

May 20 - 24, 2024

You are what you eat

by Avery Shenfeld avery.shenfeld@cibc.com

The adage that “you are what you eat” clearly applies to inflation in your waistline, but it turns out, is also befitting when it comes to core measures of price inflation in Canada. That might prove to be a helpful hint for market players in the coming week, in which the news on Canada’s CPI for April could tip the balance one way or another on the Bank of Canada’s interest rate decision in June. Should core prices rise by 0.2% or less, a rate cut in next month should be close to a lock, but one month inflation rates aren’t the easiest forecasts to make.

Remember that Canada, unlike the US, long ago dropped prices excluding food and energy as its measure of underlying inflation. Its first alternative, CPI-X, omitted fresh fruits and vegetables, but left all other elements of the food basket in the core measure, on the grounds that they weren’t particularly volatile. The more recently adopted core measures don’t exclude any particular items on a permanent basis, but instead track the median inflation rate, or one that excludes those with particularly large swings on the high or low side in any given month. So food matters when it comes to Canada’s core inflation readings.

Indeed, history suggests that food prices are often central to where the Bank of Canada’s two preferred measures of core inflation tend to head. Its correlation with CPI-trim, for example, is the tightest among the broad categories tracked by the CPI. Of course, it helps that food has a significant weight in the CPI basket. But there’s more to this fit than just its weighing. Food is one of only two categories that has a better link to core inflation than it does to the overall CPI (Chart).

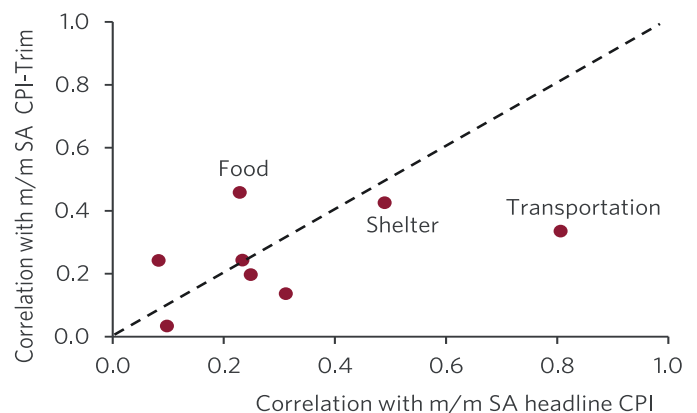
That likely rests on the fact that the “food” group in the CPI captures diverse items that depend on inputs from across the economy. It’s a mix of goods (food at home) and services (food at restaurants). While items like fruits and vegetables can see weather-related volatility, other products draw on inputs that collectively tend to follow the broad trend of inflation over time, including retail and wholesale labour, store/restaurant rents, and transportation services (local and international, using a diverse mix of modes). Moreover, since food is an essential

item, its price trends have some tie to purchasing power across a full range of income groups.

That’s why when looking at exchange rates, a popular shortcut way of assessing purchasing power parity across countries is the so-called “Big Mac Index”. A burger at the world’s biggest fast food chain isn’t just beef patties, “special sauce”, lettuce, cheese, pickles, onions and a sesame-seed bun. It also embodies retail rents, restaurant labour, and some advertising dollars as well, given that we all seem to know what’s in that Big Mac. That breadth, and of course its consistent make-up, is why it’s been used as a benchmark of what your money will buy internationally.

If food prices again prove indicative of Canada’s core CPI measures in the week ahead’s report, those hoping for interest rate relief might be in luck. The food CPI has been in a well-established cooling trend over the past year. The last three readings from the US, including in their already-released April data, told the same story. So if we are what we eat in terms of inflation, and another cliché, “the trend is your friend,” both hold true in Canada’s April inflation data, we’ll be able to stick to our forecast for a Bank of Canada rate cut in June. Bon appétit.

Chart: Food prices have higher correlation with CPI-Trim than headline inflation



Source: Statistics Canada, BoC, 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 20	-	Markets Closed (Victoria Day)	-	-	-	-	-
Tuesday, May 21	-	AUCTION: 3-M BILLS \$12.2B, 6-M BILLS \$4.4B, 1-YR - BILLS \$4.4B	-	-	-	-	-
Tuesday, May 21	8:30 AM	CPI M/M	(Apr)	(H)	0.5%	0.5%	0.6%
Tuesday, May 21	8:30 AM	CPI Y/Y	(Apr)	(H)	2.7%	2.7%	2.9%
Tuesday, May 21	8:30 AM	Consumer Price Index	(Apr)	(M)	-	160.7	159.8
Tuesday, May 21	8:30 AM	CPI Core- Median Y/Y%	(Apr)	(M)	2.7%	2.7%	2.8%
Tuesday, May 21	8:30 AM	CPI Core- Trim Y/Y%	(Apr)	(M)	2.9%	2.9%	3.1%
Wednesday, May 22	-	AUCTION: 10-YR CANADAS \$5B	-	-	-	-	-
Thursday, May 23	-	-	-	-	-	-	-
Friday, May 24	8:30 AM	RETAIL TRADE TOTAL M/M	(Mar)	(H)	-0.2%	-0.1%	-0.1%
Friday, May 24	8:30 AM	RETAIL TRADE EX-AUTO M/M	(Mar)	(H)	0.3%	-	-0.3%

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 20	8:45 AM	Speaker: Raphael W. Bostic (Atlanta) (Voter)	-	-	-	-	-
Monday, May 20	9:00 AM	Speaker: Michael S Barr (Governor) (Voter) & Christopher J. Waller (Governor) (Voter)	-	-	-	-	-
Monday, May 20	10:30 AM	Speaker: Philip N Jefferson (Governor) (Voter)	-	-	-	-	-
Monday, May 20	7:00 PM	Speaker: Raphael W. Bostic (Atlanta) (Voter)	-	-	-	-	-
Tuesday, May 21	8:30 AM	PHILADELPHIA FED - NON-MANUFACTURING	(May)	(M)	-	-	-12.4
Tuesday, May 21	9:00 AM	Speaker: Thomas I. Barkin (Richmond) (Voter) & Christopher J. Waller (Governor) (Voter)	-	-	-	-	-
Tuesday, May 21	9:05 AM	Speaker: John C. Williams (Vice Chairman, New York) (Voter)	-	-	-	-	-
Tuesday, May 21	9:10 AM	Speaker: Raphael W. Bostic (Atlanta) (Voter)	-	-	-	-	-
Tuesday, May 21	11:45 AM	Speaker: Michael S Barr (Governor) (Voter)	-	-	-	-	-
Tuesday, May 21	7:00 PM	Speaker: Raphael W. Bostic (Atlanta) (Voter)	-	-	-	-	-
Wednesday, May 22	-	AUCTION: 20-YR TREASURIES \$16B	-	-	-	-	-
Wednesday, May 22	7:00 AM	MBA-APPLICATIONS	(May 17)	(L)	-	-	0.5%
Wednesday, May 22	10:00 AM	EXISTING HOME SALES SAAR	(Apr)	(M)	-	4.2M	4.2M
Wednesday, May 22	10:00 AM	EXISTING HOME SALES M/M	(Apr)	(M)	-	-0.1%	-4.3%
Wednesday, May 22	2:00 PM	FOMC Meeting Minutes	(May 1)	-	-	-	-
Wednesday, May 22	9:40 AM	Speaker: Austan D. Goolsbee, Chicago (Non-Voter)	-	-	-	-	-
Thursday, May 23	-	AUCTION: 10-YR TIPS \$16B	-	-	-	-	-
Thursday, May 23	8:30 AM	INITIAL CLAIMS	(May 18)	(M)	-	220K	222K
Thursday, May 23	8:30 AM	CONTINUING CLAIMS	(May 11)	(L)	-	1790K	1794K
Thursday, May 23	8:30 AM	CHICAGO FED NAT.ACTIVITY INDEX	(Apr)	(M)	-	-	0.2
Thursday, May 23	9:45 AM	S&P GLOBAL US SERVICES PMI	(May P)	(L)	-	51.3	51.3
Thursday, May 23	9:45 AM	S&P GLOBAL US COMPOSITE PMI	(May P)	(L)	-	-	51.3
Thursday, May 23	9:45 AM	S&P GLOBAL US MANUFACTURING PMI	(May P)	(L)	-	49.6	50.0
Thursday, May 23	10:00 AM	NEW HOME SALES SAAR	(Apr)	(M)	650K	675K	693K
Thursday, May 23	10:00 AM	NEW HOME SALES M/M	(Apr)	(M)	-6.2%	-2.6%	8.8%
Thursday, May 23	3:00 PM	Speaker: Raphael W. Bostic (Atlanta) (Voter)	-	-	-	-	-
Friday, May 24	8:30 AM	DURABLE GOODS ORDERS M/M	(Apr P)	(H)	-0.5%	-0.8%	0.9%
Friday, May 24	8:30 AM	DURABLE GOODS ORDERS EX-TRANS M/M	(Apr P)	(H)	0.0%	0.1%	0.2%
Friday, May 24	10:00 AM	MICHIGAN CONSUMER SENTIMENT	(May)	(H)	-	67.8	67.4
Friday, May 24	9:35 AM	Speaker: Christopher J. Waller (Governor) (Voter)	-	-	-	-	-

Week Ahead's market call

by Avery Shenfeld

In the **US**, lacklustre readings on durable orders and new home sales will underscore that high interest rates may be having their intended impacts on demand in some interest sensitive sectors of the economy. But one month's retail sales softness isn't enough to conclude that's spreading to consumer spending, and the parade of Fed speakers are therefore likely to dampen any hopes for rate cuts just yet. We'll need a run of cooler CPI readings, and to help drive that, a bit less buoyancy in consumer demand, before we can expect the central bank to give a clearer signal on when they might start to ease.

In **Canada**, we'll get further evidence from retailing that while Q1 showed respectable growth overall, it ended on a softer note. But the CPI data will be key to a June rate cut, and our on-consensus call would see a further deceleration in core inflation readings. Remember that the Governor is on record as saying that he doesn't want to keep rates elevated more than is necessary to get inflation back to target. He's also expressed some satisfaction with inflation prints this year, but a couple of months ago was just looking for a bit more evidence that the trend would persist. Given the lags associated with monetary policy, and the fact that the economy is now operating with some slack, one more reading of mild core inflation should be sufficient justification to back off just a little bit on rates. Should the tame CPI trend hold up, the Bank could see clear to cutting in June and July, while not promising any more than that until we get a clear picture on how the economy and inflation then through the summer. But markets will clearly react to any upside surprise in April inflation.

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

(Tuesday, 8:30 am)

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Variable (%)	CIBC	Mkt	Prior
CPI NSA (m/m)	0.5	0.5	0.6
CPI (y/y)	2.7	2.7	2.9

A sharp rise in gasoline prices will be key in driving a 0.5% NSA (0.2% SA) increase in headline CPI during April. However, with pump prices increasing by a similar amount a year ago, that move should have little impact on the annual rate of inflation. Instead, a continued easing in food price inflation, with monthly increases much more muted than they were throughout most of 2023, should see the year-over-year pace of headline CPI ease to 2.7%, from 2.9% in March.

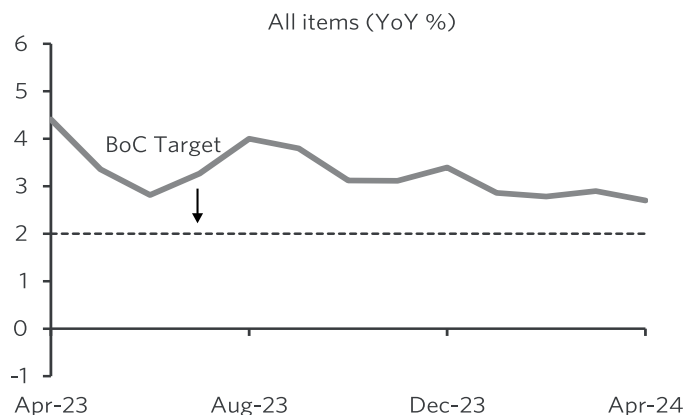
As discussed in the cover article, the levelling off in food prices also appears to have played a large role in bringing weaker monthly changes in the Bank of Canada's trim and median measures of core inflation. That should be the case again in April, seeing the year-over-year rates of those measures ease further and keeping the 3 and 6-month annualized trends much more subdued than they were last year.

Other Canadian releases: Retail sales—March

(Friday, 8:30 am)

Following a strong start to the year, Canadian retail sales appear to be struggling again. We expect a 0.2% drop in headline sales during March, although that will partly reflect a pullback in autos which also contributed to weakness in manufacturing and wholesaling for the same month. A 0.3% increase in sales excluding autos would represent little-change in inflation-adjusted terms, with a rise in gasoline prices driving most of that gain.

Chart: Canadian consumer price index



Source: Statistics Canada, Haver Analytics, CIBC

Forecast implications — While headline inflation remains above target, a continuation of the recent soft trend in core measures should provide the Bank of Canada the comfort it needs to gradually start reducing interest rates as early as the June meeting.

Week Ahead's key US number: Durable goods orders—April

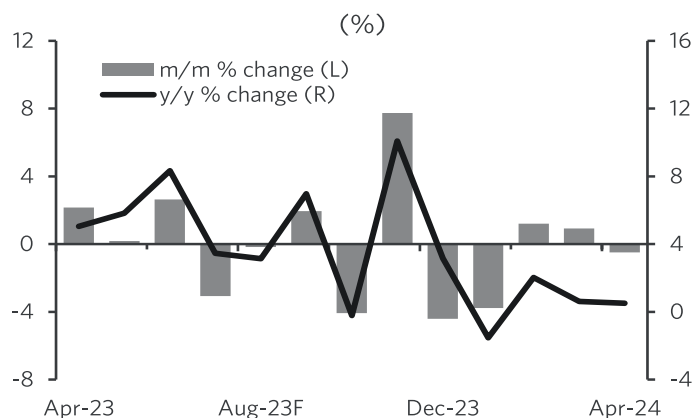
(Friday, 8:30 am)

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Variable (%)	CIBC	Mkt	Prior
Durable goods orders m/m	-0.5	-0.8	0.9
Ex. transportation m/m	0.0	0.1	0.0

Durable goods orders started the year off on a soft note, with the three-month annualized change at just under a 7% contraction as of March, or an almost 2% decline when excluding the volatile transportation category. We expect that trend to continue in April, with durable goods orders contracting by 0.5% m/m, and growth should be flat when excluding transportation. The surge in commercial aircraft orders seems behind us and there is also slower momentum in high-technology sector such as computers and electrical equipment. The softness in orders likely reflects a combination of a fading fiscal impulse from the CHIPS Act, restrictive monetary policy and slow global growth more generally.

Chart: US durable goods orders



Source: Census Bureau, Haver Analytics, CIBC

Forecast implications — Equipment investment has essentially seen no growth since the middle of 2022, its peak during this cycle. That is a reasonable guess for the Q2 forecast, particularly with a tepid start to the quarter. With structures investment also fading for similar reasons, as fiscal support that was aiding manufacturing structures appears to have peaked, overall business investment is likely to turn weaker in the quarter, and perhaps the year as a whole.

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