

Economics

THE WEEK AHEAD

April 11-15, 2022

Market and the BoC: No tiff now

by Avery Shenfeld avery.shenfeld@cibc.com

Financial markets have no tiff with the Bank of Canada at this point, since both are likely on the same page in terms of what's needed next week. Expectations have settled in on what is also a nearly universal forecast by street economists, which has Governor Macklem taking the overnight rate up 50 basis points, and letting government of Canada bonds start to roll out of the central banks holdings as they mature. So what else will there be to be gleaned from the week ahead's statement and Monetary Policy Report?

Pay no attention to what will be a hawkish tone to the rate hike statement. There's no such thing as a dovish statement when you're announcing a 50-basis point hike, unless you're sure it's the last tightening needed. The statement has to be devoted to explaining to Canadians why we need the pain of higher borrowing costs, so there's no room for anything that sounds like concerns about sub-par growth or a lack of inflation pressures.

In prior years we would have paid a good deal of attention to the estimate for the output gap, a measure of economic slack that was the single best indicator for central bank rate decisions ahead. That's no longer the case, because given all the supply chain disruptions, the Bank is using an adjusted measure that temporarily deducts supply constraints from the estimate of the economy's non-inflationary potential output, and those supply factors aren't easily quantified.

Instead of the output gap, the Bank is likely eyeing indicators of labour market slack and domestic inflation to steer policy, and imposing the "supply constraint" on potential GDP to fit that story. If there's a lot of price pressure and little labour market slack despite GDP being below its pre-Covid trend, then that must mean that the supply factors are still weighing. So we would zero in on discussions on the drivers of inflation, or estimates of labour market slack rather than the output gap, although when the Bank is raising by 50 bps, it almost has to argue that labour markets are tight. Our team will have more to say on that topic in a report we'll issue next week.

All eyes will be on the revised and likely upgraded inflation forecasts, but they reveal less about the path of future rate hikes than one might think. The projections are missing what really counts, which is how many rate hikes the BoC believes it will need to pare growth enough through 2024 to get inflation back to target. Instead of the forecast, look for any discussions about interest sensitivity, external headwinds or tailwinds for the economy, which could provide more insight.

As we wrote earlier (see our In Focus: Canadian rate hikes: where's the finish line, March 28), the best guide for where the BoC believes that short rates will ultimately settle lies in its estimate for the neutral rate, due for an update in the MPR. Even if the policy rate were to temporarily overshoot neutral, which is not our forecast, the gravitational pull back to that level implies that it's very informative for where longer yields like five-year bonds should sit. Our study found that the Fed's "long term" fed funds rate projection is a good guide to the BoC's neutral rate, so expect it to be in the 2.25-2.50% range.

If that seems low relative to today's inflation rate, it is. If inflation were forever stuck at 5%, the nominal neutral rate would likely be higher than 5%. But remember that at the finish line for the rate hike cycle, real interest rates have to be assessed by taking the nominal rate less where inflation is expected to be in the period following that tightening.

If the BoC hits the mark, it will have inflation expectations back near 2% for 2024 and beyond, so a 2023 interest rate in the mid-2% range should do the trick. If the Bank of Canada were to take a modest real rate as neutral, and then tack on an inflation rate of more than 2% to get the longer-term neutral rate, it would almost be conceding that its going to lose the battle against an accelerating CPI. That's just not in the cards.

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, April 11	-	-	-	-	-	-	-
Tuesday, April 12	-	Government Bond Purchase Program (GBPP): 30-YR	-	-	-	-	-
Tuesday, April 12	-	AUCTION: 3-M BILLS \$8.4B, 6-M BILLS \$3.2B, 1-YR BILLS \$3.2B	-	-	-	-	-
Wednesday, April 13	10:00 AM	BANK OF CANADA RATE ANNOUNCE.	(Apr 13)	(H)	1.00%	1.00%	0.50%
Wednesday, April 13	11:00 AM	Speaker: Tiff Macklem (Governor) & Carolyn Rogers (Sr. Deputy Gov.)	-	-	-	-	-
Thursday, April 14	-	Government Bond Purchase Program (GBPP): 2-YR	-	-	-	-	-
Thursday, April 14	-	AUCTION: 2-YR CANADAS \$4.5B	-	-	-	-	-
Thursday, April 14	8:30 AM	MANUFACTURING SHIPMENTS M/M	(Feb)	(M)	3.7%	-	0.6%
Thursday, April 14	8:30 AM	WHOLESALE TRADE M/M	(Feb)	(M)	0.9%	-	4.2%
Friday, April 15	-	Markets Closed (Good Friday)	-	-	-	-	-

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, April 11	-	AUCTION: 3-YR TREASURIES \$46B	-	-	-	-	-
Monday, April 11	9:30 AM	Speaker: Raphael W. Bostic (President, Atlanta)	-	-	-	-	-
Monday, April 11	9:30 AM	Speaker: Michelle W Bowman (Governor) (Voter)	-	-	-	-	-
Monday, April 11	9:30 AM	Speaker: Christopher J. Waller (Governor) (Voter)	-	-	-	-	-
Monday, April 11	12:40 PM	Speaker: Charles L. Evans (President, Chicago) (Non-Voter)	-	-	-	-	-
Tuesday, April 12	-	10-YR AUCTION: \$34B	-	-	-	-	-
Tuesday, April 12	8:30 AM	CPI M/M	(Mar)	(H)	1.2%	1.2%	0.8%
Tuesday, April 12	8:30 AM	CPI M/M (core)	(Mar)	(H)	0.5%	0.5%	0.5%
Tuesday, April 12	8:30 AM	CPI Y/Y	(Mar)	(H)	8.5%	8.4%	7.9%
Tuesday, April 12	8:30 AM	CPI Y/Y (core)	(Mar)	(H)	6.6%	6.6%	6.4%
Tuesday, April 12	2:00 PM	TREASURY BUDGET	(Mar)	(L)	-	-	-\$216.6B
Tuesday, April 12	12:10 PM	Speaker: Lael S Brainard (Governor) (Voter)	-	-	-	-	-
Tuesday, April 12	6:45 PM	Speaker: Thomas I. Barkin (President, Richmond)	-	-	-	-	-
Wednesday, April 13	-	30-YR AUCTION: \$20B	-	-	-	-	-
Wednesday, April 13	7:00 AM	MBA-APPLICATIONS	(Apr 8)	(L)	-	-	-6.3%
Wednesday, April 13	8:30 AM	PPI M/M	(Mar)	(M)	1.3%	1.2%	0.8%
Wednesday, April 13	8:30 AM	PPI M/M (core)	(Mar)	(M)	0.6%	0.5%	0.2%
Wednesday, April 13	8:30 AM	PPI Y/Y	(Mar)	(M)	-	10.6%	10.0%
Wednesday, April 13	8:30 AM	PPI Y/Y (core)	(Mar)	(M)	-	8.4%	8.4%
Thursday, April 14	8:30 AM	INITIAL CLAIMS	(Apr 9)	(M)	-	175K	166K
Thursday, April 14	8:30 AM	CONTINUING CLAIMS	(Apr 2)	(L)	-	-	1523K
Thursday, April 14	8:30 AM	RETAIL SALES M/M	(Mar)	(H)	0.8%	0.6%	0.3%
Thursday, April 14	8:30 AM	RETAIL SALES (X-AUTOS) M/M	(Mar)	(H)	1.0%	0.9%	0.2%
Thursday, April 14	8:30 AM	RETAIL SALES CONTROL GROUP M/M	(Mar)	(H)	0.2%	-0.2%	-1.2%
Thursday, April 14	8:30 AM	IMPORT PRICE INDEX M/M	(Mar)	(L)	-	2.5%	1.4%
Thursday, April 14	8:30 AM	EXPORT PRICE INDEX M/M	(Mar)	(L)	-	2.2%	3.0%
Thursday, April 14	10:00 AM	BUSINESS INVENTORIES M/M	(Feb)	(L)	-	1.3%	1.1%
Thursday, April 14	10:00 AM	MICHIGAN CONSUMER SENTIMENT	(Apr P)	(H)	-	58.7	59.4
Thursday, April 14	3:50 PM	Speaker: Loretta Mester (President, Cleveland) (Voter)	-	-	-	-	-
Thursday, April 14	6:00 PM	Speaker: atrick Harker (President, Philadelphia) (Non-Voter)	-	-	-	-	-
Friday, April 15	8:30 AM	NEW YORK FED (EMPIRE)	(Apr)	(M)	-	2.0	-11.8
Friday, April 15	9:15 AM	INDUSTRIAL PRODUCTION M/M	(Mar)	(H)	0.5%	0.4%	0.5%
Friday, April 15	9:15 AM	CAPACITY UTILIZATION	(Mar)	(M)	78.0%	77.9%	77.6%
Friday, April 15	4:00 PM	NET CAPITAL INFLOWS (TICS)	(Feb)	(L)	-	-	\$58.8B

Week Ahead's market call

by Avery Shenfeld

In the **US**, upcoming reports like the week ahead's retail sales figures have to be viewed with a lens that looks past the nominal figures for their implications for real volumes, given the inflation wedge between the two. Retail sales could do a bit better than consensus expectations, but a small gain in control group sales in nominal terms could still mean a decline in volumes, and much of the headline rise will come from higher prices for gasoline. March CPI data will leap further into the stratosphere, but our call is closely in line with the consensus.

In **Canada**, this issue's cover story previewed the Bank of Canada's rate statement and MPR report, which will come alongside a 50 basis point rate hike that is well anticipated by the market at this point. The market still has a tendency to be shocked by hawkish talk from the Governor, even when it's a given that stern language has to accompany a move to raise rates by a half percent, in order to let indebted Canadians know why that pain is necessary. Healthy gains for manufacturing and wholesaling in February were already hinted at in early "flash" estimates, contributing to a first quarter GDP pace in the 4% range, well above where we thought it would be given that Canada has been dealing with two successive Omicron waves over that period.

There are no major Canadian data releases next week.

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

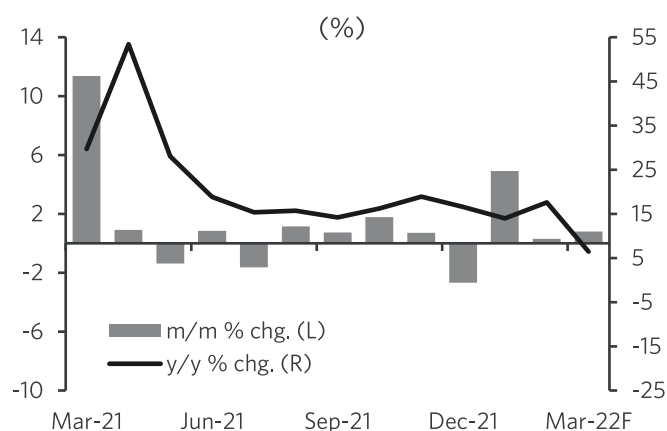
(Thursday, 8:30 am)

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Retail sales (m/m %)	CIBC	Mkt	Prior
Retail sales	0.8	0.6	0.3
- ex auto	1.0	0.9	0.2
- control group	0.2	-0.2	-1.2

Total retail sales will be flattered by higher gasoline prices in March, as well as continued improvement in restaurant traffic, likely resulting in a 0.8% advance. However, the squeeze on consumer spending power from higher gasoline prices will be apparent in control group categories, and the modest 0.2% growth we expect in that group would still be a decline in volume terms. Grocery stores are likely to experience a drop in sales volumes as dining out gained ground, while spending was likely diverted towards services as Covid faded.

Chart: US Retail sales (%)



Source: Census Bureau, Haver Analytics, CIBC

Forecast implications — Although momentum in goods consumption tapered off over Q1, a strong start to the quarter suggests that it still contributed to growth. The jump in prices at the pump will continue to squeeze consumption in Q2, and demand for goods, apart from autos, is expected to soften as pent-up demand for services is realized.

Market impact — We are above the consensus which could be positive for the greenback and give a lift to bond yields.

Other US Releases: Consumer price index—March

(Tuesday, 8:30 am)

Inflation will be driven higher by gasoline prices in March, with total CPI inflation set to reach 8.5% y/y. While used car prices eased off according to industry data, shelter prices and higher wages will prop up core prices, likely seeing that group accelerate to 6.6% y/y. While March was likely the peak for inflation, as the index will be lapping some strong year-ago readings that took place during the previous reopening ahead, the Fed will still be inclined to take rates up by 50bps at the next FOMC given elevated price pressures in cyclical factors, and the impending surge in demand for services.

Industrial production—March

(Friday, 9:15 am)

Hours worked for production workers in manufacturing grew at a solid pace in March, while rig counts continued their ascent along with the rise in oil prices. While milder than normal temperatures could provide a partial offset in the utilities component, total industrial production likely posted a healthy gain of 0.5%. Looking ahead, the lockdowns in China are likely to present a barrier to factory activity in April.

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