

Economics

THE WEEK AHEAD

January 16-20, 2023

"Transitory" wasn't ALL wrongby Avery Shenfeld avery.shenfeld@cibc.com

A word that was seen as so ill-judged that it's been banished from America's economic lexicon won't now make a comeback, but perhaps it should. Those who labelled the inflation upsurge of 2021 and early 2022 as "transitory" ended up with egg on their faces. But the CPI's behaviour in recent months suggests that at least some of what we've gone through on the inflation front was indeed befitting of that label, if we waited long enough.

It was always clear, of course, that gasoline prices would at some point at least have to level off, since world oil prices don't rise forever. But core inflation has now also decelerated notably, at least in the last three months (Chart), during which the annualized pace, at 3.1%, was no longer miles above the Fed's target.

What's key is that has happened before we've actually seen any material slack in the labour market, let alone an outright recession. That points to what the transitory team was noting, if overstating, in 2021: inflation was at least in part being driven by forces other than a simple overheating in demand.

And those forces are now dissipating. Supply chains have improved and shipping costs have retreated. Inventories of non-auto goods are no longer in short supply, and so the usual discounting of stuff that's not selling briskly is back in style. Consumers have rebalanced their purchases away from the goods that were excessively favoured at the height of the pandemic (essentially everything associated with hunkering down at home) towards a more typical mix of goods and services. That's helped relieve the price pressures on an overheated goods sector.

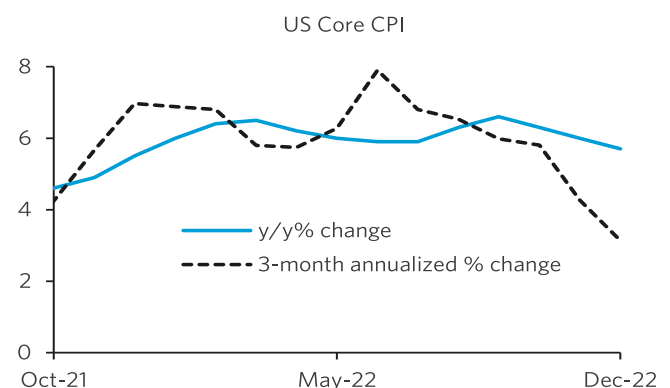
Services inflation is still running too hot, but much of that lies in the shelter component. It's capturing large rent increases that are working their way across the country as Americans' leases come due. But at the margin, those market rates are no longer climbing, which suggests that leases coming up later in 2023 will no longer be seeing large resets to higher rents.

Markets are understandably treating this as good news. If inflation wasn't all due to excess demand, we don't need as much of an economic winter to bring it back down to earth. That opens the door for a gentler path for monetary policy than would have been the case if none of the inflation pressures were transitory.

That's not to say that the Fed's work is done. Wages are still too hot to be consistent with 2% inflation, so we'll need to open up some slack. Pushing the jobless rate higher will require a few quarters of negligible growth, and we expect the central bank to carry on with a half point hike in February. They'll have to stick to that level through 2023 to allow its economic drag to take hold. A too transitory period of elevated interest rates won't do the job.

That's a more hawkish take than what's priced into the Treasuries curve right now, but not quite as threatening as the last set of "dots" from the FOMC. For equities, it means that the rough patch for corporate profits that we're facing in 2023 might not have to last as long. An earnings dip that proves transitory should prove less damaging to valuations.

Chart: US core inflation has dropped off sharply



Source: BLS, 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, January 16	8:30 AM	MANUFACTURING SHIPMENTS M/M	(Nov)	(M)	-	-	2.8%
Monday, January 16	9:00 AM	EXISTING HOME SALES M/M	(Dec)	(M)			-3.3%
Monday, January 16	10:30 AM	BoC Business Outlook Survey	(4Q)	-	-	-	-
Monday, January 16	10:30 AM	BoC Canadian Survey of Consumer Expectations	(4Q)	-	-	-	-
Tuesday, January 17	-	AUCTION: 3-M BILLS \$9.2B, 6-M BILLS \$3.4B, 1-YR BILLS \$3.4B	-	-	-	-	-
Tuesday, January 17	8:15 AM	HOUSING STARTS SAAR	(Dec)	(M)	-	-	264.2K
Tuesday, January 17	8:30 AM	INT'L. SEC. TRANSACTIONS	(Nov)	(M)	-	-	\$8.46B
Tuesday, January 17	8:30 AM	CPI M/M	(Dec)	(H)	-0.6%	-0.6%	0.1%
Tuesday, January 17	8:30 AM	CPI Y/Y	(Dec)	(H)	6.3%	6.3%	6.8%
Tuesday, January 17	8:30 AM	Consumer Price Index	(Dec)	(M)	-	-	154
Tuesday, January 17	8:30 AM	CPI Core- Median Y/Y%	(Dec)	(M)	-	-	5.0%
Tuesday, January 17	8:30 AM	CPI Core- Trim Y/Y%	(Dec)	(M)	-	-	5.3%
Wednesday, January 18	-	AUCTION: 3-YR CANADAS \$2B	-	-	-	-	-
Wednesday, January 18	8:30 AM	INDUSTRIAL PROD. PRICES M/M	(Dec)	(M)	-	-	-0.4%
Wednesday, January 18	8:30 AM	RAW MATERIALS M/M	(Dec)	(M)	-	-	-0.8%
Thursday, January 19	8:30 AM	WHOLESALE TRADE M/M	(Nov)	(M)	-	-	2.1%
Friday, January 20	8:30 AM	RETAIL TRADE TOTAL M/M	(Nov)	(H)	-0.6%	-	1.4%
Friday, January 20	8:30 AM	RETAIL TRADE EX-AUTO M/M	(Nov)	(H)	-	-	1.7%

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, January 16	-	-	-	-	-	-	-
Tuesday, January 17	8:30 AM	NEW YORK FED (EMPIRE)	(Jan)	(M)	-	-8.7	-11.2
Tuesday, January 17	3:00 PM	Speaker: John C. Williams (Vice Chairman, New York) (Voter)	-	-	-	-	-
Wednesday, January 18	-	20-YR AUCTION: \$12B	-	-	-	-	-
Wednesday, January 18	7:00 AM	MBA-APPLICATIONS	(Jan 13)	(L)	-	-	1.2%
Wednesday, January 18	8:30 AM	RETAIL SALES M/M	(Dec)	(H)	-0.9%	-0.8%	-0.6%
Wednesday, January 18	8:30 AM	RETAIL SALES (X-AUTOS) M/M	(Dec)	(H)	-0.6%	-0.5%	-0.2%
Wednesday, January 18	8:30 AM	RETAIL SALES CONTROL GROUP M/M	(Dec)	(H)	-0.4%	-0.3%	-0.2%
Wednesday, January 18	8:30 AM	PPI M/M	(Dec)	(M)	-0.1%	-0.1%	0.3%
Wednesday, January 18	8:30 AM	PPI M/M (core)	(Dec)	(M)	0.1%	0.1%	0.4%
Wednesday, January 18	8:30 AM	PPI Y/Y	(Dec)	(M)	-	6.8%	7.4%
Wednesday, January 18	8:30 AM	PPI Y/Y (core)	(Dec)	(M)	-	5.5%	6.2%
Wednesday, January 18	9:15 AM	INDUSTRIAL PRODUCTION M/M	(Dec)	(H)	-0.1%	-0.1%	-0.2%
Wednesday, January 18	9:15 AM	CAPACITY UTILIZATION	(Dec)	(M)	79.6%	79.6%	79.7%
Wednesday, January 18	10:00 AM	BUSINESS INVENTORIES M/M	(Nov)	(L)	-	0.4%	0.3%
Wednesday, January 18	10:00 AM	NAHB HOUSING INDEX	(Jan)	(L)	-	31	31
Wednesday, January 18	2:00 PM	FED'S BEIGE BOOK	-	-	-	-	-
Wednesday, January 18	4:00 PM	NET CAPITAL INFLOWS (TICS)	(Nov)	(L)	-	-	\$67.8B
Wednesday, January 18	9:00 AM	Speaker: Raphael W. Bostic (Atlanta)	-	-	-	-	-
Wednesday, January 18	2:00 PM	Speaker: Patrick Harker (Philadelphia) (Non-Voter)	-	-	-	-	-
Wednesday, January 18	5:00 PM	Speaker: Lorie K. Logan (Dallas) (Non-Voter)	-	-	-	-	-
Thursday, January 19	-	AUCTION: 10-YR TIPS \$17B	-	-	-	-	-
Thursday, January 19	8:30 AM	INITIAL CLAIMS	(Jan 14)	(M)	-	212K	205K
Thursday, January 19	8:30 AM	CONTINUING CLAIMS	(Jan 7)	(L)	-	-	1634K
Thursday, January 19	8:30 AM	BUILDING PERMITS SAAR	(Dec)	(H)	1340K	1370K	1351K
Thursday, January 19	8:30 AM	HOUSING STARTS SAAR	(Dec)	(M)	1340K	1351K	1427K
Thursday, January 19	8:30 AM	PHILADELPHIA FED	(Jan)	(M)	-	-11.0	-13.7
Thursday, January 19	9:00 AM	Speaker: Susan M. Collins (Boston) (Voter)	-	-	-	-	-
Thursday, January 19	1:15 PM	Speaker: Lael S Brainard (Governor) (Voter)	-	-	-	-	-
Thursday, January 19	6:35 PM	Speaker: John C. Williams (Vice Chairman, New York) (Voter)	-	-	-	-	-
Friday, January 20	8:30 AM	EXISTING HOME SALES SAAR	(Dec)	(M)	-	3.97M	4.09M
Friday, January 20	8:30 AM	EXISTING HOME SALES M/M	(Dec)	(M)	-	-2.9%	-7.7%
Friday, January 20	9:00 AM	Speaker: Patrick Harker (Philadelphia) (Non-Voter)	-	-	-	-	-
Friday, January 20	1:00 PM	Speaker: Christopher J. Waller (Governor) (Voter)	-	-	-	-	-

Week Ahead's market call

by Avery Shenfeld

In the **US**, we're on the weak side of consensus for December retail sales, although some of that will reflect declining prices for gasoline and some other discounts across the goods sector. As always, this first reading on retailing is subject to some significant revisions, so we'll also be seeing if November's softness in control group sales gets nudged one way or another. We're also expecting to see declines in readings on industrial production and housing starts, adding up to a week of lacklustre data overall, and consistent with what we saw in the last set of ISM indicators. Still, Q4 economic growth likely ended up topping where expectations stood at the start of the quarter, a reason why the Fed still sees the need to nudge rates higher at this point.

In **Canada**, the Bank of Canada is a bigger fan of its Business Outlook survey than we think is warranted given its small and varying sample of firms each quarter, but it will be interesting to see the impacts of developments like higher interest rates and softer gasoline prices in the survey of consumer expectations. Lower pump prices are helping to steer the CPI towards calmer waters, but there are still many non-energy categories running well above the pace consistent with the central bank's objectives. We might see a taste of what's to come in readings on November and December retail sales, with a not that merry holiday season being one potential casualty of the squeeze on Canadians from higher borrowing costs and inflation that has run faster than wages.

Week Ahead's key Canadian number: Consumer price index—December

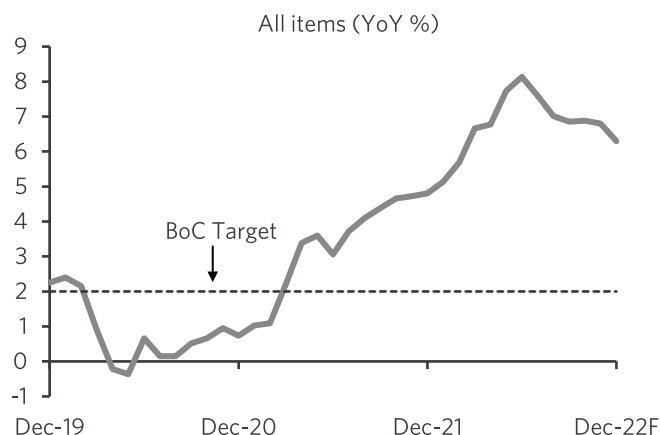
(Tuesday, 8:30 am)

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Variable (%)	CIBC	Mkt	Prior
CPI NSA (m/m)	-0.6	-0.6	0.1
CPI (y/y)	6.3	6.3	6.8

Canadians finally caught a break from ever rising prices in December, albeit mainly at the pumps. A sharp decline in gasoline prices will be the main factor behind an expected 0.6% m/m drop in headline CPI, and a deceleration in the annual rate to 6.3%, from 6.8% in the prior month. Used car prices could also have seen a slight dip. However, there are unfortunately a number of areas in which prices are likely to have risen even further, including food and potentially air fares as demand recovered closer to pre-pandemic norms over the holiday season.

Chart: Canadian consumer price index



Source: Statistics Canada, Haver Analytics, CIBC

Forecast implications — The deceleration in inflation won't be a straight line, and the partial rebound in gasoline prices seen so far in January demonstrates that. However, with inflation in food and other goods prices expected to ease shortly, and services inflation starting to decelerate as the economy slows, we should see much more muted inflationary pressures by early summer.

Other Canadian releases: Retail sales—November

(Friday, 8:30 am)

Retail sales are expected to have fallen by 0.6% in November, although that decline will at least partly reflect lower pump prices. Signs of weakness in consumer goods imports, however, could point to some softness in other retail categories as well as consumer cut back on discretionary purchases in the face of rising interest rates. The advance figure for December could point to another drop in spending during that month.

Week Ahead's key US number: Retail sales—December

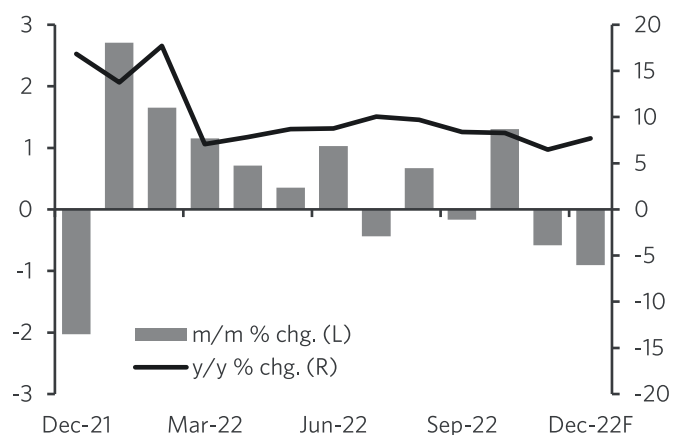
(Wednesday, 8:30 am)

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Vairable (m/m %)	CIBC	Mkt	Prior
Retail sales	-0.9	-0.8	-0.6
- ex auto	-0.6	-0.5	-0.2
- control group	-0.4	-0.3	-0.2

Consumers were cautious about opening their wallets to retailers in November amidst the squeeze from higher interest rates, and that looks to have extended into December. A sharp drop in unit auto sales, combined with a decline in gasoline prices, will weigh on total retail sales, which likely fell by 0.9% in December. That will also likely include a 0.4% decrease in the control group of sales (ex. autos, gasoline, restaurants, and building materials), as sales volumes in that group remain well above their pre-pandemic trend line, and spending likely continued to be skewed towards services in December, away from discretionary goods.

Chart: US retail sales (%)



Source: Census Bureau, Haver Analytics, CIBC

Forecast implications — Another decline in goods consumption will add to bloated inventory levels for many retailers, putting downward pressure on prices, and helping the Fed to achieve its inflation target later in the year.

Market impact — We are more pessimistic than the consensus, which could cause bond yields and the USD to ease off.

Other US Releases: Industrial production—December

(Wednesday, 9:15 am)

The drop in hours worked in manufacturing in December is in line with the deterioration in the ISM's production index, and will limit industrial production. Oil rig counts were little changed, suggesting that total industrial production likely fell by 0.1%.

Housing starts—December

(Thursday, 8:30 am)

Plummeting building permit issuance in November, a further drop in homebuilder confidence in December, and a likely reversal of fortunes for the volatile multi-family sector all point to a retrenchment in homebuilding in December, to a 1340K pace, while building permit issuance could have eased to 1340K as well.

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