

Weekly Bottom Line

May 31, 2024

Highlights

U.S.

- Revisions to economic growth in the first quarter featured a mark down to consumer spending.
- That theme continued in April, where a contraction in real personal consumption expenditures came as a confirmation that restrictive rates are working.
- Inflation also took another step in the right direction. But sticky services inflation still has room to fall before the Fed can feel confident that inflation has been tamed.

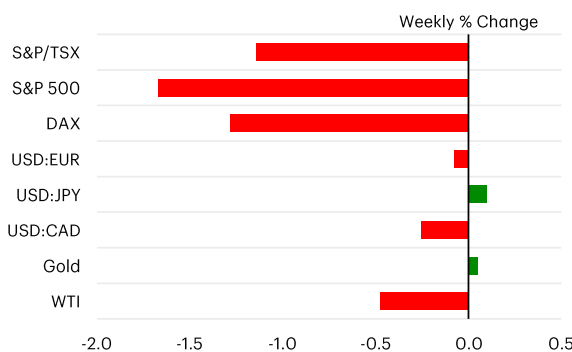
Canada

- Canadian economic growth missed to the downside in the first quarter. A strong increase in domestic demand was offset by inventory drawdowns.
- As the dust settles, markets have increased their bets for a June rate cut to their highest level since the last monetary policy meeting.
- We acknowledge the risks around a cut next week, but ultimately believe the Bank of Canada will wait until July to pull the trigger.

This Week in the Markets				
	Current*	Week Ago	52-Week High	52-Week Low
Stock Market Indexes				
S&P 500	5215	5305	5321	4117
S&P/TSX Comp.	22062	22321	22468	18737
DAX	18461	18693	18869	14687
FTSE 100	8268	8318	8446	7257
Nikkei	38488	38646	40888	30527
Fixed Income Yields				
U.S. 10-yr Treasury	4.48	4.47	4.99	3.60
Canada 10-yr Bond	3.62	3.60	4.24	3.06
Germany 10-yr Bund	2.64	2.58	2.97	1.90
UK 10-yr Gilt	4.30	4.26	4.75	3.44
Japan 10-yr Bond	1.07	1.01	1.09	0.36
Foreign Exchange Cross Rates				
C\$ (USD per CAD)	0.73	0.73	0.76	0.72
Euro (USD per EUR)	1.09	1.08	1.12	1.05
Pound (USD per GBP)	1.27	1.27	1.31	1.21
Yen (JPY per USD)	157.2	157.0	158.3	138.1
Commodity Spot Prices**				
Crude Oil (\$US/bbl)	77.9	78.7	93.7	67.1
Natural Gas (\$US/MMBtu)	1.86	2.22	13.20	1.24
Copper (\$US/met. tonne)	10007.1	10204.6	10800.8	7823.8
Gold (\$US/troy oz.)	2334.1	2333.8	2425.3	1820.3

*As of 11:01 AM on Friday. **Oil-WTI, Cushing, Nat. Gas-Henry Hub, LA (Thursday close price). Copper-LME Grade A. Gold-London Gold Bullion. Source: Bloomberg.

Risk-Off Sentiment Sends Markets Lower



Note: Data as of 11:00 AM ET, Friday, May 31, 2024.
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. – A Slight Downshift

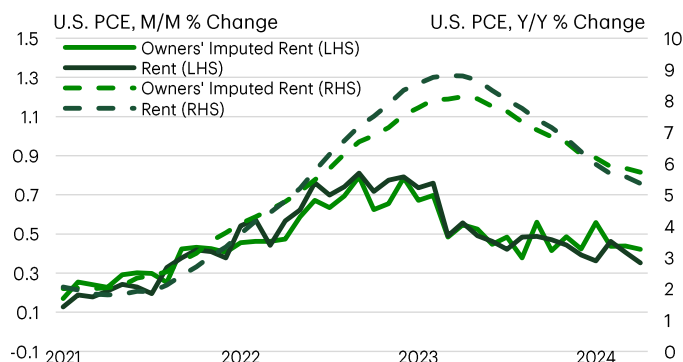
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Bond yields are climbing down from this week's highs as a pair of high-profile data releases suggest the some of the steam is being let out of the U.S. economy. While there isn't anything released this week that is going to meaningfully move the needle on the timing of the Fed's decision, it was encouraging to see that the current restrictive policy stance is cooling the economy. That said, there is still enough strength underlying the economy to keep the Fed's policy rate right where it is until later this year.

First up was the refresh of the first quarter's GDP data. Top-line economic growth was shaved down a smidge, to a below trend 1.3% quarter-on-quarter (q/q, annualized) change. Consumer spending too was marked down, from 2.5% to a more trend-like 2.0%. That said, faced with persistently strong price growth and high interest rates, the ability of households to keep buying stuff and spending money on experiences has defied expectations. Specifically, the shift back to services spending has kept demand up on the primarily domestic portion of the economy facing a tight labor market. Moreover, there is room for this trend to run if households continue to adjust their expenditures back towards a pre-pandemic mix, where household services consumption accounted for just shy of 66% of personal consumer expenditures (compared to 64.6% as of April, Chart 1).

So, it came as a welcome surprise that April's Personal Consumption and Expenditures (PCE) survey showed real PCE pull back 0.1% month-on-month (m/m). More good news came as the core PCE deflator edged down to 0.2% m/m, leaving the annual pace of price growth to

Chart 2: Housing Market Price Relief Remains Slow To Arrive



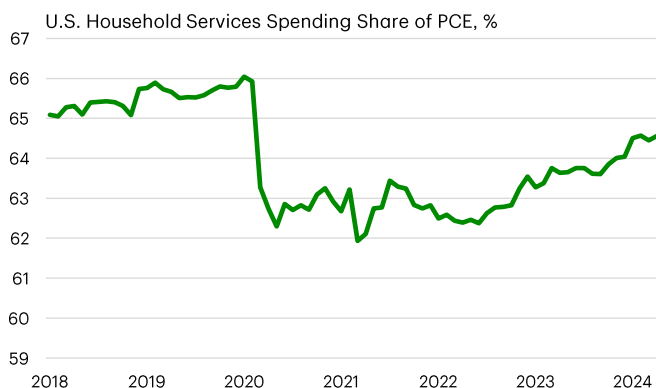
Source: Bureau of Economic Analysis, Haver Analytics, TD Economics.
Last Observation: April 2024.

2.8%. That said, the three- and six-month core PCE inflation rates are still 3.5% and 3.2% (annualized), respectively, as the past few months of strong price growth continue to be felt.

Importantly, while the deceleration in core price growth was welcome, special attention has to be paid to rents and housing costs that have been propping up core price growth. Together the two categories make up roughly 15% of PCE and will be critical to taming inflation. On this front, there was only marginal relief in April. Rent inflation came in at a “soft” 0.4% m/m (the print was 0.35% m/m unrounded). This is in line with the average reading from the prior five months (Chart 2). On the homeownership side too, implied rents came in at the same 0.4% m/m, roughly unchanged from the last few months. Sustained over a year, the 0.4% monthly pace would translate to 4.9% annual growth. The annual rates on the two shelter components are now cruising along at 5.7% and 5.4% for the imputed and actual rent measures, respectively.

For the Fed, April's data were a step in the right direction, but there is still more work to be done before rate cuts become imminent. So now, all eyes are focused on data coming next week, and specifically the May payrolls report. After April's real spending and payrolls data surprised to the downside, the focus will be for any signs that the month was not a one-off and weaker momentum continued into May.

Chart 1: Services Spending Has Room to Grow



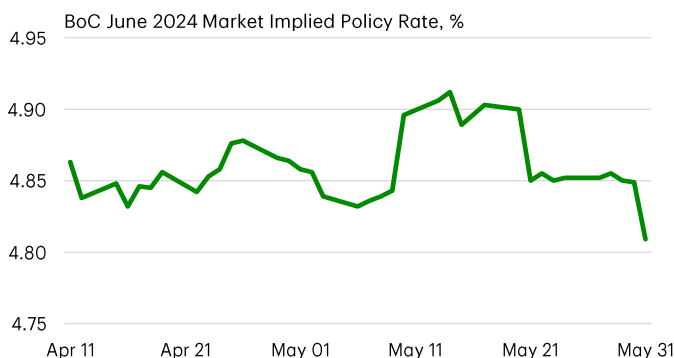
Source: Bureau of Economic Analysis, TD Economics. Last Observation: April 2024.

Marc Ercolao, Economist

Anticipation is high for the Bank of Canada's (BoC) interest rate decision next week. Interest rate relief is on the horizon, but the pressing question remains whether the BoC will cut in June or July. For the past several weeks bets were skewed towards June. With first quarter GDP growth missing to the downside compared to consensus and the BoC's estimates, the scales tipped further in June's direction, with markets pricing in nearly an 80% chance of a move. This is the most conviction markets have had since the BoC's April 10th meeting (Chart 1), but we'd argue that an interest rate reduction next week is not a slam dunk.

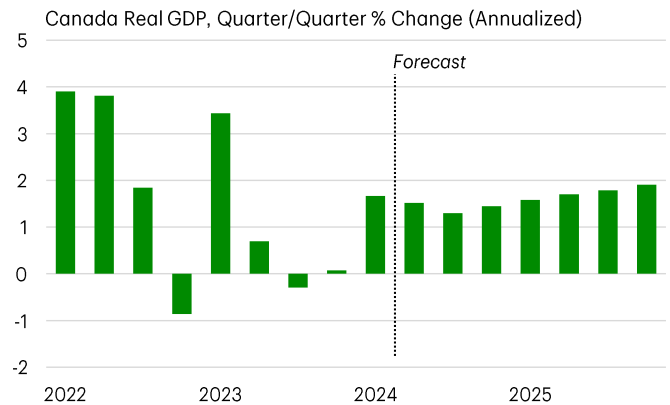
High interest rates are doing their part to cool economic activity, evidenced by the fact that economic expansion effectively flatlined for most of 2023. The Q1 GDP miss also comes on top of a downward revision to the fourth quarter, which now shows no growth. However, the details under the hood were more constructive of decent, albeit temporary, economic strength. For one, final domestic demand, a good barometer for internal economic health, grew at the fastest pace in eight quarters. Business investment and government spending contributions were also encouraging. This quarter, like many in the past two years, was heavily swayed by inventory drawdowns, which subtracted nearly 1.5 percentage points (ppts) from Canada's GDP in Q1. We expect growth will hum along at a below-trend pace for the next several quarters (Chart 1) as the economy continues to grapple with higher interest rates.

Chart 1: Market Bets for a June Cut Have Increased to the Highest Point Since the April Bank of Canada Meeting



Source: Bloomberg, TD Economics. Last Observation: May 31st, 2024.

Chart 2: Modest GDP Growth Expected in the Near-Term



Source: Statistics Canada, TD Economics.

The Bank of Canada should continue to focus their policy decisions on meeting their inflation mandate. In this sense, rate cuts have been justified for some time, especially as headline inflation has printed under 3.0% for four consecutive readings. Further, the average three month annualized change in the BoC's preferred core measures have been sub-2% for the last two months.

Despite inflation dynamics suggesting the economy is ready for a cut, we still believe the BoC will pull the trigger in July. Firstly, Governor Macklem has only acknowledged progress, but hasn't explicitly signaled any intention to make a move. Further, in the recent summary of deliberations, some council members stressed that the risk was lower that higher rates would slow activity more than necessary. In an effort to increase transparency and forward guidance, the Bank can use next week to tee up a July rate cut, while allowing themselves to see two more inflation prints to confirm that durable 2% price growth is in sight.

We also recently wrote about monetary policy divergence with the Federal Reserve and how much room the BoC can run on their own before risking a destabilization in the Canadian dollar. In short, this won't be the first time that policy [divergence](#) has happened between the two central banks. Meanwhile, Governor Macklem continues to stress that the Bank will act independently. Stay tuned for Bank's decision next week!

Exhibits

Recent Key Economic Indicators: May 27 - 31, 2024					
Release Date	Economic Indicator/Event	Data for Period	Units	Current	Prior
United States					
May 28	Conf. Board Consumer Confidence	May	Index	102.0	97.5
May 28	S&P CoreLogic CS 20-City NSA	Mar	Y/Y % Chg.	7.4	7.3
May 28	S&P CoreLogic CS US HPI NSA	Mar	Y/Y % Chg.	6.5	6.5
May 30	Advance Goods Trade Balance	Apr	Blns	-99.40	-92.30
May 30	Gross Domestic Product (Annualized)	Q1	Q/Q % Chg.	1.3	1.6
May 30	Initial Jobless Claims	May 25	Thsd	219.0	216.0
May 30	Pending Home Sales	Apr	M/M % Chg.	-7.7	3.6
May 30	Personal Consumption	Q1	Q/Q % Chg.	2.0	2.5
May 31	PCE Core Deflator	Apr	Y/Y % Chg.	2.8	2.8
May 31	PCE Deflator	Apr	Y/Y % Chg.	2.7	2.7
May 31	Personal Income	Apr	M/M % Chg.	0.3	0.5
May 31	Real Personal Spending	Apr	M/M % Chg.	-0.1	0.4
Canada					
May 28	Industrial Product Price	Apr	M/M % Chg.	1.5	0.9
May 30	CFIB Business Barometer	May	Index	56.4	47.7
May 30	Payroll Employment Change (SEPH)	Mar	Thsd	51.4	14.6
May 31	Gross Domestic Product	Mar	M/M % Chg.	0.0	0.2
May 31	Gross Domestic Product (Annualized)	Q1	Q/Q % Chg.	1.7	0.1
International					
May 30	CH Manufacturing PMI	May	Index	49.5	50.4
May 30	EZ Unemployment Rate	Apr	%	6.4	6.5
May 30	JN Jobless Rate	Apr	%	2.6	2.6
May 30	JN Retail Sales	Apr	Y/Y % Chg.	2.4	1.1
May 30	JN Tokyo Consumer Price Index	May	Y/Y % Chg.	2.2	1.8
May 31	EZ Consumer Price Index Estimate	May	Y/Y % Chg.	2.6	2.4

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

Upcoming Economic Releases and Events: Jun 03 - 07, 2024

Release Date	Time*	Economic Indicator/Event	Data for Period	Units	Consensus Forecast	Last Period
United States						
Jun 3	9:45	S&P Global US Manufacturing PMI	May	Index	50.9	50.9
Jun 3	10:00	ISM Manufacturing	May	Index	49.7	49.2
Jun 3	17:00	Wards Total Vehicle Sales	May	MIns	15.80	15.74
Jun 4	10:00	Cap Goods Orders Nondef Ex Air	Apr	M/M % Chg.	-	0.3
Jun 4	10:00	Durable Goods Orders	Apr	M/M % Chg.	0.7	0.7
Jun 4	10:00	Factory Orders	Apr	M/M % Chg.	0.6	0.8
Jun 4	10:00	Factory Orders Ex Trans	Apr	M/M % Chg.	0.3	0.4
Jun 4	10:00	Job Openings	Apr	MIns	8.40	8.49
Jun 5	8:15	ADP Employment Change	May	Thsd	180.0	192.0
Jun 5	9:45	S&P Global US Composite PMI	May	Index	-	54.4
Jun 5	9:45	S&P Global US Services PMI	May	Index	54.8	54.8
Jun 5	10:00	ISM Services	May	Index	51.0	49.4
Jun 6	8:30	Initial Jobless Claims	Jun 01	Thsd	220.0	219.0
Jun 6	8:30	Trade Balance	Apr	BIns	-75.10	-69.40
Jun 6	8:30	Unit Labor Costs	Q1	Q/Q % Chg.	4.8	4.7
Jun 7	8:30	Average Hourly Earnings	May	M/M % Chg.	0.3	0.2
Jun 7	8:30	Change in Nonfarm Payrolls	May	Thsd	180.0	175.0
Jun 7	8:30	Unemployment Rate	May	%	3.9	3.9
Jun 7	10:00	Wholesale Trade Sales	Apr	M/M % Chg.	-	-1.3
Jun 7	12:00	<i>Fed's Cook Gives Commencement Speech</i>				
Canada						
Jun 5	9:45	Bank of Canada Rate Decision	Jun 05	%	4.75	5.00
Jun 6	8:30	Int'l Merchandise Trade	Apr	BIns	-	-2.28
Jun 6	10:00	Ivey Purchasing Managers Index SA	May	Index	-	63.0
Jun 7	8:30	Net Change in Employment	May	Thsd	-	90.4
Jun 7	8:30	Unemployment Rate	May	%	-	6.1
International						
Jun 4	8:00	BZ Gross Domestic Product	Q1	Y/Y % Chg.	2.2	2.1
Jun 4	20:30	JN Jibun Bank Japan PMI Services	May	Index	-	53.6
Jun 6	5:00	EZ Retail Sales	Apr	Y/Y % Chg.	0.3	0.7
Jun 6	8:15	EZ ECB Main Refinancing Rate	Jun 06	%	4.25	4.50
Jun 7	5:00	EZ Employment	Q1	Y/Y % Chg.	-	1.0
Jun 7	5:00	EZ Gross Domestic Product SA	Q1	Y/Y % Chg.	0.4	0.4

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

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