GLOBAL
Insight
WEEKLY

Wealth
Management

Perspectives from the Global Portfolio Advisory Committee August 12, 2021

Action figures

Kelly Bogdanova – San Francisco

The $1 trillion U.S. infrastructure bill that just got the blessing of the Senate is undeniably large, with some of the biggest-ever investments in certain key areas. And an even greater amount of social and climate spending is in the works as the budget bill moves forward, which raises the prospect of tax hikes. As the legislation is debated, we look at the various scenarios.

Following $7 trillion in total federal and state COVID-19 relief, investors are now so used to seeing uber-sized spending bills from Washington that the roughly $1 trillion traditional infrastructure bill just passed in the Senate might look like a trifle. But it's not. It represents the largest level of spending in some key infrastructure categories and should make headway in upgrading and renewing the nation's infrastructure.

Overall, we view the infrastructure bill as supportive of economic growth and the market. But it doesn't meaningfully change the narrative. Among economists who have forecast its impact, thus far we're seeing estimates that it could add between 0.1 and 0.3 percentage points to GDP growth in each of the next few years.

We think much of the benefit has already been factored into the recent stock market rally. While the bill is positive for the Materials and Industrials sectors—particularly for companies focused on building materials, construction, energy grid transformation, and green infrastructure—this is not something that RBC Capital Markets' equity strategist or the strategists from our national research correspondents are focused on as a major market catalyst going forward.

We think the infrastructure bill will eventually pass in the House of Representatives and will be signed into law, likely sometime this autumn.

House Speaker Nancy Pelosi's maneuver to directly tie this bill to the fate of a much larger and more controversial $3.5 trillion budget package may ultimately be relaxed or modified for two main reasons:

- There are already at least 110 industry and other lobbying groups backing the infrastructure bill, including the influential U.S. Chamber of Commerce, National Association of Manufacturers, Business Roundtable, and National Governors Association.
- The bill passed the Senate by a wide enough bipartisan margin to sufficiently generate additional momentum in the House. Lobbyists, the White House, and even some Republicans will work hard to get this bill past the finish line—regardless of what happens to the separate $3.5 trillion budget bill. We think there will be pressure on Pelosi to pass the infrastructure bill.

Curtain rises on the budget political theater

There are no broad tax hikes in the traditional infrastructure bill. Instead, we expect tax hikes on corporations and/or higher-income individuals to be

For perspectives on the week from our regional analysts, please see pages 3–4.

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Key components of the Infrastructure Investment and Jobs Act

Overview

Roughly $1 trillion in infrastructure spending over next 10 years, including $550 billion in new spending over next five years

No broad tax hikes on corporations, individuals, or estates in this bill

Passed the Senate by a vote of 69-30 (50 Democrats, 19 Republicans); bill is now with the House of Representatives for consideration, timing TBD

Estimated to add $256 billion to the deficit

Milestones

Largest-ever federal investment in public transit

Largest investment in passenger rail since creation of Amtrak

Largest investment in bridges since interstate highway system was constructed

Largest-ever investment in clean energy transmission and electric vehicle infrastructure

Major new spending provisions

$110 billion	Roads, bridges, etc.
$66 billion	Passenger & freight rail
$11 billion	Highway & pedestrian safety; pipeline safety & repair
$39.2 billion	Public transit
$65 billion	Broadband deployment (high-speed internet)
$25 billion	Airports
$17.4 billion	Ports & waterways
$54 billion	Water infrastructure
$65 billion	Power reliability & green energy
$46 billion	Cybersecurity & disaster mitigation
$7.5 billion	Electric vehicle charging
$7.5 billion	Low-carbon & zero-emission school buses & ferries
$21 billion	Legacy pollution (brownfield/Superfund sites, etc.)

Source - RBC Wealth Management, "Bipartisan Infrastructure Investment and Jobs Act Summary" from portman.senate.gov, whitehouse.gov, Los Angeles Times, Reuters, Forbes, The Hill, Congressional Budget Office

included in the $3.5 trillion follow-on budget bill that largely focuses on new and existing social programs and climate initiatives, and includes a revamp of immigration laws. There are a lot of uncertainties about its specific provisions, as they have yet to be nailed down.

In order for a large, wide-ranging budget bill to pass, we think the scope of the legislation will need to be narrowed and the price tag lowered.

Due to Senate parliamentary rules, the budget bill can't be filibustered; only 50 votes are required to pass it. But Democrats will need all 50 of their members to support the legislation because Republican senators have vowed to oppose it. House Democrats will need to deliver almost all of their members due to their razor-thin majority and Republican opposition.

There are already fissures within the Democratic caucus. Two moderate Democratic senators, West Virginia's Joe Manchin and Arizona's Kyrsten Sinema, have strongly objected to the $3.5 trillion price tag and have leveled other criticisms, and a group of at least six moderate Democratic House members has formally raised concerns about the package. But on the other side of the Democratic ideological divide, it's unclear just how much progressives would be willing to change the bill's priorities and reduce its price tag.

Even a "smaller" bill of, say, $2 trillion or less would likely require tax hikes to offset the spending, in our view.

For this reason, some Wall Street equity strategists have incorporated a corporate tax hike into their 2022 earnings models. The consensus assumption among this group is that the corporate tax rate would rise from 21 percent to 25 percent, lower than the Biden administration's original target of 28 percent and still well below the 35 percent rate that prevailed before former President Donald Trump's tax cuts took effect. Manchin previously signaled he would support such a tax hike.

In this scenario, one of our national research correspondents' 2022 S&P 500 earnings forecast is for $230 per share, which would represent 9.5 percent year-over-year profit growth, instead of $240 per share without a tax hike. We think the market could absorb this modest headwind given that it's still early in the economic recovery cycle.

While tax hikes on high-income individuals, investments, and large estates also could be included in the budget bill, there is currently a great deal of uncertainty on this front. And the ultimate size of the bill could play a role—the smaller the size, potentially the lesser the tax hikes.

Even though the prospect of tax hikes typically creates angst for investors and, if implemented, can directly hit pocketbooks in non-trivial ways, historically the stock market has been able to cope. RBC Global Asset Management has found that U.S. equity markets have exhibited an ability to remain resilient through all but one of the 13 instances of tax increases since 1950. For this legislation, we think Wall Street would likely view any negative economic drag from tax hikes as being largely offset by the stimulative nature of the bill's spending provisions.

Bottom line: Democrats have the ability to pass a budget bill focusing on social spending and climate initiatives without one Republican vote. It's just unclear at this stage whether the various factions in the party can come to an agreement, and what such an agreement might look like. The debate could get interesting.

UNITED STATES

Alan Robinson – Seattle

- **Investors' attention switched to economic data during the week**, as the door almost closed on the Q2 2021 earnings season. With roughly 95% of the S&P 500 constituents having reported, **Q2 2021 y/y sales growth is converging around the 25% level, while earnings are closing on 87% growth** relative to the low point of the recession in Q2 2020, according to FactSet. This will almost certainly mark the peak growth rate of the rebound, although consensus forecasts suggest earnings growth will continue at an above-average pace in H2 2021.

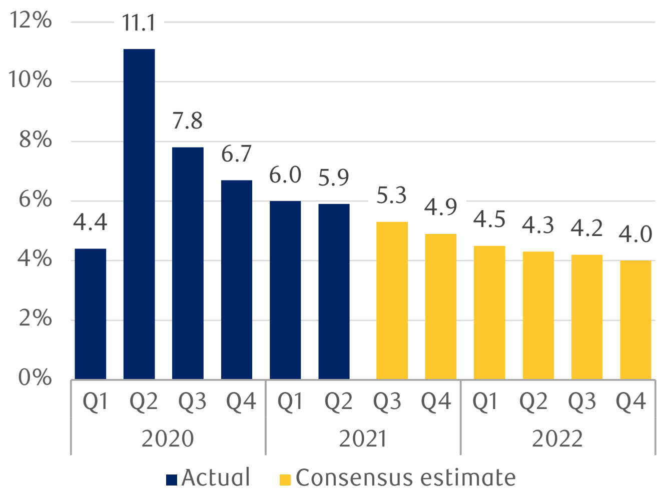
- **Traders viewed the July employment report, released Aug. 6, as a positive for stocks**. The 943,000 new jobs built on a similar number in June and was enough to push the unemployment rate down to 5.4% from 5.9% the prior month, triggering a round of upgrades to economic forecasts (see chart).

- While the recent rise in COVID-19 cases has dampened sentiment, **the strong jobs report put the reflation trade back on track and rekindled the rotation into value from growth as an investing style**. RBC Capital Markets, LLC Head of U.S. Equity Strategy Lori Calvasina addressed this trend during the week, indicating she expects the strong GDP tailwind to support value stocks into 2022, but that as economic growth reverts to "trend" levels, growth stocks should regain the mantle, particularly if the Fed starts to hike interest rates.

- **Inflation data, released during the week, underscored the risk of higher rates.** Consumer prices rose 5.4% y/y in July, or up 4.3% excluding the volatile food and energy categories. Producer prices, which feed into the prices consumers pay, were up 7.8% y/y, with the core level up 6.2%, both about 0.5 percentage points above consensus forecasts. While many of the drivers of these increases such as supply chain and labor issues may prove transitory, these figures chilled the bond market, with 10-year Treasury bond interest rates rising to a high of 1.37% after the inflation numbers from a low of 1.13% prior to the jobs report.

U.S. employment gains likely to accelerate in H2 2021

U.S. unemployment rate (%)



Source - RBC Wealth Management, Bloomberg, national research correspondent

CANADA

Simon Jones – Toronto

- **Employment growth continued to press higher in July**, albeit at a slower pace than consensus estimates. **The Canadian labour market added 94,000 jobs**, building off June's 231,000 increase. Service-producing sectors continued to recover as provinces lifted all public health restrictions aside from certain masking, capacity, and screening requirements. As virus containment measures continue to ease, RBC Economics expects employment in the hospitality and travel sectors to continue recovering. However, it noted that further employment growth outside of these sectors may be more challenging as supply chain disruptions and production capacity limits pose challenges for sectors such as manufacturing. Geographically, the majority of the job gains occurred in Ontario, though Manitoba, Nova Scotia, and Prince Edward Island also saw slight increases. The unemployment rate fell 0.3 percentage points to 7.5%; however, **long-term unemployment remains stubbornly high**, accounting for more than a quarter of July's total unemployment.

- After experiencing a swift move higher to start the year, **Government of Canada yields have been in a state of gradual decline** as the rising number of delta variant cases globally raises concerns about economic growth and inflation. However, **the continued flow of firm economic data has led to yields rebounding in recent weeks**. Consumer spending trends and employment data have strengthened as provinces ease public health restrictions following the pandemic's third wave. Statistics Canada's preliminary estimate indicates GDP rose 0.7% m/m in June. Although supply disruptions may serve as a near-term headwind, **RBC Capital Markets is expecting GDP growth to continue accelerating** into H2 2021, boosted by a recovery in service-producing sectors. Taken together, this data suggest the economy is adapting and becoming more resilient to each successive wave of the pandemic.

EUROPE

Frédérique Carrier – London

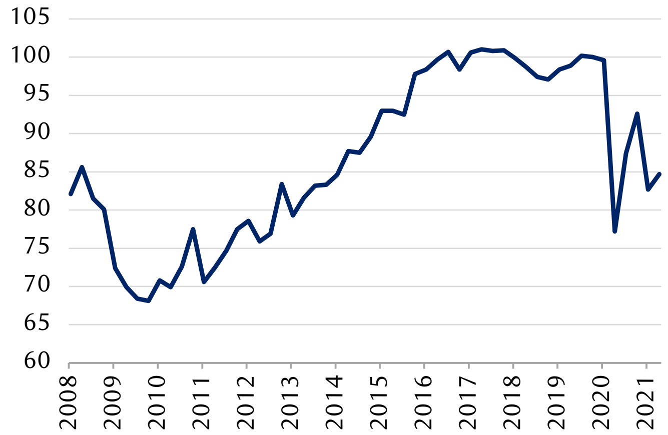
- **UK GDP grew a robust 4.8% in Q2 2021**, in line with consensus expectations. Monthly GDP growth accelerated towards the end of the quarter, with June GDP expanding 1% m/m. The growth was linked to services such as retail, accommodation, and food and education, as they reopened after the lockdown.

- **Office of National Statistics data suggest business investment made a small, positive contribution to growth as businesses reopened**, though it remains firmly below the pre-pandemic level. Net trade exerted a small drag as the UK seems to have difficulty taking full advantage of the recovery in world trade. RBC Capital Markets calculates the June GDP numbers leave the economy 2.2% smaller than it was before the pandemic.

- **While the recovery enjoyed a brisk pace up to June, higher COVID-19 infection levels in July slowed down any further improvement,** according to high frequency data such as for peaking mobility. As such, if this trend continues, the UK economy may still be a few quarters away from fully recovering to its pre-pandemic level, particularly as large parts of the government's fiscal support is unwound and withdrawn at the end of Q3.

UK business investment struggles to improve

UK business investment (Q4 2019 indexed to 100)



Source - Office of National Statistics, Haver Analytics, RBC Capital Markets

ASIA PACIFIC

Jasmine Duan – Hong Kong

- **China's regulatory tightening remains an overhang for China and Hong Kong equities.** On Aug. 11, the Chinese regulator stated it will step up scrutiny of online insurance companies, requiring them to end bad practices such as misleading marketing and inflated pricing as well as strengthen protection of consumer privacy.

- We note the **recent regulatory actions in China extend oversight in three key areas: curbing regulatory arbitrage and maintaining financial stability, enhancing data security and consumer privacy, and promoting social equality**. This process is ongoing and **may lead to further market volatility in the near term**, in our view. We think some signs that investors can monitor that could indicate this round of regulatory tightening is coming to an end include: major FinTech companies fully complying with regulatory requirements and companies such as Ant Group relaunching IPO plans; Chinese companies resuming offshore IPOs; and major digital platforms announcing measures to improve social benefits for workers.

- **China's aggregate financing in July was RMB 1.06 trillion**, weaker than the RMB 1.7 trillion consensus estimate. This translates to **slower credit growth of 10.7% y/y** vs. 11.0% in June, which may be a result of tightening measures on local government financing and shadow banking, in our view. In addition, credit expansion usually weakens in July after a spike in June, when banks rush to boost lending at the end of Q2. We don't think the data represent a sharp tightening of policy. China's Politburo meeting in July had a slightly more dovish tone, which indicated a stable policy outlook, and officials pledged to implement pro-growth adjustments as needed.

- **Singapore revised up its 2021 GDP growth forecast to a 6%–7%** range, from 4%–6% previously. The government said progressive easing of domestic and border restrictions as vaccination rates continue to rise will help to support the recovery of consumer-facing sectors and alleviate labor shortages in sectors that rely on migrant workers.

MARKET Scorecard

Data as of August 12, 2021

Equities (local currency)	Level	MTD	YTD	1 yr	2 yr
S&P 500	4,460.83	1.5%	18.8%	32.0%	54.7%
Dow Industrials (DJIA)	35,499.85	1.6%	16.0%	26.9%	37.0%
Nasdaq	14,816.26	1.0%	15.0%	34.5%	88.4%
Russell 2000	2,244.07	0.8%	13.6%	41.7%	50.2%
S&P/TSX Comp	20,520.60	1.1%	17.7%	23.8%	26.4%
FTSE All-Share	4,131.76	2.5%	12.5%	18.2%	4.7%
STOXX Europe 600	474.84	2.8%	19.0%	26.7%	28.2%
EURO STOXX 50	4,226.33	3.4%	19.0%	25.7%	27.0%
Hang Seng	26,517.82	2.1%	-2.6%	5.0%	2.7%
Shanghai Comp	3,524.74	3.7%	1.5%	6.2%	25.2%
Nikkei 225	28,015.02	2.7%	2.1%	22.6%	35.4%
India Sensex	54,843.98	4.3%	14.9%	42.9%	45.9%
Singapore Straits Times	3,182.80	0.5%	11.9%	24.2%	0.4%
Brazil Ibovespa	120,701.00	-0.9%	1.4%	18.2%	18.4%
Mexican Bolsa IPC	51,049.69	0.4%	15.8%	32.1%	28.1%

Gov't bonds (bps change)	Yield	MTD	YTD	1 yr	2 yr
U.S. 10-Yr Treasury	1.361%	13.8	44.8	68.6	-28.5
Canada 10-Yr	1.255%	5.2	57.8	64.6	5.7
UK 10-Yr	0.601%	3.6	40.4	36.4	11.1
Germany 10-Yr	-0.460%	0.1	10.9	-1.3	13.2

Fixed income (returns)	Yield	MTD	YTD	1 yr	2 yr
U.S. Aggregate	1.46%	-0.6%	-1.1%	-0.9%	18.5%
U.S. Investment-Grade Corp	2.05%	-1.1%	-1.0%	0.7%	25.7%
U.S. High-Yield Corp	4.12%	-0.4%	3.6%	9.5%	21.6%

Commodities (USD)	Price	MTD	YTD	1 yr	2 yr
Gold (spot $/oz)	1,753.24	-3.4%	-7.6%	-8.5%	16.0%
Silver (spot $/oz)	23.21	-9.0%	-12.1%	-9.0%	36.0%
Copper ($/metric ton)	9,482.50	-2.3%	22.4%	47.4%	65.9%
Oil (WTI spot/bbl)	69.09	-6.6%	42.4%	61.9%	25.8%
Oil (Brent spot/bbl)	71.19	-6.7%	37.4%	56.7%	21.5%
Natural Gas ($/mmBtu)	3.91	0.0%	54.1%	81.8%	85.9%

Currencies	Rate	MTD	YTD	1 yr	2 yr
U.S. Dollar Index	92.9940	0.9%	3.4%	-0.5%	-4.5%
CAD/USD	0.7986	-0.4%	1.7%	5.8%	5.7%
USD/CAD	1.2522	0.4%	-1.6%	-5.5%	-5.4%
EUR/USD	1.1735	-1.1%	-3.9%	-0.4%	4.6%
GBP/USD	1.3804	-0.7%	1.0%	5.9%	14.3%
AUD/USD	0.7338	-0.1%	-4.6%	2.5%	8.7%
USD/JPY	110.4400	0.7%	7.0%	3.3%	4.9%
EUR/JPY	129.6100	-0.5%	2.7%	2.9%	9.8%
EUR/GBP	0.8501	-0.4%	-4.9%	-6.0%	-8.4%
EUR/CHF	1.0836	0.8%	0.2%	0.8%	-0.3%
USD/SGD	1.3579	0.3%	2.7%	-1.0%	-2.1%
USD/CNY	6.4795	0.3%	-0.7%	-6.7%	-8.2%
USD/MXN	19.9524	0.4%	0.2%	-10.7%	1.8%
USD/BRL	5.2561	0.8%	1.1%	39.1%	31.9%

Equity returns do not include dividends, except for the Brazilian Ibovespa. Bond yields in local currencies. Copper Index data and U.S. fixed income returns as of Wednesday's close. Dollar Index measures USD vs. six major currencies. Currency rates reflect market convention (CAD/USD is the exception). Currency returns quoted in terms of the first currency in each pairing.

Examples of how to interpret currency data: CAD/USD 0.79 means 1 Canadian dollar will buy 0.79 U.S. dollar. CAD/USD 1.7% return means the Canadian dollar rose 1.7% vs. the U.S. dollar year to date. USD/JPY 110.44 means 1 U.S. dollar will buy 110.44 yen. USD/JPY 7.0% return means the U.S. dollar rose 7.0% vs. the yen year to date.

Source - Bloomberg; data as of 4:35 pm ET 8/12/21

Authors

Kelly Bogdanova – San Francisco, United States
kelly.bogdanova@rbc.com; RBC Capital Markets, LLC

Alan Robinson – Seattle, United States
alan.robinson@rbc.com; RBC Capital Markets, LLC

Simon Jones – Toronto, Canada
simon.jones@rbccm.com; RBC Dominion Securities Inc.

Frédérique Carrier – London, United Kingdom
frederique.carrier@rbc.com; RBC Europe Limited

Jasmine Duan – Hong Kong, China
jasmine.duan@rbc.com; RBC Investment Services (Asia) Limited

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Sell [Underperform]	51	3.61	4	7.84

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