Economics

THE WEEK AHEAD

January 23-27, 2023

Testing the meaning of data dependence: Stronger vs. strong

by Andrew Grantham andrew.grantham@cibc.com

Since the Bank of Canada's last meeting, when interest rates were hiked by 50bps, but policymakers stated that they would only be "considering" further increases, attention has turned towards what is truly meant by being "data dependent". Next week we will get the answer.

If data dependence means reacting to figures that were stronger than expected, then a further 25bp hike is in the cards. However, if it means reacting to data that were unequivocally strong, the Bank may choose to hold fire, as recent upside surprises have often been the result of downbeat expectations.

The labour market is the clearest area of the economy that has been stronger than the Bank of Canada previously anticipated. The surge in jobs during December, and retreat in the unemployment rate to 5.0%, clearly goes against Governor Macklem's warning back in November that the labour market needed to rebalance and that the low unemployment rate was unsustainable.

However, as we showed last week, the low jobless rate is in part a reflection of the elevated level of staff sickness and the necessity for companies to employ more people to achieve the same level of supply. It is not necessarily a signpost of strong domestic demand. Indeed, while employment surged, total working hours barely budged. So stronger than expected, yes. Unequivocally strong, no.

The recent trend of GDP is an even better example of the difference between stronger-than-expected, but not actually strong. Back in October's Monetary Policy Report, the Bank forecast growth of only 0.5% in Q4 and a stall in the economy during the first half of 2023. The current tracking estimate for Q4 2022 GDP of around 1-1½% is stronger than the Bank's previous forecast. However, it's not exactly a barnburner and is well below the pace that the US economy is projected to have achieved during that period. Moreover, with the size of the Canadian labour force rising at a 2.7% annualized rate during the quarter, Q4 GDP could actually be viewed as fairly weak.

While inflation has been somewhat of an outlier, with the 6.7% average rate in Q4 providing a downsize surprise relative to the Bank's October forecast of 7.1%, policymakers will likely point to the slump in gasoline prices towards the end of the year as the main cause of that downside surprise. While the Bank's preferred measures of core inflation (CPI-trim and CPI-median) have eased on a 3-month annualized basis, they are still tracking well above 2%. Moreover, because of its views regarding the labour market, the Bank may express concern that an easing of domestically-driven inflation today may not be sustained in future months.

Just after the December interest rate decision, Deputy Governor Sharon Kozicki stated that "if we are surprised to the upside, we are still prepared to be forceful". So it appears that simply stronger-than-expected, rather than necessarily strong, will be enough to bring a final 25bp hike to the overnight rate next week. The accompanying statement will need to sound hawkish enough to justify that move higher in interest rates, and a hiking bias of "considering" whether rates will need to "rise further" will be maintained, partly to push back against market pricing for rate cuts towards the end of the year.

In terms of the Bank's economic forecasts, we expect little change to what were already fairly downbeat expectations for growth in the year ahead. With those goalposts little changed and with past interest rate hikes starting to take hold on the economy, incoming data will no longer be either strong or stronger than expected. That will give the Bank reason to pause for the remainder of the year, before gradually starting to bring rates lower in 2024.

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, January 23	-	-	-	-	-	-	-
Tuesday, January 24	-	-	-	-	-	-	-
Wednesday, January 25	10:00 AM	BANK OF CANADA RATE ANNOUNCE.	(Jan 25)	(H)	4.50%	4.50%	4.25%
Wednesday, January 25	11:00 AM	Speaker: Tiff Macklem (Governor) & Carolyn Rogers (Sr. Deputy Gov.)	-	-	-	-	-
Thursday, January 26	-	AUCTION: 30-YR CANADAS $1.5B	-	-	-	-	-
Thursday, January 26	8:30 AM	PAYROLL EMPLOYMENT, EARNINGS & HRS	(Nov)	-	-	-	-
Friday, January 27	-	-	-	-	-	-	-

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, January 23	10:00 AM	LEADING INDICATORS M/M	(Dec)	(M)	-	-0.7%	-1.0%
Tuesday, January 24	-	AUCTION: 1-YR TREASURIES $34B	-	-	-	-	-
Tuesday, January 24	-	AUCTION: 2-YR TREASURIES $42B	-	-	-	-	-
Tuesday, January 24	9:45 AM	S&P GLOBAL US SERVICES PMI	(Jan P)	(L)	-	45.5	44.7
Tuesday, January 24	9:45 AM	S&P GLOBAL US COMPOSITE PMI	(Jan P)	(L)	-	-	45.0
Tuesday, January 24	9:45 AM	S&P GLOBAL US MANUFACTURING PMI	(Jan P)	(L)	-	46.8	46.2
Tuesday, January 24	10:00 AM	RICHMOND FED MANUF. INDEX	(Jan)	(M)	-	-5	1
Wednesday, January 25	-	AUCTION: 5-YR TREASURIES $43B	-	-	-	-	-
Wednesday, January 25	-	AUCTION: 2-YR FRN $24B	-	-	-	-	-
Wednesday, January 25	7:00 AM	MBA-APPLICATIONS	(Jan 20)	(L)	-	-	27.9%
Thursday, January 26	-	AUCTION: 7-YR TREASURIES $35B	-	-	-	-	-
Thursday, January 26	8:30 AM	INITIAL CLAIMS	(Jan 21)	(M)	-	212K	190K
Thursday, January 26	8:30 AM	CONTINUING CLAIMS	(Jan 14)	(L)	-	-	1647K
Thursday, January 26	8:30 AM	CHICAGO FED NAT.ACTIVITY INDEX	(Dec)	(M)	-	-	-0.05
Thursday, January 26	8:30 AM	GDP (annualized)	(4Q A)	(H)	2.9%	2.5%	3.2%
Thursday, January 26	8:30 AM	GDP DEFLATOR (annualized)	(4Q A)	(H)	3.3%	3.2%	4.4%
Thursday, January 26	8:30 AM	WHOLESALE INVENTORIES M/M	(Dec P)	(L)	-	0.5%	1.0%
Thursday, January 26	8:30 AM	ADVANCE GOODS TRADE BALANCE	(Dec)	(M)	-$88.1B	-$87.0B	-$83.3B
Thursday, January 26	8:30 AM	RETAIL INVENTORIES M/M	(Dec)	(H)	-	-	0.1%
Thursday, January 26	8:30 AM	DURABLE GOODS ORDERS M/M	(Dec P)	(H)	3.0%	2.9%	-2.1%
Thursday, January 26	8:30 AM	DURABLE GOODS ORDERS EX-TRANS M/M	(Dec P)	(H)	-0.3%	-0.2%	0.1%
Thursday, January 26	10:00 AM	NEW HOME SALES SAAR	(Dec)	(M)	600K	615K	640K
Thursday, January 26	10:00 AM	NEW HOME SALES M/M	(Dec)	(M)	-6.3%	-3.9%	5.8%
Friday, January 27	8:30 AM	PCE DEFLATOR Y/Y	(Dec)	(H)	4.9%	5.0%	5.5%
Friday, January 27	8:30 AM	PCE DEFLATOR Y/Y (core)	(Dec)	(H)	4.4%	4.4%	4.7%
Friday, January 27	8:30 AM	PERSONAL INCOME M/M	(Dec)	(H)	0.2%	0.2%	0.4%
Friday, January 27	8:30 AM	PERSONAL SPENDING M/M	(Dec)	(H)	-0.1%	-0.1%	0.1%
Friday, January 27	10:00 AM	PENDING HOME SALES M/M	(Dec)	(M)	-	-1.0%	-4.0%
Friday, January 27	10:00 AM	MICHIGAN CONSUMER SENTIMENT	(Jan F)	(H)	-	64.6	64.6

Week Ahead's market call

by Katherine Judge and Andrew Grantham

In the **US**, we'll receive what's likely to be one of the last pieces of good news on economic growth in the near term, as the lagged effects of past interest hikes will likely prevent any growth in early 2023. The December personal spending data will provide an indication of the handoff to Q1, and whether the caution in goods spending translated into services. The Fed will be in its pre-FOMC blackout period, but these data aren't likely to sway policymakers from a slowdown in the pace of rate hikes to 25bps in February.

In **Canada**, the Bank is expected to deliver a further rate increase, albeit of a more modest 25bp sizing. The statement will have to sound hawkish enough to justify the move, but look for indications from the following press conference that a pause will be seen from here and the conditions that the Bank eventually needs to see to start cutting interest rates again.

There are no major Canadian data releases next week.

Week Ahead's key US number: Gross domestic product—Q4 (Advance)

(Thursday, 8:30 am)

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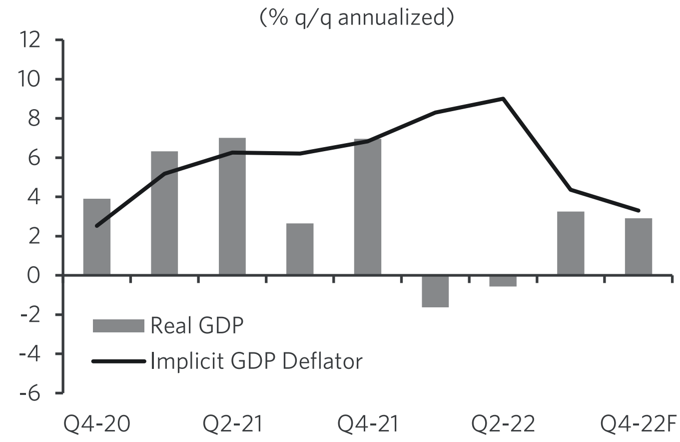
Variable (%)	CIBC	Mkt	Prior
GDP q/q annualized	2.9	2.5	3.2
GDP deflator	3.3	3.2	4.4

Chart: US GDP



Source: BEA, Haver Analytics, CIBC

Although momentum tailed off over the quarter, our forecast for an impressive 2.9% annualized advance in Q4 GDP is driven by a strong showing from consumers, reflecting expected increases in both goods and services consumption. Inventory restocking could have provided another boost as supply chain issues faded, also supporting domestic shipments of capital goods and therefore business investment. That will mask an underperformance in exports, as international demand faltered following the prior quarter's strength, while imports could have been held back by bloated inventory levels stateside, and residential investment will be a big negative given drops in existing home sales and housing starts.

Forecast implications — The tapering off of momentum in monthly indicators over the quarter suggests that there could be a contraction in activity in early 2023, as the impact of past rate hikes materializes more fully. That would be a welcome development for the Fed as it attempts to cool activity, and implies that policymakers could stop hiking after delivering two 25bp hikes in early 2023.

Market impact — We're in line with the consensus forecast and market reaction should therefore be limited.

Other US Releases: Durable goods orders—December

(Thursday, 8:30 am)

A rebound in orders in the volatile transportation group could have propelled a 3.0% advance in durable goods orders in December. But things likely looked less rosy in other categories, as dim growth prospects will likely hold back capex ahead, and could have resulted in a 0.3% drop in ex. transportation durable goods orders.

Personal income and outlays—December

(Friday, 8:30 am)

Aggregate income growth likely slowed to 0.2% in December, as wage growth softened and hours worked dropped. That's consistent with an expected 0.1% drop in spending as consumers become more cautious amidst the squeeze from higher interest rates. Core PCE inflation, the Fed's preferred measure of prices, likely eased to 4.4% y/y.

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