TD Economics

The Weekly Bottom Line

October 27, 2023

Highlights

United States

- The 10-year Treasury yield briefly surpassed 5% earlier this week. Though yields have since retraced, the 10-year looks to end the week at a still elevated 4.85%.
- The advance estimate of GDP showed the economy registered its strongest gain in nearly two years in the third quarter, with most major areas of spending recording gains.
- The FOMC is expected to hold rates steady next week, but the uptick in September inflation along with any signs of continued labor market strength in next week's data will tilt the scales in favor of another rate hike later this year.

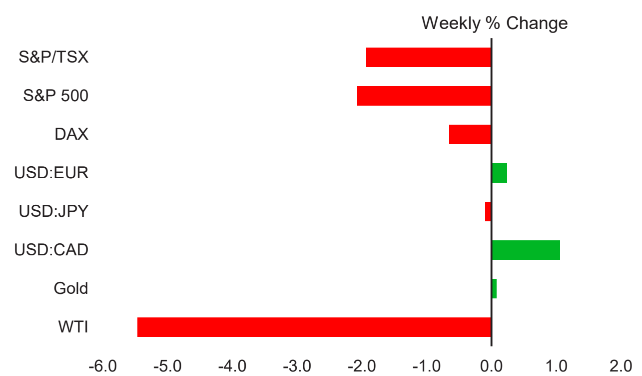
Canada

- Fears around what higher-for-longer rates might do to growth dominated markets this week. Equities were lower and yields fell. Meanwhile, easing concerns of a wider Middle East conflict weighed on oil.
- The Bank of Canada held the policy rate at 5% this week. Their Monetary Policy Report emphasized the economic toll from higher rates, consistent with no further hikes.
- However, policymakers retained a hawkish tone, given still robust wage growth, elevated inflation expectations and corporate pricing behaviour that's yet to normalize.

This Week in the Markets				
	Current*	Week Ago	52-Week High	52-Week Low
Stock Market Indexes				
S&P 500	4136	4224	4589	3720
S&P/TSX Comp.	18742	19116	20767	18742
DAX	14723	14798	16470	13130
FTSE 100	7310	7402	8014	7048
Nikkei	30992	31259	33753	25717
Fixed Income Yields				
U.S. 10-yr Treasury	4.85	4.91	4.99	3.31
Canada 10-yr Bond	3.99	4.07	4.24	2.72
Germany 10-yr Bund	2.84	2.89	2.97	1.78
UK 10-yr Gilt	4.55	4.65	4.75	3.01
Japan 10-yr Bond	0.88	0.84	0.88	0.24
Foreign Exchange Cross Rates				
C$ (USD per CAD)	0.72	0.73	0.76	0.72
Euro (USD per EUR)	1.06	1.06	1.12	0.97
Pound (USD per GBP)	1.21	1.22	1.31	1.12
Yen (JPY per USD)	149.7	149.9	150.4	127.9
Commodity Spot Prices**				
Crude Oil ($US/bbl)	84.8	88.8	93.7	66.7
Natural Gas ($US/MMBtu)	2.87	2.61	7.49	1.77
Copper ($US/met. tonne)	7911.0	7879.8	9330.8	7522.0
Gold ($US/troy oz.)	1982.0	1981.4	2050.3	1629.5

*As of 10:02 AM on Friday. **Oil-WTI, Cushing, Nat. Gas-Henry Hub, LA (Thursday close price). Copper-LME Grade A. Gold-London Gold Bullion. Source: Bloomberg.

Oil Slides on Fears of Softening Global Demand



Note: Data as of 10:48 AM ET, Friday, October 27, 2023.
Source: Bloomberg, TD Economics.

Global Official Policy Rate Targets	
Central Banks	Current Target
Federal Reserve (Fed Funds Rate)	5.25 - 5.50%
Bank of Canada (Overnight Rate)	5.00%
European Central Bank (Refi Rate)	4.50%
Bank of England (Repo Rate)	5.25%
Bank of Japan (Overnight Rate)	-0.10%

Source: Bloomberg.

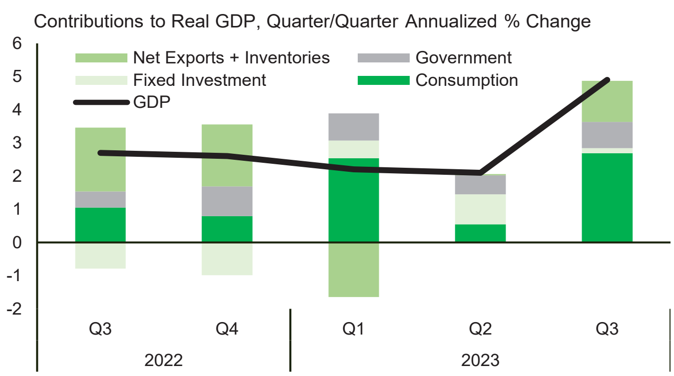
U.S. – Economic Resilience on Full Display in Third Quarter

Longer-term Treasury yields continued to creep higher through the early portion of the week, as the looming threat of a mid-November government shutdown, increased Treasury issuance, and heightened geopolitical tensions remain key drivers pressuring the term-premia higher. After briefly surpassing 5% earlier this week, the 10-Year Treasury yield has since pared its gains and currently sits at a still elevated 4.85%. Meanwhile, equities edged lower for the second straight week – down 2% at the time of writing – but remain 8% higher on the year.

Turning to the economic data calendar, the Bureau of Economic Analysis (BEA) released its advance estimate of third quarter real GDP. The report showed economic activity accelerating at more than double the rate of expansion seen in Q2. The ongoing theme of economic resilience was on full display last quarter, with most major areas of spending recording gains. The strength in consumer spending was particularly eye-catching, jumping up 4.0% (Chart 1). The summer shopping spree was fueled by a resilient labor market and a further drawdown of the excess savings accumulated during the pandemic. Moreover, because many homeowners locked-in mortgages at ultra-low rates in 2020/21, the passthrough of higher interest rates to the consumer has been more muted relative to past tightening cycles.

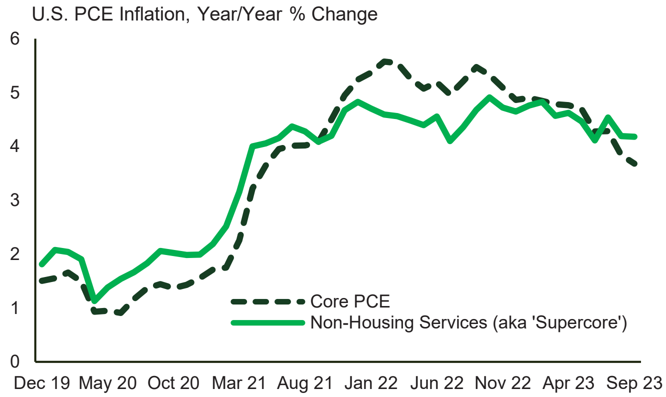
Perhaps more concerning for policymakers is that spending momentum heated up at the end of the third quarter. September's gain was the second strongest over the past eight months, and suggests consumers didn't hold back last month, despite the looming headwind of student loan repayments restarting in October. At this point, we see Q3's

Chart 1: U.S. GDP Sharply Accelerates By 4.9% in Q3



Source: Bureau of Economic Analysis, TD Economics.

Chart 2: 'Supercore' Inflation Remains Sticky



Source: Bureau of Economic Analysis, TD Economics.

blowout numbers as the 'last hurrah' and expect a more tepid pace of consumer spending (1.5-2%) for Q4, before slipping sub-1% through the first half of next year.

Should the consumer prove more resilient, that will spell trouble on the inflation front. In fact, core PCE inflation data for September has already telegraphed some evidence of progress stalling. Price growth picked up to 0.3% m/m (up from the 0.17% m/m gains averaged over the three prior months), with notable strength in Powell's 'supercore' measure, which has barely budged from last year's highs (Chart 2).

From the Fed's perspective, nothing out this week will influence next week's interest rate decision. At this point, markets are fully priced for the FOMC to hold rates steady, and only attach a 20% probability to another rate hike in December. However, that could quickly change over the next week should the FOMC statement and/or Powell's press conference strike a more hawkish tone. Next week's Employment Cost Index release for the third quarter is also important given it contains a measure of wage inflation that the Fed watches closely. As well, October's employment figures out Friday will be closely scrutinized as usual. Unless these reports show a definitive sign that the labor market is cooling, which looks unlikely given the recent strength in higher frequency indictors including jobless claims and Indeed job posting data, another rate hike come December seems inevitable.

Thomas Feltmate, Director | 416- 944-5730

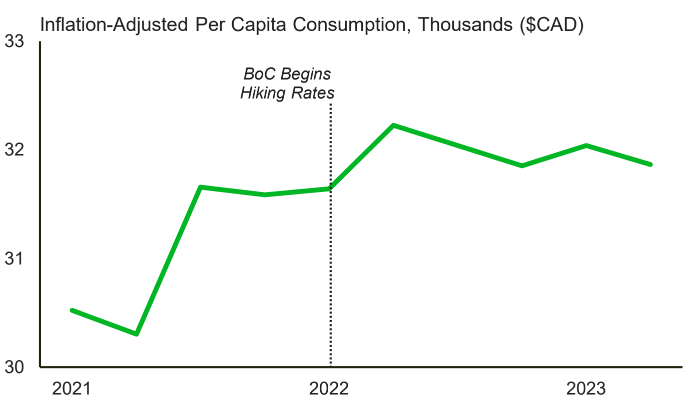
Canada – Holding the Line

The mood in financial markets was more dovish this week, on concerns on what higher-for-longer rates could mean for growth prospects. The North American benchmark WTI slid about $3 per barrel, greased by weaker-than-expected seasonal demand in the U.S. and (likely) some degree of assurance that the Israel/Hamas conflict would be regionally contained. This decline helped pull the TSX to its lowest level since October of last year. Even the sustained and severe upward march in bond yields observed over the past several months hit a pause this week, with yields down across the curve.

The pullback in yields doesn't change the fact that they remain near-multi year highs and are exerting a braking force on the Canadian economy. The Bank of Canada hammered this point home in this week's interest rate announcement (see commentary). The Bank stood pat on rates, and the accompanying Monetary Policy Report (MPR) even included a special section detailing the impact of rates on economic activity. Policymakers noted that inflation-adjusted per capita consumption has stalled since the Bank started hiking rates (Chart 1), weighed down (to varying degrees) by both rate-sensitive and non-rate-sensitive goods and services.

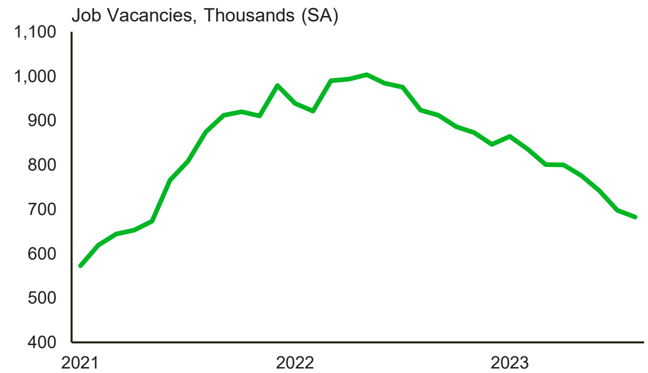
The impact of higher rates also shows up in the Bank's near-term growth projections, where they are forecasting (annualized) gains of 0.8% for GDP in both the third and fourth quarters of this year. While we wouldn't quibble too much with these projections, monthly GDP data suggests some modest downside risk to the Bank's Q3 forecast. Preliminary estimates had pointed to a 0.1% month-on-month gain in August, although we'll receive confirmation of that (alongside an early read on September) when the monthly GDP data is released next week.

Chart 1: Rate Hikes Keeping Canadian Consumption Subdued



Source: Statistics Canada, TD Economics.

Chart 2: Canadian Labour Demand Continued To Cool in August



Source: Statistics Canada, TD Economics.

While softer growth would certainly be consistent with our view that the Bank is done hiking rates this year, we can't necessarily close the book on that possibility. The Bank upgraded its inflation forecast for this year and next, while making pains to emphasize their concern that core inflation is not cooling as rapidly as expected. They also noted that inflation expectations are far from normal while corporate pricing behaviour also has yet to normalize.

In addition to these factors, the Bank remains concerned that a tight job market is keeping wage growth in the 4-5% range, which is simply too strong to move inflation to their 2% target, especially given Canada's poor productivity. Our view is that wage growth will likely cool moving forward amid robust population growth and an economy that's struggling to keep its head above water. Notably, this week's Survey of Employment Payrolls and Hours showed some cooling in wage growth, declining payroll employment and falling job vacancies for the month of August (Chart 2). Next week, all eyes will be on Friday's Labour Force Survey release, which will offer the latest temperature reading on wage growth.

Rishi Sondhi, Economist | 416-983-8806

Recent Key Economic Indicators: Oct 23 - 27, 2023							
Release Date		Economic Indicator/Event	Data for Period	Units	Current	Prior
		United States				
Oct 24		S&P Global US Manufacturing PMI	Oct	Index	50.0	49.8
Oct 24		S&P Global US Services PMI	Oct	Index	50.9	50.1
Oct 24		S&P Global US Composite PMI	Oct	Index	51.0	50.2
Oct 25		New Home Sales	Sep	Thsd	759.0	676.0
Oct 26		Advance Goods Trade Balance	Sep	Blns	-85.5	-84.6
Oct 26		Gross Domestic Product Annualized	3Q	Q/Q % Chg.	4.9	2.1
Oct 26		Personal Consumption	3Q	Q/Q % Chg.	4.0	0.8
Oct 26		Durable Goods Orders	Sep	M/M % Chg.	4.7	-0.1
Oct 26		Cap Goods Orders Nondef Ex Air	Sep	M/M % Chg.	0.6	1.1
Oct 26		Initial Jobless Claims	Oct 21	Thsd	210.0	200.0
Oct 27		Personal Income	Sep	M/M % Chg.	0.3	0.4
Oct 27		Real Personal Spending	Sep	M/M % Chg.	0.4	0.1
Oct 27		PCE Deflator	Sep	Y/Y % Chg.	3.4	3.4
		Canada				
Oct 25		Bank of Canada Rate Decision	Oct 25	%	5.0	5.0
Oct 26		CFIB Business Barometer	Oct	Index	47.2	48.8
Oct 26		Payroll Employment Change - SEPH	Aug	Thsd	-46.8	4.9
		International				
Oct 23	JN	Jibun Bank Japan PMI Mfg	Oct	Index	48.5	48.5
Oct 26	EZ	ECB Main Refinancing Rate	Oct 26	%	4.5	4.5
Oct 26	JN	Tokyo Consumer Price Index	Oct	Y/Y % Chg.	3.3	2.8

*Eastern Standard Time. Source: Bloomberg, TD Economics.

Upcoming Economic Releases and Events: Oct 30 - Nov 03, 2023							
Release Date	Time*		Economic Indicator/Event	Data for Period	Units	Consensus Forecast	Last Period
United States							
Oct 31	8:30		Employment Cost Index	3Q	Index	1.0	1.0
Oct 31	9:00		S&P CoreLogic CS 20-City NSA	Aug		-	0.1
Oct 31	9:00		S&P CoreLogic CS US HPI NSA	Aug	Y/Y % Chg.	-	1.0
Oct 31	10:00		Conf. Board Consumer Confidence	Oct	Index	100.3	103.0
Nov 01	8:15		ADP Employment Change	Oct	Thsd	135.0	89.0
Nov 01	9:45		S&P Global US Manufacturing PMI	Oct	Index	-	50.0
Nov 01	10:00		ISM Manufacturing	Oct	Index	49.0	49.0
Nov 01	14:00		FOMC Rate Decision (Upper Bound)	Nov 01	%	5.5	5.5
Nov 01	14:00		Interest on Reserve Balances Rate	Nov 02	%	-	5.4
Nov 01	14:30		*Fed Chair Holds Press Conference Following FOMC Meeting*				
Nov 01	0:00		Wards Total Vehicle Sales	Oct	Mlns	15.1	15.7
Nov 02	8:30		Unit Labor Costs	3Q	Q/Q % Chg.	1.0	2.2
Nov 02	8:30		Initial Jobless Claims	Oct 28	Thsd	210.0	210.0
Nov 02	10:00		Factory Orders	Sep	M/M % Chg.	1.1	1.2
Nov 02	10:00		Factory Orders Ex Trans	Sep	M/M % Chg.	-	1.4
Nov 02	10:00		Durable Goods Orders	Sep	M/M % Chg.	-	4.7
Nov 02	10:00		Cap Goods Orders Nondef Ex Air	Sep	M/M % Chg.	-	0.6
Nov 03	8:30		Change in Nonfarm Payrolls	Oct	Thsd	175.0	336.0
Nov 03	8:30		Unemployment Rate	Oct	%	3.8	3.8
Nov 03	8:30		Average Hourly Earnings	Oct	M/M % Chg.	0.3	0.2
Nov 03	9:45		S&P Global US Services PMI	Oct	Index	-	50.9
Nov 03	9:45		S&P Global US Composite PMI	Oct	Index	-	51.0
Nov 03	10:00		ISM Services Index	Oct	Index	53.0	53.6
Canada							
Oct 30	15:30		*Bank of Canada Governor Appears at Standing Committee on Finance*				
Oct 31	8:30		Gross Domestic Product	Aug	M/M % Chg.	-	0.0
Nov 01	9:30		S&P Global Canada Manufacturing PMI	Oct	Index	-	47.5
Nov 01	16:15		*Bank of Canada Governor Appears at Standing Senate Committee on Banking*				
Nov 03	8:30		Net Change in Employment	Oct	Thsd	-	63.8
Nov 03	8:30		Unemployment Rate	Oct	%	-	5.5
International							
Oct 30	19:30	JN	Jobless Rate	Sep	%	2.6	2.7
Oct 30	19:50	JN	Retail Sales	Sep	Y/Y % Chg.	6.0	7.1
Oct 30	21:30	CH	Manufacturing PMI	Oct	Index	50.2	50.2
Oct 30	0:00	JN	BOJ Policy Balance Rate	Oct 31	%	-0.1	-0.1
Oct 31	6:00	EZ	Gross Domestic Product SA	3Q	Y/Y % Chg.	0.2	0.5
Oct 31	6:00	EZ	Consumer Price Index Estimate	Oct	Y/Y % Chg.	3.1	-
Oct 31	20:30	JN	Jibun Bank Japan PMI Mfg	Oct	Index	-	48.5
Oct 31	21:45	CH	Caixin China PMI Mfg	Oct	Index	50.8	50.6
Nov 02	8:00	UK	Bank of England Bank Rate	Nov 02	%	5.3	5.3
Nov 03	6:00	EZ	Unemployment Rate	Sep	%	6.4	6.4

*Eastern Standard Time. Source: Bloomberg, TD Economics.