

DAILY POINTS

February 6, 2024 @ 8:45 EST

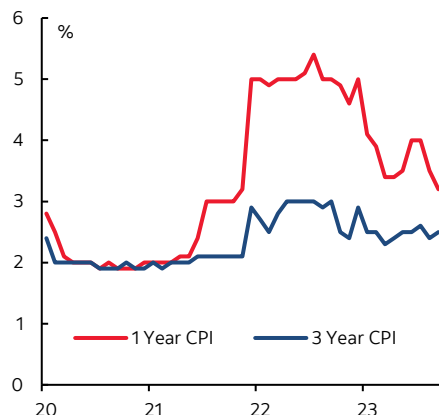
Contributors

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Chart 1

ECB Measure of Inflation Expectations



Sources: Scotiabank Economics, ECB.

On Deck for Tuesday, February 6

Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
CA	02-06	08:30	Building Permits (m/m)	Dec	--	2.0	-3.9
US	02-06	12:00	Fed's Mester Speaks on Economic Outlook				
US	02-06	13:00	Fed's Kashkari Participates in Moderated Discussion				
US	02-06	14:00	Fed's Collins Delivers Opening Remarks at Labor Market Conference				
US	02-06	19:00	Fed's Harker Speaks on Fed's Role in Economy				

KEY POINTS:

- Global markets stabilize
- Canada's housing markets is on fire again
- PMIs point to hot US and Canadian services inflation
- BoC won't cut until September if all goes really, really well, hike risk still alive
- Fed won't cut until Q3, can't rule out hikes either
- BoC's Macklem to deliver a rather awkwardly timed speech
- Eurozone inflation expectations hold firm
- RBA sounded hawkish, markets plugged their ears
- German factory orders totally embarrassed consensus
- The good and the bad and what not to do about Canadian bankruptcies

Small movements are being registered across global bond benchmarks, the USD and equities this morning in the absence of major global developments, or at least not ones that markets are choosing to put a whole lot of emphasis upon. Eurozone inflation expectations held firm, the RBA sounded hawkish but was ignored, German factory orders soared, and Canadian home sales are on fire again ahead of a speech by Governor Macklem.

BoC and Fed Forecasts

The whole Scotia Economics team throughout the Americas put out its latest forecast update this morning that revises several things compared to the prior forecast back in mid-December. The main changes are to the Fed and BoC that better reflect my views on the two central banks as written for some time.

The BoC is forecast to stay on hold until September at which point it cuts by 75bps over the final three meetings of this year. A lot has to go smashingly right to get to cuts and I think hike risk remains. To institutional investors, the advice remains to focus upon continuing to fade any nearer term cut pricing and not get too excited around views beyond the next few meetings at most after which let's just say the picture gets increasingly cloudy. To borrowers, my advice is to continue to do what you must and/or can on the assumption that no—or minimal—cuts may be delivered this year. If cuts do eventually arise—or especially if hikes resume—then you will be better positioned. I get that this is going to be easier for some than for others.

The Fed is forecast to cut in Q3 with 100bps of cuts this year. I don't like a cut by May 1st partly on the difficulty around easing on the heels of what is at present shaping up to be another ripping Q1 economy with Q1 GDP due six days before that decision. It's also difficult to imagine that the Committee would have comfort to explicitly tee up a cut in June at the May meeting. The Fed's dual mandate is the focus of course, but economic growth is among the influences upon jobs and inflation. The US economy is showing no signs of moving toward building disinflationary slack that would give comfort that 2%

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inflation can be durably achieved, while wage growth in m/m SAAR terms is trending higher and supply chain risks are material. A massive cooling of the US economy and concomitant implications for jobs and inflation would be required to get to cuts and I just don't have the faith in such a view at this point partly because the view that the US economy faces imminent slowing has been around for seven quarters now and has been blown out of the water in each and every one of them.

RBA Sounds Hawkish, Markets Didn't Listen

A hawkish sounding RBA was shaken off by markets. The 2s yield ended the session unchanged compared to just before the statement, pricing for the March decision added about 6bps to price half of a quarter point cut and a quarter point cut remains priced for the August meeting. The A\$ is flat compared to right before the communications landed.

RBA Governor Bullock et al did not sound like they were in any rush to cut rates. In fact, she described rates risks as "fairly balanced" with inflation still "too high" and said "a further increase in interest rates cannot be ruled out." Thank heavens they avoided the BoC's botched job on the latter issue. The messaging was about how "we are not ruling in anything or out anything" and "need to stay the course." Revised forecasts expect inflation to come close to the mid-point of the 2–3% inflation target range only by the end of 2026 at 2.6% for headline and trimmed mean. RBA watchers will then have an eye on things like the next wages report that is going to be set against an accelerating trend.

Eurozone Inflation Expectations

Eurozone inflation expectations held firm in December according to the ECB's measures (chart 1). Upward revisions were key. 1-year CPI expectations stood at 3.2% y/y but the prior month was revised up to 3.5% from 3.2%. 3-year CPI expectations moved up a tick to 2.5% from an upwardly revised prior reading of 2.4% (from 2.2%). How can they revise a survey, you ask?? Because they added some countries including Austria, Portugal, Ireland, Finland and Greece. I never knew these countries were not previously included as it was understood to be a Eurozone-wide survey. Who knew??!!

German factory orders embarrassed consensus. They were up by 8.9% m/m SA in December (consensus -0.2%) and revisions don't explain anything about the beat. The gain was driven by a 10.9% m/m jump in capital goods orders mostly from outside of Germany and an 8.3% increase in intermediate goods mostly from within Germany as orders for consumer goods slipped 1.3% because a surge in domestic demand was offset by a drop in foreign orders.

Canada's Housing Market is Doing it All Over Again

Canada's housing market is on fire again. Add Toronto and Quebec to the list of regions reporting strong sales after Vancouver and Calgary surged in last week's reports. Toronto's existing home sales ([here](#)) were up by 9.6% m/m SA in January as reported by TREB this morning. Montreal's sales were up by an estimated 5% m/m SA that was derived by taking NSA data from the source and applying the average January seasonal adjustment factor in recent years. Quebec City's sales were up over 2% m/m SA after a surge of about 12% m/m SA in December. The nationwide total figures for home sales will be released next week and are likely to add another strong gain to the prior month's 8.7% m/m SA surge; a high single digit gain seems assured. From what I'm gathering from various sources, more strength very much remains in the pipeline ahead of the Spring market.

This is happening even earlier than I had thought it would. I've always thought that the only folks who buy homes in January do so either because they absolutely must (job change, lifestyle change etc) or because they are masochists in this kind of climate. To be getting hot numbers like these already is a stern warning sign. That the market would be strong into Spring should shock no one, however, as I've been warning about massive immigration, little to no supply, a ripping job market that created 430k jobs last year, soaring wage gains, affordable mortgage rates, and evidence that first time homebuyers have been amassing bigger downpayments. The next question is whether the BoC should respond.

BoC Governor Macklem Cannot Ignore Housing Like Poloz Did

BoC Governor Macklem delivers a speech on "The Effectiveness and the Limitations of Monetary Policy" and hosts a press conference afterward. The speech text will be available at 12:45pmET and the press conference will be held at about 2:10pmET, give or take.

There may be a sense of helplessness in this speech. The overall tone might be an extension of some of his arguments to date. Namely, that monetary policy is working, where it is working, and how it cannot address other issues like housing. As written numerous times, I think he has been overstating where monetary policy has been working by ignoring all of the serial shocks to hit the Canadian economy. I think he is wrong to dismiss his powers over housing which is the most rate sensitive sector going.

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More fundamentally, I think he slopes off responsibility for housing excesses too readily to others by saying it's everyone else's fault in terms of supply management. Yes there are supply issues. But the BoC has serially overstimulated housing in one cycle after another and the real cost of mortgage debt is doing it again. Former Governor Poloz could get away with what he did to impair housing affordability because he could point to reasonably low inflation.

Macklem cannot do the same. This time the stakes are higher. With inflation expectations already unmoored amid evidence that behaviour has been changing as a result (eg. wages and productivity), each new serial shock to inflation risk results in people losing additional faith in ever durably hitting 2% and so they go on changing their behaviour in the same unhelpful ways. The tendency across some other economists and the BoC throughout too much of the pandemic has been to have serial excuses for inflation and to counsel ignoring it. That's how we got into this mess and imagine had the BoC looked through them all and held; CAD would be the northern Turkish lira and inflation would be totally off the charts.

Furthermore, there are other drivers of inflation risk beyond housing including ones that I'll cite below on the services side, plus others like wages, productivity, immigration, fiscal excess, an undervalued CAD etc etc.

So, if I see the Governor shrug his shoulders and say he can't do anything about immigration, housing, etc, and the ties to inflation, then it's added cause to think that inflation risk will persist without the BoC doing much about it. Go ahead, don't listen, push wage demands even higher. The BoC cannot forecast inflation and has a poor track record at doing so anyway.

On that note, maybe Canadian wage settlements will come out today after all. I was told by the source that they were supposed to be out yesterday and are about five weeks behind the normal schedule as it is.

Hot US, Canadian Services Inflation

It's not just housing that is a challenge to inflation in Canada. Another warning on Canadian inflation came in yesterday's composite PMI from S&P for January:

"Service providers also noted that typical wage costs had risen at the start of 2024, and this was a key factor behind the latest acceleration in overall input cost inflation. According to the latest data, input prices rose to the greatest degree for three months and remained historically elevated. Firms were also willing to pass on these costs to clients in the form of increased output charges. January's survey signalled that average tariffs rose to the greatest degree since last July."

That services inflation is very much alive and kicking in N.A. was further evidenced by the US ISM-services report yesterday. Here's what they had to say about prices:

"Fifteen services industries reported an increase in prices paid during the month of January, in the following order: Real Estate, Rental & Leasing; Arts, Entertainment & Recreation; Construction; Other Services; Educational Services; Health Care & Social Assistance; Wholesale Trade; Public Administration; Professional, Scientific & Technical Services; Retail Trade; Finance & Insurance; Management of Companies & Support Services; Utilities; Information; and Transportation & Warehousing. The only industry reporting a decrease in prices for January is Agriculture, Forestry, Fishing & Hunting."

US Only Faces Fed-Speak

Fed-speak will come from Cleveland's Mester (12pmET), Minneapolis President Kashkari (1pmET), Boston's Collins (2pmET) and Philly's Harker (7pmET). There are no US releases on tap today.

The Good and Bad and What Not to Do About Canadian Bankruptcies

Canada released bankruptcy figures for households and businesses yesterday. Some balanced context is needed relative to how the numbers are being portrayed elsewhere.

First, consumers continue to do what it takes to adjust as bankruptcies remain toward record lows (chart 2). Insolvencies are rising due to proposals which continues a longstanding trend, but they are not showing up in bankruptcies. This reflects public policy supports and a very different banking model in Canada. The consumer side is weighing down total consumer and business bankruptcies in Canada (chart 3). This may also have a side narrative; there can be a fuzzy line between consumer and small business finances.

Canadian business bankruptcies, however, are soaring (chart 4). That's unfortunate, but sound public policy has to take this in stride. If you want Canada to improve its moribund productivity, then let's not have governments stand in the way of this. Business bankruptcies had

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been plummeting when Canada was granting handouts galore that covered rent, wages, etc and offered preferential loans. That was sound policy at the very start when public policy did what it should in response to an awful shock no one deserved but these supports were maintained for far, far too long and were too generous. I believe that's one reason why Canada's labour productivity has stunk for years while US productivity growth is surging. The country went too far in making businesses whole. This prevented any hope of the market clearing and reallocating resources from firms and industries that were undergoing structural and cyclical changes that were dampening prospects to firms/industries that faced better prospects. The result was an inability to fill vacancies in sectors that needed the workers and hence there was a permanently lost of output, impaired productivity, excess inflation, and upward effects on the cost of capital. Now the market is working it out. There are multiple costs, but they are delayed costs that should have been allowed to unfold more gradually and earlier.

Chart 2

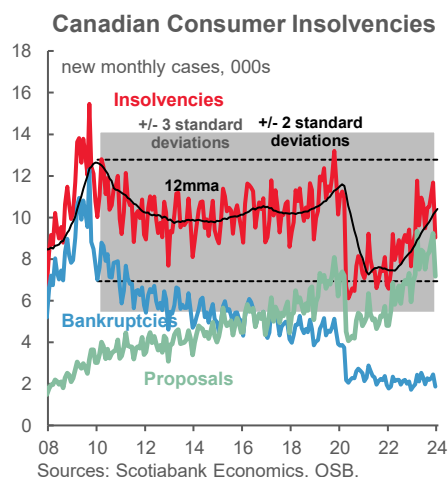


Chart 3

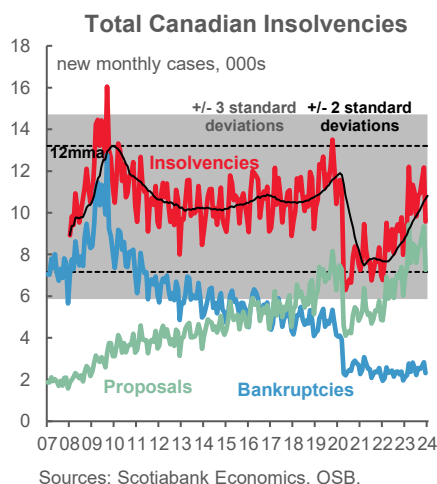
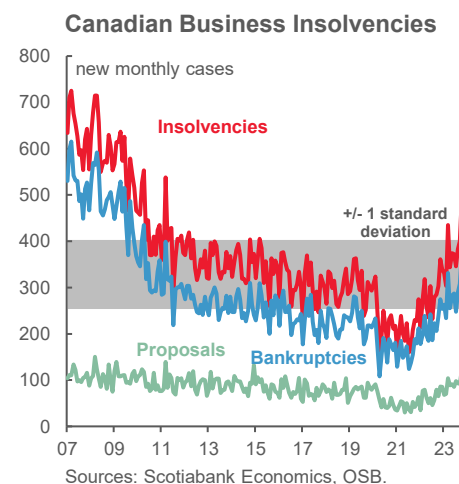


Chart 4



Fixed Income	Government Yield Curves (%):												Central Banks		
U.S. CANADA GERMANY JAPAN U.K. CANADA GERMANY JAPAN U.K.	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			
	4.46	4.47	4.34	4.11	4.12	3.97	4.16	4.16	4.03	4.35	4.34	4.25	Canada - BoC	5.00	
	4.13	4.15	4.04	3.58	3.60	3.49	3.49	3.51	3.41	3.38	3.38	3.32	US - Fed	5.50	
	2.62	2.61	2.53	2.24	2.24	2.16	2.32	2.32	2.27	2.54	2.52	2.50			
	0.12	0.11	0.06	0.32	0.33	0.30	0.72	0.73	0.72	1.80	1.79	1.82	England - BoE	5.25	
	4.47	4.51	4.34	3.97	4.00	3.86	3.99	4.01	3.90	4.59	4.62	4.53			
	Spreads vs. U.S. (bps):														
	CANADA	-33	-32	-29	-53	-52	-47	-66	-65	-63	-97	-95	-93	Euro zone - ECB	4.50
	GERMANY	-184	-186	-181	-187	-188	-181	-183	-184	-176	-181	-182	-176	Japan - BoJ	-0.10
JAPAN	-434	-436	-428	-379	-379	-367	-343	-343	-332	-255	-255	-243			
U.K.	1	3	0	-14	-12	-11	-17	-15	-13	25	28	28			
Equities	Level						% change:						Mexico - Banxico	11.25	
	Last	Change		1 Day	1-wk	1-mo	1-yr								
S&P/TSX	20872	-213.2		-1.0	-1.5	-0.3	1.2						Australia - RBA	4.35	
Dow 30	38380	-274.3		-0.7	0.1	2.4	13.2						New Zealand - RBNZ	5.50	
S&P 500	4943	-15.8		-0.3	0.3	5.2	20.2								
Nasdaq	15598	-31.3		-0.2	-0.2	7.4	31.2								
DAX	16950	46.0		0.3	-0.1	2.1	10.5								
FTSE	7669	56.1		0.7	0.0	-0.3	-2.1								
Nikkei	36161	-193.5		-0.5	0.3	8.3	30.6						Canada - BoC	Mar 06, 2024	
Hang Seng	16137	626.9		4.0	2.8	-2.4	-24.2						US - Fed	Mar 20, 2024	
CAC	7629	39.5		0.5	-0.6	2.8	6.9								
Commodities	Level						% change:								
WTI Crude	73.38	0.60		0.8	-5.7	-0.6	-1.0						England - BoE	Mar 21, 2024	
Natural Gas	2.05	-0.03		-1.3	-1.1	-29.0	-16.4								
Gold	2027.61	2.50		0.1	-0.5	-0.9	8.6						Euro zone - ECB	Mar 07, 2024	
Silver	22.51	-0.73		-3.1	-2.2	-2.1	-4.2						Japan - BoJ	Mar 19, 2024	
CRB Index	268.19	0.45		0.2	-2.1	0.9	0.7								
Currencies	Level						% change:								
USDCAD	1.3537	-0.0003		-0.0	1.0	1.4	0.7						Mexico - Banxico	Feb 08, 2024	
EURUSD	1.0732	-0.0011		-0.1	-1.0	-2.0	0.1								
USDJPY	148.64	-0.0400		-0.0	0.7	3.1	12.0						Australia - RBA	Mar 18, 2024	
AUDUSD	0.6491	0.0008		0.1	-1.7	-3.4	-5.7								
GBPUSD	1.2558	0.0022		0.2	-1.1	-1.5	4.5						New Zealand - RBNZ	Feb 27, 2024	
USDCHF	0.8730	0.0023		0.3	1.3	2.9	-6.0								
Next Meeting Date															

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