

WEEKLY COMMENTARY

Better Late Than Never

By Royce Mendes, Managing Director and Head of Macro Strategy

After insisting that there would be some kind of immaculate deceleration in inflation, officials around the world are now offering long overdue mea culpas. US Treasury Secretary Yellen echoed past comments from Fed Chair Powell that American policymakers had misjudged the persistence of price pressures. The Bank of Canada for its part has been acknowledging for some time that it got things wrong with regards to inflation and is now playing catch-up.

To make up ground, the Bank of Canada hiked rates another 50bps this week, taking its policy rate to 1.50% and cementing this hiking cycle as the fastest in the inflation targeting era. The Federal Reserve is set to unleash a similar-sized rate increase later this month. Even central bankers in economies like the eurozone are discussing the need to act forcefully in the near term to restrain inflationary tailwinds.

With 20/20 hindsight, it's easy to criticize policymakers for a series of missteps that left them well behind the curve. Quantitative easing programs were allowed to continue for too long. Even in Canada, where the Bank of Canada's asset purchase program was halted months before other central banks' bond buying sprees, quantitative easing saw the Canadian central bank hoover up more than 40% of the sovereign bond market.

The policy rate in a number of jurisdictions was also clearly left too low for too long. That was in part because central bankers were slow to recognize the scope and persistence of supply constraints. But it was also partially due to an unforced error in which officials tied their hands with overly specific forward guidance about the triggers for tighter policy. The end result has been an overheating in a number of global economies which has contributed to the excess inflation emanating from factors out of central bankers' control, like global commodity prices and supply chain disruptions.

Bank of Canada officials and their global peers are now taking steps to remediate the situation. They're also being more honest about the risks surrounding the path forward. Inflation has run high for so long that there's a realistic possibility high inflation will become embedded in expectations. That would make the task of bringing price pressures back down all the more difficult. The worst-case scenario would be if the public were to lose faith in monetary officials' ability to bring inflation back down. The building blocks of low and stable inflation are anchored inflation expectations and central bank credibility.

On that front, the Bank of Canada has stepped up its hawkish rhetoric in a bid to assure everyone that its 2% inflation target is still sacrosanct. By mentioning that policymakers could act even more forcefully if needed, this week's Bank of Canada statement opened the door to an even more aggressive hiking cycle. Central bankers in other parts of the world are taking a similarly hawkish approach. Whether or not it's just jawboning, it should help anchor inflation expectations and build back credibility. There's still a chance to reduce inflation without triggering a recession. It's a slim chance that hinges in part on the public having confidence in policymakers, but it's a chance nonetheless. So while higher interest rates will pinch the pocketbooks of households and businesses, the change in tack towards tightening financial conditions is what's needed to guide inflation back down and get the economy operating efficiently again. Better late than never.

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Week in Review

By Randall Bartlett, Senior Director of Canadian Economics, Tiago Figueiredo, Associate – Macro Strategy, Francis Génereux, Senior Economist, and Lorenzo Tessier-Moreau, Senior Economist

- ▶ **The Bank of Canada (BoC) is staying in the fast lane in its drive to normalize monetary policy.** The 50bp rate increase unleashed Wednesday cements this hiking cycle as the fastest in the inflation targeting era. The statement noted that officials could act “more forcefully if needed,” which clearly opens the door to a 75bp move at the upcoming July announcement. However, we don’t think the data will justify such a move with the housing market already reacting negatively to higher rates.
- ▶ **Financial market volatility isn’t going anywhere,** even after last week’s strong stock market comeback. Hawkish comments by Federal Reserve officials and upbeat employment figures on Friday sent US 10-year bond yields back up to about 3%. The BoC’s 50bp hike didn’t surprise markets, but the more hawkish tone in its statement drove bond yields higher. With investors mainly worried about interest rates, Friday’s solid jobs numbers pushed stock markets lower, a paradox we’re well used to.
- ▶ **Canadian real GDP grew at an annual rate of 3.1% q/q in the first quarter of 2022,** coming in well below the expectations of private sector forecasters (5.2%). Domestic demand posted a solid 4.8% gain in Q1 2022, with household consumption advancing by 3.4% while residential and non-residential business investment surged by 18.1% and 9.0% respectively. In contrast, net exports were a drag on growth, as real exports fell by 9.4%, well in excess of the 2.8% decline in import volumes. Monthly real GDP growth clocked in at 0.7% m/m in March following a downwardly revised 0.9% in February and -0.2% in January. Statistics Canada’s flash estimate for April 2022 growth is 0.2%. Our initial tracking for Q2 2022 real GDP growth is around 4%, largely on the strong handoff from the first quarter.
- ▶ **Labour productivity of Canadian businesses fell 0.5% q/q in Q1 2022,** following a similar 0.6% decline in Q4 2021, for the seventh consecutive quarterly decline. This left productivity 1.3% below its level in Q4 2019, the last quarter before the COVID-19 pandemic began. At the same time, Canadian businesses saw their unit labour costs grow 2.7% in Q1 2022 following a flat print in the final quarter of 2021.
- ▶ **According to the establishment survey, the US economy added 390,000 jobs in May,** after an increase of 436,000 in April (revised from 428,000) and 398,000 in March (also revised from 428,000). The unemployment rate remained unchanged at 3.6% for a third straight month.
- ▶ **In the United States, the ISM manufacturing index posted a surprise uptick in May,** to 56.1 from 55.4. This is the first monthly gain since February and the second since last October. The new orders, backlog of orders and manufacturers’ inventories components were all up. **Meanwhile the ISM services index fell from 57.1 to 55.9.**
- ▶ **US new car sales plummeted 12.5% in May,** after spiking 8.1% in April. Sales remain erratic due to fluctuating inventories.
- ▶ **According to the Conference Board index, US consumer confidence dipped less than expected in May,** from 108.6 (revised from 107.3) to 106.4. The Present Situation Index dropped the most, likely reflecting the recent rise in gas prices.
- ▶ **The S&P/Case-Shiller index of existing home prices continued to accelerate sharply in March,** posting a second straight 2.4% monthly gain. This bumped up the index’s annual variation from 20.3% to a new cyclical high of 21.2%.
- ▶ **Chinese PMI indexes rose in May.** The Composite index climbed from 42.7 in April to 48.4. Although it’s still below the 50 mark, indicating that the economy is still contracting, it’s a step in the right direction. The lifting of several lockdowns in China will give the economy an additional boost in June.
- ▶ **Eurozone inflation increased further.** The Harmonized Index of Consumer Prices jumped 0.8% in May, bringing its annual variation to 8.1%.

What to Watch For

By Randall Bartlett, Senior Director of Canadian Economics,
Tiago Figueiredo, Associate – Macro Strategy, and Francis Généreux, Senior Economist

TUESDAY June 7 - 15:00

April	US\$B
Consensus	34.000
Desjardins	36.000
March	52.435

FRIDAY June 10 - 8:30

May	m/m
Consensus	0.7%
Desjardins	0.8%
April	0.3%

FRIDAY June 10 - 10:00

June	
Consensus	58.7
Desjardins	58.0
May	58.4

TUESDAY June 7 - 8:30

April	\$B
Consensus	2.47
Desjardins	1.90
March	2.49

UNITED STATES

Consumer credit (April) – Consumer credit rose sharply once again in March, up US\$52.4B. This is the biggest monthly gain on record, except for when the methodology was changed. Based on weekly banking credit data, we’re expecting a more modest increase in April.

Consumer price index (May) – For the first time since last August, inflation slowed in the United States in April, from 8.5% to 8.3%, partly due to the drop in gas prices. However, prices at the pump spiked 9.4% on average in May, which is likely to prevent inflation from falling further. Energy prices should therefore make a significant upside contribution to this month’s consumer price index (CPI) reading. We’re also expecting food prices to surge again. Stripping out food and energy, core CPI is projected to rise 0.5% in May, in line with the six-month average. Supply chain disruptions are still severe, especially due to the lockdowns in China. All told, we’re anticipating a monthly variation in total CPI of 0.8%. That would keep the annual variation at 8.3%. However, we think core inflation will ease from 6.2% to 5.9%.

University of Michigan consumer confidence index (June – preliminary) – The University of Michigan consumer confidence index fell in May to its lowest level since August 2011. There’s little to suggest that June’s preliminary figure will be any better. Gasoline prices have continued to climb in recent weeks, and concerns over inflation are very real. Rising interest rates are beginning to dampen the housing market. However, the stock market has rebounded from its mid-May slump and the labour market remains solid. All told, we’re expecting the University of Michigan consumer confidence index to remain fairly stable after dropping 6.8 points in May.

CANADA

International merchandise trade balance (April) – Canada’s goods trade balance is expected to remain in positive territory in April for the fourth consecutive month, clocking in at about \$1.9 billion. This will likely reflect an increase in both nominal exports and imports, with the latter increasing modestly more than the former. The advance in imports should largely be the result of higher prices thanks to the depreciation of the Canadian dollar in April and a stabilization in oil prices in the month. In contrast, export prices are expected to move only modestly higher in April, while volumes should be flat at best. Also underlying this view is the improvement in the US goods trade balance data for April, which points to a sharp reduction in the US trade deficit relative to March, with the balance in all goods trade categories improving with the exception of autos.

FRIDAY June 10 - 8:30

May	
Consensus	12,500
Desjardins	25,000
April	15,300

Labour Force Survey (May) – Underlying momentum in the labour market likely reaccelerated after slowing sharply in April. High-frequency indicators for services industries suggest a solid pickup in activity in May. Canadians appear to have been satisfying some pent-up demand to get out and about, with statistics on restaurants showing even more seated diners than pre-pandemic. Mobility data similarly revealed more activity at retail outlets and recreation venues, as did the numbers for air passengers, especially on domestic routes. As of April, many services businesses were still operating with significantly fewer employees than pre-pandemic. That likely means that businesses needed to ramp up hiring efforts in May to meet the growing demand. A labour dispute in the construction industry may have affected hours worked, but shouldn't have dented total employment all that much. The lagged effects of this historically tight labour market should have translated into an acceleration in wage growth. Although with inflation likely having eclipsed 7% in May, even a faster pace of wage increases would have fallen well short of keeping up with consumer prices.

OVERSEAS


THURSDAY June 9 - 7:45


June	
Consensus	0.00%
Desjardins	0.00%
April 14	0.00%

Eurozone: European Central Bank meeting (June) – Several members of the ECB's Governing Council have signalled that a shift in monetary policy will be needed to combat surging inflation. The ECB will likely announce the end of its Asset Purchase Program (APP) at the meeting, but it may not start increasing interest rates until July. Until now, the ECB seemed intent on leaving a little breathing room between the end of APP and rate liftoff. It has some tough decisions ahead of it. Inflation warrants quick action, but the risks to the eurozone's economic growth are acute and favour a more gradual approach.

Economic Indicators

Week of June 6 to 10, 2022

Date	Time	Indicator	Period	Consensus		Previous data
UNITED STATES						
MONDAY 6						
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TUESDAY 7						
	8:30	Trade balance – Goods and services (US\$B)	April	-89.5	-88.6	-109.8
	15:00	Consumer credit (US\$B)	April	34.000	36.000	52.435
WEDNESDAY 8						
	10:00	Wholesale inventories – final (m/m)	April	2.1%	2.1%	2.1%
THURSDAY 9						
	8:30	Initial unemployment claims	May 30-June 3	210,000	208,000	200,000
FRIDAY 10						
	8:30	Consumer price index				
		Total (m/m)	May	0.7%	0.8%	0.3%
		Excluding food and energy (m/m)	May	0.5%	0.5%	0.6%
		Total (y/y)	May	8.3%	8.3%	8.3%
		Excluding food and energy (y/y)	May	5.9%	5.9%	6.2%
	10:00	Michigan's consumer sentiment index – preliminary	June	58.7	58.0	58.4
	14:00	Federal budget (US\$B)	May	n/a	n/a	-308.2
CANADA						
MONDAY 6						
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TUESDAY 7						
	8:30	International trade (\$B)	April	2.47	1.90	2.49
WEDNESDAY 8						
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THURSDAY 9						
	10:00	Release of the Bank of Canada <i>Financial System Review</i>				
	11:00	Speech of the Bank of Canada Governor, T. Macklem				
FRIDAY 10						
	8:30	Net change in employment	May	12,500	25,000	15,300
	8:30	Unemployment rate	May	5.2%	5.3%	5.2%
	8:30	Industrial capacity utilization rate	Q1	83.0%	82.5%	82.9%

Note: Desjardins, Economic Studies are involved every week 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 monthly, quarterly and yearly variation respectively. Following the quarter, the abbreviations f, s and t correspond to first estimate, second estimate and third estimate respectively. The times shown are Eastern Standard Time (GMT - 4 hours).  Forecast of Desjardins, Economic Studies of the Desjardins Group.

Economic Indicators

Week of June 6 to 10, 2022

Country	Time	Indicator	Period	Consensus		Previous data		
				m/m (q/q)	y/y	m/m (q/q)	y/y	
OVERSEAS								
DURING THE WEEK								
China	---	Trade balance (US\$B)	May	57.79		51.12		
MONDAY 6								
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TUESDAY 7								
Australia	0:30	Reserve Bank of Australia meeting	June	0.75%		0.35%		
Japan	1:00	Leading indicator – preliminary	April	102.5		100.8		
Japan	1:00	Coincident indicator – preliminary	April	97.4		97.5		
Germany	2:00	Factory orders	April	0.3%	-4.1%	-4.7%	-3.1%	
United Kingdom	4:30	PMI composite index – final	May	51.8		51.8		
United Kingdom	4:30	PMI services index – final	May	51.8		51.8		
Japan	19:50	Current account (¥B)	April	393.8		1,555.9		
Japan	19:50	Real GDP – final	Q1	-0.3%		-0.2%		
WEDNESDAY 8								
India	0:30	Reserve Bank of India meeting	June	4.90%		4.40%		
Germany	2:00	Industrial production	April	1.2%	-2.4%	-3.9%	-3.5%	
France	2:45	Trade balance (€M)	April	n/a		-12,374		
France	2:45	Current account (€B)	April	n/a		-3.2		
Italy	4:00	Retail sales	April	0.1%	n/a	-0.5%	5.6%	
United Kingdom	4:30	PMI construction index	May	56.6		58.2		
Euro zone	5:00	Net change in employment – final	Q1	n/a	n/a	0.5%	2.6%	
Euro zone	5:00	Real GDP – final	Q1	0.3%	5.1%	0.3%	5.1%	
THURSDAY 9								
Euro zone	7:45	European Central Bank meeting	June	0.00%		0.00%		
Japan	19:50	Producer price index	May	0.5%	9.9%	1.2%	10.0%	
China	21:30	Consumer price index	May		2.2%		2.1%	
China	21:30	Producer price index	May		6.5%		8.0%	
FRIDAY 10								
Germany	---	Current account (€B)	April	n/a		18.8		
Italy	4:00	Industrial production	April	-1.1%	0.1%	0.0%	3.0%	
Russia	6:30	Bank of Russia meeting	June	10.00%		11.00%		

Note: In contrast to the situation in Canada and the United States, disclosure of overseas economic figures is much more approximate. The day of publication is therefore shown for information purposes only. The abbreviations m/m, q/q and y/y correspond to monthly, quarterly and yearly variation respectively. The times shown are Eastern Standard Time (GMT - 4 hours).