WEEKLY COMMENTARY

The Case for a Soft-ish Recession (If There Is One)

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

The economic world remains obsessed with recession risk. The Chinese slowdown, the erosion of consumer purchasing power in most developed countries and expeditious monetary tightening are the main culprits. But a recession wouldn't necessarily be fatal. While much of the chatter has been around whether a recession can be avoided, little has been said about how a potential recession would be managed. And this is where drawing parallels with previous episodes has its limits. How policymakers handled recessions 30 or 40 years ago offers little valuable insight into how they'll handle the next one. Policy approaches and toolkits have evolved, thanks in part to lessons learned from prior downturns.

The pandemic recession was a testing ground for a number of policies that are likely to be reintroduced in the next recession. Wage subsidies are one example. They helped employers hold on to staff despite severely curtailed revenues. At their peak, these subsidies supported the wages of over 5 million workers across Canada and allowed job markets to recover quickly when lockdowns were lifted. The key lesson is that the best way to foster a robust labour market recovery is to keep people from losing their jobs in the first place.

Demographics can also limit job losses. The baby boomers entered the work force in the 1970s and 1980s and now they're leaving to retire. Today's acute, widespread labour shortages pre-date the pandemic and are likely to be with us for at least a decade, having a lasting impact on employer psychology. Our business members and clients are always telling us how difficult and expensive it is to attract and retain workers and how that limits their expansion plans. If we do see a growth recession, many employers will likely do all they can to retain their staff as opposed to laying them off and scrambling to re-hire them when the skies eventually clear. Temporary wage subsidy programs will help them do just that, and the pandemic is the proof of concept.

And for those who do lose their jobs, the government has enhanced the employment insurance system during the pandemic. This, along with various income support measures, was key to preventing financial hardship. The decline in bankruptcies and delinquencies during the pandemic shows that these programs had the intended results.

Bottom line: because of policy innovations introduced during the pandemic, job loss may no longer be synonymous with income loss. The severity of a recession depends on what happens to incomes. That said, there's one big wildcard: the Bank of Canada. The debt incurred to fund these policy innovations would have been more expensive to service if it weren't for the BoC's heavy involvement in bond markets. But given the Bank's current focus on taming inflation, it may respond more conservatively to the next recession. This would largely leave it to private investors to decide how much it will cost to borrow the money to fund these programs. Chances are borrowing costs will be higher than they were during the pandemic, forcing the government to pick and choose its policies more carefully. But the strength of the labour market recovery suggests that job retention programs would make the cut.

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Week in Review

By Randall Bartlett, Senior Director of Canadian Economics, Tiago Figueiredo, Associate – Macro Strategy, Francis Généreux, Senior Economist, and Lorenzo Tessier-Moreau, Senior Economist

- **North American stock markets rebounded strongly** only a week after the S&P 500 flirted with a bear market, defined as a drop of 20% or more from the most recent high. Markets didn't even flinch after the Federal Reserve's (Fed) last meeting minutes were released on Wednesday. Even if Fed officials feel that rates could go higher than currently forecasted, investors seem increasingly confident that inflation will be brought to heel in the coming months. Case in point: bond yields continued to move lower this week.

- **Canadian retail sales were largely unchanged in March**, coming in well below our tracking, the consensus forecast and Statistics Canada's flash estimate. Sales were up in 10 of 11 subsectors, equivalent to three quarters of retail trade, with gas stations topping the leaderboard with an advance of 7.4% m/m in March. However, a sharp 6.4% drop in sales at motor vehicle and parts dealers wiped out the gains in other subsectors. Core retail sales, which exclude gasoline stations and motor vehicle and parts dealers, still advanced by a respectable 1.5% in the month. Importantly, the March print was entirely propped up by steep price increases as volumes were down 1.0%. Looking ahead, Statistics Canada's flash estimate puts retail sales growth at 0.8% in April.

- **In the United States, sales of new single-family homes dropped for the fourth month in a row**, plunging 16.6% in April and 29.6% since December. The new home market is clearly softening. Given that new home sales are recorded before building even starts, recent construction delays can't be blamed for this market weakness. It's more likely due to high prices and the sharp rise in mortgage rates.

- **Real consumption picked up slightly in April in the United States**, with a monthly advance of 0.7% after a 0.5% uptick in March. This is the biggest gain since January. Personal disposable income stagnated in April and hasn't increased significantly since July of last year. The savings rate fell from 5.0% in March to 4.4% in April, the lowest since August 2008. The personal consumption expenditures deflator slowed with a monthly increase of 0.2% after jumping 0.9% in March. The year-over-year change fell from 6.6% to 6.3%.

- **New durable goods orders were up 0.4% in April in the United States.** As expected, civil aircraft orders increased (+4.3%), but the automotive sector slipped back 0.2%. Excluding transportation, new orders rose 0.3%, down from a 1.1% gain in March. These figures point to fairly modest growth in business investment early in the second quarter.

- **The US goods trade balance improved in April.** According to preliminary figures, it fell from a record low of -US$125.9B in March to -US$105B in April. Nominal exports of goods increased 3.1% while imports fell 5.0%, likely due to lockdowns in China. Net exports should be a much smaller drag on real GDP growth in the second quarter than they were in the first.

What to Watch For

By Randall Bartlett, Senior Director of Canadian Economics,
Tiago Figueiredo, Associate – Macro Strategy, and Francis Généreux, Senior Economist

UNITED STATES

TUESDAY May 31 - 9:00	
March	**y/y**
Consensus	19.60%
Desjardins	20.20%
February	**20.20%**

S&P/Case-Shiller index of existing home prices (March) – In February, the Case-Shiller index accelerated sharply, posting a record 2.4% monthly gain. This increase bumped up the index's annual variation to a new cyclical high of 20.2%. We expect it to rise further in March, although probably not quite as much as in February. We're forecasting monthly growth of 1.7%, which would keep the annual figure at 20.2%.

TUESDAY May 31 - 10:00	
May	
Consensus	103.5
Desjardins	103.7
April	**107.3**

Conference Board consumer confidence index (May) – The Conference Board index slipped 0.3 points in April after rising 1.9 points in March. However, we're forecasting a more substantial decline in May. The recent spike in gas prices, stock market turbulence and inflation uncertainty have all likely dragged down consumer sentiment. Other indexes including the University of Michigan Consumer Sentiment index and the TIPP Economic Optimism index were also down again in May. We expect the Conference Board index to fall from 107.3 to 103.7.

WEDNESDAY June 1 - 10:00	
May	
Consensus	54.8
Desjardins	51.5
April	**55.4**

ISM manufacturing index (May) – The ISM manufacturing index dropped to 55.4 in April, its lowest level since September 2020 and 8.3 points off its 2021 cyclical peak. However, it's still well above the 50 mark, indicating that the manufacturing sector is still expanding rather than contracting. The regional indicators released to date are pointing toward a further decline in May, which would bring the index closer to 50.

WEDNESDAY June 1	
May	**ann. rate**
Consensus	14,500,000
Desjardins	13,600,000
April	**14,290,000**

New car sales (May) – New car sales have been up and down so far this year, and this trend is expected to continue in May. We're projecting a nearly 5% contraction this month following April's 6.6% rise.

FRIDAY June 3 - 8:30	
May	
Consensus	325,000
Desjardins	300,000
April	**428,000**

Job creation according to the establishment survey (May) – Hiring slowed compared to previous months, with 428,000 new jobs added in both March and April. However, the US labour market remains robust. The jobs recovery is entering its final stretch, with the market just 1,190,000 jobs shy of its previous cyclical peak in February 2020. We're anticipating another solid—albeit slightly smaller—increase in employment in May. New jobless claims remained relatively low, though they were up from March and April's rock bottom levels. We're forecasting 300,000 net hires in May, keeping the jobless rate at 3.6%.

FRIDAY June 3 - 10:00	
May	
Consensus	56.4
Desjardins	56.4
April	**57.1**

ISM services index (May) – The ISM services index has dropped four times in the last five months and is down 11.3 points from its November 2021 cyclical peak of 68.4. We believe the index will decline further in May. Most regional non-manufacturing indicators fell during the month, as did consumer confidence. The ISM services index is expected to dip less than the manufacturing index, to 56.4.

CANADA

MONDAY May 30 - 8:30	
Q1 2022	**$B**
Consensus	3.23
Desjardins	1.10
Q4 2021	**-0.80**

Current account balance (Q1) – Canada's current account balance is expected to have moved into positive territory again in Q1 due to a sharp increase in Canada's trade balance. Export prices will deserve the lion's share of the credit, more than offsetting the drop in export volumes in the quarter and outpacing by a wide margin the still healthy increase in import prices. Look for net investment income to also provide a positive contribution to the current account balance as it has since late 2019. We believe Canada's current account balance likely reached about $1.1 billion in the first quarter, the highest level since 2007.

TUESDAY May 31 - 8:30	
March	**m/m**
Consensus	0.5%
Desjardins	0.3%
February	**1.1%**

Real GDP by industry (March) – After a big February rebound following the latest COVID lockdowns, real GDP is expected to have advanced by a more modest 0.3% m/m in March. Underpinning this uptick will likely be still respectable growth in goods-producing sectors, with all of them moving ahead in the month with the exception of construction, which posted monthly gains in excess of 2% in each of the prior two months. Looking to services-producing sectors, client-facing sectors like arts and culture and accommodation and food services are expected to continue to report solid numbers as Canadians prioritize socializing over shopping. However, this will weigh on both retail and wholesale trade. As a result, we think services will advance by a modest 0.2% in March after a strong 0.9% showing in February.

TUESDAY May 31 - 8:30	
Q1 2022	**ann. rate**
Consensus	5.2%
Desjardins	5.2%
Q4 2021	**6.7%**

Real GDP by expenditure (Q1) – Canada is expected to have started the year with another solid advance in real GDP, with growth likely to come in around 5.2% (q/q, saar) after a 6.7% print in the final quarter of 2021. We anticipate consumption to be a major contributor to this strong Q1 figure, with services outperforming earlier expectations despite the chill brought on by Omicron in January. We think goods consumption will also post robust growth in the quarter. Not surprisingly, we foresee residential investment moving higher in the first quarter as households rushed to take advantage of low interest rates while they could. Investment in non-residential structures also looks to have had a healthy quarter. But net exports are likely to be a drag on real GDP growth in Q1, as real goods exports posted a disappointing performance while export prices—particularly for energy—shot up on higher commodity prices. And with trade numbers in the dumps, inventory accumulation is expected to continue in the first quarter, albeit contributing roughly half as much to growth as it did in Q4 2021. Our forecast for Q1 real GDP growth exceeds the 3% projection published by the Bank of Canada in its April 2022 Monetary Policy Report.

WEDNESDAY June 1 - 8:30	
June	
Consensus	1.50%
Desjardins	1.50%
April 13	**1.00%**

Bank of Canada policy announcement (June) – The Bank of Canada will likely eschew anything larger than a 50bp hike, deeming it a bridge too far. And while it's easy to argue with that logic when inflation is tracking 7%, central bankers have made their feelings known. As a result, a 50bp rate increase looks like a done deal. Expect yet another 50bp move in July before policymakers shift to a more cautious approach to monetary tightening later this year.

FRIDAY June 3 - 8:30	
Q1 2022	**q/q**
Consensus	n/a
Desjardins	0.2%
Q4 2021	**-0.5%**

Labour productivity (Q1) – After a sixth-straight quarterly contraction in Q4 2021, Canadian labour productivity is expected to have grown in the first quarter of 2022. Real GDP growth is projected to have outpaced the increase in hours worked. In part this reflects the employment situation in the client-facing sectors impacted by Omicron lockdowns early in the quarter. These sectors tend to have more part-time employees working fewer hours, and these sectors typically have relatively low productivity. Additionally, the Canadian economy largely shook off Omicron's impact on overall economic activity in Q1. As such, look for real GDP growth to have continued apace while growth in hours slowed but remained positive, boosting labour productivity.

FRIDAY June 3 - 8:30	
Q1 2022	**q/q**
Consensus	n/a
Desjardins	1.0%
Q4 2021	**-0.1%**

Unit labour costs (Q1) – Hourly compensation likely rose sharply in Q1 due to an unprecedented tight labour market and the effects of COVID lockdowns on targeted segments of the job market. As a result, we expect the increase in compensation per hour worked to have outpaced growth in labour productivity, pushing unit labour cost growth back into positive territory in the first quarter. Look for unit labour costs to have advanced by around 1.1% (q/q) in the first three months of 2022. This follows a mild contraction in Q4 2021 which was preceded by four consecutive quarterly advances.

OVERSEAS

MONDAY May 30 - 21:30	
May	
Consensus	49.0
April	**47.4**

China: PMI manufacturing index (May) – Lockdowns in major cities have pushed Chinese PMI indexes lower over the last two months, reflecting difficulties with industrial production and retail sales that were particularly acute in April. It'll be interesting to see whether PMI indexes begin to normalize in May or deteriorate further.

TUESDAY May 31 - 5:00	
May	**m/m**
Consensus	0.6%
April	**0.6%**

Eurozone: Consumer price index (May – preliminary) – After accelerating for ten consecutive months, eurozone inflation stabilized at a still extremely high 7.4% in April. Several factors were behind the jump in the Harmonized Index of Consumer Prices, but rising energy prices are still the main culprit. Further increases in energy prices in May could drive inflation back up.

Economic Indicators

Week of May 30 to June 3, 2022

Date	Time	Indicator	Period	Consensus		Previous data
UNITED STATES						
MONDAY 30	---	Markets closed (Memorial Day)				
	11:00	Speech of a Federal Reserve Governor, C. Waller				
TUESDAY 31	9:00	S&P/Case-Shiller home price index (y/y)	March	19.60%	20.20%	20.20%
	9:45	Chicago PMI index	May	54.8	56.0	56.4
	10:00	Consumer confidence	May	103.5	103.7	107.3
WEDNESDAY 1	---	Total vehicle sales (ann. rate)	May	14,500,000	13,600,000	14,290,000
	10:00	Construction spending (m/m)	April	0.6%	0.4%	0.1%
	10:00	ISM manufacturing index	May	54.8	51.5	55.4
	11:30	Speech of the Federal Reserve Bank of New York President, J. Williams				
	13:00	Speech of the Federal Reserve Bank of St. Louis President, J. Bullard				
	14:00	Release of the *Beige Book*				
THURSDAY 2	8:30	Initial unemployment claims	May 23-27	210,000	210,000	210,000
	8:30	Nonfarm productivity – final (ann. rate)	Q1	-7.5%	-7.5%	-7.5%
	8:30	Unit labor costs – final (ann. rate)	Q1	11.6%	11.6%	11.6%
	10:00	Factory orders (m/m)	April	0.7%	0.9%	2.2%
	13:00	Speech of the Federal Reserve Bank of Cleveland President, L. Mester				
FRIDAY 3	8:30	Change in nonfarm payrolls	May	325,000	300,000	428,000
	8:30	Unemployment rate	May	3.5%	3.6%	3.6%
	8:30	Weekly worked hours	May	34.6	34.6	34.6
	8:30	Average hourly earnings (m/m)	May	0.4%	0.3%	0.3%
	10:00	ISM services index	May	56.4	56.4	57.1
	13:00	Speech of the Federal Reserve Bank of St. Louis President, J. Bullard				
CANADA						
MONDAY 30	8:30	Current account balance ($B)	Q1	3.23	1.10	-0.80
TUESDAY 31	8:30	Real GDP by industry (m/m)	March	0.5%	0.3%	1.1%
	8:30	Real GDP (ann. rate)	Q1	5.2%	5.2%	6.7%
WEDNESDAY 1	10:00	Bank of Canada meeting	June	1.50%	1.50%	1.00%
THURSDAY 2	8:30	Building permits (m/m)	April	0.5%	0.8%	-9.3%
FRIDAY 3	8:30	Labour productivity (q/q)	Q1	n/a	0.2%	-0.5%
	8:30	Unit labour costs (q/q)	Q1	n/a	1.0%	-0.1%

NOTE: Desjardins, Economic Studies are involved every week 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 monthly, quarterly and yearly variation respectively. Following the quarter, the abbreviations f, s and t correspond to first estimate, second estimate and third estimate respectively. The times shown are Eastern Standard Time (GMT - 4 hours). Forecast of Desjardins, Economic Studies of the Desjardins Group.

Economic Indicators

Week of May 30 to June 3, 2022

Country	Time	Indicator	Period	Consensus m/m (q/q)	Consensus y/y	Previous data m/m (q/q)	Previous data y/y
OVERSEAS							
MONDAY 30							
Euro zone	5:00	Consumer confidence – final	May	n/a		-21.1	
Euro zone	5:00	Industrial confidence	May	7.5		7.9	
Euro zone	5:00	Services confidence	May	13.7		13.5	
Euro zone	5:00	Economic confidence	May	104.9		105.0	
Germany	8:00	Consumer price index	May	0.5%	7.6%	0.8%	7.4%
Japan	19:30	Unemployment rate	April	2.6%		2.6%	
Japan	19:50	Industrial production – preliminary	April	-0.1%	-3.4%	0.3%	-1.7%
Japan	19:50	Retail sales	April	0.9%	2.6%	2.0%	0.9%
China	21:30	PMI manufacturing index	May	49.0		47.4	
China	21:30	PMI non-manufacturing index	May	45.0		41.9	
TUESDAY 31							
Japan	1:00	Consumer confidence	May	33.8		33.0	
Japan	1:00	Housing starts	April		2.4%		6.0%
France	2:45	Personal consumption expenditures	April	0.6%	7.6%	-1.3%	-2.4%
France	2:45	Consumer price index – preliminary	May	0.6%	5.2%	0.4%	4.8%
France	2:45	Real GDP – final	Q1	0.0%	5.3%	0.0%	5.3%
Euro zone	5:00	Consumer price index – preliminary	May	0.6%	7.7%	0.6%	7.5%
Italy	5:00	Consumer price index – preliminary	May	0.4%	6.3%	0.2%	6.2%
Japan	20:30	PMI manufacturing index – final	May	n/a		53.2	
WEDNESDAY 1							
United Kingdom	2:00	Nationwide house prices	May	0.6%	10.5%	0.3%	12.1%
Germany	2:00	Retail sales	April	-0.5%	4.0%	-0.1%	-5.4%
France	3:50	PMI manufacturing index – final	May	54.5		54.5	
Germany	3:55	PMI manufacturing index – final	May	54.7		54.7	
Euro zone	4:00	PMI manufacturing index – final	May	54.4		54.4	
United Kingdom	4:30	PMI manufacturing index – final	May	54.6		54.6	
Euro zone	5:00	Unemployment rate	April	6.8%		6.8%	
THURSDAY 2							
Japan	20:30	PMI composite index – final	May	n/a		51.4	
Japan	20:30	PMI services index – final	May	n/a		51.7	
FRIDAY 3							
France	2:45	Industrial production	April	0.2%	0.0%	-0.5%	0.1%
France	3:50	PMI composite index – final	May	57.1		57.1	
France	3:50	PMI services index – final	May	58.4		58.4	
Germany	3:55	PMI composite index – final	May	54.6		54.6	
Germany	3:55	PMI services index – final	May	56.3		56.3	
Euro zone	4:00	PMI composite index – final	May	54.9		54.9	
Euro zone	4:00	PMI services index – final	May	56.3		56.3	
Euro zone	5:00	Retail sales	April	0.2%	5.4%	-0.4%	0.8%

Note: In contrast to the situation in Canada and the United States, disclosure of overseas economic fi gures is much more approximate. The day of publication is therefore shown for information purposes only. The abbreviations m/m, q/q and y/y correspond to monthly, quarterly and yearly variation respectively. The times shown are Eastern Standard Time (GMT - 4 hours).