AM Charts for November 26, 2020

Commodity Prices: ‘Hand of God’ at Work?

Douglas Porter, CFA, Chief Economist
douglas.porter@bmo.com

This is one weird recession. Even in the teeth of the biggest global economic downturn in the post-war era, the BoC’s commodity price index is roughly unchanged from a year ago. Yes, it suffered through an intense 50% plunge early this year, but has since been the definition of a V-shaped recovery. Compare that to the long workout in 2009, even amid big stimulus in China.

Note the strength in the ex-energy measure. It is now up more than 10% y/y, with each and every component above year-ago levels. While Dr. Copper is leading the way, all base metals are higher. Only a 21% y/y drop in oil prices is holding commodity measures back from more fiery gains.

Supply issues are playing a supportive role for some resource prices. But the bigger drivers are the quick rebound in China, strong housing markets, and the underlying strength in goods versus services this cycle.
U.S. households overall are still quite flush. The stress is on “overall”, because clearly some are coming under severe strain as support measures wane and jobless claims climb again. Yet, even with a 0.7% drop in personal disposable incomes in October, they are still up 6.3% y/y. That’s roughly 3 percentage points stronger than pre-pandemic trends.

And, even as consumer spending continues to recover, it’s still a few points below pre-virus levels. This wedge between stronger-than-normal income levels and lower-than-normal spending (on services), has kept savings elevated. Yes, the rate has come down from the record highs, but it’s still very strong at 13.6%. We have not seen such a high savings rate since the early 1970s, when inflation was north of 10%.

And, to be clear, this measures savings on income in the past month. So, the sky-high savings from the spring are still out there.
Ending An Awful Year in Style

Sal Guatieri, Senior Economist
sal.guatieri@bmo.com

Stronger than expected U.S. consumer spending and durable goods orders in October spurred an upward adjustment to our Q4 GDP call to 5.0% annualized (from 4.0%). Of note, is that “core” shipments (see chart) zoomed 3.7%, now back to pre-virus levels, suggesting a great start for business equipment spending in the quarter. So, a year that started with the economy sliding 5% annualized could end with a similar-sized gain.

The next few months, however, will be more challenging given surging virus caseloads and possibly waning fiscal support, so we have tentatively penciled in a 1% advance in Q1.
Robert Kavcic, Senior Economist
robert.kavcic@bmo.com

Three large provinces have recently issued mid-year fiscal updates, and there are two key themes to take away:

1. The **worst deficit projections are probably behind us**. On the revenue side, Ottawa’s transfers continue to come in higher than expected (thanks to the ramped up Safe Restart Agreement), while economies have generally fared less bad than earlier feared. And, most have ample contingencies already in place to account for the impact of the current second wave of COVID.

2. We’ve also seen medium-term targets rolled out, and **the pace of deficit reduction beyond FY20/21 will be slow**. At the bullish end, Quebec is looking at just under 1% of GDP two years down the road; Ontario is at the bearish end at 3% of GDP (we think there’s meaningful upside, but that’s a story for another day). The truth is probably in between, which is still chunky.
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