

**KEY POINTS:**

- Risk-off on headline chasing...
- ...as trade policy, Brexit, virus headlines dominated
- Markets ignore one agency's Canada downgrade
- Banxico expected to cut
- More US rebound evidence on tap
- Turkey expected to cut again

**TODAY'S NORTH AMERICAN MARKETS**

A significant risk-off tone likely had multiple catalysts that were all headline driven with still nary a whisper of strategy. The Chief EU Brexit negotiator, Michel Barnier, made headlines this morning when he downplayed the possibility of a Brexit extension and guided that a deal was necessary by the October EU Summit and that the EU was standing its ground. I didn't see him speak, but assume he had on his best poker face given about four years almost to the day of bluffing by both sides.

Stocks continued to be hit by trade policy concerns as argued in this morning's note. The WTO is reportedly delaying its decision on what penalties the EU may apply against the US in the Boeing-Airbus dispute until September or October given a backlog of cases.

After multiple days of ignoring US Covid-19 cases, it's possible that today was the day to pay attention, but it's impossible to separate out the influences on stocks. Houston, for example, advised that it is expected to run out of intensive care capacity as soon as tomorrow. President Trump's apparent decision to shift the burden of testing off the federal government after June 30th and onto private sites particularly in Texas reduces the efficacy of a prime tool in combatting the virus which is frequent testing.

Through it all, the US election may be operating in the back of investors' minds.

Canada got downgraded by Fitch, but markets shook it off (see below).

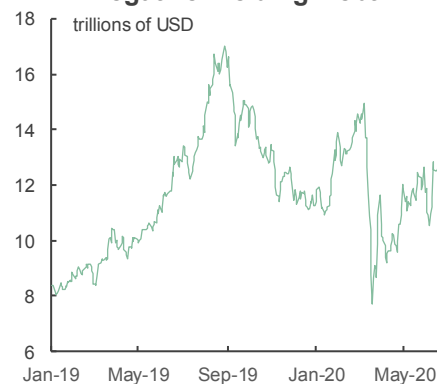
- US stocks fell by between 1.8–2.4% with the Nasdaq at the bottom and DJIA at the top of the losses. Selling on the S&P500 was widespread across sectors but led by energy (-5.5%), as well as financials and industrials that both fell by 3.5%. Toronto fell 1.6%. European stocks fell by either side of 3% across the benchmarks.
- The USD strengthened somewhat. CAD shook off a downgrade, and the weakest crosses were the real, Mexican peso, some Scandies and the A\$/NZ\$.
- The US Treasury curve bull flattened with 10s down 4bps and 30s down 6bps. Canada's curve underperformed especially toward the long end that was up 1bp.
- Oil prices fell by over 5% in terms of WTI and Brent.

**CONTACTS**

**Derek Holt, VP & Head of Capital Markets Economics**  
416.863.7707  
Scotiabank Economics  
[derek.holt@scotiabank.com](mailto:derek.holt@scotiabank.com)

**Evan Andrade, Economic Analyst**  
416.862.3080  
Scotiabank Economics  
[evan.andrade@scotiabank.com](mailto:evan.andrade@scotiabank.com)

Chart 1

**Global Aggregate Value of Negative Yielding Debt**

Sources: Scotiabank Economics, Bloomberg

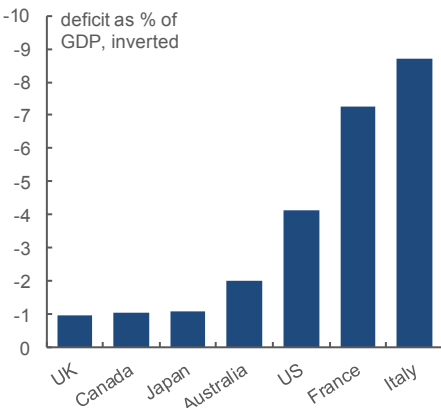
How would it feel if you threw a downgrade party and nobody came? Ask Fitch.

Canada got downgraded to AA+ with a stable outlook on its long-term foreign currency issuer default rating by Fitch today. It remains AAA with S&P and Moody's. The decision is [here](#). Markets could not have cared much less, as Government of Canada yields and the currency were unaffected.

I'm not disputing their methodology in any depth frankly, but you could have taken the first paragraph of their write-up and applied it to virtually any sovereign credit in the world today. Lagging ratings actions are a relative game, and the relatives aren't looking so good these days. Most market pricing is driven by investors that are not ratings constrained and that invest on other terms. As a case in point, when US\$13 trillion of global debt trades at negative yields (chart 1) and Canada isn't part of that, you can immediately grasp one reason behind why most investors are perfectly willing to hold a credit that offers rare yield pick-up in a yield-starved world. Besides, charts 2–4 depict the state of Canada's finances compared to other countries.

Chart 2

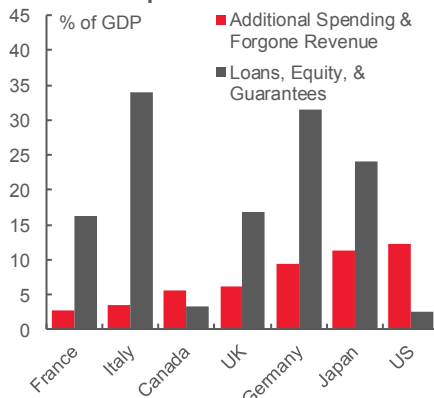
**Approximate Q1 2020 Federal Government Budget Deficits**



Sources: Scotiabank Economics, Haver Analytics.

Chart 3

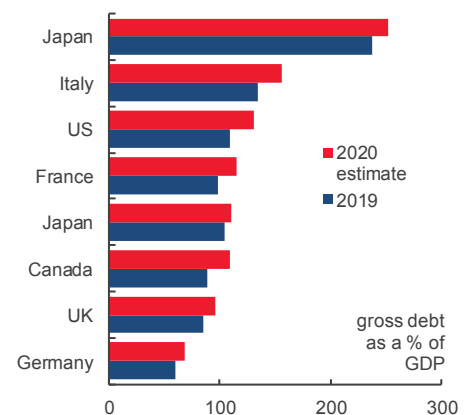
**IMF Estimated Fiscal Response to COVID-19**



Note: Fiscal response data up to June 12th. Sources: Scotiabank Economics, IMF.

Chart 4

**Projected General Government Debt**



Sources: Scotiabank Economics, IMF April Fiscal Monitor.

We'll see if Moody's and S&P feel likewise, but even if so, the points above should stand. Agencies don't have to agree with one another—they didn't when S&P went solo on the US downgraded the US from AAA to AA+ in 2011. Further, quite frankly, Fitch's US-based calls on Canada have been contentious in the past. Remember [this](#) doozie? Back in 2013, they said Canada's housing market was 20% over-valued in real terms (it has since risen by one-third in nominal terms) and this served as input into a loan loss severity regression model that they developed. They reasoned that because Canadian data during a distress period was in short supply, that they could instead use the US experience in the GFC and apply it to Canada, without noting the many differences in the markets. That didn't work out so well.

**OVERNIGHT MARKETS**

Overnight releases will be fairly light. German GfK consumer confidence for July arrives at 2amET and should reinforce the improving trend already evidence in PMIs and the IFO and ZEW surveys. Turkey's central bank is expected to cut by 25bps or 50bps (7amET). The ECB releases the account of its June 4<sup>th</sup> meeting (7:30amET).

**TOMORROW'S NORTH AMERICAN MARKETS**

**All twenty-one economists in the Bloomberg consensus including Scotia's Mario Correa expect Banxico to cut its overnight rate by 50bps tomorrow afternoon (2pmET).** With headline inflation at 2.84% y/y and core inflation at 3.64% y/y compared to a target range of 2–4%, easing and guidance would rely in part upon the expected evolution of price pressures. As argued in the Global Week Ahead, however, policy guidance since the last time it cut on May 14<sup>th</sup> has been mixed.

**US markets will digest four macro readings**, three of which may partly inform rebound expectations while the fourth is a stale third swing.

**Weekly jobless claims (8:30amET)** barely budged lower two weeks ago against consensus expectations for a sharper decline. Will figures for last week reaccelerate the decline in first time claims? We think so, but also continue to keep an eye on repeat continuing claims that have come off the peak but remain elevated. Disappointment for a second week into the nonfarm reference period likely wouldn't go over well.

**Durable goods orders will likely get a lift** from the transportation and particularly auto sectors tomorrow morning when estimates for May land (8:30amET). Consensus thinks +10% m/m and I'm at 12%. Orders excluding transportation and core orders ex defence and air will probably be lucky to post any growth. Going forward, excess capacity will put core orders on the defensive for some time.

**The advance merchandise trade deficit is expected to slightly narrow** as the economy gradually came out of the worst of the shutdowns in May (8:30amET).

**Q1 GDP will be revised** for a second time (8:30amET) and this third estimate is the one that more fully incorporates services spending. Most expect little to no change to the previously estimated -5% contraction.

Fixed Income	Government Yield Curves (%):												Central Banks	
	2-YEAR			5-YEAR			10-YEAR			30-YEAR			Current Rate	
	Last	1-day	1-wk	Last	1-day	1-wk	Last	1-day	1-wk	Last	1-day	1-wk		
U.S.	0.19	0.19	0.20	0.32	0.33	0.34	0.68	0.71	0.74	1.43	1.49	1.53	Canada - BoC	0.25
CANADA	0.30	0.30	0.29	0.38	0.39	0.38	0.55	0.54	0.53	1.03	1.01	1.03	US - Fed	0.25
GERMANY	-0.67	-0.66	-0.66	-0.68	-0.66	-0.64	-0.44	-0.41	-0.39	0.01	0.08	0.06	England - BoE	0.10
JAPAN	-0.13	-0.13	-0.14	-0.10	-0.11	-0.10	0.02	0.01	0.02	0.59	0.58	0.57	Euro zone - ECB	0.00
U.K.	-0.07	-0.06	-0.06	-0.03	-0.01	-0.01	0.19	0.21	0.19	0.64	0.69	0.58	Japan - BoJ	-0.10
	Spreads vs. U.S. (bps):													
CANADA	11	11	10	7	6	3	-13	-17	-21	-40	-48	-50	Mexico - Banxico	5.50
GERMANY	-86	-85	-85	-99	-99	-98	-112	-112	-113	-142	-142	-148	Australia - RBA	0.25
JAPAN	-32	-32	-34	-42	-44	-45	-66	-70	-72	-84	-91	-96	New Zealand - RBNZ	0.25
U.K.	-26	-25	-25	-34	-34	-36	-49	-50	-55	-79	-80	-95		
Equities	Level						% change:						Next Meeting Date	
	Last	Change		1 Day		1-wk		1-mo		1-yr				
S&P/TSX	15294	-270.4		-1.7		-0.9		2.6		-7.4		Canada - BoC	Jul 15, 2020	
Dow 30	25446	-710.2		-2.7		-2.6		4.0		-4.8		US - Fed	Jul 29, 2020	
S&P 500	3050	-81.0		-2.6		-2.0		3.2		3.6		England - BoE	Aug 06, 2020	
Nasdaq	9909	-222.2		-2.2		-0.0		6.3		23.8		Euro zone - ECB	Jul 16, 2020	
DAX	12094	-429.8		-3.4		-2.3		9.2		-1.5		Japan - BoJ	Jul 15, 2020	
FTSE	6124	-196.4		-3.1		-2.1		2.2		-17.4				
Nikkei	22534	-14.7		-0.1		0.3		8.6		6.3		Mexico - Banxico	Jun 25, 2020	
Hang Seng	24782	-125.8		-0.5		1.2		8.0		-12.1		Australia - RBA	Jul 07, 2020	
CAC	4871	-146.3		-2.9		-2.5		9.6		-11.8		New Zealand - RBNZ	Aug 11, 2020	
Commodities	Level						% change:							
WTI Crude	38.07	-2.30		-5.7		0.3		14.5		-34.2				
Natural Gas	1.60	-0.04		-2.2		-2.3		-7.5		-30.5				
Gold	1761.11	-0.06		-0.0		2.2		1.7		23.7				
Silver	17.81	-0.05		-0.3		2.3		4.8		16.5				
CRB Index	135.24	-3.35		-2.4		-0.8		4.4		-24.9				
Currencies	Level						% change:							
USDCAD	1.3636	-0.0002		-0.0		0.3		-2.5		3.5				
EURUSD	1.1253	0.0002		0.0		0.4		3.3		-1.0				
USDJPY	107.05	0.0100		0.0		0.1		-0.6		-0.1				
AUDUSD	0.6870	0.0001		0.0		0.3		5.0		-1.3				
GBPUSD	1.2425	0.0006		0.0		0.0		1.9		-2.1				
USDCHF	0.9477	-0.0002		-0.0		-0.4		-2.5		-2.8				

This report has been prepared by Scotiabank Economics as a resource for the clients of Scotiabank. Opinions, estimates and projections contained herein are our own as of the date hereof and are subject to change without notice. The information and opinions contained herein have been compiled or arrived at from sources believed reliable but no representation or warranty, express or implied, is made as to their accuracy or completeness. Neither Scotiabank nor any of its officers, directors, partners, employees or affiliates accepts any liability whatsoever for any direct or consequential loss arising from any use of this report or its contents.

These reports are provided to you for informational purposes only. This report is not, and is not constructed as, an offer to sell or solicitation of any offer to buy any financial instrument, nor shall this report be construed as an opinion as to whether you should enter into any swap or trading strategy involving a swap or any other transaction. The information contained in this report is not intended to be, and does not constitute, a recommendation of a swap or trading strategy involving a swap within the meaning of U.S. Commodity Futures Trading Commission Regulation 23.434 and Appendix A thereto. This material is not intended to be individually tailored to your needs or characteristics and should not be viewed as a “call to action” or suggestion that you enter into a swap or trading strategy involving a swap or any other transaction. Scotiabank may engage in transactions in a manner inconsistent with the views discussed this report and may have positions, or be in the process of acquiring or disposing of positions, referred to in this report.

Scotiabank, its affiliates and any of their respective officers, directors and employees may from time to time take positions in currencies, act as managers, co-managers or underwriters of a public offering or act as principals or agents, deal in, own or act as market makers or advisors, brokers or commercial and/or investment bankers in relation to securities or related derivatives. As a result of these actions, Scotiabank may receive remuneration. All Scotiabank products and services are subject to the terms of applicable agreements and local regulations. Officers, directors and employees of Scotiabank and its affiliates may serve as directors of corporations.

Any securities discussed in this report may not be suitable for all investors. Scotiabank recommends that investors independently evaluate any issuer and security discussed in this report, and consult with any advisors they deem necessary prior to making any investment.

**This report and all information, opinions and conclusions contained in it are protected by copyright. This information may not be reproduced without the prior express written consent of Scotiabank.**

<sup>TM</sup> Trademark of The Bank of Nova Scotia. Used under license, where applicable.

Scotiabank, together with “Global Banking and Markets”, is a marketing name for the global corporate and investment banking and capital markets businesses of The Bank of Nova Scotia and certain of its affiliates in the countries where they operate, including, Scotiabanc Inc.; Citadel Hill Advisors L.L.C.; The Bank of Nova Scotia Trust Company of New York; Scotiabank Europe plc; Scotiabank (Ireland) Limited; Scotiabank Inverlat S.A., Institución de Banca Múltiple, Scotia Inverlat Casa de Bolsa S.A. de C.V., Scotia Inverlat Derivados S.A. de C.V. – all members of the Scotiabank group and authorized users of the Scotiabank mark. The Bank of Nova Scotia is incorporated in Canada with limited liability and is authorised and regulated by the Office of the Superintendent of Financial Institutions Canada. The Bank of Nova Scotia is authorised by the UK Prudential Regulation Authority and is subject to regulation by the UK Financial Conduct Authority and limited regulation by the UK Prudential Regulation Authority. Details about the extent of The Bank of Nova Scotia’s regulation by the UK Prudential Regulation Authority are available from us on request. Scotiabank Europe plc is authorised by the UK Prudential Regulation Authority and regulated by the UK Financial Conduct Authority and the UK Prudential Regulation Authority.

Scotiabank Inverlat, S.A., Scotia Inverlat Casa de Bolsa, S.A. de C.V., and Scotia Derivados, S.A. de C.V., are each authorized and regulated by the Mexican financial authorities.

Not all products and services are offered in all jurisdictions. Services described are available in jurisdictions where permitted by law.