Economics

THE WEEK AHEAD

July 31 - Aug 4, 2023

Some hard truths about soft landings

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

We at CIBC Economics have never joined the herd calling for outright recessions in the US and Canada as a necessary evil to return to a 2% inflation target. With inflation having been chopped in half without an economic slump, we're now in good company, not just among private sector forecasts, but importantly including the central banks that are no longer aiming for a recession, but gaining confidence that a soft landing could do the job. But before you break out the champagne, it's worth noting that a soft landing is still only a mixed blessing for investors, workers, and those seeking re-election in North America next year.

For one, its still a "landing", in the sense that the lofty job gains we've enjoyed in the past couple of years, or even the mid-2% growth rate the US just posted for Q2, can't continue if inflation is going to be vanquished. Central bank rate hikes, including a final quarter point that could come in the US and Canada in September, are aimed at pushing the job vacancy rate down, the unemployment rate up, and slowing wages and buying power.

If not an outright recession, we could still see a three quarter period of negligible economic gains, and a half point or so climb in the jobless rate on both sides of the border. If we have a Canadian federal election in 2024, and with the presidential election coming stateside, inflation might have faded as an issue, but a lack of growth could come into sharper focus. Still, that's a better outcome for incumbents than either continued high inflation or an outright recession.

Corporate earnings have held up fairly well versus expectations because the recession that many have been forecasting failed to materialize. But the growth deceleration that we expect to see would typically be associated with a spate of negative year-on-year EPS reports, particularly with pricing power eroding in the consumer sector. That's still a much better outcome for equity investors than an outright recession, particularly for cyclicals, a good reason why the shift in expectations away from a more serious downturn has buoyed stocks. What will really lift equities is when we're getting past that stall in growth, and when a cooler CPI gives central banks room to ease up on rates and allow the economy to reaccelerate, a story for later in 2024.

There's less of a benefit, however, for more interest sensitive equities, for earnings multiples that are impacted by higher discount rates, and for the bond market. While bond yields will rally on the prospect for lower policy rates in 2024 and beyond, that rally will be much more muted than in a "hard landing" scenario. An outright recession, with the typical 2% or more climb in the unemployment rate, would see central banks shift from tight monetary policy to an outright easing stance, potentially taking overnight rates well below 2% to get the economy moving again.

But a soft landing won't open up that much economic slack. That will force central banks to be much more cautious in terms of how much they step on the gas with lower rates. Too sharp an economic rebound could send inflation higher again in a hurry. If economic slack is modest, we will likely only see overnight rates in the mid-2% territory by 2025, and that could leave 10-year rates struggling to sustain levels much below 3%.

Still, we're not complaining. Relative to the last two serious inflation threats in the early 1990s and the early 1980s, Canadians and Americans don't appear to be facing anywhere near the pain experienced back then to get inflation under control. Tamer inflation expectations, and a greater role played by temporary supply shocks in driving inflation higher this time, made the task of getting it under control more manageable. This time around, the downside risks to investors, workers and political leaders, are tied to the ability of the central bankers to avoid hiking too far, or delay easing too long, and missing their landing zone as a result.

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, July 31	-	-	-	-	-	-	-
Tuesday, August 1	-	AUCTION: 3-M BILLS $13.4B, 6-M BILLS $4.8B, 1-YR BILLS $4.8B	-	-	-	-	-
Wednesday, August 2	-	AUCTION: 2-YR CANADAS $4.8B	-	-	-	-	-
Thursday, August 3	-	AUCTION: 10-YR CANADAS $3.5B	-	-	-	-	-
Friday, August 4	8:30 AM	EMPLOYMENT CHANGE	(Jul)	(H)	25.0K	15.7K	59.9K
Friday, August 4	8:30 AM	UNEMPLOYMENT RATE	(Jul)	(H)	5.5%	5.5%	5.4%
Friday, August 4	10:00 AM	IVEY PMI	(Jul)	(L)	-	-	50.2

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, July 31	2:00 PM	Senior Loan Officer Opinion Survey	-	-	-	-	-
Tuesday, August 1	9:45 AM	S&P GLOBAL US MANUFACTURING PMI	(Jul)	(L)	-	49.0	49.0
Tuesday, August 1	10:00 AM	ISM - MANUFACTURING	(Jul)	(H)	46.0	46.9	46.0
Tuesday, August 1	10:00 AM	CONSTRUCTION SPENDING M/M	(Jun)	(M)	-	0.6%	0.9%
Tuesday, August 1	10:00 AM	JOLTS Job Openings	(Jun)	-	-	9650K	9824K
Wednesday, August 2	7:00 AM	MBA-APPLICATIONS	(Jul 28)	(L)	-	-	-1.8%
Wednesday, August 2	8:15 AM	ADP EMPLOYMENT CHANGE	(Jul)	(M)	-	190K	497K
Thursday, August 3	8:30 AM	INITIAL CLAIMS	(Jul 29)	(M)	-	223K	221K
Thursday, August 3	8:30 AM	CONTINUING CLAIMS	(Jul 22)	(L)	-	-	1690K
Thursday, August 3	8:30 AM	NON-FARM PRODUCTIVITY	(2Q P)	(M)	2.3%	1.3%	-2.1%
Thursday, August 3	9:45 AM	S&P GLOBAL US SERVICES PMI	(Jul)	(L)	-	52.4	52.4
Thursday, August 3	9:45 AM	S&P GLOBAL US COMPOSITE PMI	(Jul)	(L)	-	-	52.0
Thursday, August 3	10:00 AM	FACTORY ORDERS M/M	(Jun)	(M)	2.1%	0.2%	0.3%
Thursday, August 3	10:00 AM	DURABLE GOODS ORDERS M/M	(Jun)	(H)	-	-	4.7%
Thursday, August 3	10:00 AM	DURABLE GOODS ORDERS EX-TRANS M/M	(Jun)	(H)	-	-	0.6%
Thursday, August 3	10:00 AM	ISM - SERVICES	(Jul)	(M)	53.5	53.0	53.9
Thursday, August 3	8:30 AM	Speaker: Thomas I. Barkin (Richmond) (Non-Voter)	-	-	-	-	-
Friday, August 4	8:30 AM	NON-FARM PAYROLLS	(Jul)	(H)	185K	200K	209K
Friday, August 4	8:30 AM	UNEMPLOYMENT RATE	(Jul)	(H)	3.6%	3.6%	3.6%
Friday, August 4	8:30 AM	AVERAGE HOURLY EARNINGS ALL EMPLOYEES M/M	(Jul)	(H)	0.3%	0.3%	0.4%
Friday, August 4	8:30 AM	AVERAGE WEEKLY HOURS ALL EMPLOYEES	(Jul)	(H)	-	34.4	34.4
Friday, August 4	8:30 AM	MANUFACTURING PAYROLLS	(Jul)	(H)	-	5K	7K

Week Ahead's market call

by Katherine Judge and Andrew Grantham

In the **US**, we'll get the first readings on July activity, with the payrolls data on Friday not likely to show enough of a cooling to indicate that the Fed's job fighting inflation is done. Policymakers will also be looking for a further drop in job openings, while the ISM Services index could have eased off after an unusually strong jump in the prior month.

In **Canada**, the labour force survey is expected to show a further rise in the job count, albeit one that falls slightly short of population growth which will result in a slight tick higher in the unemployment rate. Wage growth could reverse some of the prior month's deceleration, but should remain below recent peaks.

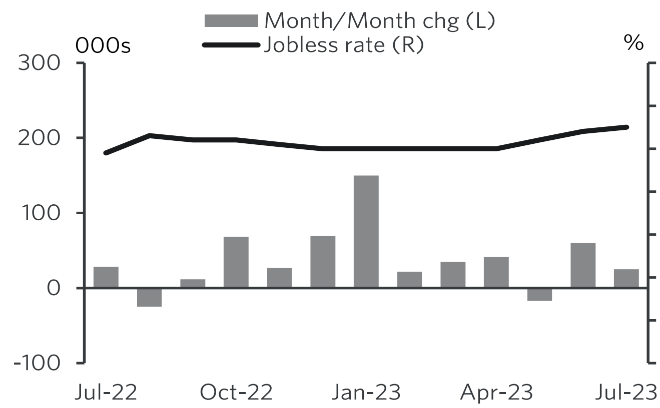
Week Ahead's key Canadian number: Employment—July

(Friday, 8:30 am)

Andrew Grantham andrew.grantham@cibc.com

Variable	CIBC	Mkt	Prior
Employment change	25.0K	15.7K	59.9K
Unemployment rate	5.5%	5.5%	5.4%

Chart: Canadian employment



Source: Statistics Canada, Haver Analytics, CIBC

While employment growth resumed in June, it failed to keep up with the surge in working age population — a trend that we expect will have continued in July. The 25K increase in job count we expect wouldn't quite keep up with projected labour force growth, and as a result would see the unemployment rate rise to 5.5%. With job vacancy rates continuing to edge lower, it is clear that demand for labour is easing at the same time that the supply of potential workers is rising quickly. While wage growth could rebound slightly after decelerating more than expected in the prior month, it should still remain well below the 5.4% peak seen towards the end of last year.

Forecast implications — With job vacancies continuing to ease as previously open positions are filled and demand for staff wanes, the unemployment rate is expected to rise further as the year goes on. Indeed, we now anticipate a peak above 6% in the first half of 2024 before interest rate cuts aid a recovery in the labour market during the second half of next year.

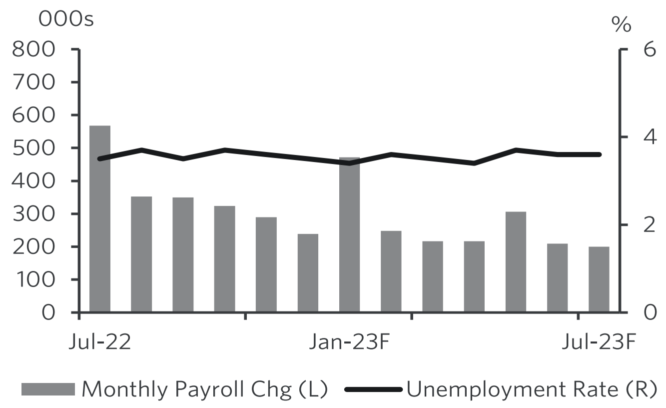
Week Ahead's key US number: Employment situation—July

(Friday, 8:30 am)

Katherine Judge katherine.judge@cibc.com

Variable	CIBC	Mkt	Prior
Employment (m/m)	185K	200K	209K
Unemployment rate	3.6%	3.6%	3.6%
Avg hourly earnings (m/m)	0.3%	0.3%	0.4%

Chart: US payroll employment



Source: BLS, Haver Analytics, CIBC

Initial jobless claims eased over the July survey reference period, suggesting that a healthy 185K jobs could have been created in the US. That's in line with the climb in participation seen lately in the prime-age working group, which coincides with a drawdown of excess savings. Still strong demand for workers, as evidenced by elevated job openings, suggest that new labor force entrants are being absorbed quickly into vacant positions. The unemployment rate could have remained steady at 3.6%, while a rise in participation also would have left more room for hiring without putting additional upwards pressure on wages, which likely slowed to 0.3% m/m.

Forecast implications — With hiring still well above the 100K pace that Powell has cited as desirable, the Fed will remain on track for a final 25bp rate in September. A continued slowdown in hiring and wage growth will limit labor income gains, and put a lid on growth in the second half of the year.

Market impact — We're slightly lower than the consensus on hiring which could result in bond yields falling.

Other US Releases: ISM Manufacturing—July

(Tuesday, 10:00 am)

Moves in regional PMIs suggest that the ISM's manufacturing index remained at 46.0 in July, leaving it entrenched in contractionary territory for the ninth month in a row, and consistent with the easing in capacity utilization and factory activity seen over the past year.

Contacts:

Avery Shenfeld
avery.shenfeld@cibc.com

Benjamin Tal
benjamin.tal@cibc.com

Andrew Grantham
andrew.grantham@cibc.com

Katherine Judge
katherine.judge@cibc.com

Ali Jaffery
ali.jaffery@cibc.com

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

economics.cibccm.com