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U.S. and Canadian economies to avoid double dip recessions: CIBC World Markets Inc.

TORONTO, Ontario, July 27, 2010 — The U.S. and Canadian economies will see growth slow over the next six months but are unlikely to experience a double-dip recession, finds CIBC's Recession Probability Index.

The Index, which has a strong track record of forecasting recessions, finds the odds of another U.S. recession occurring in the next six months are very low. The CIBC RPI measures the probability of a recession by examining trends in a number of indicators, including credit spreads, interest rates, and the Philadelphia Federal Reserve Board's ADS Index (which includes weekly U.S. unemployment benefit claims).

"We're not in material danger of a rude double dip in the next two quarters," says Avery Shenfeld, Chief Economist at CIBC. "The probability estimate is likely more consistent with a slowdown rather than a true double-dip recession. But, given the uncertainties, fiscal tightening ahead and the potential for a slow economy to be vulnerable to shocks, we will keep an eye on our new indicator nevertheless."

In his latest Economic Insights report, Mr. Shenfeld notes that consumers and investors alike are starting to fret over the possibility of a double-dip recession, but he says in the modern era, double dips are more often feared than reality. "A double dip is to be avoided at all costs when holding a potato chip at the buffet line, and less trivially, when steering economic policy.

"Indeed, if one defines a double dip as a downturn after an expansion lasting less than two years, the only post-WWII U.S. twin dives were the recessions of 1980 and 1981-82. Double dips have also been rare in other major economies of late, although Japan fell into recession in 2000 only a year after it emerged from the "Asian crisis" recession."

He cites a number of factors that he expects will keep the American economy from hitting a double-dip. First, he expects that the U.S. government will back away from shutting off the stimulus taps too aggressively in the face of lagging job growth. But since U.S. President Barack Obama's gradualist approach to deficit reduction will still be a negative for growth, monetary policy will have to remain very stimulative. As a result, even a modest tightening by the U.S. Federal Reserve Board in the second half of next year now looks premature. Best bets are that Ben Bernanke's team will seek no exit from low rates until 2012.

"Fiscal policy might move off its tightening war-path. Congress already backed away from an earlier posture that would have let extended unemployment benefits lapse, and legislators now talking like tigers on deficits could become pussycats favouring stimulus in the face of continued high joblessness in 2011."

Other factors Mr. Shenfeld sees that suggests the U.S. economy, and by extension Canada's, will avoid a second recession:

- Healthy corporate profits. These typically presage both hiring and capital spending and will likely benefit further from continued government stimulus.
- Strong market liquidity. A recent study in the Journal of Finance found that a drying up in market liquidity is often a telling sign of economic trouble ahead. Liquidity plummeted at a pace not seen in more than 20 years ahead of the recent downturn. At present, market liquidity isn't sending out the same sort of warning signal.
- Steep bond market curves. The US Treasuries curve is much steeper today than it typically is when a recession is coming up in the next few quarters. Although, with short rates near zero, curve inversions can't occur.
- Tight corporate spreads. Ahead of a recession, spreads tend to widen sharply as investors anticipate credit defaults. Spreads remain quite tight by the standards leading up to recent recessions, and don't show the sharp upward trend typically seen ahead of a downturn. It's clear that investors are far from pricing in a recession.

"Certainly, there are reasons for concern," adds Mr. Shenfeld. "The U.S. economy has been propped up by fiscal stimulus that is now winding down. Job growth has lacked its typical post-recession vigour, leaving a household sector swamped with bad mortgages having few reasons to accelerate spending. But there is still a base of ongoing support coming from healthy corporate profits and a wide-open tap on monetary stimulus. That has us projecting a sharp deceleration in U.S. growth, but not an outright recession, with a similar fate in store for Canada."

The complete CIBC World Markets Inc. report is available at:

http://research.cibcwm.com/economic_public/download/sjul10.pdf.

CIBC World Markets Inc. is the corporate and investment banking arm of CIBC. To deliver on our mandate as a premier client-focused and Canadian-based wholesale bank, we provide a wide range of credit, capital markets, investment banking, merchant banking and research products and services to government, institutional, corporate and retail clients in Canada and in key markets around the world.