

Economics

THE WEEK AHEAD

September 19-23, 2022

Is inflation coming down the track?

by Avery Shenfeld avery.shenfeld@cibc.com

Canadians look south of the border for a lot of their news, with good reason. Whether it's fashion, technology or the broad direction of our economy, most American trends eventually reach us. So news of a generous, multi-year wage settlement with US railway unions, which raised alarm bells over inflation risks stateside, have some questioning whether we should expect to see the same in Canada.

Even in the US, the rail settlement might be less about inflation than about dividing up the spoils of major gains in productivity. A vigorous efficiency drive has enabled the rails to chop headcounts relative to output, reducing labor costs in the process. So a generous wage gain might not send unit labour costs higher than they were some years back.

Still, the concerns are that this is a five-year package averaging close to 5% per year in wage hikes, partly backdated, but with a couple of years to run. That raises concerns that businesses are starting to assume that inflation will persist at elevated levels, baking in cost increases ahead that will make it tougher to winnow inflation down.

That worry had the Bank of Canada Governor waded into a bit of a PR pickle, when he warned Canadian businesses not to build in big wage hikes. He surely didn't mean that workers shouldn't bargain hard for what they could get, or that businesses shouldn't pay what the market requires to get the staff they need today, even if it came off that way in the media.

What he likely meant to say was that employers shouldn't simply assume that we'll have elevated inflation beyond the next few quarters. They should therefore be careful about locking themselves into pay gains, particularly in multi-year contracts, under the assumption that they will be able to pass them on in large price hikes.

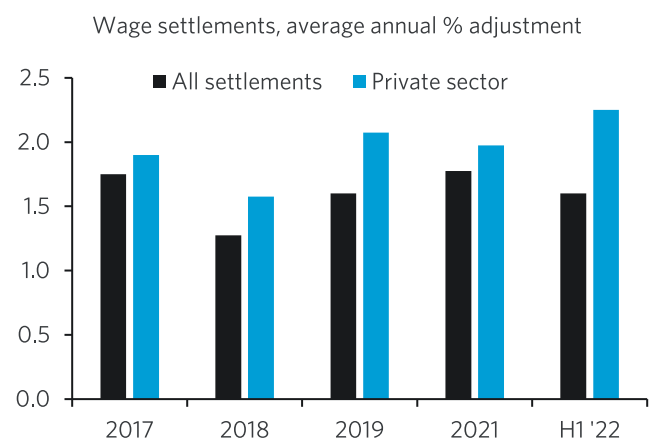
Interestingly, when it comes to union contracts in Canada, we haven't seen the type of settlements that the rail workers achieved in the US, at least not yet. Last year, the average contract entailed a moderate 1.8% annual pay gain over the life

of the agreement. In the first half of this year, the average was 1.7%. Looking only at private sector settlements, the average this year is a bit firmer, but in the mid-2% range isn't out of line with what we saw during long stretches of 2% inflation (Chart).

Admittedly, that private sector figure reflects only a small sample of contracts that happened to come due so far this year. Given what we're seeing in wages overall, which suggests pay gains in the 4-5% range aren't atypical this year, we might see greater firmness in unionized wages in the next few quarters.

While market participants typically talk about wage inflation driving the CPI, there's a greater tendency the other way, in which an upturn in inflation then leads to catch up wage gains when the labour market is tight. So the key to avoiding a self-sustaining price-wage-price spiral starts with cooling the economy, getting inflation down, and then letting that lower inflation environment influence wage gains. It's not about telling workers that they shouldn't try to keep up with the cost of living.

Chart: Canadian union wages still moderate



Source: Statistics Canada, 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, September 19	8:30 AM	INDUSTRIAL PROD. PRICES M/M	(Aug)	(M)	-	-	-2.1%
Monday, September 19	8:30 AM	RAW MATERIALS M/M	(Aug)	(M)	-	-	-7.4%
Tuesday, September 20	8:30 AM	CPI M/M	(Aug)	(H)	-0.1%	-0.1%	0.1%
Tuesday, September 20	8:30 AM	CPI Y/Y	(Aug)	(H)	7.2%	7.2%	7.6%
Tuesday, September 20	8:30 AM	CPI Core- Common Y/Y%	(Aug)	(M)	-	-	5.5%
Tuesday, September 20	8:30 AM	CPI Core- Median Y/Y%	(Aug)	(M)	-	-	5.0%
Tuesday, September 20	8:30 AM	CPI Core- Trim Y/Y%	(Aug)	(M)	-	-	5.4%
Tuesday, September 20	3:45 PM	Speaker: Paul Beaudry (Deputy Gov.)	-	-	-	-	-
Wednesday, September 21	-	-	-	-	-	-	-
Thursday, September 22	-	AUCTION: 10-YR CANADAS \$3B	-	-	-	-	-
Friday, September 23	8:30 AM	RETAIL TRADE TOTAL M/M	(Jul)	(H)	-2.0%	-2.0%	1.1%
Friday, September 23	8:30 AM	RETAIL TRADE EX-AUTO M/M	(Jul)	(H)	-1.2%	-1.1%	0.8%

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, September 19	10:00 AM	NAHB HOUSING INDEX	(Sep)	(L)	-	48	49
Tuesday, September 20	-	20-YR AUCTION: \$12B	-	-	-	-	-
Tuesday, September 20	8:30 AM	HOUSING STARTS SAAR	(Aug)	(M)	1440K	1460K	1446K
Tuesday, September 20	8:30 AM	BUILDING PERMITS SAAR	(Aug)	(H)	1600K	1616K	1685K
Wednesday, September 21	7:00 AM	MBA-APPLICATIONS	(Sep 16)	(L)	-	-	-1.2%
Wednesday, September 21	10:00 AM	EXISTING HOME SALES SAAR	(Aug)	(M)	-	4.70M	4.81M
Wednesday, September 21	10:00 AM	EXISTING HOME SALES M/M	(Aug)	(M)	-	-2.3%	-5.9%
Wednesday, September 21	2:00 PM	FOMC RATE DECISION (UPPER BOUND)	(Sep 21)	(H)	3.25%	3.25%	2.50%
Wednesday, September 21	2:00 PM	FOMC RATE DECISION (LOWER BOUND)	(Sep 21)	(H)	3.00%	3.00%	2.25%
Wednesday, September 21	2:30 PM	Speaker: Jerome H Powell (Chairman) (Voter)	-	-	-	-	-
Thursday, September 22	-	AUCTION: 10-YR TIPS \$15B	-	-	-	-	-
Thursday, September 22	8:30 AM	INITIAL CLAIMS	(Sep 17)	(M)	-	220K	213K
Thursday, September 22	8:30 AM	CONTINUING CLAIMS	(Sep 10)	(L)	-	-	1403K
Thursday, September 22	8:30 AM	CURRENT ACCOUNT BALANCE	(Q2)	(L)	-	-\$260.0B	-\$291.4B
Thursday, September 22	10:00 AM	LEADING INDICATORS M/M	(Aug)	(M)	-	0.0%	-0.4%
Friday, September 23	9:45 AM	S&P GLOBAL US SERVICES PMI	(Sep P)	(L)	-	45.0	43.7
Friday, September 23	9:45 AM	S&P GLOBAL US COMPOSITE PMI	(Sep P)	(L)	-	-	44.6
Friday, September 23	9:45 AM	S&P GLOBAL US MANUFACTURING PMI	(Sep P)	(L)	-	51.3	51.5
Friday, September 23	2:00 PM	Speaker: Jerome H Powell (Chairman) (Voter)	-	-	-	-	-

Week Ahead's market call

by Avery Shenfeld

In the **US**, after the fire and brimstone of the past week's core CPI data, the least the Fed can do is raise rates another 75 bps to a ceiling of 3.25% and pledge that more is coming. The case could easily be made for 100 bps. Nobody on the FOMC really believes that rates won't get to 3.5% at some point, and the Fed could take the shock out of such a move by explaining that it's only about getting rates to the required level sooner, just as the Bank of Canada did after its 100 bp move. But the fact that the Fed declined to do 100 bps when rates were at a much lower level suggests that it's probably not on the drawing board now. Housing data are likely to show a slowdown on its way more visibly in permits data than in starts.

In **Canada**, markets will be on edge heading into CPI data given what the US showed for August, but monthly changes don't actually correlate so tightly, particularly ex-gasoline. The different methodology for calculating the shelter component should allow the overall inflation rate to cool to a still-high 7.2%, even if, as in the US, we don't yet make progress on food or new vehicle inflation. Cheaper gasoline and softer vehicle sales will be key to a big drop in retail sales for July, but that won't come as a surprise for markets.

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

(Tuesday, 8:30 am)

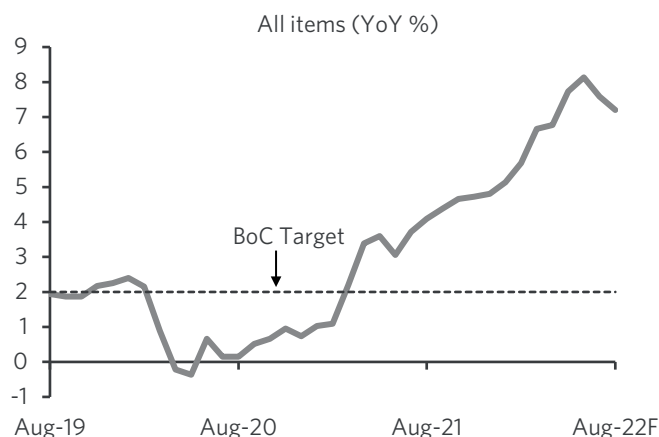
Andrew Grantham andrew.grantham@cibc.com

Variable (%)	CIBC	Mkt	Prior
CPI NSA (m/m)	-0.1	-0.1	0.1
CPI (y/y)	7.2	7.2	7.6

The continued downtrend in gasoline prices will be key behind a 0.1% decline in CPI during August and a deceleration in the annual rate of inflation to 7.2%. However, the earlier US figure suggests that food and other goods prices, including autos, may have remained strong positive contributors to inflation, despite reductions in shipping costs and agricultural commodity prices suggesting that there may be some good news later in the year on these fronts.

One difference between the US and Canadian figures that should bring a larger deceleration north of the border is the treatment of owned accommodation. Homeowners' rebuilding costs should be broadly flat month-over-month, while the other owned accommodation category (largely real estate agents' fees) should be a big negative again as it picks up the ongoing correction in house prices.

Chart: Canadian consumer price index



Source: Statistics Canada, Haver Analytics, CIBC

Forecast implications — The differing treatment of shelter within the Canadian numbers should see ex food/energy CPI decelerate faster compared to the US over the next few months. However, with goods prices excluding food/energy still seeing inflationary pressures linked to supply chains, and domestically driven services inflation likely to only peak in Q2 2023, we forecast that core inflation will only dip below 3% in the second half of next year. Headline inflation could, however, dip below 2% next year if the recent pull back in energy prices is maintained.

Other Canadian releases: Retail sales—July

(Friday, 8:30 am)

A drop in auto sales and a reduction in gasoline prices will weigh heavily on the headline number in July. We expect a 2% decline in overall sales and a 1.2% decline excluding autos. Sales excluding both autos and gasoline should have fared better, with only a marginal reduction expected, however that would still represent a decline in spending in inflation-adjusted terms.

Week Ahead's key US number: Housing starts—August

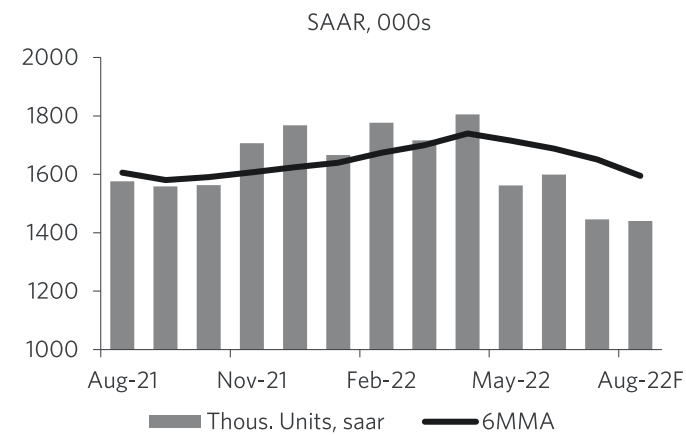
(Tuesday, 8:30 am)

Katherine Judge katherine.judge@cibc.com

Variable	CIBC	Mkt	Prior
Housing starts	1440K	1460K	1446K
Building permits	1600K	1616K	1685K

Mortgage rates climbed in August after easing off in July, denting housing demand prospects and homebuilder confidence. However, the sharp drop in homebuilding activity seen in July, combined with the sizeable gap between the pace of building permit issuance and housing starts, suggest that homebuilding could have fallen only modestly in August, to a 1440K pace. Building permit issuance likely fell further, also working to narrow the gap with housing starts.

Chart: US housing starts



Source: Census Bureau, Haver Analytics, CIBC

Forecast implications — With the Fed now on a more aggressive rate hiking path than previously thought, there will be more pain felt in the housing market in the next few quarters as mortgage rates rise further, and remain elevated in 2023.

Contacts:

Avery Shenfeld
416 594-7356
avery.shenfeld@cibc.com

Benjamin Tal
416 956-3698
benjamin.tal@cibc.com

Andrew Grantham
416 956-3219
andrew.grantham@cibc.com

Karyne Charbonneau
613 552-1341
karyne.charbonneau@cibc.com

Katherine Judge
416 956-6527
katherine.judge@cibc.com

CIBC Capital Markets
PO Box 500
161 Bay Street, Brookfield Place
Toronto, Canada, M5J 2S8
Bloomberg @ CIBC

economics.cibccm.com

CIBC World Markets Inc., CIBC World Markets Corp., CIBC World Markets Plc., CIBC Australia Limited and certain other corporate banking and capital markets activities of Canadian Imperial Bank of Commerce operate under the brand name CIBC Capital Markets.

This report is issued and approved for distribution by (a) in Canada, CIBC World Markets Inc., a member of the Investment Industry Regulatory Organization of Canada, the Toronto Stock Exchange, the TSX Venture Exchange and a Member of the Canadian Investor Protection Fund, (b) in the United Kingdom, CIBC World Markets plc, which is regulated by the Financial Services Authority, and (c) in Australia, CIBC Australia Limited, a member of the Australian Stock Exchange and regulated by the ASIC (collectively, "CIBC") and (d) in the United States either by (i) CIBC World Markets Inc. for distribution only to U.S. Major Institutional Investors ("MII") (as such term is defined in SEC Rule 15a-6) or (ii) CIBC World Markets Corp., a member of the Financial Industry Regulatory Authority. U.S. MIIs receiving this report from CIBC World Markets Inc. (the Canadian broker-dealer) are required to effect transactions (other than negotiating their terms) in securities discussed in the report through CIBC World Markets Corp. (the U.S. broker-dealer).

This report is provided, for informational purposes only, to institutional investor and retail clients of CIBC World Markets Inc. in Canada, and does not constitute an offer or solicitation to buy or sell any securities discussed herein in any jurisdiction where such offer or solicitation would be prohibited. This document and any of the products and information contained herein are not intended for the use of private investors in the United Kingdom. Such investors will not be able to enter into agreements or purchase products mentioned herein from CIBC World Markets plc. The comments and views expressed in this document are meant for the general interests of wholesale clients of CIBC Australia Limited.

This report does not take into account the investment objectives, financial situation or specific needs of any particular client of CIBC. Before making an investment decision on the basis of any information contained in this report, the recipient should consider whether such information is appropriate given the recipient's particular investment needs, objectives and financial circumstances. CIBC suggests that, prior to acting on any information contained herein, you contact one of our client advisers in your jurisdiction to discuss your particular circumstances. Since the levels and bases of taxation can change, any reference in this report to the impact of taxation should not be construed as offering tax advice; as with any transaction having potential tax implications, clients should consult with their own tax advisors. Past performance is not a guarantee of future results.

The information and any statistical data contained herein were obtained from sources that we believe to be reliable, but we do not represent that they are accurate or complete, and they should not be relied upon as such. All estimates and opinions expressed herein constitute judgments as of the date of this report and are subject to change without notice. This report may provide addresses of, or contain hyperlinks to, Internet web sites. CIBC has not reviewed the linked Internet web site of any third party and takes no responsibility for the contents thereof. Each such address or hyperlink is provided solely for the recipient's convenience and information, and the content of linked third-party web sites is not in any way incorporated into this document. Recipients who choose to access such third-party web sites or follow such hyperlinks do so at their own risk.

© 2022 CIBC World Markets Inc. All rights reserved. Unauthorized use, distribution, duplication or disclosure without the prior written permission of CIBC World Markets Inc. is prohibited by law and may result in prosecution.

The CIBC logo and "CIBC Capital Markets" are trademarks of CIBC, used under license.