WEEKLY COMMENTARY

Don't Sweat the Technical Recession Meme

By Jimmy Jean, Vice-President, Chief Economist and Strategist

With less than two months to go in 2023, the global economic picture remains intriguing. In contrast to the US, which posted huge GDP numbers recently, the euro area registered a 0.1% non-annualized contraction in the third quarter, led lower by Germany. If these preliminary estimates are confirmed, the euro area's economy would have expanded in only one of the last three quarters, though there hasn't been a large contraction during that period.

It's a similar story in Canada, where the GDP by industry data released on Tuesday suggested GDP may have contracted by an annualized 0.1% in Q3. Since that would come after a 0.2% decline in Q2, there was buzz this week that Canada may have entered a technical recession. However, there are several reasons to approach this with caution. First, there's often a disparity between GDP by industry figures and the final results from quarterly national accounts. It wouldn't be unusual if the latter came in slightly positive, as our nowcast tools currently suggest. Second, the Q2 contraction was fairly minimal, leaving room for revisions to a flat or positive number for the quarter. So even if Q3 turns out to be negative, it wouldn't guarantee a technical recession. Third, technical recessions are primarily warning signs. A conclusive recession diagnosis requires a thorough evaluation of many indicators after the data has been adequately revised.

Instead of a not-so-constructive debate about whether Canada is currently in a mild technical recession or still attempting a soft landing, a more all-encompassing description of the present economic situation is stagnation. Some would argue it's stagflation, but the most recent data from both Europe and Canada indicates that inflation is cooling faster than anticipated. If below-potential growth and stronger lagged policy effects help get inflation back to central bank targets, it wouldn't be like previous instances of stagflation—especially if job markets manage to remain relatively healthy. In previous episodes of stagflation, unemployment was high.

The fact that the world's largest economy remains resilient is a key factor supporting a base case scenario of roughly stagnation elsewhere heading into 2024. But significant downside risks remain, including for the US. The nod to tighter financial conditions was just about the only change made to the Federal Reserve's statement, but that didn't necessarily make it an insignificant adjustment. The message is that the Fed is taking the risk of persistently tighter financial conditions derailing growth seriously enough that it's leaning towards forgoing the additional hike it believed was warranted only six weeks ago. This despite strong economic momentum—including well above potential growth in Q3—and the fact that the much stronger than expected payroll gain in September was accompanied by an increase in job openings, not a decrease. Mercifully, the productivity-led decline in unit labour costs, coupled with a term premia-led tightening of financial conditions, gives the Fed the latitude to substitute financial market-induced tightening for its own policies while remaining confident in the disinflation process.

It also helps that yields are now falling again; as of this writing, the US 10-year yield was on track for a weekly decline of more than 30 basis points. But what if we see new episodes of financial conditions tightening that go too far? That's where fiscal policy is an important wildcard. US fiscal management is on a deteriorating path amid soaring debt servicing charges and with little clarity on what will be the catalyst for a turnaround and when. This makes market reaction to fiscal sustainability signals a concern for central banks as they need to incorporate financial conditions into their calculus, and yet—unlike in 2019—are hamstrung in their ability to credibly push back against tightening in financial conditions. This is not only because inflation is not yet under control, but also because they need to ward off potential perceptions of fiscal dominance should government largesse come to drive market action.

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To be sure, financial conditions are only the latest channel through which fiscal policy choices have created complications for central banks. Pursuing expansionary fiscal policy comes at the risk of potentially delaying monetary policy accommodation. Bank of Canada Governor Tiff Macklem suggested as much when he informed senators that 2024 government spending plans were counteracting the Bank's efforts to get inflation back to target.

But governments aren't necessarily all being profligate. In its Fall Economic Statement, Ontario vowed to keep spending growth at 3.8% this fiscal year and 2.0% next. This seems ambitious, as spending growth of this magnitude would be below the path suggested by the combination of expected demographic expansion and inflation. In other words, Canada's largest province effectively bakes in a contraction in spending on an inflation-adjusted per capita basis. Failing to contain expenditures to this degree wouldn't make Ontario a lavish spender, but it would contribute to casting upside risk on the Bank of Canada's assumption, which already holds that government spending growth should double next year. So make no mistake, those fiscal–monetary policy tensions playing out everywhere are quite palpable in Canada.

What to Watch For

By Randall Bartlett, Senior Director of Canadian Economics, Tiago Figueiredo, Associate – Macro Strategy, Marc Desormeaux, Principal Economist, Marc-Antoine Dumont, Economist, and Francis Généreux, Principal Economist

UNITED STATES

TUESDAY November 7 - 15:00	
September	**US$B**
Consensus	10.00
Desjardins	10.00
August	**-15.62**

Consumer credit (September) – Consumer credit suffered its worst contraction since May 2020 in August. However, the decline was concentrated in student loans issued by the federal government. Outstanding revolving credit (credit cards and lines of credit) and other term loans continued to rise, despite higher interest rates. This trend likely continued in September. Weekly information on banking credit is pointing to an increase of about US$10 billion. However, the continued impact of student loans may shift things once again.

FRIDAY November 10 - 10:00	
November	
Consensus	64.0
Desjardins	62.5
October	**63.8**

University of Michigan consumer sentiment index (November – preliminary) – Consumer sentiment as measured by the University of Michigan index fell in October to its lowest level since May. The index shed a total of 7.7 points between August and October and could drop further in November. The Conference Board consumer confidence index also declined again in October and often leads the University of Michigan index. The stock market has been in the red for a month and retail interest rates are trending higher. Even initial unemployment claims are creeping up, although they remain very low. However, gasoline prices have continued to edge down over recent weeks, which may have a positive effect. November's upcoming TIPP index will give us a better idea of where this month's University of Michigan index print will land. For now, we're expecting it to fall to 62.5.

CANADA

TUESDAY November 7 - 8:30	
September	**$B**
Consensus	0.95
Desjardins	1.30
August	**0.72**

International merchandise trade (September) – Canada's trade surplus is expected to have widened in September. On the export side, OPEC+ supply cuts coincided with the end of the US refinery maintenance season, supporting higher Canadian crude exports. Although the Canadian dollar depreciated, prices probably also helped exports last month on the back of rising commodity prices. On the import side, the economic slowdown likely continued to be a drag. But inputs to our forecast suggest stronger industrial activity lifted Canadian imports while boosting exports even more.

OVERSEAS

TUESDAY November 7 - 2:00	
September	**m/m**
Consensus	-0.4%
August	**-0.2%**

Germany: Industrial production (September) – German industrial production has declined in five of the past six months and by a total of 4.4% since its February peak. Production fell in most of the main industries, led by fabricated metal products and pharmaceuticals. The automotive sector has also dropped from its recent peaks but nonetheless rebounded 7.6% in August. It'll be interesting to see whether this sector continued to recover in September and whether the other main industries improved. Unfortunately, the weakness of the manufacturing PMI—at just 39.6 in September and 40.8 in October—doesn't bode well.

WEDNESDAY November 8 - 20:30	
October	**y/y**
Consensus	-0.2%
September	**0.0%**

China: Consumer price index (October) – Chinese inflation was flat last month as pork prices—which are an indicator of domestic demand—fell 22% year-over-year. This price growth weakness, which has been ongoing for seven months now, shows how stubborn and chronic the challenges China is facing are. That said, core inflation excluding food and energy has been rising steadily in 2023 at a year-over-year pace of around 0.8%. October's data is a mixed bag. On the one hand, the stimulus measures announced by the government in recent months are starting to have an effect and should support a gradual rise in inflation. However, last month's PMIs—both manufacturing and non-manufacturing—declined unexpectedly, which means that we're likely to see a weak price growth print.

FRIDAY November 10 - 2:00	
Q3 2023	**q/q**
Consensus	-0.1%
Q2 2023	**0.2%**

United Kingdom: Real GDP (third quarter) – The UK economy has expanded in every quarter since the end of last year. However, the gains have been modest, at 0.1% in the fourth quarter of 2022 and 0.3% and 0.2% in the first two quarters of 2023. Barring a sharp rebound in economic activity in September, real GDP likely contracted in the third quarter, as July's 0.6% contraction generated a substantial negative carry-over effect. That said, the Bank of England indicated in its recent Monetary Policy Report that it expects GDP to be flat.

Economic Indicators

Week of November 6 to 10, 2023

Day	Time	Indicator	Period	Consensus	Desjardins	Previous reading
UNITED STATES						
MONDAY 6	11:00	Speech by Federal Reserve Governor L. Cook				
TUESDAY 7	8:30	Trade balance – goods and services (US$B)	Sept.	-60.5	-58.8	-58.3
	10:00	Speech by Federal Reserve Governor C. Waller				
	13:25	Speech by Federal Reserve Bank of Dallas President L. Logan				
	15:00	Consumer credit (US$B)	Sept.	10.00	10.00	-15.62
WEDNESDAY 8	9:15	Speech by Federal Reserve Chair J. Powell				
	10:00	Wholesale inventories – final (m/m)	Sept.	0.0%	0.0%	0.0%
THURSDAY 9	8:30	Initial unemployment claims	Oct. 30–Nov. 3	218,000	218,000	217,000
	9:30	Speech by Federal Reserve Bank of Atlanta President R. Bostic				
	12:00	Speech by Federal Reserve Bank of St. Louis Interim President K. O'Neill Paese				
	14:00	Speech by Federal Reserve Chair J. Powell				
FRIDAY 10	10:00	University of Michigan consumer sentiment index – preliminary	Nov.	64.0	62.5	63.8
	14:00	Federal budget (US$B)	Oct.	n/a	n/a	-171.0
CANADA						
MONDAY 6	---	---				
TUESDAY 7	8:30	International trade ($B)	Sept.	0.95	1.30	0.72
	11:00	Speech by Bank of Canada Deputy Governor S. Kozicki				
	---	Government of Quebec's 2023 Economic and Fiscal Update				
WEDNESDAY 8	8:30	Building permits (m/m)	Sept.	1.1%	-1.8%	3.4%
	13:30	Release of the Bank of Canada Summary of Deliberations				
THURSDAY 9	11:45	Speech by Bank of Canada Senior Deputy Governor C. Rogers				
FRIDAY 10	10:30	Release of the Bank of Canada's Senior Loan Officer Survey				

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 November 6 to 10, 2023

Country	Time	Indicator	Period	Consensus m/m (q/q)	Consensus y/y	Previous reading m/m (q/q)	Previous reading y/y
OVERSEAS							
DURING THE WEEK							
China	---	Trade balance (US$B)	Oct.	84.20		77.83	
MONDAY 6							
Germany	2:00	Factory orders	Sept.	-1.5%	-3.0%	3.9%	-4.2%
Italy	3:45	Composite PMI	Oct.	47.7		49.2	
Italy	3:45	Services PMI	Oct.	48.5		49.9	
France	3:50	Composite PMI – final	Oct.	45.3		45.3	
France	3:50	Services PMI – final	Oct.	46.1		46.1	
Germany	3:55	Composite PMI – final	Oct.	45.8		45.8	
Germany	3:55	Services PMI – final	Oct.	48.0		48.0	
Eurozone	4:00	Composite PMI – final	Oct.	46.5		46.5	
Eurozone	4:00	Services PMI – final	Oct.	47.8		47.8	
United Kingdom	4:30	Construction PMI	Oct.	46.0		45.0	
Australia	22:30	Reserve Bank of Australia meeting	Nov.	4.35%		4.10%	
TUESDAY 7							
Germany	2:00	Industrial production	Sept.	-0.4%	-3.0%	-0.2%	-2.0%
Eurozone	5:00	Producer price index	Sept.	0.5%	-12.5%	0.6%	-11.5%
WEDNESDAY 8							
Japan	0:00	Leading indicator – preliminary	Sept.	108.7		109.2	
Japan	0:00	Coincident index – preliminary	Sept.	114.7		114.6	
Germany	2:00	Consumer price index – final	Oct.	0.0%	3.8%	0.0%	3.8%
France	2:45	Trade balance (€M)	Sept.	n/a		-8,202	
France	2:45	Current account (€B)	Sept.	n/a		-0.8	
Italy	4:00	Retail sales	Sept.	n/a	n/a	-0.4%	2.4%
Japan	18:50	Current account (¥B)	Sept.	2,269.7		1,634.9	
China	20:30	Consumer price index	Oct.		-0.2%		0.0%
China	20:30	Producer price index	Oct.		-2.8%		-2.5%
THURSDAY 9							
France	2:45	Wages – preliminary	Q3	n/a		1.0%	
Eurozone	5:00	Retail sales	Sept.	-0.2%	-2.9%	-1.2%	-2.1%
Mexico	14:00	Bank of Mexico meeting	Nov.	11.25%		11.25%	
FRIDAY 10							
United Kingdom	2:00	Trade balance (£M)	Sept.	-2,600		-3,415	
United Kingdom	2:00	Construction	Sept.	-0.4%	2.7%	-0.5%	2.3%
United Kingdom	2:00	Index of services	Sept.	0.0%		0.4%	
United Kingdom	2:00	Monthly GDP	Sept.	-0.1%		0.2%	
United Kingdom	2:00	Real GDP – preliminary	Q3	-0.1%	0.6%	0.2%	0.6%
United Kingdom	2:00	Industrial production	Sept.	-0.1%	1.1%	-0.7%	1.3%
Italy	4:00	Industrial production	Sept.	-0.3%	n/a	0.2%	-4.2%

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).