Economics

THE WEEK AHEAD

August 14 - 18, 2023

The China Syndrome

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

The 1979 Jane Fonda flick, “The China Syndrome”, depicted a fictional meltdown of a nuclear reactor, not the recent meltdown of China’s economic recovery. A host of indicators have confirmed that the Middle Kingdom’s post-lockdown spurt has given way to little if any momentum. How worried should commodities markets be, particularly those that feasted on Chinese demand gains in prior decades?

In part, a 2020s downshift for China was inevitable. Productivity gains tied to moving rural people to urban industrialized centres had to slow as the scope for that shift diminished. While policy decisions exacerbated the trend, income gains tend to lower fertility rates, reducing growth tied to an expanding workforce.

But China’s prior gains leaned heavily on growth in its export market share, and related massive advances in industrial capital spending. While there’s still work to be done in areas like green energy, there was less room for further industrial modernization. As that slowed, capital spending was then tilted towards a similarly unsustainable pace for residential investment.

Two additional headwinds have emerged more recently. First, there is a bipartisan US move to wean itself off some Chinese exports and starve its access to certain advanced technologies. That generates uncertainty in the corporate world about relying on supply chains with heavy Chinese content. Beijing’s policies also tilted to favour state-owned enterprises, raising uncertainties for private sector entrepreneurs who had previously been growth leaders.

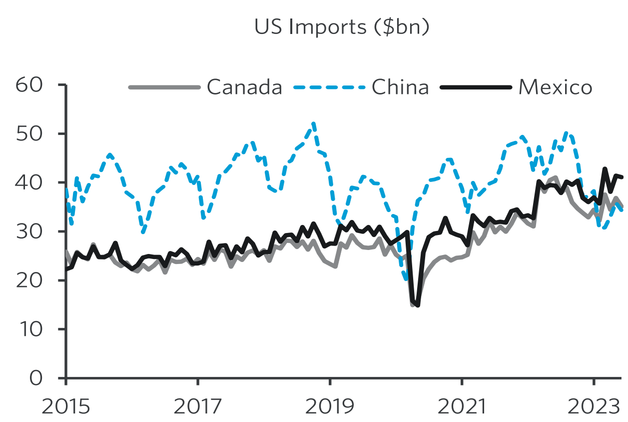
China’s economy won’t melt down forever, nor will it be fully supplanted as a major source for goods it already dominates. But at the margin, plant location decisions could favour other countries. Friendshoring, re-globalization, and subsidization may be part of what’s allowed Mexico to exclipse China as a source for US imports, and for Canada to pull into a dead heat for the number two position (Chart), while also sparking a boom in manufacturing-related construction in America.

China will respond with more aggressive steps to envigorate domestic consumer demand. That might see it become more of an importer of final consumption goods, and will entail less need for commodities-intensive capital investment in heavy industry. Still, even 5% growth might be difficult to sustain given the new trade and geopolitical realities.

Make no mistake. China will remain a major consumer of industrial materials. Last year, even with lockdowns, China accounted for more than half of the world’s refined copper usage.

But as growth in its resource consumption falls short of previous decades or forecasts, resource producers might not feel as much pain as a focus on China would indicate. We might find replacement markets in the likes of Mexico, Vietnam, India and perhaps even in the US to the extent that some of that missing Chinese industrial and construction activity is picked up elsewhere. We’re still mired in a slow patch for global growth as central banks fend off inflation, but the next upleg could be a bit less reliant on China than what we’ve seen in the past.

Chart: US imports: Mexico passes China, Canada catches up



Source: US Census Bureau, 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, August 14	10:30 AM	Release: Senior Loan Officer Survey	-	-	-	-	-
Tuesday, August 15	-	AUCTION: 3-M BILLS $14.6B, 6-M BILLS $5.2B, 1-YR BILLS $5.2B	-	-	-	-	-
Tuesday, August 15	8:30 AM	MANUFACTURING SHIPMENTS M/M	(Jun)	(M)	-2.0%	-2.0%	1.2%
Tuesday, August 15	8:30 AM	CPI M/M	(Jul)	(H)	0.4%	0.3%	0.1%
Tuesday, August 15	8:30 AM	CPI Y/Y	(Jul)	(H)	3.1%	3.0%	2.8%
Tuesday, August 15	8:30 AM	Consumer Price Index	(Jul)	(M)	-	-	157.2
Tuesday, August 15	8:30 AM	CPI Core- Median Y/Y%	(Jul)	(M)	-	-	3.9%
Tuesday, August 15	8:30 AM	CPI Core- Trim Y/Y%	(Jul)	(M)	-	-	3.7%
Tuesday, August 15	9:00 AM	EXISTING HOME SALES M/M	(Jul)	(M)	-	-	1.5%
Wednesday, August 16	8:15 AM	HOUSING STARTS SAAR	(Jul)	(M)	240K	-	281.4K
Thursday, August 17	-	AUCTION: 2-YR CANADAS $4.8B	-	-	-	-	-
Thursday, August 17	8:30 AM	INT'L. SEC. TRANSACTIONS	(Jun)	(M)	-	-	$11.2B
Friday, August 18	8:30 AM	INDUSTRIAL PROD. PRICES M/M	(Jul)	(M)	-	-	-0.6%
Friday, August 18	8:30 AM	RAW MATERIALS M/M	(Jul)	(M)	-	-	-1.5%

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 14	-	-	-	-	-	-	-
Tuesday, August 15	8:30 AM	RETAIL SALES M/M	(Jul)	(H)	0.2%	0.4%	0.2%
Tuesday, August 15	8:30 AM	RETAIL SALES (X-AUTOS) M/M	(Jul)	(H)	0.3%	0.4%	0.2%
Tuesday, August 15	8:30 AM	RETAIL SALES CONTROL GROUP M/M	(Jul)	(H)	0.4%	0.5%	0.6%
Tuesday, August 15	8:30 AM	IMPORT PRICE INDEX M/M	(Jul)	(L)	-	0.2%	-0.2%
Tuesday, August 15	8:30 AM	EXPORT PRICE INDEX M/M	(Jul)	(L)	-	0.2%	-0.9%
Tuesday, August 15	8:30 AM	NEW YORK FED (EMPIRE)	(Aug)	(M)	-	-0.4	1.1
Tuesday, August 15	10:00 AM	BUSINESS INVENTORIES M/M	(Jun)	(L)	-	0.2%	0.2%
Tuesday, August 15	10:00 AM	NAHB HOUSING INDEX	(Aug)	(L)	-	56.0	56.0
Tuesday, August 15	4:00 PM	NET CAPITAL INFLOWS (TICS)	(Jun)	(L)	-	-	$25.8B
Tuesday, August 15	11:00 AM	Speaker: Neel Kashkari (Minneapolis) (Voter)	-	-	-	-	-
Wednesday, August 16	7:00 AM	MBA-APPLICATIONS	(Aug 11)	(L)	-	-	-3.1%
Wednesday, August 16	8:30 AM	BUILDING PERMITS SAAR	(Jul)	(H)	1450K	1470K	1441K
Wednesday, August 16	8:30 AM	HOUSING STARTS SAAR	(Jul)	(M)	1435K	1448K	1434K
Wednesday, August 16	9:15 AM	INDUSTRIAL PRODUCTION M/M	(Jul)	(H)	0.3%	0.3%	-0.5%
Wednesday, August 16	9:15 AM	CAPACITY UTILIZATION	(Jul)	(M)	79.2%	79.1%	78.9%
Wednesday, August 16	2:00 PM	FOMC Meeting Minutes	(Jul 26)	-	-	-	-
Thursday, August 17	8:30 AM	INITIAL CLAIMS	(Aug 12)	(M)	-	239K	248K
Thursday, August 17	8:30 AM	CONTINUING CLAIMS	(Aug 5)	(L)	-	1700K	1684K
Thursday, August 17	10:00 AM	LEADING INDICATORS M/M	(Jul)	(M)	-	-0.4%	-0.7%
Friday, August 18	-	-	-	-	-	-	-

Week Ahead's market call

by Avery Shenfeld

In the **US**, we're a touch weaker than consensus in our calls for retail sales, but the control group would still represent a healthy gain coming off a strong prior month. We're looking for a flat reading on housing starts, but industrial production could see a rebound as hot weather boosts utility output. The FOMC minutes won't shed much light on a September decision, since that move is clearly data dependent, and we still have readings on CPI and payrolls before the Fed actually has to make that call.

In **Canada**, we're on the high side of consensus for the headline CPI, but market reaction and the Bank of Canada's take on the news will still rest on the details and the various core measures. As in the US, we're losing the easy disinflation that we've enjoyed from falling year-on-year prices for oil and gasoline, and we're still facing upward pressure in the mortgage interest component. We're confident about reaching a 2% inflation pace ahead of the Bank of Canada's schedule, but we'll need some elapsed time for the trend towards more labour market slack to dampen both wages and prices ahead. We're likely to see some softness in both housing starts and manufacturing shipments, consistent with our call for an economic cooling ahead.

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

(Tuesday, 8:30 am)

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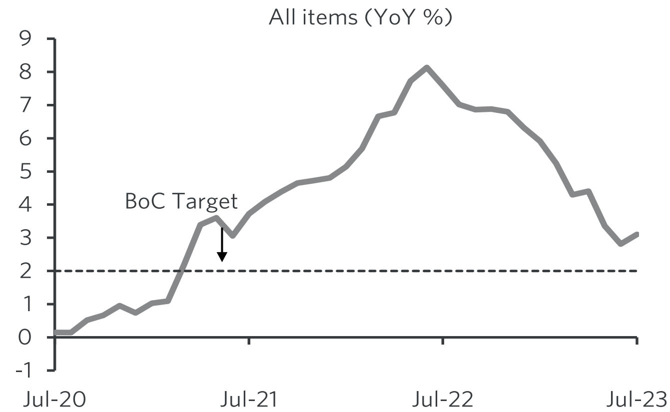
Variable (%)	CIBC	Mkt	Prior
CPI NSA (m/m)	0.4	0.3	0.1
CPI (y/y)	3.1	3.0	2.8

Chart: Canadian consumer price index



Source: Statistics Canada, Haver Analytics, CIBC

With gasoline prices on the rise this July, in contrast to a decline seen twelve months ago, Canadian inflation will likely look a little hotter than it did in June. Indeed, we see headline inflation accelerating to 3.1%, from 2.8%, even with a modest deceleration in food price inflation. The monthly increase in prices excluding food & energy could also look a bit hotter than in the prior two months, with the deceleration in mortgage interest costs potentially stalling and prior negative contributions to inflation from internet and telephone services unlikely to be repeated. Still, even penciling in a monthly gain in ex food/energy prices of 0.3% on a seasonally adjusted basis, the annual rate of inflation for that core measure would still decelerate to 3.4%, from 3.6% in June.

Forecast implications — With gasoline prices on the rise again in August, headline inflation could accelerate further to roughly 3½% by the end of the summer. Unless core measures of inflation show signs of deceleration beneath this headline acceleration, one more interest rate hike by the Bank of Canada cannot yet be ruled out.

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

(Tuesday, 8:30 am)

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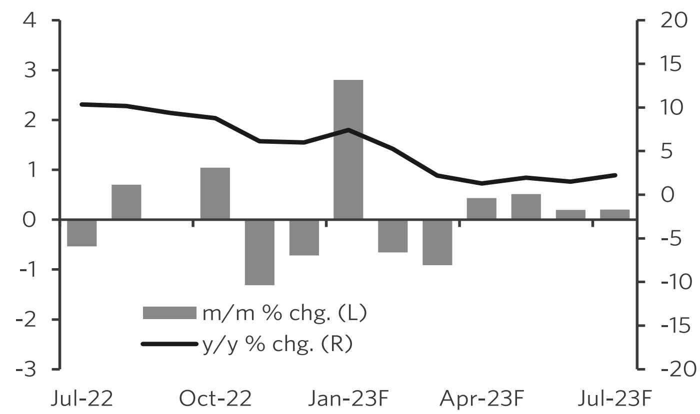
Variable (%)	CIBC	Mkt	Prior
Retail sales	0.2	0.4	0.2
Retail sales - ex auto	0.3	0.4	0.2
Retail sales - control group	0.4	0.5	0.6

Chart: US retail sales (%)



Source: Census Bureau, Haver Analytics, CIBC

Aggregate personal income growth appears to have slowed in July, and nominal retail sales growth was likely limited as a result, compounded by a decline in core goods prices. Total retail sales likely rose by 0.2% m/m, with the more important control group of sales, which excludes gasoline, autos, restaurants, and building materials, that feeds more directly into non-auto goods consumption in GDP, poised to cool to a still-respectable 0.4% m/m.

Forecast implications — Goods consumption slowed sharply in the second quarter, and is likely to be limited further ahead by the weight of higher interest rates. With the inventory-to-sales ratio comfortably at pre-pandemic levels (outside of auto dealerships), core goods prices aren't likely to present a threat to the Fed's inflation target.

Market impact — We're more pessimistic than the consensus on the headline, but we're nearly in line on the more important control group, which should limit any market reaction.

Other US Releases: Industrial production—July

(Wednesday, 9:15 am)

Hours worked plummeted for factory workers in July, while manufacturers reduced headcounts, and oil rig counts continued their descent. However, heat waves across the country will have supported utilities production, suggesting a rebound in total industrial production to 0.3% m/m, which would have left capacity utilization a little off of its pandemic peak at 79.2%.

Housing starts—July

(Wednesday, 8:30 am)

Homebuilding plunged in June and could have remained steady at 1435K in July, moving into closer alignment with the typical gap to the pace of building permit issuance. Home purchase intentions receded in July as mortgage rates climbed, and we expect elevated interest rates over the rest of the year to keep a lid on housing market activity.

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