

Economics

THE WEEK AHEAD

October 14 - 18, 2024

Could fiscal follies foil the Fed?

by Avery Shenfeld avery.shenfeld@cibc.com

With a US election only weeks away, fixed income investors need to give some thought to how its outcome could impact the Fed's decisions in 2025. Trade policy is an unpredictable wild card that we addressed elsewhere, but fiscal policy could also weigh on the Fed's room to continue on its path towards lower rates. Could an inflationary lift from fiscal stimulus prevent the rate cuts that markets are now counting on?

US budget deficits are unlikely to be materially lower in the years ahead, as neither Harris nor Trump have offered a recipe for restraint. Instead, campaign speeches have sounded more like the giveaways on the Oprah Winfrey show: you get a tax cut, you get a tax cut, you get a government payout. We've learned to be skeptical about campaign pledges' relevance for what actually gets enacted. But an analysis from the fiscally-conservative-leaning Committee for a Responsible Federal Budget estimated that Trump's pledges could add a further \$7.5 trillion to deficits in the decade ahead, while Harris's plan would run to an additional \$3.5 tn.

Still, there's nothing new in running annual deficits near the \$2 trillion mark, and it's the rate of change rather than the level of budget red ink that matters for monetary policy. Budget projections from the CBO, as well as estimates of the fiscal impulse from the likes of the Brookings Institute and the OECD, show, if anything, a small net drag as the deficit narrows marginally in the fiscal year ahead. While that might not pick up the lagged impacts as funds already appropriated work their way into renewable power or auto sector projects, fiscal policy as it stands should be not far from neutral for growth.

A new President may not have much ability to alter that course until we move into fiscal 2026. Congress will have to extend a temporary spending deal reached just before the election adjournment which expires in December, during the dying days of the current Administration. That could cement spending levels for fiscal 2025.

Tax cuts offered by a new President aren't likely to come up for a vote in time to be applicable in 2025. Recall that it took a full year after his inauguration for Trump to sign his tax cut bill into law. And the Fed isn't in the habit of basing its outlook, or its policy decisions, on what might be in store fiscally in years ahead, if those measures have not yet been enacted.

If anything, market expectations for a long run of fiscal red ink beyond 2025 could force the Fed into more, rather than fewer, rate cuts for 2025. Higher borrowing needs can be a factor that leans towards a steeper yield curve, preventing 10 year corporate bond yields, or households' 30 year mortgage rates, from getting as much of a benefit from a lower fed funds rate. There's no reason to expect one more year of high deficits to lead to a sudden eruption of bond market vigilantism, but at the margin, fiscal fears seem to already be keeping the long end from a more material rally.

So for the Fed, and the bond market, the election result might not provide much impetus for at least the first half of 2025. We'll learn more when, further into the year, Congress takes up appropriations and tax policy for 2026 and beyond. And as we've seen in recent years, it's the make-up of Congress, not only in the division among the parties, but within the GOP, the balance between MAGA deficit doves and more traditional fiscal hawks, that will draw any fiscal lines in the sand. If the economy remains sound, the hawks might not win a vote for outright restraint, but could still be positioned to block a net increase in stimulus.

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, October 14	-	Markets Closed (Thanksgiving)	-	-	-	-	-
Tuesday, October 15	8:30 AM	WHOLESALE SALES EX-PETROLEUM M/M	(Aug)	(M)	-1.0%	-1.1%	0.4%
Tuesday, October 15	8:30 AM	CPI M/M	(Sep)	(H)	-0.4%	-0.2%	-0.2%
Tuesday, October 15	8:30 AM	CPI Y/Y	(Sep)	(H)	1.7%	1.9%	2.0%
Tuesday, October 15	8:30 AM	Consumer Price Index	(Sep)	(M)	-	161.5	161.8
Tuesday, October 15	8:30 AM	CPI Core- Median Y/Y%	(Sep)	(M)	2.3%	2.3%	2.3%
Tuesday, October 15	8:30 AM	CPI Core- Trim Y/Y%	(Sep)	(M)	2.5%	2.4%	2.4%
Tuesday, October 15	9:00 AM	EXISTING HOME SALES M/M	(Sep)	(M)	-	-	1.3%
Wednesday, October 16	8:15 AM	HOUSING STARTS SAAR	(Sep)	(M)	225.0K	235.0K	217.4K
Wednesday, October 16	8:30 AM	MANUFACTURING SHIPMENTS M/M	(Aug)	(M)	-1.5%	-1.5%	1.4%
Thursday, October 17	-	AUCTION: 10-YR CANADAS \$5B	-	-	-	-	-
Thursday, October 17	8:30 AM	INT'L. SEC. TRANSACTIONS	(Aug)	(M)	-	-	\$11.0B
Friday, October 18	-	-	-	-	-	-	-

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, October 14	-	Treasury Markets Closed (Columbus Day)	-	-	-	-	-
Monday, October 14	-	Bond Market Closed (Columbus Day)	-	-	-	-	-
Monday, October 14	9:00 AM	Speaker: Neel Kashkari (Minneapolis) (Non-Voter)	-	-	-	-	-
Monday, October 14	3:00 PM	Speaker: Christopher J. Waller (Governor) (Voter)	-	-	-	-	-
Monday, October 14	5:00 PM	Speaker: Neel Kashkari (Minneapolis) (Non-Voter)	-	-	-	-	-
Tuesday, October 15	8:30 AM	NEW YORK FED (EMPIRE)	(Oct)	(M)	-	1.0	11.5
Tuesday, October 15	8:30 AM	TREASURY BUDGET	(Sep)	(L)	-	\$4.3B	\$380.1B
Tuesday, October 15	11:30 AM	Speaker: Mary C. Daly (San Francisco) (Voter)	-	-	-	-	-
Tuesday, October 15	1:00 PM	Speaker: Adriana D. Kugler (Governor) (Voter)	-	-	-	-	-
Wednesday, October 16	7:00 AM	MBA-APPLICATIONS	(Oct 11)	(L)	-	-	-5.1%
Wednesday, October 16	8:30 AM	IMPORT PRICE INDEX M/M	(Sep)	(L)	-	-0.3%	-0.3%
Wednesday, October 16	8:30 AM	EXPORT PRICE INDEX M/M	(Sep)	(L)	-	-0.4%	-0.7%
Thursday, October 17	8:30 AM	INITIAL CLAIMS	(Oct 12)	(M)	-	-	258K
Thursday, October 17	8:30 AM	CONTINUING CLAIMS	(Oct 5)	(L)	-	-	1861K
Thursday, October 17	8:30 AM	RETAIL SALES M/M	(Sep)	(H)	0.4%	0.2%	0.1%
Thursday, October 17	8:30 AM	RETAIL SALES (X-AUTOS) M/M	(Sep)	(H)	0.0%	0.1%	0.1%
Thursday, October 17	8:30 AM	RETAIL SALES CONTROL GROUP M/M	(Sep)	(H)	0.2%	0.3%	0.3%
Thursday, October 17	9:15 AM	INDUSTRIAL PRODUCTION M/M	(Sep)	(H)	-0.2%	-0.1%	0.8%
Thursday, October 17	9:15 AM	CAPACITY UTILIZATION	(Sep)	(M)	78.0%	77.8%	78.0%
Thursday, October 17	10:00 AM	BUSINESS INVENTORIES M/M	(Aug)	(L)	-	0.3%	0.4%
Thursday, October 17	10:00 AM	NAHB HOUSING INDEX	(Oct)	(L)	-	43.0	41.0
Thursday, October 17	4:00 PM	NET CAPITAL INFLOWS (TICS)	(Aug)	(L)	-	-	\$135.4B
Thursday, October 17	11:00 AM	Speaker: Austan D. Goolsbee, Chicago (Non-Voter)	-	-	-	-	-
Friday, October 18	8:30 AM	HOUSING STARTS SAAR	(Sep)	(M)	1400K	1350K	1356K
Friday, October 18	8:30 AM	BUILDING PERMITS SAAR	(Sep)	(H)	1500K	1460K	1470K
Friday, October 18	10:00 AM	Speaker: Neel Kashkari (Minneapolis) (Non-Voter)	-	-	-	-	-
Friday, October 18	10:00 AM	Speaker: Neel Kashkari (Minneapolis) (Non-Voter)	-	-	-	-	-
Friday, October 18	12:10 PM	Speaker: Christopher J. Waller (Governor) (Voter)	-	-	-	-	-

Week Ahead's market call

by Ali Jaffery and Katherine Judge

In the **US**, we're slightly below consensus in calling for a soft retail sales print and industrial production report. Fed speakers next week will likely talk about the benefits of gradualism again given the labor market does not look like its breaking and inflation is still slightly above target. Waller's speech on the outlook on Monday is the main event.

In **Canada**, the CPI data will be the final piece of major information that the Bank of Canada receives on the economy ahead of the October meeting. Headline inflation is expected to dip below target and look even more muted excluding mortgage interest costs. Forward-looking indicators of inflation in the BoC's business outlook survey suggest ongoing muted demand and wage pressures, which make the possibility of a 50bp cut likely at the meeting, should its core inflation measures not surprise to the upside.

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

(Tuesday, 8:30 am)

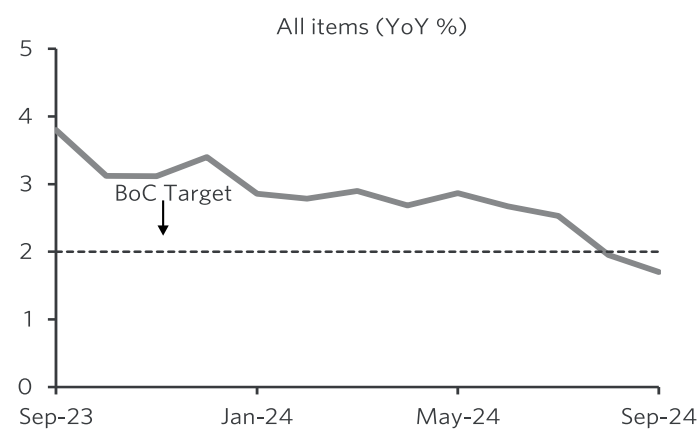
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Variable (%)	CIBC	Mkt	Prior
CPI NSA (m/m)	-0.4	-0.2	-0.2
CPI (y/y)	1.7	1.9	2.0

After hitting the 2% target in August, inflation likely dipped below that mark in September. A further drop in gasoline prices likely drove a 0.4% decline in the CPI index during the month (0.0% seasonally adjusted), seeing the annual rate of inflation decelerate to 1.7% year-over-year. High inventory levels in the retail space should keep goods prices under pressure, despite a modest pick up in spending recently. The last remaining source of inflationary pressure, shelter, should continue to decelerate as mortgage interest payments rise at a slower pace.

The core measures of CPI-trim and CPI-median are likely to have risen by 0.2% on the month. However, due to base effects, this could result in a marginal bump up in the annual rate of the former. We continue to view other cores measures of inflation, such as CPI-X, as being better indicators of underlying price pressures and that is likely to continue running weaker than CPI-Trim and Median.

Chart: Canadian consumer price index



Source: Statistics Canada, Haver Analytics, CIBC

Forecast implications — With gasoline prices up modestly so far in October, inflation may reaccelerate slightly ahead and as a result September's print could mark the low point in inflation for the year. However, we continue to believe that there is ample spare capacity within the Canadian economy so, unless growth recovers quicker than we think, inflation could fall further below the 2% target during certain points in 2025.

Week Ahead’s key US number:
Retail sales—September

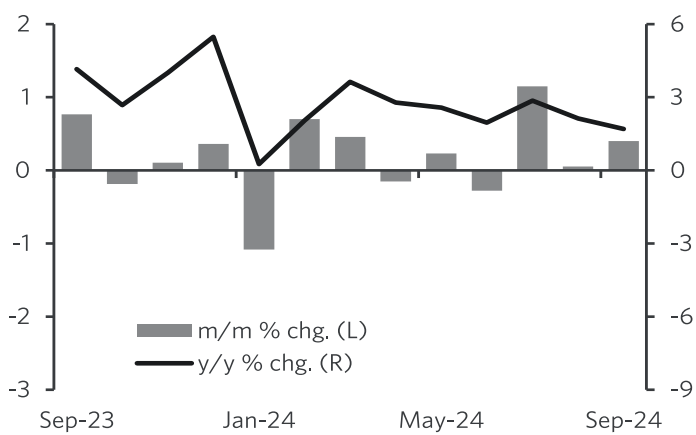
(Thursday, 8:30 am)

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Variable (m/m,%)	CIBC	Mkt	Prior
Retail sales	0.4	0.2	0.1
Retail sales - ex auto	0.0	0.1	0.1
Retail sales - control group	0.2	0.3	0.3

We expect consumer spending to remain solid in September, with headline retail sales boosted by a rebound in auto sales. Excluding autos, however, growth should be flat and the control group, which feeds into non-auto goods consumption in the national accounts, should come in a bit softer at 0.2%. The revisions to income and the saving rate mean consumers’ wallets are still pretty full, benefitting from higher asset income. Although the labor market has cooled, it has not cooled enough to materially crimp income yet. These solid fundamentals, combined with a new preference for durable goods means the trend in consumption isn’t likely to bend much in the near-term.

Chart: US retail sales



Source: Census Bureau, Haver Analytics, CIBC

Forecast implications — We expect growth of 2.5% in 24Q3 and consumption growth to be around 3% again. The CPI data this week suggests a high hurdle rate for retail sales to add further to that growth, with core goods prices increases by 0.2% in September. Based on our forecast, we are expecting flat retail sales in inflation-adjusted terms in the month.

Market implications — With the labor market data and CPI data showing a firmer economy, markets will look for more signals for the end of Powell’s “front-loading” of rate cuts.

Other US Releases:
Industrial production—September

(Thursday, 9:15 am)

Industrial production should decrease by 0.2% in the month, as manufacturing production is slowed down by hurricane-related disruptions.

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