Weekly Updates Issue # 770

1. Weekly Markets Changes

[June 26, 2020]

S&P TSX	S&P 500	Dow Jones	NASDAQ	CAD/USD	Gold	WTI Crude
15,188.98 -285.23 -1.84%	3,009.05 -88.7 -2.86%	25,015.55 -855.9 -3.31%	9,757.22 -188.9 -1.90%	$0.7312 -0.48c -0.65%	$1,771.29 +27.42 +1.57%	$38.49 -1.26 -3.17%

2. Canadians saving less because of Covid-19

[June 26, 2020] Half of Canadians who've been financially impacted by Covid-19 have reduced the amount of money they save to invest, according to a survey from Toronto-based Fidelity Investments Canada ULC.

Fidelity's latest retirement survey found that 40% of respondents had their salary or earnings reduced as a result of the pandemic, with data indicating Covid-19 has had a more damaging impact on Canadians in or near retirement than the financial crisis.

Close to 50% of respondents in British Columbia had taken a financial hit as a result of the virus, and more than 40% of respondents in the Prairies and Ontario saw their income plummet. Atlantic Canadians were relatively insulated from the financial impact of Covid-19; just over 30% reported a drop in income.

Thirty-nine per cent of all respondents surveyed — including those who weren't financially impacted by the pandemic — said they were spending less than they did the previous year, up significantly from 25% in 2019.

Forty per cent of respondents who'd been financially impacted by Covid-19 said they would make only "very safe investments for a long time" as a result of recent market volatility. Thirty-eight per cent of respondents who hadn't suffered financially as a result of the pandemic said the same.

Fidelity polled 1,929 respondents between May 20 and May 30, 2020. Respondents' median age was 57. The results of the survey are considered accurate to +/- 2.2 percentage points, 19 times out of 20.

3. Boomers OK when it comes to wealth, StatsCan says

[June 26, 2020] Baby boomers still hold the most wealth in Canada, and generation X are the biggest consumers, according to a new report from Statistics Canada.

The report examines wealth distribution by demographic cohort — boomers (born 1946 to 1964), gen X (1965 to 1980) and millennials (after 1980) — finding that Boomers remain the wealthiest with an average net worth of $1.2 million, and accounting for about half of all household wealth.

The boomers' share of wealth was essentially unchanged between 2010 and 2019, StatsCan reported.

The share for the pre-1946 crowd has diminished as they draw down assets in retirement and sat at about 15% in 2019. The younger cohorts (gen X and millennials) are increasing their share of wealth as they accumulate assets.

StatsCan also reported that gen X has the highest debt-to-income ratio at 220%, although this is down by 18 percentage points since 2010.

And, gen X households are the biggest consumers, spending on average over $100,000 in 2019.

"While Generation X households spend more in most categories, boomers spend more on insurance and financial services, the pre-1946 generation spend more on health, and millennials spend more on education," the report said.

Millennials also saw their debt-to-income ratio rise by 21 points between 2010 and 2019 to 199%. At the same time, their debt-to-asset ratio declined from 45.6% to 39.7%.

StatsCan noted that "growing real estate values for millennials have more than compensated for their increased debt holdings since 2010, [but that] disposable income has not kept pace, growing at an average rate of 5% per year compared with 6% for total debt."

For gen X, the debt-to-asset ratio dropped from 38.3% in 2010 to 23.2% in 2019, "as the growth in real estate, pension plans and investment funds outpaced debt," the report said.

Given that gen X and millennials both have high debt-to-income ratios, the report noted that they are also "more susceptible to reductions in disposable income in 2020, as the effects of the Covid-19 pandemic have negatively impacted employment."

4. Easing of Volcker Rule boosts U.S. bank stocks

[June 25, 2020] The Federal Reserve and four other regulatory agencies announced on Thursday that they have finalized a rule that will ease restrictions curtailing the ability of banks to make investments in such areas as hedge funds.

The announcement of the easing of regulations know as the "Volcker Rule" gave an immediate boost to bank stocks because the rule change could free up billions of dollars in capital in the banking industry.

The Volcker Rule was part of the overhaul of banking regulation approved in the Dodd-Frank Act passed by Congress in 2010 in an effort to curtail excesses that had led to the 2008 financial crisis, the country's worst banking crisis since the 1930s.

However, President Donald Trump had campaigned in 2016 on rolling back what he saw as over-regulation of the banks that he said had weighed on the economy by preventing the banks from making loans to qualified borrowers.

The Fed said the final rule, which will take effect on Oct. 1, is broadly similar to a proposal the agencies had put forward last January.

The rule rollback, which was opposed by Democratic appointees at both the Fed and the Federal Deposit Insurance Corp., represents one of the biggest victories for the Trump administration's deregulation drive.

The Volcker rule, named for its chief proponent, the late Fed Chairman Paul Volcker, generally prohibited banks from engaging in proprietary trading and from acquiring ownership interests in hedge funds and private equity funds.

The looser restrictions approved on Thursday will allow banks to more easily make investments in various areas of venture capital.

The rule change will also allow banks to avoid having to set aside cash when making derivatives trades between different affiliates of the same firm. That change is expected to free up billions of dollars that banks will now have available for other investments.

Swaps are a form of derivatives trade in which two parties agree to exchange payments based on market movements such as changes in interest rates. A lack of transparency in this market was a key contributor to the 2008 financial crisis.

Before he died in December at age 92, Volcker criticized the rule change, saying it “amplifies risk in the financial system, increases moral hazard and erodes protections against conflicts of interest that were so glaringly on display during the last crisis.”

In addition to the Federal Reserve and the FDIC, the changes were approved by the Securities and Exchange Commission, the Office of the Comptroller of the Currency and the Commodity Futures Trading Commission.

5. Fed orders banks to suspend buybacks, dividends until Sept. 30

[June 25, 2020] A worst-case scenario for the U.S. economy ravaged by the coronavirus pandemic would cause nation’s 34 largest banks to collectively lose roughly $700 billion, the Federal Reserve said Thursday.

To bolster the banks ahead such a potentially damaging recession, the Fed ordered the banks to suspend buybacks of their own stock and halt dividend payouts until Sept. 30.

The move comes as the central bank unveiled its latest “stress tests,” which are designed to test the resiliency of the nation’s largest banks. The annual tests change every year, and passing the tests is a requirement for the banks to start buying back shares or paying out dividends.

Typically the Fed’s testing parameters are hypothetical — an international debt crisis or a deep recession. But this year, the Fed based its tests around a very real, and ongoing scenario — the coronavirus pandemic. In the most dire of tests the U.S. unemployment rate would peak at 19.5%.

The Fed tested the banks using an economic model simulating a quick downturn and quick recovery, often called a “V-shaped” recession, as well as a slower U-shaped recovery. In the V-shaped scenario, the U.S. economy would contract 31.5% on an annualized basis, only to recover through 2020 and 2021.

The Fed’s worst case scenario, a double-dip recession, would have caused roughly a quarter of all the biggest banks to breach their minimum capital requirements. This scenario would show the U.S. economy contracting by 37.5% on an annualized basis and start to recover through the summer, but a second outbreak of infections would cause the U.S. economy to slip back into recession.

The Fed, as part of its announcement, also said it would suspend the banks from buying back their own shares at least until Sept. 30. Some banks were already doing this, but those voluntary limits would come to an end in the next two weeks. Further the Fed is capping these banks from paying dividends and requiring each bank to revisit their long-term capital plans.

"Today's actions by the board to preserve the high levels of capital in the U.S. banking system are an acknowledgement of both the strength of our largest banks as well as the high degree of uncertainty we face," said Federal Reserve Vice Chair Randal Quarles, in a statement.

6. Markets taking Canada's downgrade in stride

[June 25, 2020] Markets and economists are largely shrugging off Canada's loss of its unanimous AAA credit rating.

"How would it feel if you threw a downgrade party and nobody came?" Scotiabank Economics asked in a research note.

On Wednesday, Fitch Ratings downgraded Canada from AAA to AA+, citing the large increase in budgetary deficits and the deterioration of the debt-to-GDP ratio as the government grapples with the economic fallout from the Covid-19 outbreak.

Despite the downgrade economists are largely sanguine on the move, noting that it wasn't a surprise and that the underlying rationale reflects the unavoidable consequences of a global pandemic rather than a loss of fiscal discipline.

"Markets could not have cared much less, as government of Canada yields and the currency were unaffected," Scotia said.

For now, Canada remains AAA-rated by the other big three rating agencies — S&P, Moody's Investors Service and DBRS Morningstar.

In a research note, National Bank Financial Inc. (NBF) said Fitch's rating approach considers the finances at all levels of government, not just the federal level. Deteriorating provincial finances due to Covid-19 "appear to be a contributing factor to the downgrade."

Two of the other big rating agencies — Moody's and DBRS — have recently affirmed Canada at AAA, NBF said.

"We're still waiting to hear from S&P, which is a rating agency that carries a lot of weight and where the sovereign rating/ceiling has potentially broader implications, given that S&P rates more names in Canada," it said.

As for whether the other rating agencies will downgrade Canada, BMO Economics said: "It wouldn't be surprising at all to see, at minimum, some negative outlooks on the remaining AAA ratings. There's still plenty of uncertainty on the shape of the recovery and fiscal path, particularly beyond this year."

The one certainty is that the federal deficit will balloon to at least $250 billion this year, BMO said.

"But, the appetite for deficit reduction post-Covid will be a big question mark for some time," it noted.

Still, the lack of immediate market reaction appears to reflect the fact that many other countries are in the same boat.

"One reason the loonie didn't sell off too much might be the fact that investors know that all major developed economies are facing a very uniform shock to their economies and public finances. If Canada was best going in, on a relative basis, maybe they'll still be best when the dust settles," BMO said.

Scotia echoed this sentiment, saying, "Lagging ratings actions are a relative game, and the relatives aren't looking so good these days."

BMO said the Fitch downgrade "shouldn't have a major impact on the market or borrowing costs," but that it also "serves a message that Canada is not fiscally immune, and that governments will have plenty of work to do after the pandemic (and necessary support measures) come to pass."

7. Inability to meet financial obligations has secondary effects

[June 24, 2020] The financial fallout from the Covid-19 outbreak is weighing on Canadians' mental health and increasing food insecurity, according to new research from Statistics Canada.

The StatsCan study found that just over half (54%) of Canadians report they've enjoyed very good or excellent mental health during the pandemic.

However, results were closely related to the financial effects of the crisis.

Among those who faced a moderate to major impact on their ability to meet financial obligations, only 25% reported very good to excellent mental health. Conversely, for those who hadn't been significantly affected financially, over three-quarters (76%) reported very good or excellent mental health.

"The ability to meet financial obligations […] had a significant impact on Canadians' mental health," the study said.

StatsCan also found that certain demographic groups reported higher mental health impacts, including women, youth and people with underlying health conditions.

"For many Canadians, the challenges of physical distancing, the reduced ability to work or contribute to society, and pressures related to taking care of family in lockdown may lead to greater anxiety, loneliness and stress," it said.

Additionally, the study found that approximately four in five Canadians were concerned about overloading the health system and about the health of vulnerable people.

In a separate study, StatsCan found an increase in food insecurity due to the financial effects of the pandemic.

Specifically, it reported that 14.6% of Canadian households experienced food insecurity — such as going hungry or running out of food — in April and early May, up from 10.5% in previous research.

It also found that 28.4% of Canadian workers who were laid off, or otherwise out of work due to Covid-19, reported food insecurity, compared with 10.7% of those still able to work.

8. European chocolates, olives and 28 other items could be hit with $3.1 billion in new US tariffs

[June 24, 2020] European olives, chocolate, gin and beer made with malt are among the latest products that could be hit with steep tariffs as part of a US-European dispute over government subsidies to aircraft makers.

The US Trade Representative announced a list of 30 total products that could be subjected to new tariffs, noting the United States imports about $3.1 billion of these goods annually from Europe.

The United States already levied 15% to 25% tariffs on $7.5 billion worth of other European goods as part of this dispute. The new items could be hit with tariffs of as much as 100%, according to the notice.

The World Trade Organization has already sided with the United States in the dispute, which goes back to 2004. The WTO concluded in 2018 that the European Union helped Airbus with unfair subsidies that hurt sales of US-based Boeing's wide-body jets.

That decision opened the way for the United States to put tariffs on European goods.

The WTO also found that Boeing had received improper tax breaks from Washington state. The state removed the tax breaks earlier this year, but the European Union is still threatening to put tariffs on US goods in response to the earlier ruling.

Now, with the announcement of the new tariffs, the agency will start to hear comments from those who will be affected. Beyond the food and beverage items, most of the 30 items on the list are business tools such as metal stamping and punching equipment.

The EU criticized the US announcement, saying it is possible these next rounds of tariffs could go beyond what is allowed by the WTO.

"It creates uncertainty for companies and inflicts unnecessary economic damage on both sides of the Atlantic," said the EU in its statement. "This is particularly the case as companies are now trying to overcome the economic difficulties in the aftermath of the Covid-19 crisis."
It said the only way to settle the dispute is through negotiations. It said it made "concrete proposals" to resolve the underlying aircraft dispute.
Tariffs are typically paid by American consumers if the exporter does not pay the cost of the tax itself. Some businesses which have been hit by previous tariffs were quick to object to this latest action.
The Distilled Spirits Council of the United States, which said its members have already lost hundreds of millions in sales from other earlier rounds of tariffs on both sides, said it is concerned this latest action will only lead to more escalation.
"EU and US distilled spirits companies have suffered enough as a result of this trade war," said the trade group. "The longer these disputes go unresolved, the greater the threat of even more tariffs on our industry."
The latest in the fight over government support for Boeing and Airbus comes as the two aircraft makers are facing a sharp drop in demand for their planes because of the drop in demand for air travel and the grounding of much of the world's passenger jets caused by the Covid-19 pandemic. Both have cut their production rates, and Boeing has announced plans to cut 16,000 US jobs.

9. CMHC expects lower demand for housing as economy takes Covid-19 hit

[June 23, 2020] Canada Mortgage and Housing Corp. expects a drop in home prices in the country’s biggest cities amid “severe declines” in home sales and construction.
The federal housing agency says a combination of factors related to the pandemic, such as higher unemployment and lower income, will slow housing starts and push sales and home prices below pre-Covid levels.
CMHC says the market likely won’t see a return to pre-pandemic levels before the end of 2022.
Average home prices in Toronto, Montreal and Ottawa are expected to rebound sooner, starting in late 2020 and rolling into early 2021.
Prices in Vancouver, Edmonton and Calgary likely won’t rebound until later in the forecast period, it added.
Calgary and Edmonton will see average home prices decline, it said, due to uncertainty around oil prices and economic recovery in the region.

CMHC deputy chief economist Aled ab Iorwerth says Covid had “unprecedented impacts” on the country’s urban centres.
“Short-term uncertainty will lead to severe declines in sales activity and in new construction,” he said in a statement.
“As the virus is overcome, cities will bounce back but there is significant uncertainty with respect to the path and timing of the recovery.”

10. Recovery will be ‘prolonged and bumpy,’ Macklem warns

[June 22, 2020] Canada’s top central banker says there will be long-term economic damage from the Covid-19 pandemic as the country charts a “prolonged and bumpy” course to recovery.
In his first speech as governor, Tiff Macklem says the central bank expects to see growth in the third quarter of this year as people are called back to work and households resume some of their normal activities as restrictions ease.
But he warns that Canadians shouldn’t expect the short and sharp economic bounce-back expected over the coming months to last.
The combination of uneven reopenings across provinces and industries, the unknown course of consumer confidence, and unemployment rates will “likely inflict some lasting damage to demand and supply,” Macklem says in a speech Monday.
He said ongoing physical distancing rules may mean workplaces can’t be as productive as they once were, adding that many services will remain difficult to deliver.
The combination suggests the economy’s productive capacity will take a hit that will persist even as public health restrictions ease, Macklem says in a webcast speech to Canadian Clubs.
“The recovery will likely be prolonged and bumpy, with the potential for setbacks along the way,” he said in a prepared text of his speech released by the bank.
Macklem said the Covid-19 pandemic has created an economic shock unlike anything seen in our lifetimes. Entire sectors of the economy have shuttered, more than three million people lost their jobs through April and even more had their hours slashed.
“As the economy reopens, we should see very strong job growth. We should also see some pent-up demand giving a boost to spending,” Macklem said in his speech.
“But not everyone’s job will come back, and uncertainty will linger.”

The central bank's response to the pandemic has been a drop to its policy interest rate to 0.25%, which Macklem says is as low as it will go.

The Bank of Canada has also launched a purchasing program of bonds and government debt to help markets function and make borrowing cheaper for households and businesses.

Such purchases, known as quantitative easing, also send a signal that the bank's key rate "is likely to remain low for a long period," he said.

For the Bank of Canada, the impact of structurally low interest rates and the scale of the shock are having what Macklem said is "a profound impact" on the inflation-rate target.

The central bank targets an annual inflation rate of 2% as measured by Statistics Canada's consumer price index.

The basket of goods used to form the index has been shaken by a shift in consumer spending habits during the pandemic. People are spending less on gasoline, which usually receives a heavier weight in calculating inflation, as its price has plunged and the frequency of car travel has dropped. Spending is also down on travel, while grocery spending is up.

Last week, Statistics Canada reported the annual pace of inflation was -0.4% in May, marking the second consecutive month for negative annual inflation after a reading of -0.2% in April.

Macklem said the Bank of Canada will provide "a central planning scenario for output and inflation" and related risks when it releases an updated monetary policy report next month.

"If, as we expect, supply is restored more quickly than demand, this could lead to a large gap between the two, putting a lot of downward pressure on inflation," Macklem said.

"Our main concern is to avoid a persistent drop in inflation by helping Canadians get back to work."

Have a nice and fruitful week!