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**AMBER KANWAR, BNN BLOOMBERG:**

All right, we've got a number of things to unpack today in the BNN Bloomberg newsroom. I know that inflation is still topical because of the amount of people that tweet about it or retweet about it or thread about it, though I haven't really found time to spend time on that platform. It is still an acute issue for Canadians. Even as headline inflation fell to 2.8%, lowest level that we've seen since March 2021, it also was lower than even economists were expecting. But before we break out the bubbly, the details are less inspiring. Core inflation remains stubbornly sticky, certainly well above the Bank of Canada's target. It's why most economists today believe another rate hike is on the table, not a done deal, but on the table for September. Let's bring in Tiffany Wilding. She's managing director and North American economist at PIMCO. Tiffany, thank you so much for being with us. Let's get the take from your perspective. What does today's read on inflation mean for interest rates going forward?

**TIFFANY WILDING, PIMCO:**

Yeah, well, I think you really hit the nail on the head. The downside surprise on headline inflation in Canada this morning was really driven by categories that look like they had one-off adjustments. You had internet services prices that were adjusted lower, which caused a big decline in that category. And you also had travel services, which tend to be noisy. So obviously, central banks like to try to smooth through some of this noise. The Bank of Canada does it with their trimmed-mean, immediate measures, and obviously those weren't as great. We at PIMCO like to look at what we call the sticky inflation measures, which is inflation in the less volatile categories, and that's really been trending sideways. So this was a bit of a mixed bag for the Bank of Canada in terms of an inflation report. So it's obviously good in terms of inflation expectations that headline inflation is moving down. But nevertheless, like some of these stickier categories aren't maybe making as much progress as to be expected. We agree that a rate hike is on the table for September. We're kind of leaning towards that they probably don't hike, but I think ultimately it's going to be a close call. We're still going to get some more data between now and then for them to chew over and figure it out.

**KANWAR:**

These rate hikes for Canadians are getting harder and harder to swallow, because in some ways it's also contributing to inflation through mortgage costs. They were told to kind of look through that. But at the same time, you know, grocery prices are still very elevated. It seems frustrating to expect a rate hike to be able to fix that.

**WILDING:**

Yeah, it already is starting to squeeze consumers who have mortgages that they need to roll over. If you look at economy-wide mortgage payments to income, that has been increasing quite dramatically. As you would expect, given higher rates over the last year or so. So certainly consumers are starting to feel the effects. But offsetting that, we have seen a lot of immigration into Canada. That's keeping rents stickier for longer. It's keeping consumption somewhat elevated, even though you do have these other headwinds to consumers. So if you look at a per capita basis, consumption doesn't look as good in Canada because of this increase in immigration and population. So the bank of Canada has to basically balance that because they can't do a lot about that. Immigration is ultimately over the long run a good thing. What the Bank of Canada's trying to do is slowly reduce demand in line with ultimately supply. And this is a really tough balancing act. And that's why it's going to be a debate in September as to whether they hike interest rates again.

**KANWAR:**

And what do you think the threshold is? Is there anything in particular you think this hinges on?

**WILDING:**

Well, I think it's been a little bit tough to read exactly the Bank of Canada's signals because I think they surprisingly hiked interest rates in June, saying that policy wasn't restrictive enough. They've done a couple of more rate hikes since then. In the July rate hike increase, they took this comment out of their statement that policy wasn't restrictive enough to kind of suggest that they're about where there should be, but nevertheless, I think they're going to be continuing to watch the data, the wage inflation data, the labor market data is what's going to be really important. It did look like wages were starting to cool in the last labor market report. Obviously increases in immigration and labor supply that come with that, that reduced wage inflation will be helpful to bringing overall inflation down. So I think these are the things they're going to have to be weighing as they make their decision.

**KANWAR:**

The other point that's been made is that Canada is not an island. There's only a certain extent to which we can decouple with what's going on in the United States. A rate hike is fully baked in the cake for July by the Federal Reserve, not so much come the September meeting. I'm wondering how you're thinking about the retail sales data that was mixed on a headline basis. It slowed, but then the control group advanced a little bit more. What does that tell you?

**WILDING:**

I think the retail sales data this morning in the US, like the core control group measure, which matters for the GDP accounts in the US was obviously very strong. But actually, that strength is coming off of several months of really lackluster consumption. So for the quarter overall, the second quarter overall looks like it's going to be tracking around 1% for US consumption, real consumption, maybe a little bit higher. And that's coming off of a 4% consumption number in the first quarter. So consumption is definitely cooling in the United States. And I would say overall, if you look at a range of different indicators in the US, the US is slowing. The labor markets, although they're pretty strong, they're also slowing in the US. Inflation in the United States is recently looking a lot better. We've actually gotten some more progress on some of these stickier measures for inflation in the US than what we've seen in Canada recently. So we think the Federal Reserve does hike again in July. There's a really high bar for them not to hike, but then we think there's more of a question, similar to Canada, around whether they hike in the back half of this year. Now the US banking sector stress is impacting credit creation in the United States. And we do think that's going to be a growing headwind even though US policy makers were able to contain the contagion and the deposit run risk in the US banking sector. Nevertheless, US banks are adjusting their businesses. They're issuing less credit as a result of some of the stress and increases in cost to capital. So that will be a headwind for the US. You also have the student loan payments that are going to start again in the United States. So the US has some headwinds in the back half of the year that will slow and will probably spill over into Canada.

**KANWAR:**

I think that's important to underline. I’m hearing more and more economists reference the fact that students in the US have not had to pay on their loans as they try and figure out — President Biden has been trying to basically expunge those debts. It’s looking unlikely, so payments resume. How much of a headwind do you think that is? Is that going to be a drop off a cliff moment or a marginal weakness?

**WILDING:**

We think that's something that could potentially grow over time. Most of the people that are going to be affected by the student loan payment increase or restart are people that aren't the lowest income core tile or desk tile, however you want to break it up. They're kind of the middle to upper income folks. Those folks also are the ones that when we look, they have more excess savings as a result of the pandemic related transfers. They still have some of that excess savings, but nevertheless, this is going to reduce that excess savings. And there's also some research out there that suggests that because the student loan payments were stopped, it allowed these consumers to take out more debt and to increase their payments on other things like car loans, mortgages, credit cards, et cetera. So now that student loan payments are going to restart, they have this other debt load that they need to service in addition to the student loan payments that are going to be coming due. So we do think this is going to be a headwind to consumption and we do think it could be quite a meaningful headwind. Maybe not a fall off the cliff type of moment, but it's going to be another headwind in addition to just a more broadly slowing economy and tight monetary policy. That's going to have an effect on growth and probably will have an effect on the labor market.

**KANWAR:**

Tiffany, thank you so much for this broad perspective. We appreciate it. That's Tiffany Wilding joining us, Managing Director and North American Economist at PIMCO.