Economics

THE WEEK AHEAD

March 27 - 31, 2023

Canada's Federal Budget: A Readers Guide

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

Canadian budget secrecy ain't what it used to be, back in the days when mum was the word about what it will contain. So much is already known about what Finance Minister Freeland will unveil in the coming week.

Canada will respond to heavy US subsidies with its own initiatives in the green energy space, with a focus on electricity and the power grid, but perhaps touching on some elements of manufacturing or minerals related to containing carbon emissions. Some steps will be taken to extend the cushion against a rising cost of living for low income Canadians. An allocation will have to be made to cover the recent health care deal with the provinces.

They say there's nothing certain other than death and taxes, but taxation is one policy area where budget secrecy tends to apply. Speculation about an increase in the GST, following recommendations to do so from some policy experts, seems likely to be way off the mark. A GST hike a year ahead of a potential election just isn't in the cards given its political peril, and the same would be true for any broad-based increase in taxes. Deficits won't be large enough to make the case for a big revenue grab at this point.

Every year there are those worried about a move to raise the inclusion rate on capital gains income. A review of the alternative minimum tax is also due. Hikes to taxes that hit upper-income earners have been more characteristic of this Liberal government over its terms of office, making such measures a more realistic risk than a higher GST. But it might simply be too close to an election to consider any sizeable revenue source.

In a year in which the central bank is still applying high interest rates to contain growth, fiscal policy should not add stimulus that would only be countered by further rate hikes. That's a principle that not all provincial budgets are respecting of late, but the federal finance minister has acknowledged that this should be a time for restraint. Even so, given the pledges made on the spending side, and a likely aversion to major tax hikes, we're expecting a light hand on that restraint.

Weaker forecasts for nominal GDP will mean that, in all likelihood, we'll see a rise in both the deficit/GDP and debt/GDP ratios in the coming fiscal year. That's not necessarily a net injection of stimulus, since that should really be measured by the change in the cyclically-adjusted budget balance. That more nuanced concept takes out the impacts on the deficit associated with below-trend GDP growth. Past budgets have allocated funds towards supporting innovation and growth, and Ottawa might contain deficits by repurposing some of those funds towards initiatives in green energy. Still, our fixed income strategists are anticipating a nearly $11 bn increase in gross issuance that markets will have to absorb relative to the outgoing fiscal year, reflecting both the fiscal balance and the diminishing draw down of cash.

That additional borrowing, as well as quantitative tightening, will slow any reduction in bond yields as inflation subsides. But even so, Canada still looks to be in decent shape on overall federal/provincial balances relative to other major industrialized countries.

For those watching for signposts of longer-term federal fiscal sustainability, the budget could have some important clues. Keep an eye on spending targets several years out as a share of GDP. While they are down sharply on that benchmark relative to the pandemic years, they're still higher than they were prior to 2020 as a share of GDP.

The 2019 budget reported that programs ate up 14.4% of GDP in 2017/18, and projected a decline to 13.8% by 2023/24. Last year's budget estimated that programs would cost 15% of GDP in 2024/25. If that uptrend continues or accelerates, containing debts and deficits would eventually require an offsetting increase in tax rates. But we see much more longer term pressure for US tax hikes as fiscal imbalances seem more out of line south of the border.

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, March 27	-	-	-	-	-	-	-
Tuesday, March 28	-	AUCTION: 3-M BILLS $10.4B, 6-M BILLS $3.8B, 1-YR BILLS $3.8B	-	-	-	-	-
Tuesday, March 28	-	Federal Budget	-	-	-	-	-
Wednesday, March 29	12:45PM	Speaker: Toni Gravelle (Deputy Gov.)	-	-	-	-	-
Thursday, March 30	-	AUCTION: 30-YR CANADAS $1.5B	-	-	-	-	-
Thursday, March 30	8:30AM	PAYROLL EMPLOYMENT, EARNINGS & HRS	(Jan)	-	-	-	91.4K
Friday, March 31	8:30 AM	GDP M/M	(Jan)	(H)	0.6%	-	-0.1%

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, March 27	-	AUCTION: 2-YR TREASURIES $42B	-	-	-	-	-
Monday, March 27	5:00PM	Speaker: Philip N Jefferson (Governor) (Voter)					
Tuesday, March 28	-	AUCTION: 5-YR TREASURIES $43B	-	-	-	-	-
Tuesday, March 28	8:30 AM	WHOLESALE INVENTORIES M/M	(Feb P)	(L)	-	-	-0.4%
Tuesday, March 28	8:30 AM	ADVANCE GOODS TRADE BALANCE	(Feb)	(M)	-$89.7B	-$89.9B	-$91.5B
Tuesday, March 28	8:30 AM	RETAIL INVENTORIES M/M	(Feb)	(H)	-	-	0.3%
Tuesday, March 28	9:00 AM	HOUSE PRICE INDEX M/M	(Jan)	(M)	-	-	-0.1%
Tuesday, March 28	9:00 AM	S&P CORELOGIC CS Y/Y	(Jan)	(H)	-	-	4.65%
Tuesday, March 28	10:00 AM	CONF.BOARD CONSUMER CONFIDENCE	(Mar)	(H)	102.0	101.5	102.9
Tuesday, March 28	10:00 AM	RICHMOND FED MANUF. INDEX	(Mar)	(M)	-	-8	-16
Wednesday, March 29	-	7-YR AUCTION: $35B	-	-	-	-	-
Wednesday, March 29	-	AUCTION: 2-YR FRN $22B	-	-	-	-	-
Wednesday, March 29	7:00 AM	MBA-APPLICATIONS	(Mar 24)	(L)			3.0%
Wednesday, March 29	8:30 AM	PENDING HOME SALES M/M	(Feb)	(M)	-	-2.3%	8.1%
Thursday, March 30	8:30 AM	INITIAL CLAIMS	(Mar 25)	(M)	-	-	191K
Thursday, March 30	8:30 AM	CONTINUING CLAIMS	(Mar 18)	(L)	-	-	1694K
Thursday, March 30	8:30 AM	GDP (annualized)	(4Q T)	(H)	-	2.7%	2.7%
Thursday, March 30	8:30 AM	GDP DEFLATOR (annualized)	(4Q T)	(H)	-	3.9%	3.9%
Thursday, March 30	12:45PM	Speaker: Thomas I. Barkin (Richmond) (Non-Voter)	-	-	-	-	-
Thursday, March 30	12:45PM	Speaker: Susan M. Collins (Boston)	-	-	-	-	-
Friday, March 31	8:30 AM	PCE DEFLATOR Y/Y	(Feb)	(H)	5.1%	5.1%	5.4%
Friday, March 31	8:30 AM	PCE DEFLATOR Y/Y (core)	(Feb)	(H)	4.7%	4.7%	4.7%
Friday, March 31	8:30 AM	PERSONAL INCOME M/M	(Feb)	(H)	0.2%	0.3%	0.6%
Friday, March 31	8:30 AM	PERSONAL SPENDING M/M	(Feb)	(H)	0.3%	0.3%	1.8%
Friday, March 31	10:00 AM	MICHIGAN CONSUMER SENTIMENT	(Mar)	(H)	-	63.4	63.4
Friday, March 31	10:00AM	Speaker: Michael S Barr (Governor) (Voter)	-	-	-	-	-
Friday, March 31	3:00PM	Speaker: John C. Williams (Vice Chairman, New York) (Voter)	-	-	-	-	-
Friday, March 31	4:00PM	Speaker: Christopher Waller (Governor) (Voter)	-	-	-	-	-
Friday, March 31	5:45PM	Speaker: Lisa D Cook (Governor) (Voter)	-	-	-	-	-

Week Ahead's market call

by Avery Shenfeld

In the **US**, mild weather and strong employment gains helped consumers get off to a strong start in January, but we're expecting a soft February, particularly in inflation-adjusted terms. A monthly 0.4% print for core PCE prices is still too hot for the Fed's tastes, but not alarming since we've made some progress before seeing any loosening in the labour market, and rent inflation looks to abate ahead. Weaker imports and price movements could help the nominal trade balance. All told, a quiet week for data that will keep the focus on banking sector developments at home and abroad.

In **Canada**, softer growth and some spending initiatives will likely bump up federal debt/GDP and Government of Canada bond issuance for the upcoming year, but the track thereafter should look more favourable from a bond market perspective. We previewed other federal budget issues in our cover story. January GDP looks likely to easily top the advance estimate to show a strong start to Q1, but that's after a flat Q4, and some of the momentum could be undone by a weak advance figure for February.

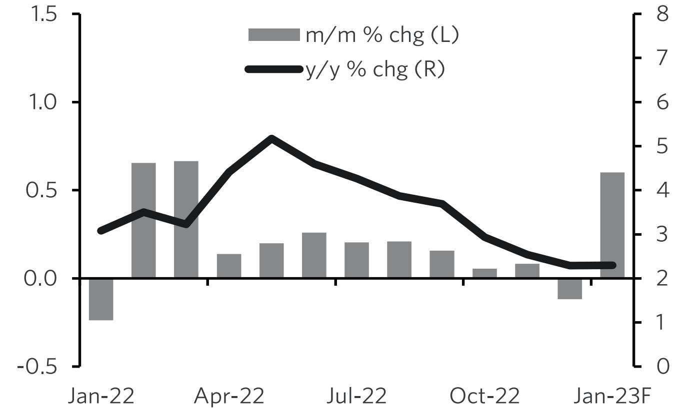
Week Ahead's key Canadian number: GDP — January

(Friday, 8:30 am)

Andrew Grantham andrew.grantham@cibc.com

Variable (%)	CIBC	Mkt	Prior
GDP m/m (Jan)	0.6	-	-0.1

Chart: Canadian GDP at basic prices



Source: Statistics Canada, Haver Analytics, CIBC

A disappointing end to 2022 for the Canadian economy was driven in part by unplanned maintenance in the oil & gas sector alongside the impact of harsh weather on transportation, with both of those areas expected to have bounced back in January. Add in a big jump in employment, a surge in manufacturing shipments and solid gains in retail and wholesale spending, and it looks like the economy started 2023 with a bang. The 0.6% gain in monthly GDP we forecast would be a few ticks better than the advance estimate, although early indications for February point to a modest giveback during that month.

Forecast implications — While growth during the second half of 2022 turned out to be weaker than the Bank of Canada penciled into its January MPR forecast, the first quarter of 2023 is likely to prove stronger than previously expected. Indeed, we could be tracking between a 1.5-2.0% annualized pace for Q1 following next week's monthly data, which would be well above the 0.5% MPR projection. However, with growth driven by strength in oil & gas, manufacturing and wholesale, this could represent improvements on the supply side of the economy which shouldn't add to inflationary concerns.

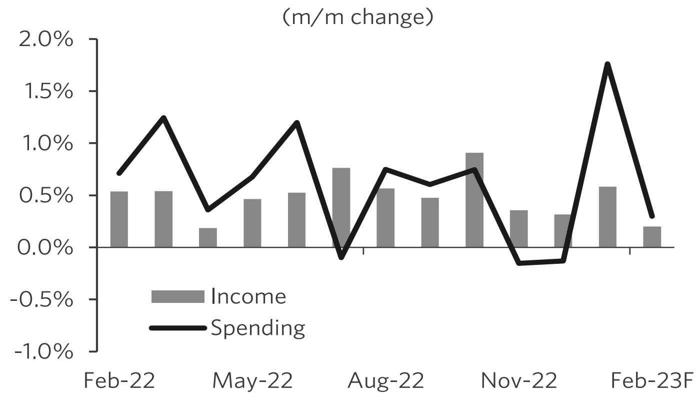
Week Ahead's key US number: Personal income & outlays —February

(Friday, 8:30 am)

Katherine Judge katherine.judge@cibc.com

Variable (%)	CIBC	Mkt	Prior
Personal income m/m	0.2	0.3	0.6
Personal spending m/m	0.3	0.3	1.8
Core PCE price index y/y	4.7	4.7	4.7

Chart: US Personal income and spending



Source: BEA, Haver Analytics, CIBC

Personal spending likely slowed in February, following a strong start to the year that was likely boosted by unseasonably warm weather. Total spending likely decelerated to 0.2% m/m, as the sizeable drop in restaurant spending could portend weakness in other discretionary service categories, leaning against the strength seen in the control group of retail sales. That would also likely reflect some caution tied to slower income gains, as momentum in the labor market waned, which will be behind a likely deceleration in income growth to 0.2% m/m.

The Fed's preferred gauge of inflation, core PCE prices, likely decelerated to a 0.4% monthly pace, slightly slower than its CPI counterpart given the lower weight of shelter in the index, but still too hot to reach on-target inflation, and justifying the Fed's decision to raise rates further in March.

Forecast implications— Our forecast for spending implies an only modest contraction in volume terms. Further out, concerns about the economic hit from higher rates and any spillover impacts from banking sector issues could reduce confidence and lead to a climb in the savings rate.

Market impact— We are roughly in line with the consensus, which should limit any market reaction.

Other US Releases: Advance trade in international goods— February

(Tuesday, 8:30 am)

The US trade deficit in goods likely narrowed in February, as the jump in imports at the start of the year is unlikely to have been repeated, consistent with the recovery in inventory-to-sales ratios in non-auto consumer goods. The increase in export prices against a decline in import prices also leans toward a narrowing of the deficit to $89.7bn.

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