

Weekly Bottom Line

May 17, 2024

Highlights

U.S.

- After three consecutive months of hotter-than-expected inflation, consumer prices in the U.S. finally broke the heat streak in April, with headline and core inflation decelerating.
- Retail sales also lost momentum in April, with spending coming in flat for the month.
- With the data showing some slowing in economic activity, markets are hopeful that the Federal Reserve will deliver on rate cuts this year. However, Fed Governors are touting that holding rates higher for longer is still on the table, while they wait for more convincing data.

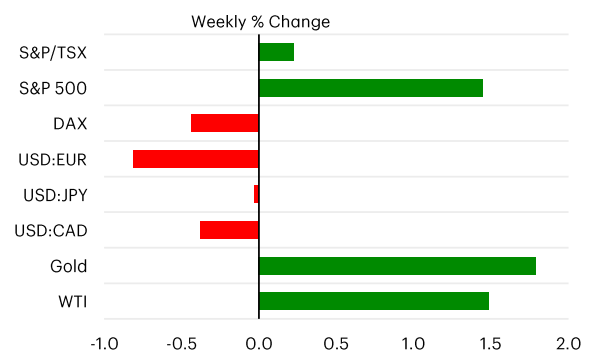
Canada

- Housing starts were firm in April, although nowhere near levels required to hit federal targets under their new plan or restore affordability to solid levels, per CMHC's analysis.
- The weak spring selling season for existing homes continued in April, with sales down month-on-month and benchmark prices flat. However, softness now could set the stage for a rebound later.
- Next week brings the release of the April inflation report, and expectations are that cooler trends will prevail in the Bank of Canada's preferred metrics.

This Week in the Markets				
	Current*	Week Ago	52-Week High	52-Week Low
Stock Market Indexes				
S&P 500	5298	5223	5308	4115
S&P/TSX Comp.	22359	22309	22376	18737
DAX	18693	18773	18869	14687
FTSE 100	8418	8434	8446	7257
Nikkei	38787	38229	40888	30527
Fixed Income Yields				
U.S. 10-yr Treasury	4.40	4.50	4.99	3.60
Canada 10-yr Bond	3.59	3.70	4.24	3.06
Germany 10-yr Bund	2.51	2.52	2.97	1.90
UK 10-yr Gilt	4.12	4.17	4.75	3.44
Japan 10-yr Bond	0.95	0.91	0.96	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	1.25	1.31	1.21
Yen (JPY per USD)	155.7	155.8	158.3	138.0
Commodity Spot Prices**				
Crude Oil (\$US/bbl)	79.2	78.3	93.7	67.1
Natural Gas (\$US/MMBtu)	2.32	2.14	13.20	1.24
Copper (\$US/met. tonne)	10343.2	9897.5	10343.2	7823.8
Gold (\$US/troy oz.)	2402.8	2360.5	2402.8	1820.3

*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.

Rising Fed Rate Cut Prospects Boosts Equities



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. – Inflation Breaks Its Heat Streak

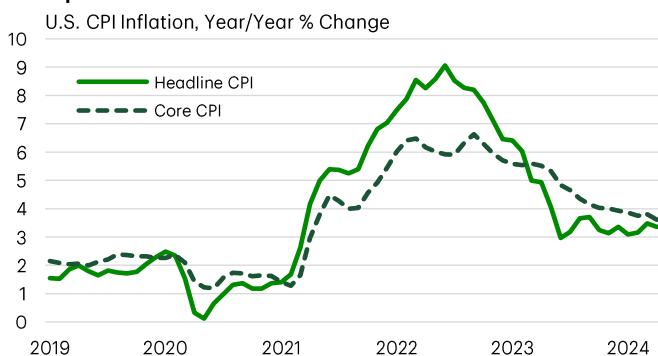
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A combination of data releases this week pointed to a cooling U.S. economy. Retail sales were weak, and inflation slowed, which revived hopes of a Fed rate cut sooner rather than later. Markets responded to the news with the S&P 500 edging higher (up 1.4% relative to last Friday's close) and 10-year Treasury yield easing (down 9 basis points), at the time of writing.

The April [Consumer Price Index](#) was much anticipated after a string of disappointing readings. Markets hoped the report would snap the string of three consecutive months of hotter-than-expected inflation. Good news – it did (Chart 1). Relative to March, headline inflation in April decelerated on both an annual and monthly basis. The same was true for core inflation. While the reprieve from the string of upside surprises was welcomed, the out turn on its own is not enough to undo the elevated numbers in Q1. Further adding to the price picture, were higher-than-expected readings for producer prices in April, even as March's figures were revised lower. Given the mixed bag, the central bank is likely to remain on the sidelines awaiting more information before taking any policy action (see [here](#)).

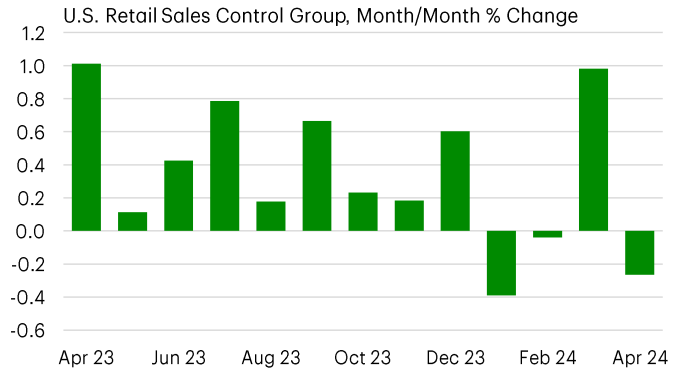
This was the position articulated by both Fed Chair Powell and Fed Governor Mester this week. Chair Powell reiterated that the central bank is likely to hold rates at their current level until more compelling data shows that inflation has resumed its downward trek. Governor Mester highlighted that she believes rates are high enough to slow economic activity and bring inflation down. As such, holding rates steady is appropriate.

Chart 1: Inflation Snaps Three Months of Upside Surprises in April



Note: Core CPI excludes food and energy prices.
Source: Bureau of Labor Statistics, TD Economics.

Chart 2: The Control Group Points to Slowing Retail Spending Momentum



Note: The "control group" excludes retail spending in the autos, building materials, gas stations and food services categories. Source: Census Bureau, TD Economics.

Data showing that consumers pumped the brakes on retail spending, seemed to support Mester's position. [Retail sales](#) were flat in April, with data for March revised lower. Of note, the "control group" which feeds into the calculation of personal consumption expenditure in GDP, outright declined in April, marking its third decline in four months (Chart 2). The out turn is pointing to slowing consumer momentum, which is a key ingredient to achieving the Fed's 2% inflation target.

The outlook among small businesses was a bit better in April with the [NFIB small business optimism index](#) increasing. Despite the marginal increase, the index remains well below its historical average. Business owners continued to be concerned about inflation and quality of labor issues. Additionally, concerns about sales are rising among small business owners, with fewer of them having raised or planning to raise prices.

Turning to the [housing market](#), signals were mixed. Housing starts rose, while building permits fell in April. The overall tally was boosted by multi-family starts, as single-family starts declined slightly. April's uptick did not completely undo the decline in March and suggests that builders remain wary as higher home prices and interest rates weigh on buyer demand.

The Fed had much to digest this week as they ponder their next policy move. While the break in inflation's heat streak is a welcome development, it's still too early to breathe a sigh of relief. As it stands, markets (and us) expect any rate cut to materialize closer to the end of the year.

Canada – April Showers Rain on Housing

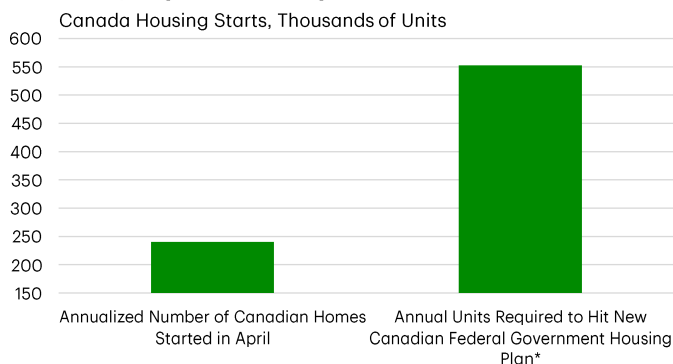
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Probably the most significant development for Canadian financial markets this week flowed from south of the border. Weaker-than-expected data sent U.S. bond yields lower, with Canadian yields following suit. Indeed, the benchmark Canadian 10-year yield was down around 10 bps on the week (at time of writing). Otherwise, housing was the name of the economic game this week, with April pulse-checks on new home construction and the state of Canada's resale market.

Housing starts dipped a tad last month, but the underlying trend remained healthy. There are a few things to note here. First, the trend in starts was about 15% above the pre-pandemic run-rate. Second, this trend has been supported by condo units and purpose-built rental housing. Current condo starts reflect gains in pre-sales several years ago when borrowing costs were lower, while purpose-built rental construction is being supported by steep increases in rents and government programs. Meanwhile, construction of other units, like detached housing, remains at low levels.

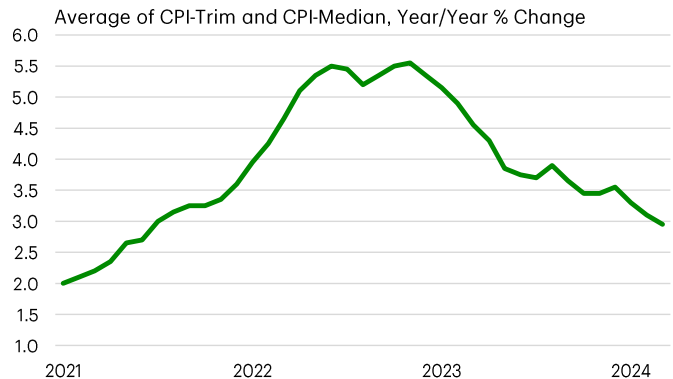
Third, even though the trend in starts is healthy, it's clearly on the decline. This is consistent with our view that starts will fall in 2024, as borrowing and construction costs remain high, and demand for new homes has been notably weak in markets like Toronto recently. Fourth, even this robust pace of homebuilding comes nowhere near levels required to hit the federal government's target under its [new housing plan](#), or to restore affordability to solid levels, per CMHC's analysis (Chart 1).

Chart 1: At Even at a Healthy Run-Rate, Homebuilding Massively Lags Federal Targets



Federal plan targets 3.87 million new homes by 2031
Source: CMHC, Federal Government, TD Economics.

Chart 2: Rate Cuts on the Horizon Amid Canada's Improved Inflation Backdrop



Source: Bank of Canada, TD Economics. Last Observation: March 2024.

As for the resale market, April was a subdued month. Home sales declined month-on-month while benchmark prices were flat. We were expecting a soft spring market to unfold given stretched affordability conditions and our view that buyers and sellers would wait for more clarity on rates from the Bank of Canada. However, home sales are on track to disappoint even our modest expectations in the second quarter. The upshot of this weaker performance is that pent-up demand continues to build, waiting to be unleashed in the second half of this year and 2025, when rates should be moving lower (see [report](#)).

This anticipated rise in home sales will push home prices higher, although strained affordability in key markets will limit the gain. Rising home prices would imply upward pressure on consumer inflation via the shelter component, although this will likely be more of a second half story. In the here and now, we eagerly await next week's CPI report for April. The consensus expects that the average of the Bank's preferred core inflation measures (CPI-trim and CPI-median) decelerated from March, continuing the improvements we've seen since the beginning of the year (Chart 2). Both we and the markets anticipate that July will be the start of the Bank of Canada's rate cutting campaign. After all, waiting until July will give the Bank an opportunity to see two more inflation and jobs reports, along with a Business Outlook Survey. However, a significant downside surprise in next week's report could revive expectations for a June move.

Exhibits

Recent Key Economic Indicators: May 13 - 17, 2024					
Release Date	Economic Indicator/Event	Data for Period	Units	Current	Prior
United States					
May 13	NY Fed 1-Yr Inflation Expectations	Apr	%	3.3	3.0
May 14	NFIB Small Business Optimism	Apr	Index	89.7	88.5
May 14	PPI Ex Food and Energy	Apr	M/M % Chg.	0.5	-0.1
May 14	PPI Final Demand	Apr	M/M % Chg.	0.5	-0.1
May 15	Consumer Price Index	Apr	M/M % Chg.	0.3	0.4
May 15	Consumer Price Index	Apr	Y/Y % Chg.	3.4	3.5
May 15	Consumer Price Index Ex Food and Energy	Apr	M/M % Chg.	0.3	0.4
May 15	Consumer Price Index Ex Food and Energy	Apr	Y/Y % Chg.	3.6	3.8
May 15	Empire Manufacturing	May	Index	-15.6	-14.3
May 15	Retail Sales Advance	Apr	M/M % Chg.	0.0	0.6
May 15	Retail Sales Ex Auto and Gas	Apr	M/M % Chg.	-0.1	0.7
May 15	Business Inventories	Mar	M/M % Chg.	-0.1	0.3
May 15	NAHB Housing Market Index	May	Index	45.0	51.0
May 16	Building Permits	Apr	Thsd	1440.0	1485.0
May 16	Housing Starts	Apr	Thsd	1360.0	1287.0
May 16	Initial Jobless Claims	May 11	Thsd	222.0	232.0
May 16	New York Fed Services Business Activity	May	Index	3.0	-0.6
May 16	Capacity Utilization	Apr	%	78.4	78.5
May 16	Industrial Production	Apr	M/M % Chg.	0.0	0.1
May 16	Manufacturing (SIC) Production	Apr	M/M % Chg.	-0.3	0.2
Canada					
May 14	Wholesale Sales ex Petroleum	Mar	M/M % Chg.	-1.1	0.2
May 15	Housing Starts	Apr	Thsd	240.2	242.3
May 15	Manufacturing Sales	Mar	M/M % Chg.	-2.1	0.9
May 15	Existing Home Sales	Apr	M/M % Chg.	-1.7	0.5
International					
May 14	UK ILO Unemployment Rate 3Mths	Mar	%	4.3	4.2
May 15	EZ Employment	Q1	Y/Y % Chg.	1.0	1.2
May 15	EZ Gross Domestic Product SA	Q1	Y/Y % Chg.	0.4	0.4
May 15	JN Gross Domestic Product Annualized SA	Q1	Q/Q % Chg.	-2.0	0.0
May 16	CH Retail Sales	Apr	Y/Y % Chg.	2.3	3.1
May 16	CH Surveyed Jobless Rate	Apr	%	5.0	5.2
May 17	EZ Consumer Price Index	Apr	Y/Y % Chg.	2.4	2.4

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

Upcoming Economic Releases and Events: May 20 - 24, 2024						
Release Date	Time*	Economic Indicator/Event	Data for Period	Units	Consensus Forecast	Last Period
United States						
May 20	10:30	<i>Fed's Jefferson Speaks on Economic Outlook, Housing</i>				
May 21	9:00	<i>Fed's Waller Discusses US Economy</i>				
May 22	10:00	Existing Home Sales	Apr	Mlns	4.2	4.2
May 22	14:00	<i>FOMC Meeting Minutes</i>	May 01			
May 23	8:30	Initial Jobless Claims	May 18	Thsd	-	222.0
May 23	9:45	S&P Global US Manufacturing PMI	May	Index	50.2	50.0
May 23	9:45	S&P Global US Services PMI	May	Index	51.6	51.3
May 23	9:45	S&P Global US Composite PMI	May	Index	-	51.3
May 23	10:00	New Home Sales	Apr	Thsd	680.0	693.0
May 24	8:30	Durable Goods Orders	Apr	M/M % Chg.	-0.7	0.9
May 24	8:30	Cap Goods Orders Nondef Ex Air	Apr	M/M % Chg.	0.1	-0.2
May 24	9:35	<i>Fed's Waller Gives Keynote Address on R*</i>				
Canada						
May 21	8:30	Consumer Price Index NSA	Apr	M/M % Chg.	0.5	0.6
May 21	8:30	Consumer Price Index	Apr	Y/Y % Chg.	2.7	2.9
May 24	8:30	Retail Sales	Mar	M/M % Chg.	-0.1	-0.1
May 24	8:30	Retail Sales Ex Auto	Mar	M/M % Chg.	-	-0.3
International						
May 22	2:00	Consumer Price Index	Apr	Y/Y % Chg.	2.1	3.2
May 22	20:30	Jibun Bank Japan PMI Mfg	May	Index	-	49.6
May 23	19:30	Natl Consumer Price Index	Apr	Y/Y % Chg.	2.4	2.7
May 24	2:00	Retail Sales Ex Auto Fuel	Apr	Y/Y % Chg.	-0.8	0.4

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

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