The Weekly Bottom Line

September 8, 2023

Highlights

United States

- Hard economic data was thin on the ground over the Labor Day shortened week, with survey indicators and Fed speakers grabbing attention.
- A slew of Federal Reserve speakers hint that the central bank may skip a rate hike at the next meeting, as the Beige Book (the Fed's survey of economic conditions) suggests that the economy closed out the summer on a modest note.
- Oil markets were also on the move, after Saudi & Russian supply cuts were extended. Higher energy prices are a challenge to the needed cooling in inflation.

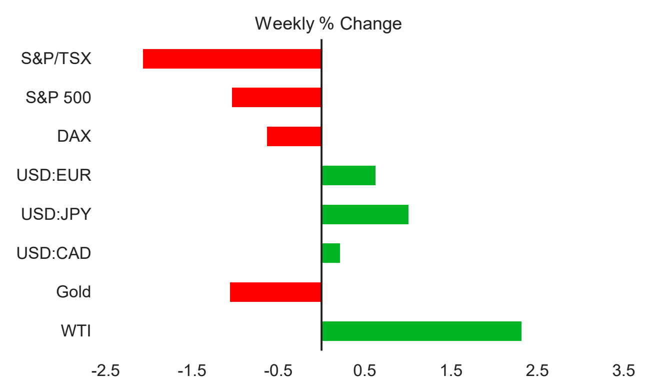
Canada

- As widely anticipated, the BoC remained on hold, keeping the overnight lending rate at 5% while keeping the door open for another hike.
- The labour market moved towards greater balance in August with job gains not keeping pace with population growth, although wage growth remains too strong.
- The Bank of Canada needs to see more softness in the labour market to put a permanent end to this tightening cycle. We expect this to manifest more clearly by the October decision.

This Week in the Markets				
	Current*	Week Ago	52-Week High	52-Week Low
Stock Market Indexes				
S&P 500	4468	4516	4589	3577
S&P/TSX Comp.	20134	20545	20767	18206
DAX	15727	15840	16470	11976
FTSE 100	7476	7465	8014	6826
Nikkei	32607	32711	33753	25717
Fixed Income Yields				
U.S. 10-yr Treasury	4.23	4.18	4.34	3.31
Canada 10-yr Bond	3.66	3.56	3.82	2.72
Germany 10-yr Bund	2.60	2.55	2.75	1.65
UK 10-yr Gilt	4.42	4.43	4.75	3.01
Japan 10-yr Bond	0.66	0.63	0.67	0.22
Foreign Exchange Cross Rates				
C$ (USD per CAD)	0.73	0.74	0.77	0.72
Euro (USD per EUR)	1.07	1.08	1.12	0.96
Pound (USD per GBP)	1.25	1.26	1.31	1.07
Yen (JPY per USD)	147.6	146.2	150.2	127.9
Commodity Spot Prices**				
Crude Oil ($US/bbl)	87.3	85.6	92.6	66.7
Natural Gas ($US/MMBtu)	2.45	2.71	8.63	1.77
Copper ($US/met. tonne)	8309.3	8479.3	9330.8	7422.0
Gold ($US/troy oz.)	1921.1	1940.1	2050.3	1622.4

*As of 11:27 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 Prices Rise on Supply Cuts



Note: Data as of 12:18 PM ET, Friday, September 8, 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)	4.25%
Bank of England (Repo Rate)	5.25%
Bank of Japan (Overnight Rate)	-0.10%

Source: Bloomberg.

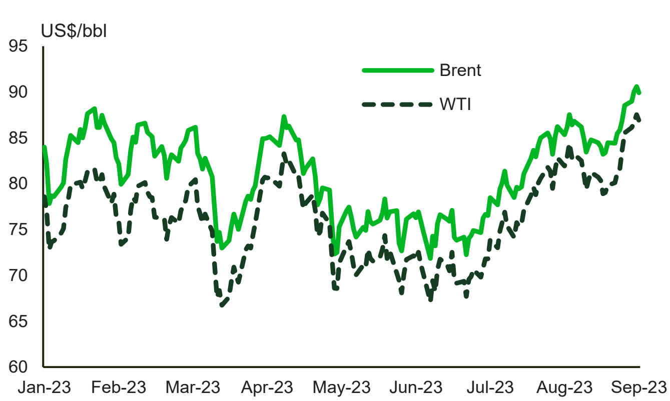
U.S. – Higher for Longer Seems Surer

Hard economic data was thin on the ground over the Labor Day shortened week, with survey indicators and Fed speakers the main highlights on the calendar. Crude oil markets were also a bit livelier after Saudi Arabia and Russia both announced extensions to their supply cuts through to the end of the year.

Since July, Saudi Arabia has voluntary removed 1 million barrels per day (b/d) of crude from global oil markets. While the measure was cited to be temporary, it was already extended to September, with this week's announcement extending it once again. Russia added their own export reduction of 300,000 b/d. On the day of the announcement, Brent crude, the international benchmark, rose 1.2% to close at $90.04 – exceeding $90 a barrel for the first time this year (Chart 1). Prices have since given back some of the gain, but the general move higher in oil prices over the past few weeks is likely to threaten efforts to tame inflation.

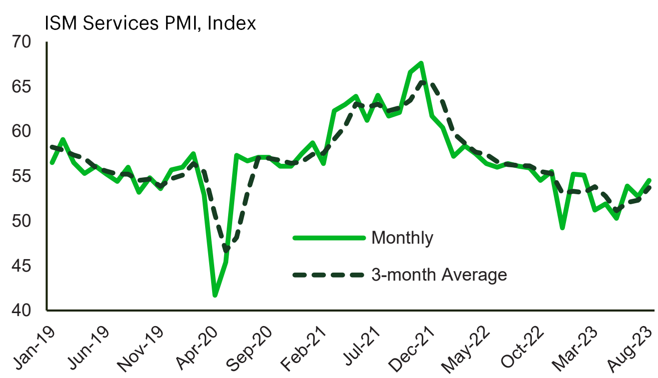
On that front, this week featured a full roster of Fed speakers. Governor Waller was also in the news making more dovish than usual statements. He noted that data showing a cooling job market meant the Fed should "proceed carefully", and does not necessitate an imminent rate hike. Bostic echoed these sentiments. Logan noted that it could be appropriate' to skip an interest-rate increase in September. Williams left whether the Fed would hike again as an open question, while Goolsbee, hinting at a higher for longer stance, sees a "golden opportunity" for the Fed to tame inflation without triggering a recession. All speakers emphasized that the Fed will be paying close attention to the data.

Chart 1: Crude Oil Prices Rise on Extended Supply Cuts



Source: ICE, CME, TD Economics. Last observation: September 7, 2023.

Chart 2: U.S. Service Sector Expands for the Eight Consecutive Month



Note: Readings above (below) 50 indicate expansion (contraction).
Source: Institute of Supply Management, TD Economics.

The Fed's latest survey of economic conditions, the Beige Book, noted that the U.S. economy grew at a modest pace during July and August, relative to slight growth in the previous report. This was bolstered by a final bout of pent-up demand for leisure activities. Outside of leisure travel and a rise in auto sales due to better inventory, nonessential retail sales slowed. Job growth was generally subdued nationwide with wage growth elevated but expected to moderate in the months ahead. Prices for consumer goods fell faster than in many other categories. Demand for manufactured goods waned while the supply constrained single-family housing market continued to be challenged by higher financing costs and rising insurance premiums.

The ISM services index surprised to the upside this week, reaching a six-month high of 54.5 in August (Chart 2). The survey continued to highlight a service sector that is still in expansion mode, with survey respondents expressing positive sentiments about business and economic conditions. Beneath the headline, the positive details were an increase in business activity (+0.2 pts), new orders (+2.5 pts), and employment (+4.0 pts).

The tone of the economic news this week is likely to keep policymakers in a wait and see mode. Consumers are keeping the service sector humming along, even as the labor market cools. All good news for the Fed, but higher energy prices remain a wildcard that will require close monitoring so as not to undo the progress on inflation thus far.

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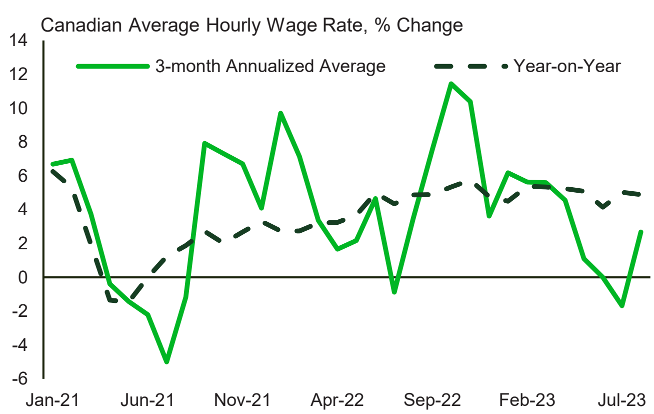
Canada – Finding a Balance

There was no surprise in the Bank of Canada's announcement this Wednesday. As widely anticipated, the benchmark overnight lending rate remained at 5%. In the wake of the decision, the market implied policy rate moved lower by roughly 10 basis points over the week. This shift put more pressure on Canadian dollar. When measured in U.S. currency, the loonie got cheaper by almost one cent. The loonie is down nearly three cents since the BoC's July interest rate announcement.

This was the second pause in this tightening cycle, but this time, the BoC did not characterize it as such. The tone of the message remained hawkish, with Governor Macklem reiterating his loud promise "to take further action", if needed. Indeed, the first time the Bank went on hold earlier in the year markets resolved that rate cuts won't be too long in coming. This helped ease financial conditions enough to reinvigorate the housing market and consumer spending in the first quarter.

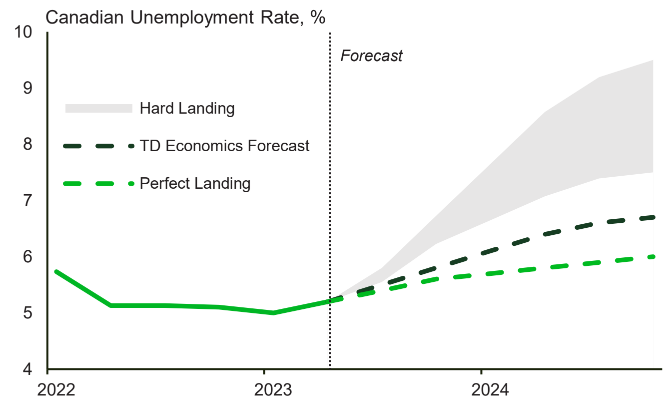
Fifty basis points of hikes later, the risk of overtightening is higher as weakness in economic activity is more convincing. Recent readings of GDP, retail trade and home sales provide compelling evidence that demand is moderating. Nonetheless, the labour market continues to give mixed signals. August's headline employment gain at 40K new jobs was twice as high as expected by the consensus, but the pace of employment growth is lower than population growth, leading to a slight rise in the unemployment rate – at least at the second decimal place.

Chart 1: Wage Growth Remains Persistent



Source: Statistics Canada, TD Economics. Last observation: August 2023.

Chart 2: Unemployment Rate is Set to Rise



Source: Statistics Canada, TD Economics.

Meanwhile, headline wage growth eased slightly in August (on a year-on -year basis). The three-month annualized average change in wages did pick up, but still points to a cooler pace of wage gains in the months ahead (Chart 1). Overall, the pace remains too strong for broad inflation to move to its target. Additionally, when coupled with a decline in productivity, high wage growth means unit labour costs are rising for businesses. In a strong demand environment, businesses may pass this onto consumers, keeping inflation up, or they may cut costs by reducing investment or shedding workers.

Persistent wage pressure remains the most unfading signal of an unbalanced labour market. Still, we expect it to move to a lower trajectory as employees' ability to negotiate a pay raise diminishes as job vacancies become scant. As outlined in our recent report, the job market has reached an inflection point, setting a path for the unemployment rate to rise to 6.7% over the next year, slightly overshooting the level required to balance the market (Chart 2).

All told, while the market odds of another rate hike are lower, the Bank of Canada will need to see more softness the labour market and continued slowing in economic momentum through the rest of this year to remain on the sidelines. Until the Bank meets again on October 25th, we will have several economic releases, including two more inflation reports. By then, we expect the progress in rebalancing demand and supply in the economy will manifest more clearly, putting a permanent end to the tightening cycle.

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Recent Key Economic Indicators: Sep 04 - 08, 2023						
Release Date		Economic Indicator/Event	Data for Period	Units	Current	Prior
United States						
Sep 05		Cap Goods Orders Nondef Ex Air	Jul	M/M % Chg.	0.1	0.1
Sep 05		Durable Goods Orders	Jul	M/M % Chg.	-5.2	-5.2
Sep 05		Factory Orders	Jul	M/M % Chg.	-2.1	2.3
Sep 05		Factory Orders Ex Trans	Jul	M/M % Chg.	0.8	0.3
Sep 06		Trade Balance	Jul	Blns	-65.0	-63.7
Sep 06		S&P Global US Composite PMI	Aug	Index	50.2	50.4
Sep 06		S&P Global US Services PMI	Aug	Index	50.5	51.0
Sep 06		ISM Services Index	Aug	Index	54.5	52.7
Sep 07		Initial Jobless Claims	Sep 02	Thsd	216.0	229.0
Sep 07		Unit Labor Costs	2Q	Q/Q % Chg.	2.2	1.6
Sep 08		Wholesale Trade Sales	Jul	M/M % Chg.	0.8	-0.8
Canada						
Sep 06		Int'l Merchandise Trade	Jul	Blns	-1.0	-4.9
Sep 06		Bank of Canada Rate Decision	Sep 06	%	5.0	5.0
Sep 08		Net Change in Employment	Aug	Thsd	39.9	-6.4
Sep 08		Unemployment Rate	Aug	%	5.5	5.5
International						
Sep 06	EZ	Retail Sales	Jul	Y/Y % Chg.	-1.0	-1.0
Sep 07	EZ	Employment	2Q	Y/Y % Chg.	1.3	1.5
Sep 07	EZ	Gross Domestic Product SA	2Q	Y/Y % Chg.	0.5	0.6
Sep 07	JN	Gross Domestic Product Annualized SA	2Q	Q/Q % Chg.	4.8	6.0

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

Upcoming Economic Releases and Events: Sep 11 - 15, 2023							
Release Date	Time*		Economic Indicator/Event	Data for Period	Units	Consensus Forecast	Last Period
United States							
Sep 11	11:00	US	NY Fed 1-Yr Inflation Expectations	Aug	%	-	3.6
Sep 12	6:00	US	NFIB Small Business Optimism	Aug	Index	91.3	91.9
Sep 13	8:30	US	Consumer Price Index	Aug	M/M % Chg.	0.6	0.2
Sep 13	8:30	US	Consumer Price Index	Aug	Y/Y % Chg.	3.6	3.2
Sep 13	8:30	US	Consumer Price Index Ex Food and Energy	Aug	M/M % Chg.	0.2	0.2
Sep 13	8:30	US	Consumer Price Index Ex Food and Energy	Aug	Y/Y % Chg.	4.3	4.7
Sep 14	8:30	US	Initial Jobless Claims	Sep 9	Thsd	-	216.0
Sep 14	8:30	US	Producer Price Index Ex Food and Energy	Aug	M/M % Chg.	0.2	0.3
Sep 14	8:30	US	Producer Price Index Final Demand	Aug	M/M % Chg.	0.4	0.3
Sep 14	8:30	US	Retail Sales Advance	Aug	M/M % Chg.	0.1	0.7
Sep 14	8:30	US	Retail Sales Ex Auto and Gas	Aug	M/M % Chg.	0.1	1.0
Sep 14	10:00	US	Business Inventories	Jul	M/M % Chg.	0.1	0.0
Sep 15	8:30	US	Empire Manufacturing	Sep	Index	-10.4	-19.0
Sep 15	9:15	US	Capacity Utilization	Aug	%	79.3	79.3
Sep 15	9:15	US	Industrial Production	Aug	M/M % Chg.	0.1	1.0
Sep 15	9:15	US	Manufacturing (SIC) Production	Aug	M/M % Chg.	0.1	0.5
Canada							
Sep 14	8:30	CA	Wholesale Sales ex Petroleum	Jul	M/M % Chg.	-	-2.8
Sep 15	8:30	CA	Manufacturing Sales	Jul	M/M % Chg.	-	-1.7
Sep 15	9:00	CA	Existing Home Sales	Aug	M/M % Chg.	-	-0.7
International							
Sep 12	2:00	UK	ILO Unemployment Rate 3Mths	Jul	%	4.3	4.2
Sep 13	2:00	UK	Monthly GDP (3M/3M)	Jul	M/M % Chg.	0.3	-
Sep 14	8:15	EZ	ECB Main Refinancing Rate	Sep 14	%	4.25	4.25
Sep 14	22:00	CH	Retail Sales	Aug	Y/Y % Chg.	3.0	2.5
Sep 14	22:00	CH	Surveyed Jobless Rate	Aug	%	5.3	5.3

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

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