

Economics

THE WEEK AHEAD

April 15 - 19, 2024

Are tax hikes also certain?

by Avery Shenfeld avery.shenfeld@cibc.com

They say that there's nothing certain but death and taxes, but does that certainty also apply to tax increases in the upcoming federal budget? Here's our take on why there's chatter among our clients on that topic, and what we ought to see based on sound tax and fiscal policy.

The talk about impending tax hikes has arisen from some simple arithmetic. The Finance Minister has rightly noted the importance of staying within previous guidelines for the budget deficit, not only for prudence on the debt burden, but to avoid net stimulus that could add to inflation and forestall much-needed interest rate relief. But her team has announced tens of billions in new spending initiatives, and Ottawa will also face increases in wages and other operating costs driven by last year's inflation. Without tax measures, revenue forecasts don't look likely to be upgraded given a sluggish near-term economic backdrop.

To keep the deficit on track, there are really three options. One is to have long phase-in periods for all these new programs, so that they come into effect after a revenue-boosting economic pick-up. That will likely be part of the story, judging by past budgets. A second would be to offset new spending by reallocating money from existing buckets, which we've also seen under this government. Ottawa's staff headcount has escalated in recent years, suggesting that there should be room for an efficiency drive. But if that still leaves a gap, tax hikes are a tool that the Liberals have previously reached for, with increases in top marginal personal tax rates, alternative minimum taxes, and more recently, higher taxes on banks and insurers.

The Liberals have ruled out taxes on the middle class, and we're too close to an election for a governing party to apply a small broad tax hike across the economy, even if that's what economic theory would favour when revenue measures are deemed necessary. Small businesses also carry a lot of voting clout. So, the list of targets narrows down to large corporates and high-income earners. Our clients at larger, profitable companies have told us that they fear that the precedent set by imposing higher taxes on large financial institutions will

be extended to large companies in other selected sectors. A parliamentary committee recommended something along those lines, although such advice is often ignored.

The phrase "windfall profits tax" is often applied to such moves, but in reality, that's not how they end up working. Estimating "normal" profits isn't a simple task for industries that see large cyclical swings, and need years of high earnings to offset weaker years just to earn a competitive return on investment. The resource sector, for example, has that characteristic.

So often, "windfall" profits translate into just a tax on larger entities with more total earnings, but not necessarily higher rates of return. Picking specific sectors, perhaps those that just happen to be making more money in the last year, goes against the grain of having a tax system that doesn't arbitrarily tilt capital flows to one part of the economy and not another in the absence of a specific public policy purpose.

It would also conflict with addressing one of Canada's other economic challenges: weak productivity. Taxes on profits will, unless passed on to consumers in higher prices, serve as a disincentive for the capital spending needed to improve output per hour, a key to affording higher pay for employees. And taxes on larger companies runs against substantial evidence that Canada's productivity gap with the US is at least partly tied to the fact that more of our economic output comes from smaller firms that don't have the scale needed to adopt productivity-enhancing technology.

We, like others, won't have to wait long to see whether tax increases are as certain as death and taxes. But we're hoping that in addition to avoiding inflationary stimulus, or running higher deficits, Ottawa first takes a hard look at reallocating existing spending envelopes, opts for program phase-ins so that spending can be financed by revenue gains driven by economic growth, applies any new taxes as a last resort, and in a way that avoids barriers to much-needed productivity gains.

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 15	8:15 AM	HOUSING STARTS SAAR	(Mar)	(M)	240.0K	239.3K	253.5K
Monday, April 15	8:30 AM	MANUFACTURING SHIPMENTS M/M	(Feb)	(M)	0.7%	0.7%	0.2%
Monday, April 15	8:30 AM	WHOLESALE SALES EX PETROLEUM M/M	(Feb)	(M)	-	-	0.1%
Tuesday, April 16	8:30 AM	CPI M/M	(Mar)	(H)	0.7%	0.7%	0.3%
Tuesday, April 16	8:30 AM	CPI Y/Y	(Mar)	(H)	2.9%	3.0%	2.8%
Tuesday, April 16	8:30 AM	Consumer Price Index	(Mar)	(M)	-	159.7	158.8
Tuesday, April 16	8:30 AM	CPI Core- Median Y/Y%	(Mar)	(M)	3.0%	3.0%	3.1%
Tuesday, April 16	8:30 AM	CPI Core- Trim Y/Y%	(Mar)	(M)	3.2%	3.1%	3.2%
Tuesday, April 16	-	Federal Budget	-	-	-	-	-
Wednesday, April 17	8:30 AM	INT'L. SEC. TRANSACTIONS	(Feb)	(M)	-	-	\$8.9B
Thursday, April 18	-	AUCTION: 10-YR CANADAS \$5B	-	-	-	-	-
Friday, April 19	-	-	-	-	-	-	-

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 15	8:30 AM	NEW YORK FED (EMPIRE)	(Apr)	(M)	-	-5.0	-20.9
Monday, April 15	8:30 AM	RETAIL SALES M/M	(Mar)	(H)	0.5%	0.4%	0.6%
Monday, April 15	8:30 AM	RETAIL SALES (X-AUTOS) M/M	(Mar)	(H)	0.7%	0.5%	0.3%
Monday, April 15	8:30 AM	RETAIL SALES CONTROL GROUP M/M	(Mar)	(H)	0.4%	0.3%	0.0%
Monday, April 15	10:00 AM	BUSINESS INVENTORIES M/M	(Feb)	(L)	-	0.3%	0.0%
Monday, April 15	10:00 AM	NAHB HOUSING INDEX	(Apr)	(L)	-	52.0	51.0
Monday, April 15	2:30 AM	Speaker: Lorie K. Logan (Dallas) (Non-Voter)	-	-	-	-	-
Monday, April 15	8:00 PM	Speaker: Mary C. Daly (San Francisco) (Voter)	-	-	-	-	-
Tuesday, April 16	-	AUCTION: 1-YR TREASURIES \$46B	-	-	-	-	-
Tuesday, April 16	8:30 AM	BUILDING PERMITS SAAR	(Mar)	(H)	1450K	1520K	1524K
Tuesday, April 16	8:30 AM	HOUSING STARTS SAAR	(Mar)	(M)	1450K	1480K	1521K
Tuesday, April 16	9:15 AM	INDUSTRIAL PRODUCTION M/M	(Mar)	(H)	0.5%	0.4%	0.1%
Tuesday, April 16	9:15 AM	CAPACITY UTILIZATION	(Mar)	(M)	79.0%	78.5%	78.3%
Tuesday, April 16	9:00 AM	Speaker: Philip N Jefferson (Governor) (Voter)	-	-	-	-	-
Wednesday, April 17	-	AUCTION: 20-YR TREASURIES \$13B	-	-	-	-	-
Wednesday, April 17	7:00 AM	MBA-APPLICATIONS	(Apr 12)	(L)	-	-	0.1%
Wednesday, April 17	2:00 PM	FED'S BEIGE BOOK	-	-	-	-	-
Wednesday, April 17	4:00 PM	NET CAPITAL INFLOWS (TICS)	(Feb)	(L)	-	-	\$36.1B
Wednesday, April 17	5:30 PM	Speaker: Loretta Mester (Cleveland) (Voter)	-	-	-	-	-
Wednesday, April 17	-	Speaker: Michelle W Bowman (Governor) (Voter)	-	-	-	-	-
Thursday, April 18	-	AUCTION: 5-YR TIPS \$23B	-	-	-	-	-
Thursday, April 18	8:30 AM	INITIAL CLAIMS	(Apr 13)	(M)	-	215K	211K
Thursday, April 18	8:30 AM	CONTINUING CLAIMS	(Apr 6)	(L)	-	-	1817K
Thursday, April 18	10:00 AM	LEADING INDICATORS M/M	(Mar)	(M)	-	0.0%	0.1%
Thursday, April 18	10:00 AM	EXISTING HOME SALES SAAR	(Mar)	(M)	-	4.2M	4.4M
Thursday, April 18	10:00 AM	EXISTING HOME SALES M/M	(Mar)	(M)	-	-5.1%	9.5%
Thursday, April 18	9:15 AM	Speaker: John C. Williams (Vice Chairman, New York) (Voter) & Michelle W Bowman (Governor) (Voter)	-	-	-	-	-
Thursday, April 18	11:00 AM	Speaker: Raphael W. Bostic (Atlanta) (Voter)	-	-	-	-	-
Thursday, April 18	5:45 PM	Speaker: Raphael W. Bostic (Atlanta) (Voter)	-	-	-	-	-
Friday, April 19	10:30 AM	Speaker: Austan D. Goolsbee, Chicago (Non-Voter)	-	-	-	-	-

Week Ahead's market call

by Avery Shenfeld

In the **US**, a solid gain in core group retail sales will likely overstate that month's overall consumer spending, as it won't factor in softness in autos and a deceleration we expect in services after an outsized February gain. Still, consumer spending will have posted a healthy first quarter, helped by incomes tied to job gains, but also an ever-weaker savings rate that at some point should see more temperate consumption growth. We expect mixed news on industrial output and homebuilding. Fed speakers will join the chorus of others that are paring back their expectations for the extent of rate cuts in 2024 in the wake of a third-successive disappointment in CPI readings, with our last published call for 75 bps of easing now in jeopardy if we don't see a deceleration in growth and a set of cooler readings on rent and other services prices.

In **Canada**, pre-announcements of major program initiatives and a commitment to stick to earlier deficit targets leaves taxes and the timing for new programs as the major items still to be unveiled in Tuesday's federal budget (see cover). Our rates strategist has already noted that several factors will still combine to make the year ahead a busy one for bond issuance. Inflation looks to heat up in the headline rate for March, but we're hoping that Bank of Canada core measures remain sufficiently tame to leave the door open for a cut in June, although we get one more CPI print before that decision, so we won't yet be able to decisively pin down the timing for that first move.

Week Ahead's key Canadian number: CPI—March

(Tuesday, 8:30 am)

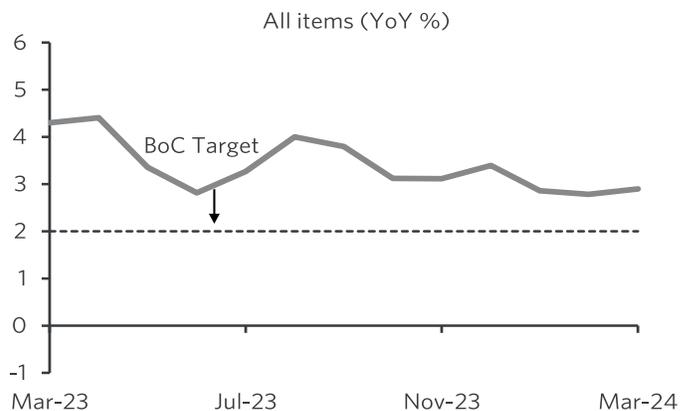
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Variable (%)	CIBC	Mkt	Prior
CPI NSA (m/m)	0.7	0.7	0.3
CPI (y/y)	2.9	3.0	2.8

After decelerating by more than expected so far this year, inflation likely picked up again slightly in March. For the headline figure this is largely due to the increase in gasoline prices seen during the month. However, the monthly increase in seasonally adjusted prices excluding food/energy may have also perked up (to 0.3% m/m) if clothing and internet prices fail to provide the same drag as in the prior two months.

The Bank of Canada's trim and median measures of inflation won't be as impacted by swings in those previous volatile elements, and as such should continue to show decelerating trends. We expect CPI-median to tick down slightly on a year-over-year basis, and for both measures to be tracking at or even slightly below 2% on a 3-month annualized basis.

Chart: Canadian consumer price index



Source: Statistics Canada, Haver Analytics, CIBC

Forecast implications — Inflation may have heated up slightly in March, but that is unlikely to offset all of the better-than-expected progress seen in the first two months of the year. More importantly, the Bank of Canada's CPI-trim and CPI-median measures of core inflation likely continued to track softer than last year, leaving a June rate cut within the realm of possibility.

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

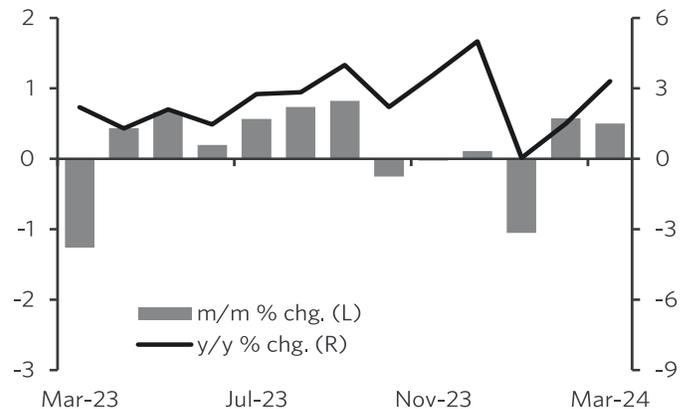
(Monday, 8:30 am)

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Variable (%)	CIBC	Mkt	Prior
Retail sales (m/m)	0.5	0.4	0.6
Retail sales - ex auto	0.7	0.5	0.3
Retail sales - control group	0.4	0.3	0.0

We expect US retail sales to reaccelerate in March, with the control group of retail sales increasing by 0.4% m/m, after a flat reading in February. The headline advanced reading should be even stronger at 0.5% given higher gasoline prices. With a still low saving rate and solid labor income gains after the March payroll report, it's hard for us to believe that the US consumer will stay on the sidelines for another month. Rising wealth and a slightly warmer-than-normal March also suggest consumer appetite will be strong.

Chart: US Retail sales



Source: Census Bureau, Haver Analytics, CIBC

Forecast implications — Given the softness in core goods prices in March, a weak auto sales reading in the month and an assumption of a modest increase in service spending — our tracking for 24Q1 consumption is slightly above 2% annualized given our forecast for the control group of retail sales. We continue to expect GDP growth to be around 2% in the quarter.

Other US Releases: Industrial production—March

(Tuesday, 9:15 am)

Industrial production should rise by 0.5% supported by stronger manufacturing and utilities production. PMI data point to firming manufacturing sentiment in both the US and China in March and we see some room for domestic auto production to increase further, as it remains somewhat below its pre-UAW strike levels.

Housing starts—March

(Tuesday, 8:30 am)

Housing starts and permits should pullback in March as mortgage rates have picked up. Starts have remained in a volatile sideways pattern, centered slightly above 1400K, since the summer of 2022. We expect that trend to continue until the Fed is confident inflation is headed for 2%.

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