Economics

THE WEEK AHEAD

August 29-September 2, 2022

Time for some Schadenfreude?

by **Avery Shenfeld** avery.shenfeld@cibc.com

It's fitting that the term "schadenfreude" is of German origin, since soon enough, Canadians might get a taste of it at that country's expense, or more broadly, at Europe's expense. Typically, gaining any joy out of someone else's misery isn't all that virtuous, but in this case, we need to think about whether the US and Canada might actually benefit if, as seems increasingly probable, both the EU and the UK tumble into recession.

In Canada, we're almost always rooting for strong growth in all corners of the planet, since it can still contribute to buoyant prices and demand for our country's resource-tilted exports. Indeed, this past week featured a high profile visit by the German Chancellor that highlighted prospects for Canada's green energy and critical minerals sectors, albeit relating to exports that will be some years out.

But right now, at least in the aggregate if not in each sector, we're cheering for slower growth to contain inflation. Could weaker global activity, including a recession in Europe and ongoing sluggishness in China, be just what we need in terms of help on the inflation front?

Perhaps not as much as one might think. Slower growth has helped contain oil demand, but prices have recouped some lost ground on chatter that OPEC+ could pare supply. In the face of actual and threatened Russian export curtailments, natural gas prices soared overseas, with a ripple effect on North American benchmarks. Elsewhere, many industrial commodities are off their highs, as are a number of food commodities, although the latter group tends to be less tied to economic growth.

A weak European economy will include softness in their demand for consumer and industrial goods, which should provide a bit of downward pressure on North American export demand, as well as on some prices. We won't need to cool domestic sectors as much with higher interest rates if our exports are lacklustre.

But there's a catch. Some of the economic turmoil in European industry from soaring power costs and uncertain energy supply will impact their exports to North America. That works against central bank hopes for improvements in supply chains as a buffer against inflation. That's been the case with China's troubles with Covid-19 lockdowns this year – helpful for gasoline inflation, but not such good news for the supply of other consumer goods.

What would recessions in the EU and the UK say about prospects for avoiding one in Canada? On the downside, part of the story across the Atlantic clearly raises some doubts about our central bank's plan for a soft landing. The Bank of England raised rates even as its own staff forecast a not-so-mild recession ahead; if those on the policy committee agree with that forecast, they're essentially conceding that they need a recession to get inflation under control, something that the Bank of Canada's forecast doesn't yet admit to.

That said, the Bank of England is in a greater pickle, as UK inflation is expected to top 13%. While their ex-energy inflation isn't as elevated as ours, the soaring headline price gauge is spilling over into inflation expectations, and surging strike activity suggests that could quickly spill over into a broader wage-price spiral.

History reveals that while a US recession almost always causes one in Canada, the correlation between Europe and Canada isn't nearly as tight. The EU had a second dip back into recession in 2012 while Canada remained on the recovery path. Canada was also growing in the mid-90s when the EU fell into recession. So the beating of the recession drums overseas doesn't guarantee an outright decline here, but certainly underscores that the best case outcome will be a protracted period of quite sluggish growth ahead.

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, August 29	-	AUCTION: 2-YR CANADAS $4B	-	-	-	-	-
Tuesday, August 30	-	AUCTION: 3-M BILLS $6B, 6-M BILLS $3.4B, 1-YR BILLS $3.4B	-	-	-	-	-
Tuesday, August 30	8:30 AM	CURRENT ACCOUNT BAL.	(Q2)	(M)	$6.40B	-	$5.03B
Wednesday, August 31	8:30 AM	GDP M/M	(Jun)	(H)	0.1%	-	0.0%
Wednesday, August 31	8:30 AM	GDP (annualized)	(Q2)	(H)	4.2%	-	3.1%
Thursday, September 1	-	AUCTION: 30-YR RRB $300M	-	-	-	-	-
Thursday, September 1	8:30 AM	BUILDING PERMITS M/M	(Jul)	(M)	-	-	-1.5%
Friday, September 2	8:30 AM	LABOUR PRODUCTIVITY Q/Q	(Q2)	(M)	-	-	-0.5%

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, August 29	2:15 PM	Speaker: Brainard (Governor) (Voter)	-	-	-	-	-
Tuesday, August 30	9:00 AM	HOUSE PRICE INDEX M/M	(Jun)	(M)	-	0.8%	1.4%
Tuesday, August 30	9:00 AM	S&P CORELOGIC CS Y/Y	(Jun)	(H)	-	19.0%	20.5%
Tuesday, August 30	10:00 AM	CONF.BOARD CONSUMER CONFIDENCE	(Aug)	(H)	96.8	97.4	95.7
Tuesday, August 30	10:00 AM	JOLTS Job Openings	(Jul)	-	-	10300K	10698K
Tuesday, August 30	8:00AM	Speaker: Barkin (President, Richmond)	-	-	-	-	-
Tuesday, August 30	11:00AM	Speaker: Williams (Vice Chair, New York) (Voter)	-	-	-	-	-
Wednesday, August 31	7:00 AM	MBA-APPLICATIONS	(Aug 26)	(L)	-	-	-1.2%
Wednesday, August 31	9:45 AM	CHICAGO PMI	(Aug)	(M)	-	53.1	52.1
Wednesday, August 31	8:00 AM	Speaker: Mester (President, Cleveland) (Voter)	-	-	-	-	-
Wednesday, August 31	6:30 PM	Speaker: Bostic (President, Atlanta)	-	-	-	-	-
Thursday, September 1	8:30 AM	INITIAL CLAIMS	(Aug 27)	(M)	-	250K	243K
Thursday, September 1	8:30 AM	CONTINUING CLAIMS	(Aug 20)	(L)	-	1450K	1415K
Thursday, September 1	8:30 AM	NON-FARM PRODUCTIVITY	(2Q F)	(M)	-	-4.6%	-4.6%
Thursday, September 1	10:00 AM	ISM - MANUFACTURING	(Aug)	(H)	51.9	52.1	52.8
Thursday, September 1	10:00 AM	CONSTRUCTION SPENDING M/M	(Jul)	(M)	-	-0.1%	-1.1%
Thursday, September 1	-	NEW VEHICLE SALES	(Aug)	(M)	-	13.6M	13.4M
Thursday, September 1	3:30 PM	Speaker: Bostic (President, Atlanta)	-	-	-	-	-
Friday, September 2	8:30 AM	NON-FARM PAYROLLS	(Aug)	(H)	250K	300k	528K
Friday, September 2	8:30 AM	UNEMPLOYMENT RATE	(Aug)	(H)	3.5%	3.5%	3.5%
Friday, September 2	8:30 AM	AVERAGE HOURLY EARNINGS ALL EMPLOYEES M/M	(Aug)	(H)	0.4%	0.4%	0.5%
Friday, September 2	8:30 AM	AVERAGE WEEKLY HOURS ALL EMPLOYEES	(Aug)	(H)	-	34.6	34.6
Friday, September 2	8:30 AM	MANUFACTURING PAYROLLS	(Aug)	(H)	-	18K	30K
Friday, September 2	10:00 AM	FACTORY ORDERS M/M	(Jul)	(M)	-0.2%	0.2%	2.0%

Week Ahead's market call

by Avery Shenfeld

In the **US**, payrolls measures of employment have been running hotter than the household survey, and if August brings those into better alignment, we could see a somewhat below consensus reading on the former, but enough job growth in the latter to keep the unemployment rate steady. Our forecasts are a shade below consensus for other indicators (ISM, confidence, factory orders) so this could be a week that sees a pause in the sell-off in Treasuries and the rally in the USD that has accompanied a few weeks of hawkish Fed messaging in the lead-up to Powell's speech today. We'll need some of these downside surprises to hold the Fed to our forecast for a 50bp hike in September.

In **Canada**, real GDP should be essentially in line with Bank of Canada expectations for Q2, but we'd note that monthly GDP for June, and some of the earliest indicators already out for July, show a notable deceleration. Canada's sizeable outperformance versus the US in Q2 owes to the later re-awakening in services activity as Covid-19 restraints eased, spurring a huge lift to consumption in the spring. But as in the US, a moderation is likely in interest-sensitive consumption (particularly on items that are tied to housing). Still, barring a big miss on Q2 GDP, the Bank of Canada still seems likely to opt for a 75 basis point hike in September given the recent momentum in core inflation readings.

Week Ahead's key Canadian number: Gross domestic product—June and Q2

(Wednesday, 8:30 am)

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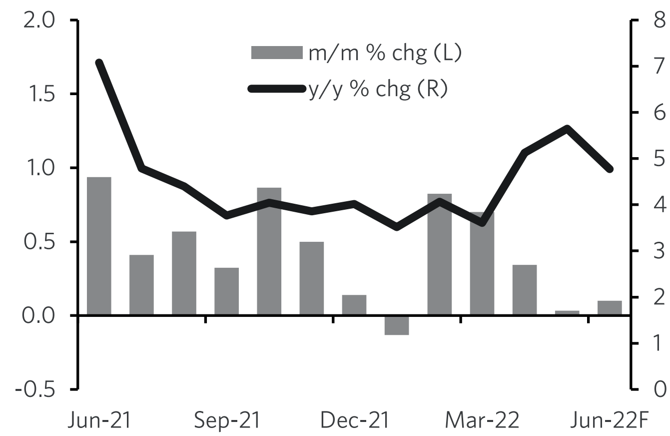
Variable (%)	CIBC	Mkt	Prior
GDP Jun (m/m)	0.1	-	0.0
GDP Q2 (annualized)	4.2	-	3.1

Chart: Canadian Gross domestic product



Source: Statistics Canada, Haver Analytics, CIBC

A quick start likely meant that Q2 growth was stronger than Q1's solid pace, despite the second quarter ending with a whimper. The drivers of growth in Q2 were very different from those that underpinned the advance at the start of the year. Residential investment went into a quick reverse as interest rates started to rise rapidly, but consumer spending on services has ramped up strongly with the lifting of travel and other restrictions. Export volumes also rebounded from Q1's decline, but remain well below their pre-pandemic levels due to the persistence of supply chain disruptions in some areas.

While the monthly industry data appear to be tracking an annualized growth rate of roughly 4½% in Q2, we are forecasting a little below that at 4.2% due to the large negative impact expected from housing. The advance estimate for July may show Q3 started on a weak footing, with industry data suggesting declines in retail, manufacturing and wholesale during the month (albeit partly due to lower prices).

Forecast implications — Quarterly GDP figures are often viewed as old news when they are released, and that is probably even more valid in this instance because the strong headline growth rate will largely reflect an economic acceleration over the spring. The broadly flat trend in monthly GDP more recently, combined with our expectation that July's advance print will be on the soft side, likely sets us up for a marked deceleration in Q3.

Other Canadian releases: Current account—Q2

(Tuesday, 8:30 am)

Surging commodity prices, swelling the goods trade surplus, likely outweighed a widening deficit on the services side within Q2's current account data. The $6.4bn surplus we forecast would be the largest since Q1 2006.

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

(Friday, 8:30 am)

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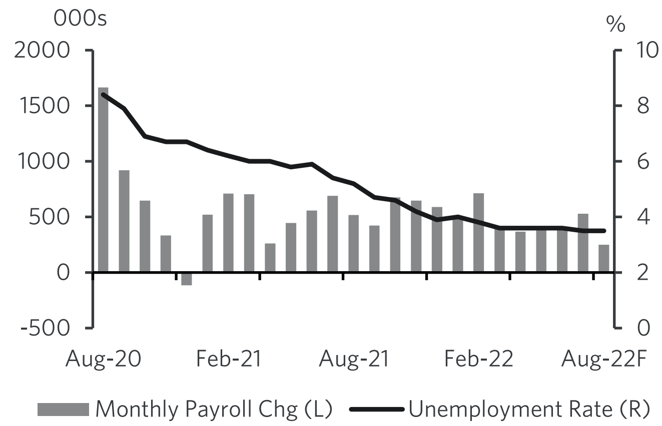
Variable	CIBC	Mkt	Prior
Employment (m/m)	250K	-	528K
Unemployment rate	3.5%	-	3.5%
Avg hourly earnings (m/m)	0.4%	-	0.5%

Chart: US payroll employment



Source: BLS, Haver Analytics, CIBC

After a stellar performance in July, the US labor market is poised for a slowdown in August, in line with the cooling in interest-sensitive sectors. The likely creation of 250K jobs would still be a healthy print, however, and that could leave the unemployment rate at a tight 3.5%, assuming some increase in labor force participation.

The expected slowdown in hiring would also be better aligned with other measures of activity that have looked softer lately, including the household survey employment figures, the ISM services employment sub-index, the Conference Board's labor differential, the easing in the job vacancy rate, and the GDP data. While the GDI data released this week showed growth in Q2, in contrast to the decline in the GDP data, employment growth in the establishment survey still looks overstated relative to that measure.

Forecast implications — We expect hiring to slow ahead as higher interest rates weigh on activity, something that is a precursor for the Fed to slow the pace of rate hikes.

Market impact — We're below the consensus which could be negative for the USD and see bond yields fall.

Other US Releases: ISM Manufacturing—August

(Thursday, 10:00 am)

Moves in regional PMIs suggest that the ISM's manufacturing index could have fallen to 51.9 in August. That could reflect softness in new orders as the outlook for demand has dimmed, a slowdown in the production measure, and a further drop in the supplier deliveries sub-index, which would be consistent with the easing in supply chain issues.

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