The Weekly Bottom Line

April 23, 2021

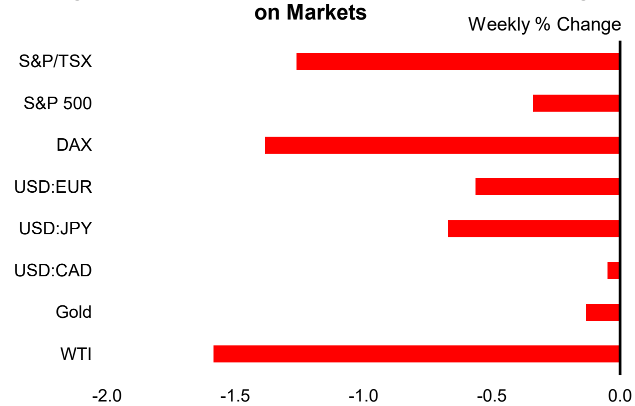
Highlights

- Without much noteworthy economic data this week, market sentiment soured on a leaked Biden administration proposal to raise the maximum tax rate on capital gains of high-income taxpayers.
- First quarter GDP data and a rate announcement from the Federal Reserve are also on the docket next week. Growth in the first half of this year is coming in faster than we expected, raising the risk of earlier Fed hikes.
- An increase in shipping costs and shortages of key manufacturing inputs have reminded us of the vulnerabilities of relying too much on efficient rather than resilient supply chains.
- Supply-side bottlenecks are likely to increase cost-push inflation in the near-term. While shortening supply chains will make businesses less vulnerable, it could also push up prices in the medium to long-term.

This Week in the Markets	Current*	Week Ago	52-Week High	52-Week Low
Stock Market Indexes				
S&P 500	4170	4185	4185	2798
S&P/TSX Comp.	19098	19351	19351	14251
DAX	15252	15460	15460	10336
FTSE 100	6927	7020	7020	5577
Nikkei	29021	29683	30468	19262
Fixed Income Yields				
U.S. 10-yr Treasury	1.57	1.58	1.74	0.51
Canada 10-yr Bond	1.52	1.54	1.61	0.43
Germany 10-yr Bund	-0.26	-0.26	-0.23	-0.64
UK 10-yr Gilt	0.75	0.76	0.88	0.08
Japan 10-yr Bond	0.07	0.09	0.16	-0.04
Foreign Exchange Cross Rates				
C$ (USD per CAD)	0.80	0.80	0.81	0.71
Euro (USD per EUR)	1.21	1.20	1.23	1.08
Pound (USD per GBP)	1.38	1.38	1.41	1.21
Yen (JPY per USD)	108.1	108.8	110.7	102.7
Commodity Spot Prices**				
Crude Oil ($US/bbl)	61.6	63.1	66.1	12.3
Natural Gas ($US/MMBtu)	2.69	2.62	15.83	1.35
Copper ($US/met. tonne)	9421.4	9227.0	9459.5	5081.0
Gold ($US/troy oz.)	1775.8	1776.5	2063.5	1683.5

*As of 11:12 AM on Friday. **Oil-WTI, Cushing, Nat. Gas-Henry Hub, LA (Thursday close price). Copper-LME Grade A. Gold-London Gold Bullion. Source: Bloomberg.

Rising Covid-19 Infections and Potential Tax Hikes Weigh on Markets



Note: Data as of 11:00 AM ET, Friday, April 23, 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			
	4/23/21	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	0.15	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	1.57	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	2.25	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.

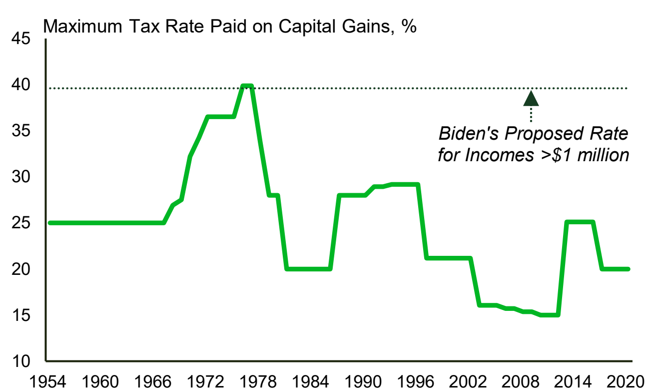
U.S. – Big Events Next Week Drive Markets

Without much noteworthy economic data this week, market sentiment took its cue from policy announcements that are expected next week from the Biden administration. Sentiment seemingly soured on the news that the spending under the American Families Plan will be funded by tax hikes on higher income taxpayers. President Biden had outlined his intention to raise taxes on higher incomes in his campaign platform (see details). Particularly relevant for investors is the proposal to tax capital gains at 39.6% (up from 20%) for people with incomes above $1 million, which would be the same rate as the top marginal rate on income under Biden's proposals (Chart 1). That would match the late 1970s, the highest rate historically, however, Bloomberg estimates this would only affect about 0.3% of the population.

These changes need to be passed by Congress, and so will either require Republican support or budget reconciliation. The latter is more likely, and therefore the support of moderate Dems, like Joe Manchin and Kyrsten Sinema, may mean tax hikes could be watered down before they are passed. The White House is still finalizing the details of its plan. The key spending items will likely include funding for platform promises like: paid family leave, child care, universal pre-K and free community college.

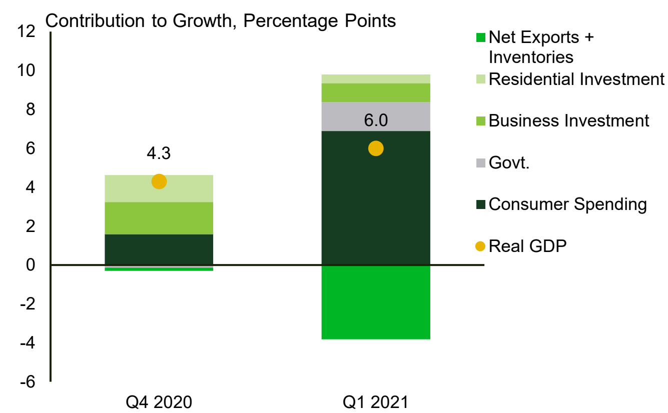
There is also some big economic news coming next week: first quarter GDP and a Federal Reserve interest rate announcement. We expect economic growth to accelerate to a 6% annualized pace in Q1, up from 4.3% in Q4 (Chart 2). This acceleration will be largely due to jump up in consumer spending – from 2.3% in Q4 to 10% in Q1. The second wave of Covid-19 infections and associated restrictions had held back spending at the end of 2020, but fiscal stimulus that has come in two waves over the course of Q1 has boosted spending. Recall eligible Americans received $600 payments back in January, and a further $1400 in late March. We have seen in retail sales and high-frequency data that consumers haven't hesitated to spend these windfalls.

Chart 1: Biden Proposes Tax Hike on Capital Gains for Millionaires



Source: U.S. Treasury, TD Economics.

Chart 2: Consumers to Drive Faster Growth in Q1



Personal income and spending details for March will also be released on Friday, which will tell us a lot about momentum heading into Q2. We expect it to be healthy. Overall, growth in the first half of the year is tracking better than we expected in March, and on its own is enough to raise 2021 real GDP growth forecast from 5.7% to 6.2%.

This upgrade to economic growth raises the risk the Fed will hike rates sooner than we expected in March. So we will be listening very closely to how Chair Powell talks about the outlook on Wednesday. This is not a meeting with a summary of economic projections but shifts in messaging will be closely parsed. We will be publishing Dollars and Sense next week – so stay tuned for our updated view on the Federal Reserve.

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Global - Supply Chain Disruptions Are Harbingers of the Future

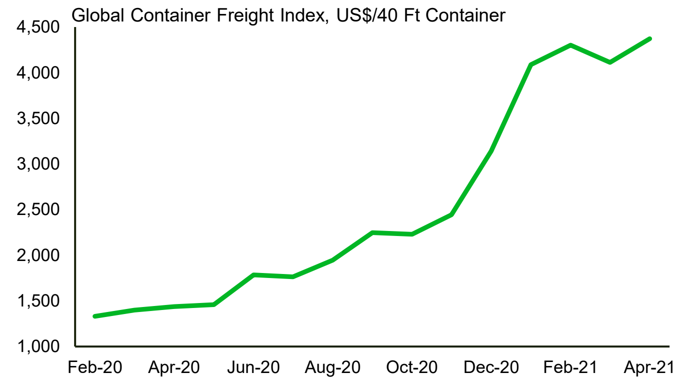
The pandemic has laid bare the vulnerabilities of relying too much on efficient rather than resilient supply chains. Rising shipping costs and shortages of key manufacturing inputs have once again reminded us of the fragility of the global trading system.

For context, lets start with developments in 2020. In the first half of last year, thousands of empty shipping containers were left stranded on European and American shores due to lockdowns. In the second half of 2020, European and American demand for Asian-made goods rebounded. This led to a sharp rise in freight rates. Why? Because too much money was chasing too few containers! In fact, the cost of shipping between China and Europe hit a record high late last year on the back of recovery in consumer demand and container shortages.

Fast forward to 2021. The Suez canal incident further exacerbated container shortages. The canal's blockage prevented its usage by other cargo ships, some of which were forced to take longer and costlier detours. This delayed the arrival of containers at their destinations and contributed to a temporary increase in shipping costs which are already more than three times the level a year ago (Chart 1). The Suez Canal carries over 10% of global trade. The six-day incident held up almost $60 billion ($9.6 billion each day) of global trade. The long-term trade impact of these disruptions is likely to be small given that the global trade in goods amounts to roughly $18 trillion a year. However, the delays will have a domino effect, which will reverberate across global supply chains for months to come.

To make matters worse, a recovery in global demand has contributed to a shortage of microchips and semiconductors. A blaze in one of the world's leading auto chip makers in Japan and an uncharacteristically cold winter in southern U.S. added fuel to the fire. A drought in Taiwan further threatens to slowdown chip production since large quantities of water are used in the process. If that wasn't enough, U.S.-China tensions and concerns of a prolonged shortage have pushed Chinese companies to stockpile supplies. These developments have been especially problematic for the auto industry, which had already slashed production due to a semiconductor shortage. It doesn't stop there. A global chip shortage has also hampered production of other durables such as home appliances and computers.

Chart 1: Shipping Costs in Choppy Waters



Note: The chart shows the last weekly value for each month. For April 2021, the last value is from April 23.
Source: Freightos, TD Economics.

As a result, businesses are faced with high supplier delivery times and low inventories. Consumer demand is likely to jump as restrictions are eased, but logistical bottlenecks will keep a lid on supply. This could further increase costs for businesses. What this means for consumer price inflation depends on how much of the increase in costs is passed on. Businesses have two options:

1. Pass on all or part of the increase in input costs to consumers. This approach would increase (cost-push) inflation. But businesses are faced with a trade-off. Such an approach could prompt consumers to switch demand to other businesses who don't pass on the costs to consumers.
2. Businesses absorb the increase in costs. This approach would lower business profits but have little to no impact on inflation. The upside to this approach is that consumer demand for goods produced by businesses that absorb costs will remain stable. It may even increase, depending on how much of their excess savings households unleash.

The impact of supply chain disruptions will also be felt in the medium to long-term. Businesses are already reshoring and shortening their supply chains. This makes them less vulnerable to future supply chain disruptions. But it would also reduce their access to cheaper inputs from other parts of the world. It would also entail higher costs for consumers. Exporters would also become less competitive as they would have to rely on more expensive domestic inputs rather than cheaper foreign inputs.

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Release Date		Economic Indicator/Event	Data for Period	Units	Current	Prior
Recent Key Economic Indicators: Apr 19 - 23, 2021						
United States						
Apr 22		Initial Jobless Claims	Apr 17	Thsd	547.0	586.0
Apr 22		Existing Home Sales	Mar	Mlns	6.01	6.24
Apr 23		Markit US Manufacturing PMI	Apr	Index	60.6	59.1
Apr 23		Markit US Services PMI	Apr	Index	63.1	60.4
Apr 23		New Home Sales	Mar	Thsd	1021.0	846.0
Canada						
Apr 19		Housing Starts	Mar	Thsd	335.2	275.6
Apr 20		Teranet/National Bank HPI	Mar	Y/Y % Chg.	10.8	9.8
Apr 21		Consumer Price Index	Mar	Y/Y % Chg.	2.2	1.1
Apr 21		Consumer Price Index NSA	Mar	M/M % Chg.	0.5	0.5
Apr 21		Bank of Canada Rate Decision	Apr 21	%	0.25	0.25
International						
Apr 20	UK	ILO Unemployment Rate 3Mths	Feb	%	4.9	5.0
Apr 21	UK	Consumer Price Index	Mar	Y/Y % Chg.	0.7	0.4
Apr 22	EZ	ECB Main Refinancing Rate	Apr 22	%	0.00	0.00
Apr 22	JN	Natl Consumer Price Index	Mar	Y/Y % Chg.	-0.2	-0.4
Apr 22	JN	Jibun Bank Japan PMI Mfg	Apr	Index	53.3	52.7
Apr 23	UK	Retail Sales Ex Auto Fuel	Mar	Y/Y % Chg.	7.9	-1.0
Apr 23	EZ	Markit Eurozone Manufacturing PMI	Apr	Index	63.3	62.5
Apr 23	UK	Markit UK PMI Manufacturing SA	Apr	Index	60.7	58.9

Source: Bloomberg, TD Economics.

Upcoming Economic Releases and Events: Apr 26 - 30, 2021							
Release Date	**Time***		**Economic Indicator/Event**	**Data for Period**	**Units**	**Consensus Forecast**	**Last Period**
United States							
Apr 26	8:30		Cap Goods Orders Nondef Ex Air	Mar	M/M % Chg.	1.5	-0.9
Apr 26	8:30		Durable Goods Orders	Mar	M/M % Chg.	2.3	-1.2
Apr 27	9:00		S&P CoreLogic CS US HPI NSA	Feb	Y/Y % Chg.	-	11.2
Apr 27	10:00		Conf. Board Consumer Confidence	Apr	Index	112.0	109.7
Apr 28	8:30		Advance Goods Trade Balance	Mar	Blns	-87.5	-86.7
Apr 28	14:00		FOMC Rate Decision (Upper Bound)	Apr 28	%	0.25	0.25
Apr 28	14:30		*Powell Holds Press Conference Following FOMC Meeting*				
Apr 29	8:30		Core Personal Consumption Expenditure	1Q	Q/Q % Chg.	1.6	1.3
Apr 29	8:30		Gross Domestic Product Annualized	1Q	Q/Q % Chg.	6.6	4.3
Apr 29	8:30		Initial Jobless Claims	Apr 24	Thsd	555.0	547.0
Apr 29	8:30		Personal Consumption	1Q	Q/Q % Chg.	10.5	2.3
Apr 29	10:00		Pending Home Sales	Mar	M/M % Chg.	4.5	-10.6
Apr 29	11:00		*Fed's Quarles Discusses Financial Regulation*				
Apr 30	8:30		Employment Cost Index	1Q	Q/Q % Chg.	0.7	0.7
Apr 30	8:30		Personal Consumption Expenditure Deflator	Mar	Y/Y % Chg.	2.3	1.6
Apr 30	8:30		Personal Income	Mar	M/M % Chg.	20.1	-7.1
Apr 30	8:30		Real Personal Spending	Mar	M/M % Chg.	3.5	-1.2
Canada							
Apr 28	8:30		Retail Sales	Feb	M/M % Chg.	-	-1.1
Apr 28	8:30		Retail Sales Ex Auto	Feb	M/M % Chg.	-	-1.2
Apr 29	6:00		CFIB Business Barometer	Apr	Index	-	68.2
Apr 27	16:00		*BoC's Macklem Makes an Appearance in a Webinar about Finance*				
Apr 30	8:30		Gross Domestic Product	Feb	M/M % Chg.	-	0.7
Apr 30	8:30		Industrial Product Price	Mar	M/M % Chg.	-	2.6
International							
Apr 27	19:50	JN	Retail Sales	Mar	Y/Y % Chg.	4.6	-1.5
Apr 27		JN	BOJ Policy Balance Rate	Apr 27	%	-0.10	-0.10
Apr 29	19:30	JN	Jobless Rate	Mar	%	2.9	2.9
Apr 29	19:30	JN	Tokyo Consumer Price Index	Apr	Y/Y % Chg.	-0.2	-0.2
Apr 29	20:30	JN	Jibun Bank Japan PMI Mfg	Apr	Index	-	53.3
Apr 29	21:00	CH	Manufacturing PMI	Apr	Index	51.7	51.9
Apr 30	5:00	EZ	Consumer Price Index Estimate	Apr	Y/Y % Chg.	1.6	1.3
Apr 30	5:00	EZ	Gross Domestic Product SA	1Q	Y/Y % Chg.	-2.0	-4.9
Apr 30	5:00	EZ	Unemployment Rate	Mar	%	8.3	8.3
Apr 30	7:00	MX	GDP NSA	1Q	Y/Y % Chg.	-3.1	-4.3

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

Disclaimer