RBC Economics

Daily Economic Update

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Bank of Canada surveys flag intensifying inflation pressures

- Business future sales growth expected to be limited by production capacity limits
- Russian invasion to add to higher input costs and global supply chain disruptions (and also increase revenues for commodity producers)
- Inflation expectations (both business and consumer) moved higher, although have yet to come unanchored in the longer-run.
- Bank of Canada expected to continue to (rapidly) hike rates on strong economy and near-term price pressures

Business Outlook Survey Summary

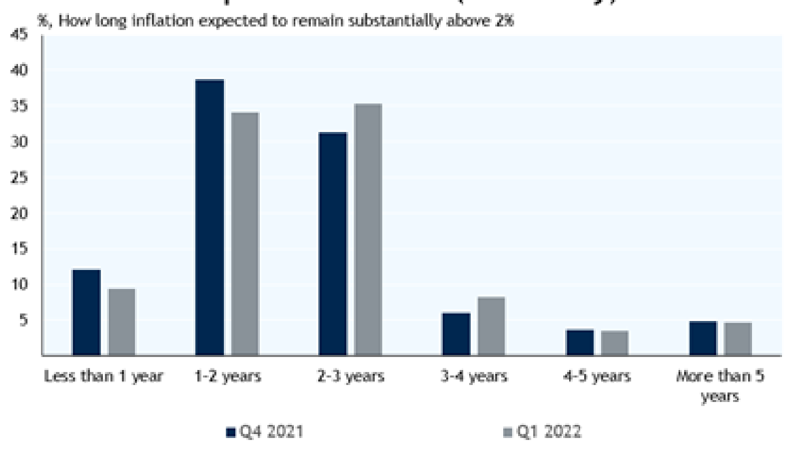
	2021/Q3	2021/Q4	2022/Q1
Balance of opinion (%) unless otherwise indicated			
BOS indicator	**4.4**	**5.9**	**5.0**
Past sales growth	30.0	63.0	42.0
Future sales growth	9.0	3.0	-11.0
M&E Investment	46.0	47.0	42.0
Future Employment	67.0	77.0	63.0
Difficulty meeting demand (%)	65.0	78.0	81.0
Labour shortages (yes %)	36.0	41.0	40.0
Input price inflation	8.0	7.0	16.0
Output price inflation	8.0	16.0	26.0

Source: Bank of Canada, RBC Economics Research

The Bank of Canada's Q1 Business Outlook Survey continued to flag binding long-run capacity pressures and surging input costs as larger issues for businesses than any shortfall in orders. Firms in high-contact service-sectors that have been hit hard by the pandemic are still expecting to see growth as the economic impact of the virus eases, but other firms are bumping up firmly against production capacity limits. Expected future sales growth decelerated, but from very high levels, and over 80% of businesses reported they would have trouble filling an unexpected increase in orders. Hiring and investment plans remained strong - but acute labour shortages pushed up expected wage growth to 5.2% over the next year. Input costs continued to surge higher.

Survey responses were collected before the Russian invasion of Ukraine, but follow-up interviews showed businesses expect the conflict to add to those pre-existing supply chain and input cost increases - along with potentially boosting sales and revenues among energy and commodity producers.

Most business expect inflation to (eventually) slow



Source: RBC Economics Research

Price pressures continued to firm, with 70% of businesses expecting inflation growth to exceed the Bank of Canada's 1% to 3% target range over the next two years. And consumer price expectations also moved higher in the separately released Survey of Consumer Expectations (to 5.1% and 4.6% over the next one and two years, respectively). The Bank of Canada will take some comfort from the fact that longer-run inflation expectations have yet to come unanchored with most businesses expecting a return to near a 2% rate after three years. But that was also contingent on expectations that the central bank will continue to increase rates. Clearly, the economy and inflation pressures are too firm to justify emergency-low levels of interest rates and we think the Bank of Canada is most likely to hike the overnight rate by another 50 bps later this month to follow up on the 25 bps increase in March.

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