

WEEKLY COMMENTARY

Tariffs and the Price of Money

By Royce Mendes, Managing Director and Head of Macro Strategy

When the Bank of Canada releases its interest rate decision next week, it will be doing so under a cloud of trade uncertainty. More than a month before President-elect Trump is set to be inaugurated, he's already roiling global markets by threatening to slap Canada and Mexico with 25% tariffs and China with an additional 10% levy over and above what's currently in place.

Businesses are already taking action. Reports from Canada to China suggest that firms are frontloading exports to US buyers in an attempt to avoid potential tariffs. That's building up the resilience of global supply chains so that any sudden change in US trade policy can at least temporarily be weathered. It's also boosting the exports of these countries.

Our economists have upgraded their GDP growth forecasts for Canada next year as US importers look to stockpile goods sourced from across the border. Of course, the flip side of such a change is that our team has lowered its view of 2026. While monetary policymakers will be tasked with navigating that choppy growth outlook, they'll also need to think about the impacts of tariffs on consumer prices.

Typically, central banks try to look through one-time price level shifts, instead focusing on the underlying inflation rate. In theory, tariffs and retaliatory actions only affect prices once, so protectionism would seem to engender only one-time price increases. The question is whether the central bank is willing to bet all its chips on the theory that tariffs don't have any lasting impact on the pace of inflation.

The Bank of Canada recently said that one of the main reasons inflation returned to the 2% target post-COVID is that monetary policymakers were successful in keeping inflation expectations anchored around 2%. While it's true that the greater the

magnitude of tariffs Canada faces, the greater the likelihood of more rate cuts, we don't view it as a linear relationship. The more retaliatory tariffs are placed on American goods, the greater the increase in Canadian consumer prices and, as a result, the greater the threat to inflation expectations.

What's more, rewiring global trade, as Donald Trump wants to do, will also weigh on productivity. In lowering the non-inflationary speed limits of economies around the world, protectionism will raise the prospect of unwanted inflation. Central banks still don't have models that can accurately forecast the supply sides of economies, even after facing massive supply shocks during the pandemic. With the magnitude of any increase in price pressures as a result of rewiring global trade unknown, an extra degree of caution on aggressive rate cutting is warranted.

Our analysis shows the Bank of Canada cutting rates more under more severe levies. But the most bullish bond investors may still be disappointed at how little we see the central bankers cutting rates over and above our base case forecast, particularly if a weaker loonie offsets some of the costs of tariffs for US consumers.

CONTENTS

Musing of the Week.....	1	What to Watch For.....	2	Economic Indicators.....	4
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What to Watch For

WEDNESDAY December 11 - 8:30

November	m/m
Consensus	0.3%
Desjardins	0.2%
October	0.2%

WEDNESDAY December 11 - 9:45

December	
Consensus	3.25%
Desjardins	3.50%
October 23	3.75%

FRIDAY December 13 - 8:30

Q3 2024	
Consensus	n/a
Desjardins	79.5%
Q2 2024	79.1%

FRIDAY December 13 - 8:30

October	m/m
Consensus	n/a
Desjardins	1.3%
September	-0.5%

SUNDAY December 8 - 20:30

November	y/y
Consensus	0.4%
October	0.3%

UNITED STATES

Consumer price index (November) – After edging up slightly in October, US headline inflation was likely flat in November. We expect that the Consumer Price Index (CPI) picked up 0.2% month over month, in line with the gains recorded in the previous 4 months. Energy prices likely came down as pump prices continued to fall in November, and food prices probably rose modestly. Meanwhile core CPI is expected to have grown 0.3% as it did in the previous three months, once again driven primarily by service prices. It's also possible that goods prices increased amid rising pressure on used vehicle prices. The year-over-year change in headline inflation should once again be 2.6% in November, while core inflation likely held steady at 3.3%.

CANADA

Bank of Canada meeting (December) – Market participants are looking for another 50-basis-point rate cut from the Bank of Canada next week, and central bankers could justify a second jumbo reduction. Early indications suggest that the fourth quarter began on softer footing than previously anticipated. However, with employment holding up, underlying measures of inflation reaccelerating and the Canadian dollar depreciating, we're leaning towards a more standard 25-basis-point move. The data for October would not have captured much impact from the 50-basis-point rate cut late in the month or any of the upcoming sales tax reduction. Moreover, upward revisions to the level of GDP heading into the second half of 2024 point to less slack in the Canadian economy than the Bank of Canada was previously estimating. A risk management approach to monetary policymaking would also need to account for the perception that a larger move was driven by major concerns about the upcoming Trump presidency. So while we're not pounding the table, we continue to believe that a 25-basis-point cut is slightly more probable than a 50-basis-point move.

Industrial capacity utilization rate (Q3) – We anticipate that industrial capacity utilization ticked up to 79.5% in Q3 2024, from 79.1% in Q2. We expect this modest move higher reflected a small boost in activity in the construction, forestry and logging sectors. In contrast, the current weakness in mining, quarrying and oil and gas extraction due to maintenance across oil and gas facilities probably led to lower activity in Q3. We also anticipate manufacturing plant retooling to be a drag on capacity utilization. Looking ahead, we expect capacity utilization to stabilize as the economy experiences conflicting forces of falling but still-high interest rates, increased oil exports, potential tariffs from the incoming Trump administration and slowing population growth.

Manufacturing sales (October) – On manufacturing sales, we anticipate growth of 1.3% in October, in line with Statistics Canada's flash estimate. Strong sales of energy, motor vehicles and petroleum likely drove this uptick. Despite the strength in sales of energy and petroleum products, seasonally adjusted energy prices fell in October. In real terms, manufacturing sales appear to have increased by 1.0%, with seasonally adjusted industrial product prices rising slightly in October (up 0.2%).

OVERSEAS

China: Consumer price index (November) – Headline inflation has been coming down for the past two months, as has core inflation, which excludes food and energy. Year-on-year consumer price growth came in at 0.3% for the total index and 0.2% for the core index. While some indicators, like industrial production and retail sales, have improved, inflation remains low as the country continues to grapple with a beleaguered property market. Average home prices have fallen since the beginning of

THURSDAY December 12 - 8:15

December	
Consensus	3.00%
Desjardins	3.00%
October 17	3.25%

FRIDAY December 13 - 2:00

October	m/m
Consensus	0.1%
September	-0.1%


the year, and the announced stimulus measures are struggling to gain traction. As a result, we don't expect prices to pick up anytime soon.


Eurozone: European Central Bank meeting (December) – The European Central Bank (ECB) is set to make its next monetary policy decision and publish its latest economic and inflation forecasts amid a more precarious economic and financial backdrop. Political uncertainty in France has sparked lively fluctuations in bond yields while undermining confidence in the economic outlook for the next few quarters. Other eurozone members are also beset with difficulties, particularly Germany. There's clearly room for another interest rate cut and even for several more over the coming quarters. The real question is whether the ECB will opt for a 50-point or 25-point reduction in December. Some data may still support a more modest cut. Inflation rose slightly in November, but the ECB will likely be more concerned about the acceleration in negotiated wage growth, which makes a rapid decline in services inflation less likely. We expect the ECB to announce a 25-point cut.

United Kingdom: Monthly GDP (October) – The UK's economy slowed in the third quarter. Non-annualized real GDP rose a mere 0.1% compared to 0.5% in the previous quarter. In fact, monthly GDP fell 0.1% in September, the first decline since April. Once the monthly GDP data for October are in, we should have a better sense of whether the fourth-quarter results will be any rosier. But so far, October's indicators aren't very promising. PMI levels slid and retail sales were down 0.7%.

Economic Indicators

Week of December 9 to 13, 2024

Day	Time	Indicator	Period	Consensus		Previous reading
UNITED STATES						
MONDAY 9	10:00	Wholesale inventories – final (m/m)	Oct.	n/a	0.2%	0.2%
TUESDAY 10	8:30	Nonfarm productivity – final (ann. rate)	Q3	2.2%	2.2%	2.2%
	8:30	Unit labor costs – final (ann. rate)	Q3	1.4%	2.0%	1.9%
WEDNESDAY 11	8:30	Consumer price index				
		Total (m/m)	Nov.	0.3%	0.2%	0.2%
		Excluding food and energy (m/m)	Nov.	0.3%	0.3%	0.3%
		Total (y/y)	Nov.	2.7%	2.6%	2.6%
		Excluding food and energy (y/y)	Nov.	3.3%	3.3%	3.3%
THURSDAY 12	8:30	Initial unemployment claims	Dec. 2–6	n/a	220,000	224,000
	8:30	Producer price index				
		Total (m/m)	Nov.	0.3%	0.3%	0.3%
		Excluding food and energy (m/m)	Nov.	0.2%	0.3%	0.2%
FRIDAY 13	8:30	Export prices (m/m)	Nov.	-0.3%	-0.1%	0.8%
	8:30	Import prices (m/m)	Nov.	-0.3%	0.1%	0.3%
CANADA						
MONDAY 9	---	---				
TUESDAY 10	---	---				
WEDNESDAY 11	9:45	Bank of Canada meeting	Dec.	3.25%	3.50%	3.75%
	10:30	Speech by Bank of Canada Governor T. Macklem and Senior Deputy Governor C. Rogers				
THURSDAY 12	8:30	Building permits (m/m)	Oct.	n/a	-3.4%	11.5%
FRIDAY 13	8:30	Industrial capacity utilization rate	Q3	n/a	79.5%	79.1%
	8:30	Wholesale sales (m/m)	Oct.	n/a	0.5%	0.8%
	8:30	Manufacturing sales (m/m)	Oct.	n/a	1.3%	-0.5%

Note: Each week, Desjardins Economic Studies takes part in the Bloomberg survey for Canada and the United States. Approximately 15 economists are consulted for the Canadian survey and a hundred or so for the United States. The abbreviations m/m, q/q and y/y correspond to month-over-month, quarter-over-quarter and year-over-year change respectively. Following the quarter, the abbreviations f, s and t correspond to first estimate, second estimate and third estimate respectively. Times shown are Eastern Standard Time (GMT -5 hours).  Desjardins Economic Studies forecast.

Economic Indicators

Week of December 9 to 13, 2024

Country	Time	Indicator	Period	Consensus		Previous reading	
				m/m (q/q)	y/y	m/m (q/q)	y/y
OVERSEAS							
DURING THE WEEK							
China	---	Trade balance (US\$B)	Nov.	93.90		95.72	
SUNDAY 8							
Japan	18:50	Current account (¥B)	Oct.	2,255.1		1,271.7	
Japan	18:50	Real GDP – final	Q3	0.3%		0.2%	
China	20:30	Consumer price index	Nov.		0.4%		0.3%
China	20:30	Producer price index	Nov.		-2.8%		-2.9%
MONDAY 9							
Australia	22:30	Reserve Bank of Australia meeting	Dec.	4.35%		4.35%	
TUESDAY 10							
Germany	2:00	Consumer price index – final	Nov.	-0.2%	2.2%	-0.2%	2.2%
Italy	4:00	Industrial production	Oct.	-0.1%	-3.6%	-0.4%	-4.0%
Japan	18:50	Producer price index	Nov.	0.2%	3.4%	0.2%	3.4%
WEDNESDAY 11							
Brazil	16:30	Central Bank of Brazil meeting	Dec.	12.00%		11.25%	
THURSDAY 12							
Germany	---	Current account (€B)		n/a		22.6	
Sweden	3:30	Bank of Sweden meeting	Dec.	0.75%		1.00%	
Eurozone	8:15	European Central Bank meeting	Dec.	3.00%		3.25%	
Japan	18:50	Tankan Large Manufacturers Index	Q4	13		13	
United Kingdom	19:01	Consumer confidence	Dec.	-18		-18	
Japan	23:30	Industrial production – preliminary	Oct.	n/a	n/a	3.0%	1.6%
FRIDAY 13							
United Kingdom	2:00	Trade balance (€M)	Oct.	-3,250		-3,462	
United Kingdom	2:00	Construction	Oct.	0.2%	0.0%	0.1%	-0.4%
United Kingdom	2:00	Index of services	Oct.	0.1%		0.0%	
United Kingdom	2:00	Monthly GDP	Oct.	0.1%		-0.1%	
United Kingdom	2:00	Industrial production	Oct.	0.3%	0.2%	-0.5%	-1.8%
France	2:45	Consumer price index – final	Nov.	-0.1%	1.3%	-0.1%	1.3%
France	2:45	Wages – final	Nov.	n/a		0.3%	
Eurozone	5:00	Industrial production	Oct.	-0.1%	-2.3%	-2.0%	-2.8%

Note: Unlike release times for US and Canadian economic data, release times for overseas economic data are approximate. Publication dates are provided for information only. The abbreviations m/m, q/q and y/y correspond to month-over-month, quarter-over-quarter and year-over-year change respectively. Times shown are Eastern Standard Time (GMT -5 hours).