and risks of missing to the downside are certainly growing. Market pricing for a recession over the next year currently sit at about one-third.

Indeed, economic data for May released this week showed signs that rate hikes are doing their work to slow economic growth. U.S. [housing starts](#) fell much further than expected, down 14% in May. While these are always a very volatile series on a month-to-month basis, building permits were also weaker reinforcing the expectation for starts to trend lower, following weakness in the resale market.

May [retail sales](#) came in weaker than expected, falling by 0.4% m/m. Sales in the two prior months were also revised lower. While the weak auto sales number earlier in the month already telegraphed a soft print on motor vehicle durables spending, weakness was evident across most major sub-categories after adjusting for inflation. This is consistent with our expectation that spending will shift away from goods consumers loaded up on in the pandemic towards services like concert tickets and vacations. Indeed looking at trends over the past three months, this shift is well underway (Chart 2), as spending on durable goods ex-autos – things like furniture and appliances – have downshifted, while spending on going out has accelerated. We will be publishing our updated economic forecast on Monday, which will feature an increase to our forecasts for interest rate hikes, alongside a slower growth trajectory for the economy.

Chart 1: Fed Maps an Aggressive Course for Rate Hikes



Source: FOMC Summary of Economic Projections - March 2022, TD Economics.

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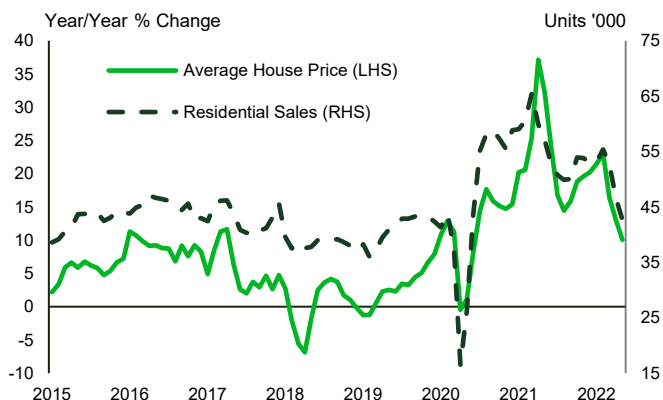
Canada - Market Volatility Spikes, While Housing Cools

It was a wild week in financial markets as changing expectations for interest rates and inflation cloud the economic outlook. Volatility was apparent in money markets, as investors priced greater odds of a 75 basis point hike by the Bank of Canada at its July meeting – following the Fed's supersized move on Wednesday. Fears over higher interest rates spread to equity markets, as the TSX dropped around 6% this week (Chart 1)!

We also heard from Deputy Prime Minister and Finance Minister Chrystia Freeland, who outlined financial supports for Canadians struggling with high inflation. The support comes under the government's Affordability Plan, which will augment the Canada Workers Benefit, increase Old Age Security, give a Housing Affordability Payment to low-income Canadians, amongst other initiatives. As none of this is net new spending from previously announced policy, the government's focus is clearly on not adding to inflationary pressures through new expenditures.

On the data front, housing statistics were closely watched, with sales and prices continuing their decline in May. Canadian existing home sales dropped 8.6% month-over-month (m/m), reaching their lowest levels since June 2020. Declines were recorded across nearly every province, with B.C. (-16.3% m/m), Alberta (-10.5%), and Ontario (-9.9%) leading the way. While sales pulled back, new listings increased by 4.5% m/m, pushing the sales-to-new-listings ratio down into balanced territory at 57.5%. At the

Chart 2: Housing Sales and Prices Drop



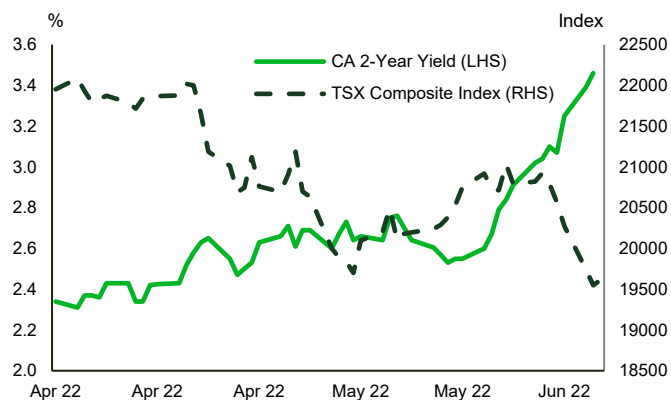
Source: CREA, TD Economics. Last observation: May 2022.

same time, the number of months of inventory jumped to 2.7 months. Though this is an improvement, it is still well below historical norms. This more balanced market helped the Canadian average home price to fall by 3.8% m/m. The biggest declines were in the high-priced markets in B.C. (-4.7%) and Ontario (-2.5%).

Though it is quite clear that current home sales and prices are being hit by higher interest rates, the pipeline of new homes is still supported by past housing strength. In fact, Canadian housing starts grew by 8% m/m in May. This was driven by the multi-family segment (+13% m/m), though the single-detached category also rose in May (4% m/m). Given the low inventory and high rate of family formation, a continuation of building will be a welcomed development.

Finally, the national balance sheet data for the first quarter of 2022 came out on Monday. This data showed the household debt-to-income ratio fell to 182.5%, as income gains rose more than debt accumulation. This caused the ratio of debt payments to disposable income to fall to 13.5%. Net worth also rose in Q1, as the final surge in house prices supported overall wealth gains. Given the deterioration in financial market assets and real estate values since Q1, we expect a significant drop in wealth for Q2. Additionally, higher interest rates are likely to cause a big rise in debt service ratios through the remainder of this year.

Chart 1: Market Volatility Heightened on Higher Rates



Source: BoC, WSJ, TD Economics.

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Recent Key Economic Indicators: Jun 13 - 17, 2022					
Release Date	Economic Indicator/Event	Data for Period	Units	Current	Prior
United States					
Jun 14	NFIB Small Business Optimism	May	Index	93.1	93.2
Jun 14	PPI Ex Food and Energy	May	M/M % Chg.	0.5	0.2
Jun 14	PPI Final Demand	May	M/M % Chg.	0.8	0.4
Jun 15	Empire Manufacturing	Jun	Index	-1.2	-11.6
Jun 15	Retail Sales Advance	May	M/M % Chg.	-0.3	0.7
Jun 15	Retail Sales Ex Auto and Gas	May	M/M % Chg.	0.1	0.8
Jun 15	Business Inventories	Apr	M/M % Chg.	1.2	2.4
Jun 15	NAHB Housing Market Index	Jun	Index	67.0	69.0
Jun 15	FOMC Rate Decision (Upper Bound)	Jun 15	%	1.75	1.00
Jun 15	Interest on Reserve Balances Rate	Jun 16	%	1.7	0.9
Jun 16	Building Permits	May	Thsd	1695.0	1823.0
Jun 16	Housing Starts	May	Thsd	1549.0	1810.0
Jun 16	Initial Jobless Claims	Jun 11	Thsd	229.0	232.0
Jun 17	Capacity Utilization	May	%	79.0	79.0
Jun 17	Industrial Production	May	M/M % Chg.	0.2	1.1
Jun 17	Manufacturing (SIC) Production	May	M/M % Chg.	-0.1	0.8
Canada					
Jun 14	Manufacturing Sales	Apr	M/M % Chg.	1.7	3.5
Jun 15	Housing Starts	May	Thsd	287.3	265.7
Jun 15	Existing Home Sales	May	M/M % Chg.	-8.6	-12.6
Jun 16	Wholesale Trade Sales	Apr	M/M % Chg.	-0.5	0.3
Jun 17	Industrial Product Price	May	M/M % Chg.	1.7	0.8
International					
Jun 13	UK Monthly Gross Domestic Product (3M/3M)	Apr	M/M % Chg.	0.2	0.8
Jun 14	UK ILO Unemployment Rate 3 Months	Apr	%	3.6	3.7
Jun 14	CH Retail Sales	May	Y/Y % Chg.	-6.7	-11.1
Jun 14	CH Surveyed Jobless Rate	May	%	5.9	6.1
Jun 16	UK Bank of England Bank Rate	Jun 16	%	1.25	1.00
Jun 16-17	JN BOJ Policy Balance Rate	Jun 17	%	-0.10	-0.10
Jun 17	EZ Consumer Price Index	May	Y/Y % Chg.	8.1	7.4

Source: Bloomberg, TD Economics.

Upcoming Economic Releases and Events: Jun 20 - 24, 2022						
Release Date	Time*	Economic Indicator/Event	Data for Period	Units	Consensus Forecast	Last Period
United States						
Jun 20	12:45	<i>Fed's Bullard Discusses Inflation and Interest rates</i>				
Jun 21	10:00	Existing Home Sales	May	Mlns	5.40	5.61
Jun 21	12:00	<i>Fed's Mester Speaks at Women in Leadership Event</i>				
Jun 21	15:30	<i>Fed's Barkin Speaks in Richmond</i>				
Jun 22	9:30	<i>Powell Delivers Semi-Annual Testimony Before Senate Panel</i>				
Jun 22	12:50	<i>Fed's Evans Discusses Economic Outlook</i>				
Jun 22	13:30	<i>Fed's Harker and Barkin Discuss the Economic Outlook</i>				
Jun 23	8:30	Initial Jobless Claims	Jun 18	Thsd	232.0	229.0
Jun 23	9:45	S&P Global US Composite PMI	Jun	Index	-	53.6
Jun 23	9:45	S&P Global US Manufacturing PMI	Jun	Index	56.3	57.0
Jun 23	9:45	S&P Global US Services PMI	Jun	Index	53.5	53.4
Jun 23	10:00	<i>Powell Testifies Before House Financial Services Panel</i>				
Jun 24	7:30	<i>Fed's Bullard Discusses Central banks and Inflation</i>				
Jun 24	10:00	New Home Sales	May	Thsd	595.0	591.0
Jun 24	16:00	<i>Fed's Daly Speaks at Shadow Open Market Conference</i>				
Canada						
Jun 21	8:30	Retail Sales	Apr	M/M % Chg.	-	0.0
Jun 21	8:30	Retail Sales Ex Auto	Apr	M/M % Chg.	-	2.4
Jun 22	8:30	Consumer Price Index	May	Y/Y % Chg.	-	6.8
Jun 22	8:30	Consumer Price Index NSA	May	M/M % Chg.	-	0.6
Jun 22	10:40	<i>BoC's Carolyn Rogers, Senior Deputy Governor, Gives Remarks at Canadian Banking Event</i>				
Jun 24	8:30	Payroll Employment Change - SEPH	Apr	Thsd	-	118.1
International						
Jun 22	2:00	UK Consumer Price Index	May	Y/Y % Chg.	9.1	9.0
Jun 22	20:30	JN Jibun Bank Japan PMI Manufacturing	Jun	Index	-	53.3
Jun 23	19:30	JN National Consumer Price Index	May	Y/Y % Chg.	2.5	2.5
Jun 24	2:00	UK Retail Sales Ex Auto Fuel	May	Y/Y % Chg.	-5.1	-6.1

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

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