

The Weekly Bottom Line

August 4, 2023

Highlights

United States

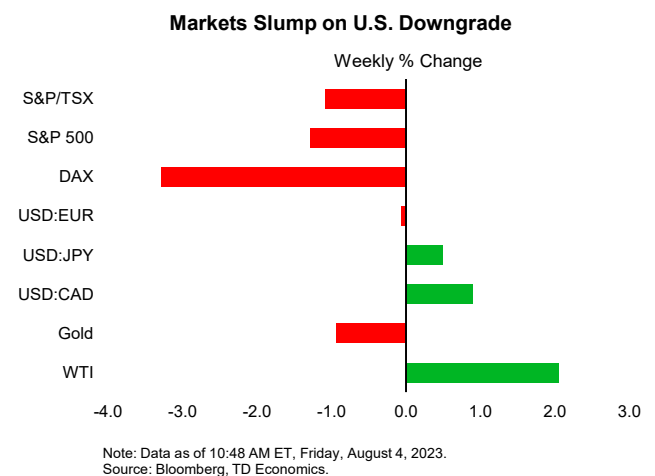
- Fitch became the second major credit rating agency to downgrade the U.S. from the top AAA rating, citing the growing fiscal debt burden and an erosion in governance.
- The U.S. economy added 187k new jobs in July, representing the slowest pace of hiring in over two years.
- The Federal Reserve's Senior Loan Officer Opinion Survey showed credit standards tightened across the board in the second quarter, weighing on loan demand.

Canada

- The Canadian economy shed employment in July, pointing to looser labour market conditions. Wage growth accelerated on the month but is expected to normalize in the coming months.
- Our internal data suggests that Canadian families tightened their purses in June. All in, it looks like personal consumption expenditures are poised to decelerate notably in the second quarter.
- With employment and consumption shifting into a lower gear, the Bank of Canada will feel less pressure to hike again.

This Week in the Markets				
	Current*	Week Ago	52-Week High	52-Week Low
Stock Market Indexes				
S&P 500	4528	4582	4589	3577
S&P/TSX Comp.	20195	20519	20767	18206
DAX	15852	16470	16470	11976
FTSE 100	7509	7694	8014	6826
Nikkei	32193	32759	33753	25717
Fixed Income Yields				
U.S. 10-yr Treasury	4.11	3.95	4.24	2.69
Canada 10-yr Bond	3.60	3.52	3.71	2.67
Germany 10-yr Bund	2.58	2.49	2.75	0.80
UK 10-yr Gilt	4.41	4.33	4.66	1.89
Japan 10-yr Bond	0.65	0.57	0.65	0.17
Foreign Exchange Cross Rates				
C\$ (USD per CAD)	0.75	0.76	0.78	0.72
Euro (USD per EUR)	1.10	1.10	1.12	0.96
Pound (USD per GBP)	1.28	1.29	1.31	1.07
Yen (JPY per USD)	141.7	141.2	150.2	127.9
Commodity Spot Prices**				
Crude Oil (\$US/bbl)	81.6	80.4	97.0	66.7
Natural Gas (\$US/MMBtu)	2.48	2.53	9.84	1.77
Copper (\$US/met. tonne)	8570.5	8625.5	9330.8	7422.0
Gold (\$US/troy oz.)	1946.4	1959.5	2050.3	1622.4

*As of 9:37 AM on Friday. **Oil-WTI, Cushing, Nat. Gas-Henry Hub, LA (Thursday close price). Copper-LME Grade A. Gold-London Gold Bullion. Source: Bloomberg.



Global Official Policy Rate Targets	
Central Banks	Current Target
Federal Reserve (Fed Funds Rate)	5.25 - 5.50%
Bank of Canada (Overnight Rate)	5.00%
European Central Bank (Refi Rate)	4.25%
Bank of England (Repo Rate)	5.25%
Bank of Japan (Overnight Rate)	-0.10%

Source: Bloomberg.

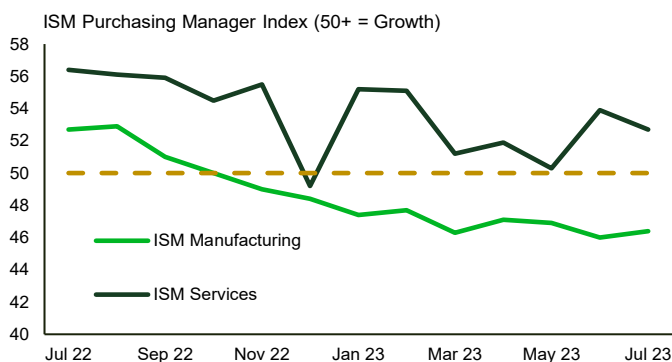
U.S. – Tighter Credit Weighs on Resilience

Nearly twelve years to the day of the first U.S. credit rating downgrade in 2011, Fitch became the second major rating agency to lower its evaluation of the government's credit-worthiness. Fitch's rationale was related to growing fiscal deficits in the near-term, medium-term fiscal challenges stemming from aging demographics, and a multi-decade erosion of governance. Since the decision was announced on Tuesday, Treasury yields rose and equities fell, with the ten-year Treasury up 11 basis-points (bps) and the S&P 500 down 1.8% as of the time of writing. Broader implications are expected to be muted as the U.S. economy continues to have strong fundamentals, however it comes at a time when credit standards are already tight.

Monday's Federal Reserve's Senior Loan Officer Opinion Survey (SLOOS) showed that a significant share of banks had tightened business and consumer lending standards in the second quarter. Unsurprisingly, demand for most loan types fell over the period, with the only exception being credit card loans, which saw no change in demand. The economy is clearing feeling the effects of the rapid rise in interest rates over the past 17 months.

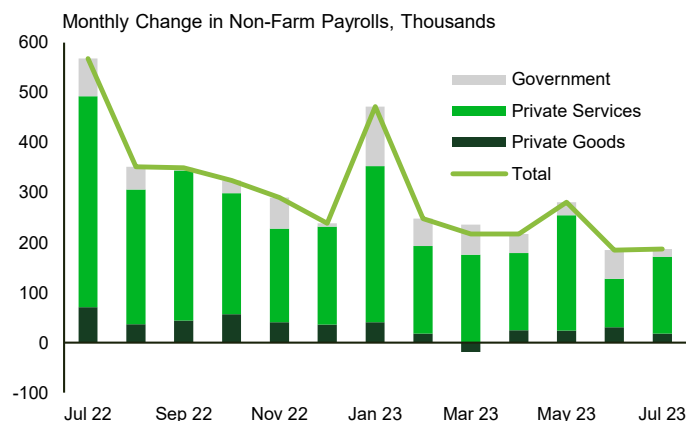
Despite tightening credit conditions, pockets of resilience remain. The ISM PMI data this week continued to show a notable divergence between the manufacturing and service sectors, with the former contracting for a ninth consecutive month and the latter expanding for a seventh straight month in July (Chart 1). Employment growth in both sectors slowed last month, but the services sector is still creating jobs as demand remains robust, whereas the manufacturing

Chart 1: U.S. Manufacturing Remains in Decline, Services Strength Easing



Source: ISM, TD Economics.

Chart 2: U.S. Job Gains Slowing Gradually



Source: U.S. Bureau of Labor Statistics, TD Economics.

employment subindex hit its lowest level in three years.

Looking more closely at the most recent labor market update, 187k jobs were created in July, which along with the revised reading for June, represent the slowest pace of job creation in over two years (Chart 2). While this puts job growth on a more sustainable footing, the labor market remains tight, as evidenced by the 4.4% year-on-year(y/y) growth in average weekly earnings in July. The moderation in hiring will be seen as a positive development by the Federal Reserve, but it is unlikely that they will take the prospect of further policy tightening off table until the sustainability of the trend is determined.

The Fed will get another important indicator next week in the form of the CPI inflation reading for July. June's print showed core CPI fell below 5% y/y for the first time since December 2021 and the Federal Reserve will be looking to see further progress. With preliminary evidence that the cumulative effects of past rate hikes are working to cool inflationary pressures, we expect that the FOMC will leave the policy rate unchanged when they meet in September. However, they are likely to continue to emphasize the importance of incoming data on determining the future path of interest rates as the ultimate form of 'landing' for the economy becomes clearer.

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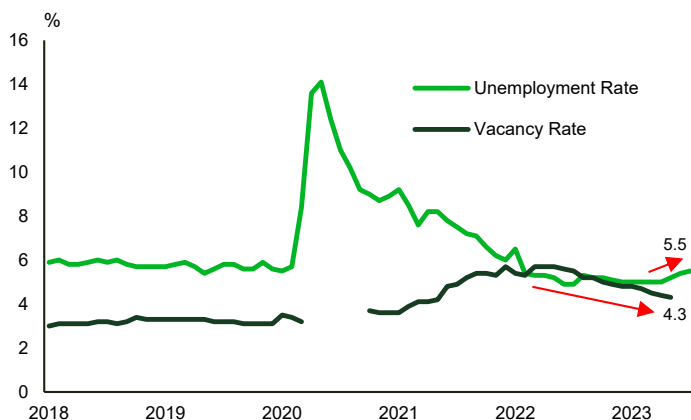
Canada – Shifting Into Lower Gear

The weather cooled this week and so did the economy. A negative employment surprise helped prop the S&P TSX Index, which had suffered a steep selloff throughout the week, finishing 1.5% lower (at the time of writing). The 5-year Government of Canada Bond yield move lower, as financial markets recalibrated the expected probability of another Bank of Canada rate hike in September from 30% to 25%.

Canada's economy [shed 6k jobs in July](#), missing consensus forecast for 25k growth. Smoothing out the employment numbers over the peaks and valleys of the last three months, provides good evidence of cooling in the labour market: the three-month average change in employment moved decisively below the pre-pandemic average. Likewise, the unemployment rate ticked up to 5.5%, marking a third consecutive month of increases. The speed of the increase in the unemployment rate (half a percent in three months) suggests that a cooling trend is starting to take hold in the job market, even as the level of unemployment rate remains below the 2019 average. The vacancy rate (the share of unfilled positions relative to total number of vacancies) has also been on the downward trend since May 2022, shedding 1.4 percentage points over the course of the last year (Chart 1).

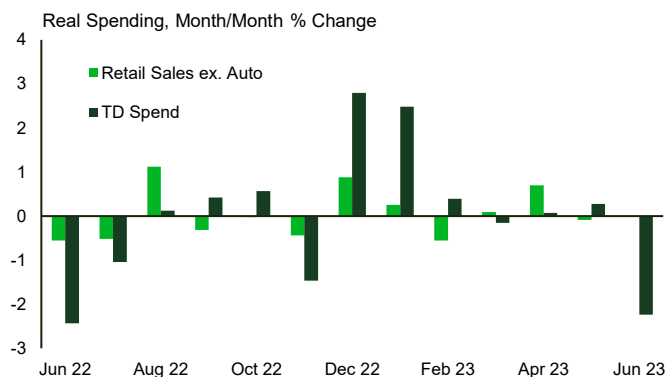
However, wage growth moved in the wrong direction. Average hourly earnings growth accelerated relative to the previous month, increasing by 5.0% over the past year. This is good news for consumer purchasing power, but bad news for inflation dynamics. Typically, looser labour conditions

Chart 1: Canada's Job Market Is Cooling



Source: Statistics Canada, TD Economics.
Last observations: Unemployment Rate - July 2023, Vacancy Rate - May 2023.

Chart 2: Canadian Consumers Are Tightening Purse Strings



Source: Statistics Canada, TD Economics.

should be followed by slower wage growth with a bit of a lag. We expect wage growth will step back on the downward trend as the labour market cools further in the months ahead, helping to turn the heat down on inflation.

Another sign that the economy is shifting into lower gear is consumer spending. According to our internal card spending data, Canadian families tightened their purse strings in June, spending 2% less than a month prior, with sales up 1.6% versus a year ago, down from a 1.8% pace in May (Chart 2). The series are understandably volatile and affected by TD's geographic concentration, but they usually offer a good directional guide for retail spending and personal consumption expenditures. A closer look at this data shows that the higher cost of living and rising interest rates are starting to catch up with consumers, as discretionary items, such as travel and entertainment were low on consumers' shopping list in June.

With recent data incorporated, real consumption is expected to slow to below 1% in Q2 from an impressive 5.7% growth in Q1 2023. This is good news for the Bank of Canada, as it lowers the pressure for it to hike again at the time when cumulative hikes are starting to play a more prominent role in stemming consumer demand. We expect that the Bank will remain on pause for the rest of the year.

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Recent Key Economic Indicators: Jul 31 - Aug 04, 2023					
Release Date	Economic Indicator/Event	Data for Period	Units	Current	Prior
United States					
Aug 01	Wards Total Vehicle Sales	Jul	Mlns	15.7	15.7
Aug 01	S&P Global US Manufacturing PMI	Jul	Index	49.0	49.0
Aug 01	ISM Manufacturing	Jul	Index	46.4	46.0
Aug 02	ADP Employment Change	Jul	Thsd	324.0	455.0
Aug 03	Initial Jobless Claims	Jul 29	Thsd	227.0	221.0
Aug 03	Unit Labor Costs	2Q	Q/Q % Chg.	1.6	3.3
Aug 03	S&P Global US Composite PMI	Jul	Index	52.0	52.0
Aug 03	S&P Global US Services PMI	Jul	Index	52.3	52.4
Aug 03	Cap Goods Orders Nondef Ex Air	Jun	M/M % Chg.	0.1	0.2
Aug 03	Durable Goods Orders	Jun	M/M % Chg.	4.6	4.7
Aug 03	Factory Orders	Jun	M/M % Chg.	2.3	0.4
Aug 03	Factory Orders Ex Trans	Jun	M/M % Chg.	0.2	-0.4
Aug 03	ISM Services Index	Jul	Index	52.7	53.9
Aug 04	Average Hourly Earnings	Jul	M/M % Chg.	0.4	0.4
Aug 04	Change in Nonfarm Payrolls	Jul	Thsd	187.0	185.0
Aug 04	Unemployment Rate	Jul	%	3.5	3.6
Canada					
Aug 01	S&P Global Canada Manufacturing PMI	Jul	Index	49.6	48.8
Aug 04	Net Change in Employment	Jul	Thsd	-6.4	59.9
Aug 04	Unemployment Rate	Jul	%	5.5	5.4
International					
Jul 31	EZ Consumer Price Index Estimate	Jul	Y/Y % Chg.	5.3	5.5
Jul 31	EZ Gross Domestic Product SA	2Q	Y/Y % Chg.	0.6	1.1
Jul 31	JN Jobless Rate	Jun	%	2.5	2.6
Jul 31	JN Jibun Bank Japan PMI Mfg	Jul	Index	49.6	49.4
Jul 31	CH Caixin China PMI Mfg	Jul	Index	49.2	50.5
Aug 01	EZ Unemployment Rate	Jun	%	6.4	6.4
Aug 03	UK Bank of England Bank Rate	Aug 03	%	5.25	5.00
Aug 04	EZ Retail Sales	Jun	Y/Y % Chg.	-1.4	-2.4

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

Upcoming Economic Releases and Events: Aug 07 - 11, 2023						
Release Date	Time*	Economic Indicator/Event	Data for Period	Units	Consensus Forecast	Last Period
United States						
Aug 07	8:30	<i>Fed's Bostic & Bowman Speak at Fed Listens Event</i>				
Aug 08	6:00	NFIB Small Business Optimism	Jul	Index	90.5	91.0
Aug 08	8:15	<i>Fed's Harker Speaks on Economic Outlook in Philadelphia</i>				
Aug 08	8:30	Trade Balance	Jun	Blns	-65.0	-69.0
Aug 08	10:00	Wholesale Trade Sales	Jun	M/M % Chg.	-	-0.2
Aug 10	8:30	Initial Jobless Claims	Aug 05	Thsd	-	227.0
Aug 10	8:30	Consumer Price Index	Jul	M/M % Chg.	0.2	0.2
Aug 10	8:30	Consumer Price Index Ex Food and Energy	Jul	M/M % Chg.	0.2	0.2
Aug 10	8:30	Consumer Price Index	Jul	Y/Y % Chg.	3.3	3.0
Aug 10	8:30	Consumer Price Index Ex Food and Energy	Jul	Y/Y % Chg.	4.8	4.8
Aug 10	15:00	<i>Fed's Bostic Gives Remarks at Event About Employment</i>				
Aug 11	8:30	PPI Final Demand	Jul	M/M % Chg.	0.2	0.1
Aug 11	8:30	PPI Ex Food and Energy	Jul	M/M % Chg.	0.2	0.1
Canada						
Aug 08	8:30	Int'l Merchandise Trade	Jun	Blns	-	-3.4
International						
Aug 08	21:30	CH Consumer Price Index	Jul	Y/Y % Chg.	-0.5	0.0
Aug 11	2:00	UK Gross Domestic Product	2Q	M/M % Chg.	0.2	0.2

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

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