

Economics

THE WEEK AHEAD

May 1 - 5, 2023

If you don't know where you're going

by Avery Shenfeld avery.shenfeld@cibc.com

The Cheshire cat's advice, paraphrased as "if you don't know where you're going, any road will take you there," isn't much help to the US Federal Reserve these days. Unlike Alice, the Fed knows where it wants to get to — a 2% inflation rate — but at this point, it can't possibly know with any certainty which road will take it there.

Although final demand was healthy in Q1, it was spurred by spending from one-off tax relief, and job gains that look to be slowing. Moreover, the economy showed less momentum at the end of the quarter than at its start, and most interest sensitive sectors are in outright decline. Even with some inventory rebuilding, second quarter growth could be zero or negative.

The Fed's willingness to hike another quarter point in the week ahead lies in the fact that it needs more than one anemic quarter to bring inflation back to target. But there's a huge hole in its ability to assess what policy path will take it to that few quarters of softness.

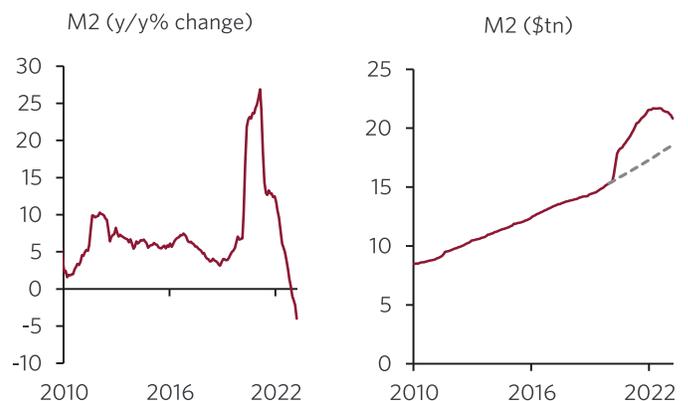
That hole lies, of course, in the banking system. The Fed's forecasting model can estimate the lagged impacts of rate hikes on growth, but doesn't have an equation that tacks on the impact of a few bank failures, or a broader squeeze on regional bank funding. Trimming the March hike to a quarter point from what would have been 50 bps, and likely making the same adjustment to the move in May, suggests that Powell's team is equating the banking developments to the equivalent of 50 basis points in fed funds hikes.

But that's pulled out of thin air as far as we can tell. There have been banking squeezes in the past (the S&L failures, the 2008 financial crisis), but each one is unique, and it's much too early to assess the scope of the current one. With thousands of regional banks, and the credit losses from a slowing economy mostly lying ahead, we haven't yet seen the full picture. There could be more banks that will make their first appearance on the front page of the business section for all the wrong reasons.

Moreover, all of this is complicated by the fact that we were overdue for a retrenchment from the bloated liquidity seen during the pandemic. The 4% year-on-year decline in the money supply is without precedent since the Great Depression, but in level terms, the money supply still looks ample relative to its prior trend line (Chart). The trend needn't spell doom as long as the plunge is arrested before too long. But will it be? That's going to depend on how deep a retreat we see in lending activity, since that's what can drive monetary aggregates further into the abyss.

There's only one cure for the Fed's lack of a roadmap: time. The Fed needs to hike in May and go away. By standing pat for a couple of quarters, the FOMC will gain considerable insight into the drag from developments at regional banks. With growth slowing, inflation is unlikely to run away to the upside, but we'll need time to let it ease off enough. So our call is for May's move to be the final hike for this cycle, but for the FOMC to also wait until 2024 to start cutting rates, as we're hoping that the Fed follows some wiser words from the Cheshire cat, who said that "haste makes waste, so I rarely hurry."

Chart: US M2 money supply: scary (L) or not (R)



Source: FRB, CIBC

Week Ahead Calendar And Forecast—Canada

H, M, L = High, Medium or Low Priority

SAAR = Seasonally Adjusted Annual Rate

Consensus Source: Bloomberg

Date	Time	Economic Releases, Auctions and Speakers	Month	Priority	CIBC	Consensus	Prior
Monday, May 1	-	-	-	-	-	-	-
Tuesday, May 2	-	-	-	-	-	-	-
Wednesday, May 3	-	-	-	-	-	-	-
Thursday, May 4	8:30 AM	MERCHANDISE TRADE BALANCE	(Mar)	(H)	-\$0.2B	-	\$0.4B
Thursday, May 4	10:00 AM	IVEY PMI	(Apr)	(L)	-	-	58.2
Thursday, May 4	1:05 PM	Speaker: Tiff Macklem (Governor)	-	-	-	-	-
Friday, May 5	8:30 AM	EMPLOYMENT CHANGE	(Apr)	(H)	20K	-	34.7K
Friday, May 5	8:30 AM	UNEMPLOYMENT RATE	(Apr)	(H)	5.1%	-	5.0%

Week Ahead Calendar And Forecast—United States

H, M, L = High, Medium or Low Priority

SAAR = Seasonally Adjusted Annual Rate

Consensus Source: Bloomberg

Date	Time	Economic Releases, Auctions and Speakers	Month	Priority	CIBC	Consensus	Prior
Monday, May 1	9:45 AM	S&P GLOBAL US MANUFACTURING PMI	(Apr)	(L)	-	50.4	50.4
Monday, May 1	10:00 AM	ISM - MANUFACTURING	(Apr)	(H)	47.5	46.8	46.3
Monday, May 1	10:00 AM	CONSTRUCTION SPENDING M/M	(Mar)	(M)	-	0.2%	-0.1%
Tuesday, May 2	10:00 AM	JOLTS Job Openings	(Mar)	-	-	-	9931K
Tuesday, May 2	10:00 AM	FACTORY ORDERS M/M	(Mar)	(M)	1.1%	1.4%	-0.7%
Tuesday, May 2	10:00 AM	DURABLE GOODS ORDERS M/M	(Mar)	(H)	-	-	3.2%
Tuesday, May 2	10:00 AM	DURABLE GOODS ORDERS EX-TRANS M/M	(Mar)	(H)	-	-	0.3%
Wednesday, May 3	7:00 AM	MBA-APPLICATIONS	(Apr 28)	(L)	-	-	3.7%
Wednesday, May 3	8:15 AM	ADP EMPLOYMENT CHANGE	(Apr)	(M)	-	140K	145K
Wednesday, May 3	9:45 AM	S&P GLOBAL US SERVICES PMI	(Apr)	(L)	-	53.7	53.7
Wednesday, May 3	9:45 AM	S&P GLOBAL US COMPOSITE PMI	(Apr)	(L)	-	-	53.5
Wednesday, May 3	10:00 AM	ISM - SERVICES	(Apr)	(M)	51.4	51.9	51.2
Wednesday, May 3	2:00 PM	FOMC RATE DECISION (UPPER BOUND)	(May 3)	(H)	5.25%	5.25%	5.00%
Wednesday, May 3	2:00 PM	FOMC RATE DECISION (LOWER BOUND)	(May 3)	(H)	5.00%	5.00%	4.75%
Wednesday, May 3	2:30 PM	Speaker: Jerome H Powell (Chairman) (Voter)	-	-	-	-	-
Thursday, May 4	8:30 AM	INITIAL CLAIMS	(Apr 29)	(M)	-	245K	230K
Thursday, May 4	8:30 AM	CONTINUING CLAIMS	(Apr 22)	(L)	-	-	1858K
Thursday, May 4	8:30 AM	GOODS & SERVICES TRADE BALANCE	(Mar)	(H)	-\$63.5B	-\$68.5B	-\$70.5B
Thursday, May 4	8:30 AM	NON-FARM PRODUCTIVITY	(1Q P)	(M)	-2.1%	0.1%	1.7%
Friday, May 5	8:30 AM	NON-FARM PAYROLLS	(Apr)	(H)	160K	180K	236K
Friday, May 5	8:30 AM	UNEMPLOYMENT RATE	(Apr)	(H)	3.6%	3.6%	3.5%
Friday, May 5	8:30 AM	AVERAGE HOURLY EARNINGS ALL EMPLOYEES M/M	(Apr)	(H)	0.3%	0.3%	0.3%
Friday, May 5	8:30 AM	AVERAGE WEEKLY HOURS ALL EMPLOYEES	(Apr)	(H)	-	34.5	34.4
Friday, May 5	8:30 AM	MANUFACTURING PAYROLLS	(Apr)	(H)	-	-3K	-1K
Friday, May 5	3:00 PM	CONSUMER CREDIT	(Mar)	(L)	-	\$17.3B	\$15.3B
Friday, May 5	1:00 PM	Speaker: James Bullard (St Louis)	-	-	-	-	-
Friday, May 5	1:00 PM	Speaker: Lisa D Cook (Governor) (Voter)	-	-	-	-	-

Week Ahead's market call

by Avery Shenfeld

In the **US**, expect the Fed to announce a quarter point hike, but sound much less convinced about the need to do more. Markets are now keeping a close eye on the debt ceiling debate, with money market investors, for example, piling into one month bills rather than 3-month bills that would mature after the deadline. March's ISM survey respondents might have been spooked by the news that was just breaking on bank failures, so we could see rebounds in April that still show the factory sector in retreat and modest services growth. A retreat in job openings in the JOLTS data could be as important as a rising unemployment rate in cooling wage inflation.

In **Canada**, a rising unemployment rate is the litmus test for a Bank of Canada that needs an excuse to keep rates on hold in June. Productivity can't stay as bad as it's appeared to be in the data of late, so weak GDP growth over February and March should show up in softer hiring in April, weak enough given labour force growth to nudge the jobless rate up one tick. The goods trade balance could dip into negative territory in March data also due this coming week.

Week Ahead's key Canadian number: Employment—April

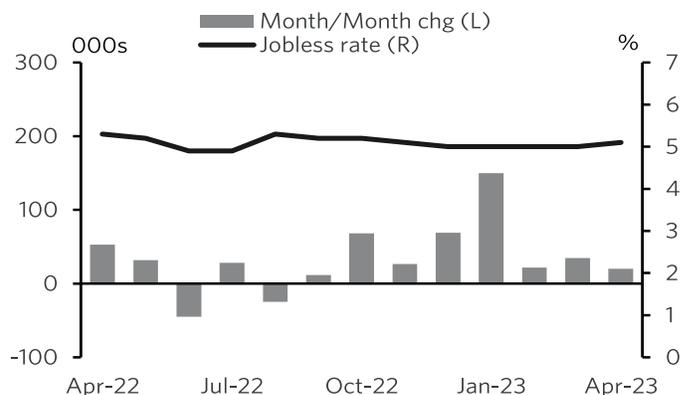
(Friday, 8:30 am)

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Variable	CIBC	Mkt	Prior
Employment change	20K	-	34.7K
Unemployment change	5.1%	-	5.0%

A surge in population growth is creating a larger pool of potential workers, but cooling demand due to past interest rate hikes should see employment gains start to undershoot the pace of growth in the population. While the 20K gain in jobs we expect for April would have been considered pretty solid in prior years, in 2023 it would be weak enough to see the unemployment rate rise a tick to 5.1%. The current strike by public sector workers started too late in the month to have an impact on the hours worked figures, which we expect to show a further modest advance.

Chart: Canadian employment



Source: Statistics Canada, Haver Analytics, CIBC

Forecast implications — With unfilled vacancies starting to come back closer to more normal levels, an easing of demand within the economy should start to be reflected by a slower pace of hiring. That will likely see the unemployment rate continue to edge up through to the second half of the year, before plateauing and finally coming back down again in 2024.

Other Canadian releases: Merchandise trade—March

(Thursday, 8:30 am)

The Canadian trade balance may have moved back into deficit territory in March, driven by stronger imports of cars from the US and lower oil exports. We project a deficit of \$0.2bn, which would be a \$600mn swing relative to a \$0.4bn surplus in the prior month.

Week Ahead's key US number: Employment situation—April

(Friday, 8:30 am)

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Variable	CIBC	Mkt	Prior
Employment (m/m)	160K	180K	236K
Unemployment rate	3.6%	3.6%	3.5%
Avg hourly earnings (m/m)	0.3%	0.3%	0.3%

Initial jobless claims were little changed during the April employment survey reference period, but continuing claims trended higher, suggesting that unemployed workers weren't being re-absorbed as readily into the labor market. That's in line with the easing in job openings recently and ongoing layoff announcements in the tech and media sectors. Combined with weakness in interest-sensitive industries, where the drop in capex in the Q1 GDP report signaled that businesses have become more pessimistic, we expect total hiring to have slowed to a 160K pace in April. That likely caused the unemployment rate to tick up to 3.6%. Wage growth could have continued at a 0.3% pace, but the risks to that figure are to the downside, as hiring was likely concentrated in lower-paying services where labor shortages still remain.

Chart: US payroll employment



Source: BLS, Haver Analytics, CIBC

Forecast implications — Our forecast for hiring is still above the 100K pace that Fed Chair Powell has suggested is consistent with on-target inflation, and we continue to expect a 25bp rate hike at next week's FOMC. We anticipate that will be the Fed's final rate hike in this cycle, as layoff announcements are still coming to fruition, and the impact of tighter lending standards will add to the slowdown ahead.

Market impact — We're slightly below the consensus on the payrolls figure, which could weigh on the USD and cause bond yields to fall.

Other US Releases: ISM Manufacturing—April

(Monday, 10:00 am)

The ISM's manufacturing index likely ticked up in April, in line with moves in regional indices, but remained entrenched in negative territory at 47.5. Indeed, businesses are pessimistic about what lies ahead, and have pulled back on investing in equipment, suggesting that the production and new orders indices could have fallen.

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