September 2021 market update

Less stimulus needed as inflation ticks higher.

Oct. 7, 2021

Introduction

Global economic activity during the month of September was relatively slow as a result of the COVID-19 Delta variant and supply shortages that weighed on the manufacturing sector. Inflation remained elevated around the world given strong demand and supply chain issues. Despite the slowdown, global central banks expressed a relatively positive tone, particularly in the U.S. The U.S. Federal Reserve Board ("Fed") announced it may soon reduce bond purchases, while comments from officials suggested a rate increase may be on the way in 2022.

Global equity markets finished lower over September. Investors were uncertain about the impact from a potential default of China Evergrande Group. Supply chain issues and signs of stagflation also concerned investors. In Canada, the S&P/TSX Composite Index declined. Weakness in the Health Care and Information Technology sectors dragged down Canada's main index. U.S. equity markets also finished in the red. The Materials sector suffered the largest losses on the S&P 500 Index, which ended down over the quarter. Yields on 10-year government bonds in Canada finished higher after a late month surge, in part due to expectations of higher federal spending after the election. The yields on 10-year U.S. Treasury Bonds also advanced as a result of expectations that the Fed will reduce bond purchases.

Less stimulus needed

Many central banks expressed a more optimistic tone during the month, suggesting that extensive stimulus measures may be scaled back despite ongoing risks from the pandemic and supply shortages. This trend was led by the Fed. While the Fed's announcement was largely expected by markets, half of the Fed's officials believed an interest rate increase may be needed next year. With inflation running at elevated levels and the labour market largely improving, a hike to its federal funds rate may not be that far off. The European Central Bank announced it would scale back asset purchases in the fourth quarter, but still maintain total spending under its Pandemic Emergency Purchase Programme at €1.85 trillion (C$2.7 trillion) to the end of March 2022. In the U.K., the Bank of England alluded to the possible need of removing some stimulus amid persistently high inflation. Investors are recalibrating their expectations based on a more bullish tone from global central banks.

Debt struggles raising contagion fear

Financial markets experienced some volatility in September, due in part to the developing situation of Chinese property company, China Evergrande Group. The company came under immense pressure, raising doubts it would be able to make the interest payments on its debts totalling US$300 billion. Given its size in China's property market, concerns mounted that the fall of the company could spillover to other sectors of the economy, hurting both the Chinese and global economies. In late September, it was able to make interest payments to local bondholders, but foreign bondholders were not so lucky. Markets were highly volatile during this time.

The People's Bank of China stepped in to inject CNY750 billion (C$148 billion) into the banking system in late September to help support the rest of the economy and ease investor concerns. Chinese regulators are trying to work with China Evergrande Group and instructed the company to do everything possible to avoid a default. Late in September, the Chinese government agreed to purchase China Evergrande Group's stake in Shengjing Bank, the proceeds of which will be used to pay back its debt owed to Shengjing Bank. The situation will be closely monitored by investors as there is uncertainty about what a default may mean for the Chinese and global economies.

Canadian inflation ticks higher

Higher inflation in Canada is persisting. In August, Canada's inflation rate was 4.1% compared to the same month last year, and surpassing the 3.9% rate economists had expected. It was also the highest rate of inflation since March 2003. Contributing to the increase was a rise in prices for gasoline, which surged 32.5% higher year-over-year. The BoC maintains inflation is largely transitory and will eventually ease. Retail sales fell by 0.6% in July, while Statistics Canada projected it increased by 2.1% in August. Still, the impact on consumers could begin to be felt. With prices for food, gasoline and other necessities hitting Canadians' pockets, discretionary spending could be negatively impacted. Now, with the real estate sector seeing a slowdown in activity in recent months, the combination of these two key components of Canadian gross domestic product may weigh on growth.

Supply issues weigh on manufacturing sector

Manufacturing sector activity around the world cooled off during the month of September, largely in response to supply shortages that weighed on output. Shortages of computer chips, steel, plastic and other raw materials is wreaking havoc on the output of manufacturers struggling to keep up with rising demand. There are a variety of issues causing the shortages, including shipping challenges, bad weather and the spread of the COVID-19 Delta variant in some areas of the world, which is hurting production. In response, production of items such as cars, furniture and appliances are being held up. Manufacturing activity in the U.S, Germany and Japan all slowed during the month, while China's manufacturing sector contracted. The challenges being faced by manufacturers could spillover to other industries, including car companies, clothing retailers and home construction. The supply chain challenges become more acute for retailers with the holiday season quickly approaching. If the shortages impact sales volumes, it could slow the economic recovery.

Market performance - as at September 30, 2021

Equity Markets	Level	Month to date	Year to date	One year
S&P/TSX Composite Index C$	20,070.25	-2.49%	15.13%	24.49%
S&P 500 Index US$	4,307.54	-4.76%	14.68%	28.09%
Dow Jones Industrial Average US$	33,843.92	-4.29%	10.58%	21.82%
MSCI EAFE Index US$	2,281.29	-3.19%	6.23%	22.68%
MSCI Emerging Markets Index US$	1,253.10	-4.25%	-2.96%	15.51%

Fixed Income Markets	Level	Month to date	Year to date	One year
FTSE Canada Universe Bond Index C$	1,172.97	-1.40%	-3.95%	-3.35%
FTSE World Investment Grade Bond Index US$	246.47	-1.85%	-4.47%	-1.74%

Currencies	Level	Month to date	Year to date	One year
CAD/USD	0.7885	-0.52%	0.41%	5.04%

Commodities	Level	Month to date	Year to date	One year
West Texas Intermediate (US$/bbl)	75.12	9.66%	54.82%	94.01%
Gold (US$/oz)	1,756.91	-3.13%	-7.45%	-6.84%