August 25, 2023

In focus

Global equity markets ended the week on a mixed note. Investors took comfort in what many believed to be a balanced message from the Federal Reserve (the Fed). Markets in Asia, however, were overshadowed by fears of contagion risk due to adverse developments in China's real estate sector.

In the U.S., Fed Chair Jerome Powell acknowledged the progress achieved on easing price pressures and highlighted the surprising resilience of the economy. However, hawkish comments from other Fed officials kept investors on edge. Philadelphia Fed President Patrick Harker said the central bank may keep monetary policy restrictive for some time. In addition, Boston Fed President Susan Collins said that more interest rate hikes may still be needed. It is widely expected that the central bank could hold policy rates steady in September, while bets increased on a rate hike in November.

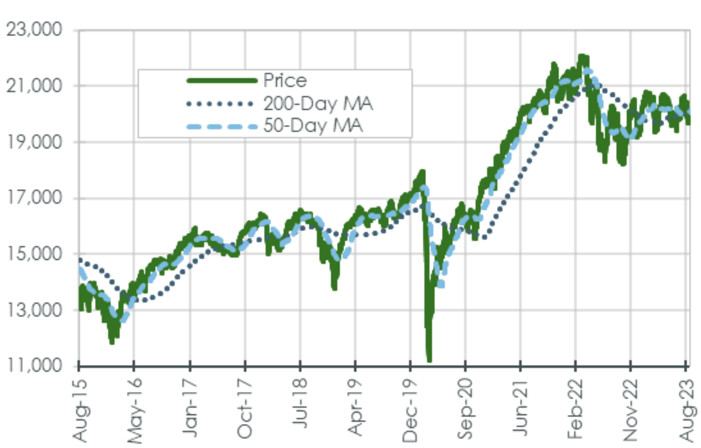
In commodities, crude oil prices fell, but commodities, including gold, silver and copper, were higher. Many traders attributed the setback to weak economic data from China.

In fixed income, the ten-year U.S. Treasury yield eased by mid-week, from multi-year highs, in response to weak business activity data. However, the yield retreated somewhat on Friday, after data showed initial claims for unemployment benefits fell unexpectedly last week, suggesting that the labour market remains tight.

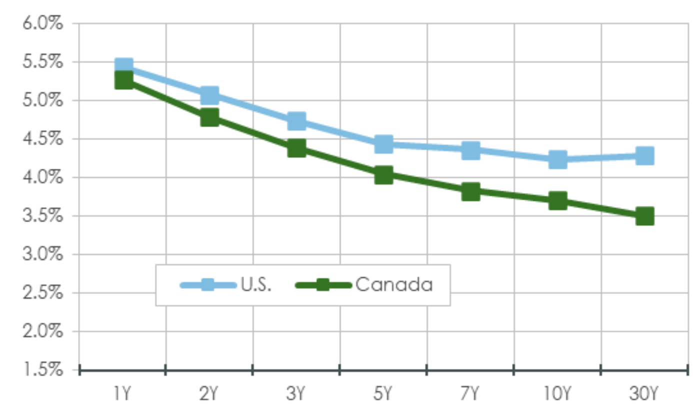
Indexes	Close	Weekly	MTD	YTD
S&P/TSX	19,835.75	0.09%	-3.83%	2.33%
S&P500	4,405.71	0.82%	-3.99%	14.75%
NASDAQ	13,590.65	2.26%	-5.27%	29.85%
DJIA	34,346.90	-0.45%	-3.41%	3.62%
Russell 2000	1,853.63	-0.31%	-7.47%	5.25%
FTSE 100	7,338.58	1.05%	-4.69%	-1.52%
Euro Stoxx 50	4,236.25	0.55%	-5.26%	11.67%
Nikkei 225	31,624.28	0.55%	-4.67%	21.19%
Hang Seng	17,956.38	0.03%	-10.57%	-9.23%
Shanghai Comp.	3,064.08	-2.17%	-6.90%	-0.82%
MSCI ACWI	670.23	0.52%	-5.22%	10.71%
MSCI EM	971.04	0.68%	-7.25%	1.53%
MSCI ACWI ESG Leaders	2,434.78	0.79%	-4.44%	13.16%
Fixed income	**Close**	**Weekly**	**MTD**	**YTD**
FTSE Canada Uni.	1,052.70	0.21%	-1.21%	0.15%
BBG Global Agg.	444.77	-0.08%	-2.34%	-0.26%
TSX Pref	1,557.12	-1.96%	-3.99%	-2.45%
Bond yields	**Close**	**bps chg Weekly**	**bps chg MTD**	**bps chg YTD**
10 yr Canada Govt.	3.70%	-1.2	20.4	40.4
10 yr U.S. Govt.	4.24%	-1.9	27.7	36.1
30 yr Canada Govt.	3.50%	-2.6	19.7	22.7
30 yr U.S. Govt.	4.28%	-9.1	27.5	32.1
Commodities	**Close**	**Weekly**	**MTD**	**YTD**
Oil	79.83	-1.03%	-1.83%	1.93%
Natural gas	2.54	-0.43%	-3.57%	-38.20%
Gold	1,914.96	1.36%	-2.55%	4.99%
Silver	24.23	6.49%	-2.10%	1.13%
Copper	378.40	1.16%	-5.99%	-0.68%
Currencies	**Close**	**Weekly**	**MTD**	**YTD**
CAD/USD	0.7352	-0.37%	-3.02%	-0.35%
USD/EUR	0.9263	0.72%	1.87%	-0.84%
CAD/EUR	0.6809	0.32%	-1.25%	-1.23%
USD/JPY	146.4400	0.72%	2.92%	11.68%
USD/CNY	7.2872	0.04%	2.02%	5.63%
USD/MXN	16.7476	-1.81%	0.03%	-14.11%
GBP/CAD	1.7112	-0.83%	1.09%	4.37%
GBP/USD	1.2578	-1.23%	-2.00%	4.10%

*Please refer to the Appendix for the above table in Canadian dollar terms. Natural gas prices subject to change post-settlement.

S&P/TSX Composite Index



Treasury yield curves



Source: Bloomberg and Refinitiv DataStream. Index returns are in local currency. All equity indexes are price returns and do not include dividends.

Economic indicators	Period	Survey	Actual	Prior period
Canada retail sales MoM	Jun	0.0%	0.1%	0.1%
Canada retail sales ex auto MoM	Jun	0.3%	-0.8%	-0.3%
U.S. initial jobless claims	19-Aug	240k	230k	240k
U.S. University of Michigan sentiment	Aug	71.2	69.5	71.2
U.S. durable goods orders	Jul	-4.0%	-5.2%	4.4%
China industrial profits YoY	Jul	--	-6.7%	-8.3%

Canada

Canadian equities posted meagre gains over the week as investors grappled with a slowdown in China and higher borrowing costs.

At the sector level, information technology stocks followed their U.S. counterparts and outperformed the market. In contrast, financial stocks underperformed, with growing expenses weighing on bank earnings. Royal Bank of Canada edged higher after beating investor estimates and announcing cost reduction measures, while TD Bank fell after missing analysts' estimates for quarterly profit. Energy stocks also underperformed, due mainly to weaker oil prices.

U.S.

U.S. equity markets remained mixed for the week as investors digested a neutral message from Fed. However, a contraction in the manufacturing sector, paired with slowing growth in the services sector, kept sentiment in check.

A preliminary estimate of the S&P Global U.S. Composite PMI fell to 47 in August 2023 from 49 in July. Meanwhile, the services PMI fell to 51 in August 2023, from 52.3 in the previous month; high interest rates and broad-based inflationary pressures weighed on consumer spending.

Initial claims for unemployment benefits fell by 10,000 last week, to 230,000, from 240,000 the week before, suggesting that the U.S. labour market remains historically tight. This could encourage the Fed to extend its hawkish momentum to curb inflation.

By sector, information technology outperformed the market, especially artificial intelligence-related stocks such as NVIDIA, which posted better-than-expected sales and profit, driven by strong demand for AI chips. On the flip side, energy stocks fell, tracking lower oil prices. Financials came under pressure after rating agency S&P Global Ratings joined Moody's to downgrade several regional banks, citing tough operating conditions.

Rest of the world

European equities posted weekly gains. All sectors participated in the rally led by utilities, travel and leisure and food and beverages stocks. In contrast, media stocks fell for the week.

On the economic data front, preliminary estimates showed the HCOB Eurozone Composite PMI fell to 47.0 in August 2023, from 48.6 in the previous month. While the manufacturing PMI edged higher, it remains deep in contraction. Services activity contracted for the first time since the end of 2022, dropping to 48.3 in August 2023, from 50.9 in July.

Elsewhere, Germany's economy shrank 0.2% year-over-year in the second quarter, following a similar contraction in the previous period. A survey showed German business confidence deteriorated further in August for the fourth month in a row. These developments painted a picture of a gloomy economic outlook in Germany, Europe's largest economy.

In Asia, Chinese equities ended the week on a negative note. Overall sentiment remained subdued amid liquidity concerns and lingering worries about the health of the Chinese economy. The People's Bank of China lowered its one-year loan prime rate (LPR) by ten basis points to a record low of 3.45%, in an effort to boost the economy. However, the central bank maintained the five-year LPR, a reference for mortgages, at 4.2%, in contrast to market expectations of cuts to that reate as well. Meanwhile, Japanese equity rose as investors bought stocks following their recent decline following concerns about U.S. interest rates.

Looking ahead

Economic indicators	Period	Survey	Prior period
Canada GDP YoY	Jun	1.4%	1.9%
Canada current account balance	Q2	-$11.2bn	-$6.17bn
U.S. initial jobless claims	26-Aug	235k	230k
U.S. GDP annualized QoQ	Q2	2.4%	2.4%
U.S. ISM manufacturing	Aug	47.0	46.4
U.S. Conference Board consumer confidence	Aug	116.2	117.0

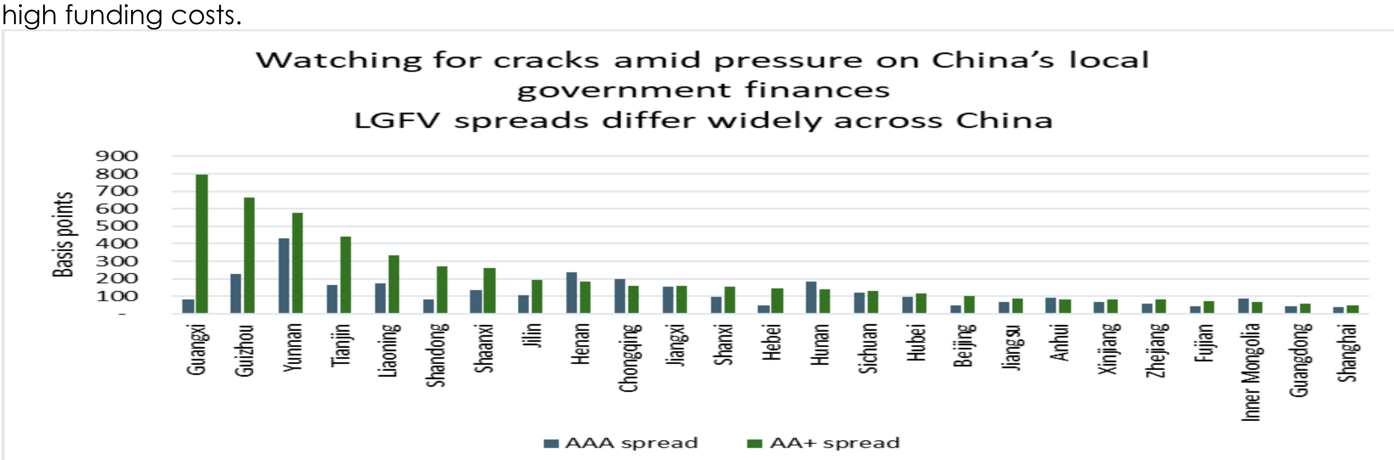
Central bank meetings			
Central banks	**Date**	**Probability of change**	**Current rate**
Bank of Canada	6-Sep-23	23.80%	5.00%
European Central Bank	14-Sep-23	33.70%	4.25%
Federal Open Market Committee	20-Sep-23	21.80%	5.50%
Bank of England	21-Sep-23	106.30%	5.25%
Bank of Japan	22-Sep-23	2.90%	-0.10%

Source: Bloomberg. Probability of change implies the possibility of a central bank hiking interest rates during their upcoming meeting. A negative number in this case means chances of a rate cut rather than a hike.

Spotlight

Watching for cracks amid pressure on China's local government finances

Several of China's local government financing vehicles (LGVFs) have made recent headlines for their struggles to service debts, rattling the country's financial markets. But not all LGFVs are created equal. And while the slowing economy could send some of the weakest issuers to the wall, the fallout so far is contained and does not suggest signs of a systemic crisis. We see LGFVs in weaker provinces and with bond yields above 6% as more vulnerable, because their funding costs are less sustainable. Weakening land sales amid China's property downturn have made a key contribution to LGFV stress. Many LGFVs, especially those in poorer regions, used to rely on land sales for a big portion of their income, and they are now struggling to find new sources of revenue. In this environment, we think investors should exercise caution and steer clear of LGFVs with high leverage and high funding costs.



Source: ChinaBond and Fidelity International, August 2023. A region's spread is an average based on the difference between yields on LGFV bonds from that region and yields on similar-maturity China Development Bank bonds.

Appendix

Global markets (Returns in Canadian dollar terms)				
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Hang Seng	17,956.38	0.46%	-8.05%	-9.14%
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Oil	108.58	-0.67%	1.23%	2.29%
Natural gas	3.45	-0.07%	-0.57%	-37.98%
Gold	2,605.04	1.74%	0.51%	5.39%
Silver	32.95	6.88%	0.93%	1.52%
Copper	514.69	1.53%	-3.06%	-0.33%
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