

WEEKLY COMMENTARY



Is This the Year Inflation Comes Down?

By Francis Généreux, Principal Economist

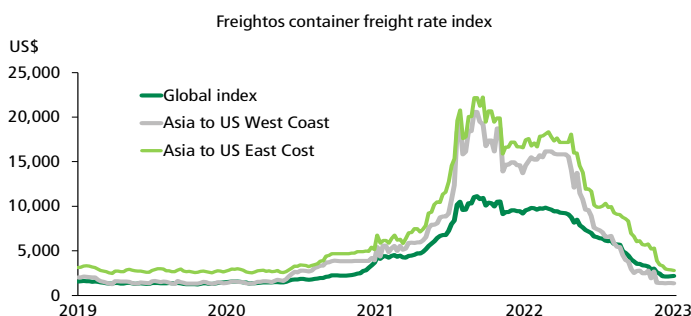
Inflation was rampant just about everywhere in 2022. Price gains picked up steam in 2021, but the rising cost of living didn't really start to bite until last year. Inflation was higher than it's been since the early 1980s and was a common theme of year-end retrospectives.

Fortunately, there are increasing signs that inflation has turned the corner.

Look no further than oil and gasoline prices, which have fallen sharply since mid-2022. Oil is down 40% globally, and prices at the pump are down 35% in the US.

In 2021 and 2022, businesses were contending with soaring container shipping rates, especially from Asia. The cost to ship a container across the Pacific from China to the US surged fifteenfold between late 2019 and September 2021. These price hikes hit importers hard and helped drive up goods prices over the last two years. Fortunately, shipping costs are almost back to normal. They're down 93.3%, below their 2019 average (graph 1).

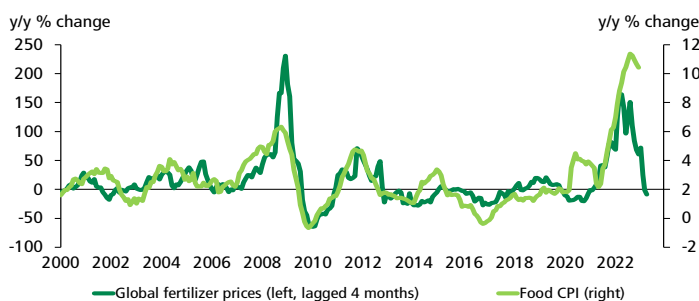
GRAPH 1
International freight costs are back to normal



Sources: Datastream and Desjardins Economic Studies

Meanwhile food prices generally remain high, with recent increases eating into household incomes. We expect an improvement on this front as well, however. Fertilizer prices have come down after spiking at the outset of the war in Ukraine. This should help annual food inflation to moderate in 2023 (graph 2).

GRAPH 2
Food inflation is also expected to slow sharply



Sources: Variant Perception, World Bank, Bureau of Labor Statistics and Desjardins Economic Studies

In fact, many of the global supply chain issues we saw over the course of the pandemic have now cleared up. They were a key driver of inflation, so recent improvements should mean slower consumer price growth around the globe (graph 3 on page 2).

So is inflation over? Given the events of the last year, it's hard to say. The inflation outlook has been revised upward repeatedly since early 2021, particularly when war broke out in Ukraine. And we have to be careful not to confuse disinflation with deflation. We now expect consumer price growth to slow (disinflation). By year's end, it could be back near central banks' 2% annual targets.

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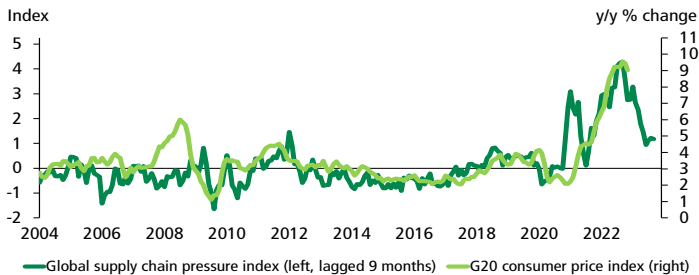
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Desjardins, Economic Studies: 514-281-2336 or 1 866-866-7000, ext. 5552336 • desjardins.economics@desjardins.com • desjardins.com/economics

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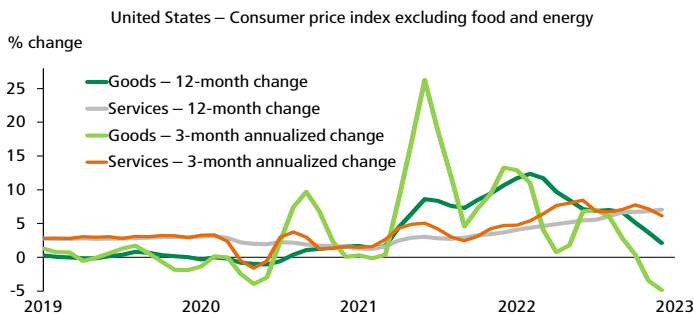
GRAPH 3
Improved supply chains are good news for global inflation



Sources: Federal Reserve Bank of New York, Organisation for Economic Co-operation and Development and Desjardins Economic Studies

But that doesn't mean we'll see lower prices (deflation). It's hard to imagine prices returning to anywhere near 2020 levels. We also don't expect the cost of living to come down much, though some commodity prices are already lower than they were. So too are a growing number of consumer goods prices. That's especially true in the US, where recent data suggests prices for goods excluding food and energy fell last quarter (graph 4).

GRAPH 4
Goods prices are down, but price growth remains strong on the services side



Sources: Bureau of Labor Statistics and Desjardins Economic Studies

However, it's a much different story on the services side, where we're seeing continued price pressure. And when it comes to shelter costs, that pressure is mounting. That said, some US rent indicators are starting to show signs of softening this year.

But the cost picture is much different for service businesses than it is for goods businesses. The component of the ISM Services PMI that measures prices paid by businesses came in at 67.6 in December. A reading above 50 indicates upward price pressure, while a reading below it suggests downward pressure. For the ISM Manufacturing PMI, the price component fell to 39.4, its lowest reading since February 2016 if you exclude the first wave of the pandemic.

This is where tighter monetary policy can help bring inflation closer to central bank targets. Yes, the global factors that drove up goods prices are now easing. In order to see price relief on the services side, however, we'll need both lower demand and a weaker labour market, which means slower wage gains. So until central banks can see the finish line, they may continue to raise interest rates. But they no longer need to hike rates as aggressively as they did in 2022, as the impact of those increases will continue to be felt this year.

What to Watch For

By Randall Bartlett, Senior Director of Canadian Economics, Tiago Figueiredo, Associate – Macro Strategy, Marc Desormeaux, Principal Economist, and Francis G  n  reux, Principal Economist

WEDNESDAY, January 18 - 8:30

December	m/m
Consensus	-0.8%
Desjardins	-0.5%
November	-0.6%

WEDNESDAY, January 18 - 9:15

December	m/m
Consensus	-0.1%
Desjardins	-0.3%
November	-0.2%

THURSDAY, January 19 - 8:30

December	
Consensus	1,358,000
Desjardins	1,360,000
November	1,427,000

FRIDAY, January 20 - 10:00

December	
Consensus	3,950,000
Desjardins	3,975,000
November	4,090,000

MONDAY, January 16 - 8:30

November	m/m
Consensus	0.5%
Desjardins	0.9%
October	2.8%

UNITED STATES

Retail sales (December) – After a surprise 1.3% increase in October, retail sales dropped 0.6% in November, providing an early warning sign about the strength of holiday sales. So far, December’s indicators are rather mixed. The number of new motor vehicles sold in the past month decreased. Gasoline prices also dropped significantly, which is likely to have a significant impact on the value of gasoline station receipts. Excluding motor vehicles and gasoline, preliminary card transaction data is quite positive and even suggests significant rebounds in categories that had struggled in November. All in all, we expect total retail sales to fall 0.5%, while sales excluding motor vehicles and gasoline are projected to rise 0.3%. However, the severe winter storm that affected much of the United States over Christmas could have seriously impacted figures for the last week of the month.

Industrial production (December) – Monthly US industrial production has only increased twice since May 2022. We expect another weak print in December. Hours worked in the manufacturing sector are down sharply, which makes sense given that the ISM Manufacturing PMI is now below 50. We’re forecasting a 0.7% decline in overall manufacturing output. However, the rest of industrial production—energy production and mining—should rise, leading us to forecast a decrease of 0.3% for total industrial production in December. Here again, we’ll have to keep a close eye on the effects of the storm that hit the United States at the end of the month.

Housing starts (December) – Housing starts fell for the third consecutive month in November and are down 20.9% from April’s peak. Based on November’s 10.6% decline in building permits, we expect this downward trend to have continued in December. That said, new home sales have been stabilizing for a few months now. Employment in residential building construction also increased in December. However, the severe storm that occurred after the labour market survey was completed could have impacted these figures. We think December’s housing starts print will come in at 1,360,000 units.

Existing home sales (December) – Monthly existing home sales have only risen once so far in 2022, and that was in January. Sales have dropped 37.0% since then, impacting single-family homes and multi-unit properties alike. Based on the 4.0% contraction in pending home sales, we expect existing home sales to have fallen further in December. Although mortgage interest rates have eased back from their recent peak, they’re still high enough to cause further pain on the real estate market. However, mortgage applications for home purchases rose in December. That said, we think that sales of existing homes will still drop below 4,000,000 units.

CANADA

Manufacturing sales (November) – Manufacturing shipments are expected to have increased by 0.9% in November, likely outpacing Statistics Canada’s flash estimate of 0.6%. But the nominal gain projected for the month may mask divergent trends under the surface. On the upside, manufacturing volumes are likely to have increased on the back of a rebound in auto production, imports of manufacturing inputs and a bounce in manufacturing employment. In contrast, manufacturing prices likely turned south on falling prices of traded goods and a drop in energy prices. While good news for the Canadian economy, it isn’t expected to last. The December flash estimate for manufacturing shipments is expected to come in negative on lower volumes and broadly flat prices.

MONDAY, January 16 - 9:00

December	m/m
Consensus	n/a
Desjardins	-1.0%
November	-3.3%

Existing home sales (December) – Existing home sales probably moved lower again in December, likely falling 1.0% on mixed activity across major urban centres. Starting with Ontario, sales were broadly flat in Toronto in the month, following three consecutive monthly declines. Judging by year-over-year sales growth, other large markets like Ottawa and Durham seemed to outperform the Big Smoke, while Mississauga and Windsor lagged behind. All in all, sales in Canada's most populous province may have posted a slight gain in December. The same is true for housing-centric British Columbia. However, Quebec, the Prairie provinces and Atlantic Canada are projected to have weighed on home sales nationally in December, more than offsetting the rebound elsewhere.

TUESDAY, January 17 - 8:15

December	
Consensus	257,500
Desjardins	264,000
November	264,200

Housing starts (December) – Housing starts were likely flat in December, as the ongoing decline in existing home sales came up against the surge in building permits in November. Construction employment also increased in December, providing additional support to residential construction.

TUESDAY, January 17 - 8:30

December	m/m
Consensus	-0.6%
Desjardins	-0.5%
November	0.1%

Consumer Price Index (December) – After posting a surprising increase in November, consumer prices likely declined in December, finally giving Canadians a much-needed break from inflation. Look for total prices to have fallen 0.5% due mainly to sharply lower energy prices. That said, shoppers would have still had to contend with rising prices elsewhere, most notably in food prices at grocery stores. Excluding food and energy, we expect holiday discounting was in line with pre-pandemic seasonal trends. As a result, we see core prices having grown a seasonally adjusted 0.3% in December, with a boost from rising shelter costs. That would have the three-month annualized rate of that stripped down measure falling to 3.7%, the slowest pace since January 2022. Much focus will be on the three-month annualized rates of the Bank of Canada's preferred core measures, which we will calculate and report immediately after the data is released. Despite the likely progress being made on controlling inflation, we still see the Bank of Canada nudging rates up another 25bps later this month before hitting the pause button.

WEDNESDAY, January 18 - 8:30

December	m/m
Consensus	n/a
Desjardins	-0.1%
November	-0.4%

Industrial Product Price Index (December) – The Industrial Product Price Index is projected to have taken a step back in December, likely falling 0.1% on the back of substantially lower commodity prices largely offset by a depreciation in the Canadian dollar in the month.

WEDNESDAY, January 18 - 8:30

December	m/m
Consensus	n/a
Desjardins	-3.2%
November	-0.8%

Raw Materials Price Index (December) – The Raw Materials Price Index is expected to have moved sharply lower in December. We estimate a decline of 3.2% in the month as a result of a drop in commodity prices swamping the modest offset coming from the weaker Canadian dollar.

THURSDAY, January 19 - 8:30

November	m/m
Consensus	n/a
Desjardins	1.4%
October	2.1%

Wholesale trade (November) – After posting an outsized gain in October, wholesale trade is likely to have advanced by 1.4% in November due to both higher prices and sales volumes. Notably, this is below the early indicator published by Statistics Canada just before the holiday, which estimated an advance of 1.9% based on just over half of survey respondents. Looking ahead, the early indicator for December could come in broadly flat, as a slowing pace of goods price growth combines with headwinds to spending in the form of higher prices and interest rates.

FRIDAY, January 20 - 8:30

November	m/m
Consensus	n/a
Desjardins	0.0%
October	1.4%

Retail sales (November) – Retail sales are expected to have been unchanged in November. We anticipate strength in auto sales offset weakness in other categories. This projected print for headline sales would be marginally stronger than the -0.5% flash estimate published by Statistics Canada. Retail sales excluding autos should show a decline in November, with holiday spending seemingly getting off to a slow start. Looking ahead to December, seasonally-adjusted goods prices south of the border fell sharply in the month, driven by declines in energy and used motor vehicle prices. A possible similar decline in Canada could lead to a negative sign on Statistics Canada's flash estimate for December retail sales growth even before considering sales volumes.

MONDAY, January 16 - 21:00

Q4 2022

Consensus

Q3 2022**y/y**


1.6%


3.9%**OVERSEAS**

China: Real GDP (fourth quarter) – Driven by the reopening of its economy following last spring's strict lockdowns, China's real GDP rebounded strongly in the third quarter of 2022, rising 3.9% year-over-year. However, the situation has since deteriorated again. Although the Chinese authorities have backed away from their zero-COVID policy, the economic benefits of more flexible public health measures are likely to be offset by the rapid spread of the virus. As such, we expect real GDP to decline in the fourth quarter.

Economic Indicators

Week of January 16 to 20, 2023

Day	Hour	Indicator	Period	Consensus		Previous data
UNITED STATES						
MONDAY 16	---	Markets closed (Martin Luther King, Jr. Day)				
TUESDAY 17	8:30	Empire manufacturing index	Jan.	-8.3	-11.0	-11.2
WEDNESDAY 18	8:30	Retail sales				
		Total (m/m)	Dec.	-0.8%	-0.5%	-0.6%
		Excluding automobiles (m/m)	Dec.	-0.5%	-0.2%	-0.2%
	8:30	Producer price index				
		Total (m/m)	Dec.	-0.1%	-0.3%	0.3%
		Excluding food and energy (m/m)	Dec.	0.1%	0.0%	0.4%
	9:15	Industrial production (m/m)	Dec.	-0.1%	-0.3%	-0.2%
	9:15	Production capacity utilization rates	Dec.	79.6%	79.4%	79.7%
	10:00	Business inventories (m/m)	Nov.	0.4%	0.4%	0.3%
	10:00	NAHB housing market index	Jan.	31	n/a	31
	14:00	Release of the Beige Book				
	17:00	Speech of Federal Reserve Bank of Dallas President L. Logan				
THURSDAY 19	8:30	Initial unemployment claims	Jan. 9-13	212,000	212,000	205,000
	8:30	Housing starts (ann. rate)	Dec.	1,358,000	1,360,000	1,427,000
	8:30	Building permits (ann. rate)	Dec.	1,370,000	1,360,000	1,351,000
	8:30	Philadelphia Fed index	Jan.	-11.0	-11.0	-13.8
	9:00	Speech of Federal Reserve Bank of Boston President S. Collins				
FRIDAY 20	10:00	Existing home sales (ann. rate)	Dec.	3,950,000	3,975,000	4,090,000
CANADA						
MONDAY 16	8:30	Manufacturing sales (m/m)	Nov.	0.5%	0.9%	2.8%
	8:30	Existing home sales (m/m)	Dec.	n/a	-1.0%	-3.3%
	10:30	Release of the Bank of Canada Business Outlook Survey				
TUESDAY 17	8:15	Housing starts (ann. rate)	Dec.	257,000	264,000	264,200
	8:30	Consumer price index				
		Total (m/m)	Dec.	-0.6%	-0.5%	0.1%
		Total (y/y)	Dec.	6.3%	6.4%	6.8%
	8:30	International transactions in securities (\$B)	Nov.	n/a	n/a	8.46
WEDNESDAY 18	8:30	Industrial product price index (m/m)	Dec.	n/a	-0.1%	-0.4%
	8:30	Raw materials price index (m/m)	Dec.	n/a	-3.2%	-0.8%
THURSDAY 19	8:30	Wholesale sales (m/m)	Nov.	n/a	1.4%	2.1%
FRIDAY 20	8:30	Retail sales				
		Total (m/m)	Nov.	n/a	0.0%	1.4%
		Excluding automobiles (m/m)	Nov.	n/a	-0.7%	1.7%

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 - 5 hours).  Forecast of Desjardins, Economic Studies of the Desjardins Group.

Economic Indicators

Week of January 16 to 20, 2023

Country	Hour	Indicator	Period	Consensus		Previous data	
				m/m (q/q)	y/y	m/m (q/q)	y/y
OVERSEAS							
MONDAY 16							
China	21:00	Real GDP	Q4	-1.2%	1.6%	3.9%	3.9%
China	21:00	Industrial production	Dec.		0.2%		2.2%
China	21:00	Retail sales	Dec.		-9.5%		-5.9%
Japan	23:30	Tertiary industry activity index	Nov.	0.2%		0.2%	
TUESDAY 17							
Germany	2:00	Consumer price index – final	Dec.	-0.8%	8.6%	-0.8%	8.6%
Germany	2:00	ZEW survey – current situation	Janv.	-15.0		-23.3	
Germany	2:00	ZEW survey – expectations	Janv.	-57.0		-61.4	
Japan	18:50	Industrial production – final	Nov.	n/a	n/a	-0.1%	-1.3%
WEDNESDAY 18							
Japan	---	Bank of Japan meeting	Janv.	n/a		-0.10%	
Euro Zone	5:00	Construction	Nov.	n/a	n/a	1.3%	2.2%
Euro Zone	5:00	Consumer price index – final	Dec.	-0.3%	9.2%	-0.3%	9.2%
Italy	4:00	Trade balance (€M)	Nov.	n/a		-2,123	
Japan	18:50	Trade balance (¥B)	Dec.	-1,631		-1,732	
THURSDAY 19							
Euro Zone	4:00	Current account (€B)	Nov.	n/a		-0.4	
Japan	18:30	Consumer price index	Dec.		4.0%		3.8%
FRIDAY 20							
Germany	2:00	Producer price index	Dec.	-1.2%	20.8%	-3.9%	28.2%

NOTE: In contrast to the situation in Canada and the United States, disclosure of overseas economic figures 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 - 5 hours).