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GLOBAL ECONOMICS

DAILY POINTS

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On Deck for Wednesday, January 22							
Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
US	01-22	07:00	MBA Mortgage Applications (w/w)	Jan 17	--	--	33.3
CA	01-22	08:30	IPPI (m/m)	Dec	--	0.6	0.6
CA	01-22	08:30	Raw Materials Price Index (m/m)	Dec	--	0.5	-0.5
US	01-22	10:00	Leading Indicators (m/m)	Dec	--	-0.1	0.3

KEY POINTS:

- **Apart from Chinese equities, most markets shake off Trump's latest tariff missiles**
- **Trump resurrects tariff threat against China and Europe**
- **Light developments: NZ CPI, Negara, Lagarde on tap, Canadian PPI**
- **The US may be in a rush to renegotiate CUSMA/NAFTA 2.0…**
- **…but here's why Canada won't be**
- **Would the Great Canadian Oil Deal actually work?**

It's a very quiet start with little by way of new information to consider. Trump's renewed threat to impose tariffs on China and Europe is having little effect on markets outside of China. Stocks are broadly higher; tariffs lift prices and equity indices are in nominal terms so they won't react to greater tensions just yet, but evaluate forward returns in real terms. An exception is China where the main equity indices fell by around 1% or more with the Hang Seng off 1.6% on tariffs. Sovereign bonds are mostly treading water. The dollar is mixed but slightly weaker except versus CAD and the yen.

TRUMP RESURRECTS TARIFF THREAT ON CHINA, EUROPE

As noted last evening, Trump's daily dose of internet hubris had him saying:

> "We're talking about a tariff of 10% on China, based on the fact that they're sending fentanyl to Mexico and Canada," and indicated February 1st as the same target date that he mentioned for a 25% tariff on Canada and Mexico the day before.

And he also said:

> "Other countries are big abusers also, you know it's not just China. We have a $350 billion deficit with the European Union. They treat us very, very badly, so they're going to be in for tariffs."

Everybody's an abuser, everybody's unfair, especially toward Trump. Trump's logic for tariffs changes by the day. Fentanyl and migrants are ruses designed to create a national security issue in order to exploit two pieces of ancient legislation that give him authority to bypass Congress and impose tariffs. At the core is flawed logic that if you damage other countries, you will motivate stronger investment in the US while drawing upon a very, very baaaaad, horrible, worse than ever understanding of trade and economics. This US regime is intent on a more insular, protectionist, isolationist and autocratic approach to global relations.

Light Developments

Overnight developments were otherwise very light. The kiwi curve registered little reaction to mixed inflation readings for Q4. Bank Negara Malaysia held its policy rate unchanged at 3% as widely expected. SARB watchers got a lighter than expected inflation report with core CPI flat (0.2% m/m consensus) which tees up another possible cut next week.

ECB President Lagarde will speak at Davos before the caviar and champagne set (10:05amET). Read the room on the perils attached to being associated with that bunch. Her panel is titled "Beyond Crisis: Unlocking Europe's Potential." Now which crisis is that? Health or trade? Markets are priced for a cut on January 30th (one week from Thursday).

Canadian producer prices in December (8:30amET) don't much matter as they largely reflect currency and commodity movements without the translation into other inflation measures that happens in the US.

THE GREAT CANADIAN OIL SWAP WOULD PROBABLY BE A DUD

It's encouraging to see brain storming around how Canada can work with the US in the face of trade threats such that all proposals should be welcomed and evaluated on their own merits. It's also correct to try to exploit other means of working with the US before retaliating, though the window appears to be closing and retaliation has to be on the table.

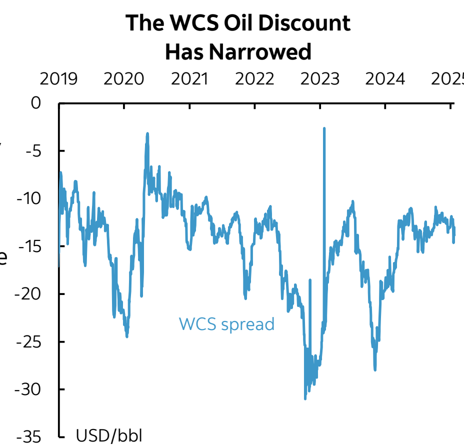
But among the proposals out there is to offer to export more Canadian heavy oil in order to allow the US to free up more of its light sweet oil in the pursuit of continental energy security. Would it fly as a means of signalling cooperation with Trump and avoiding tariffs? Count me skeptical.

First, how would that help the trade deficit, which is Trump's obsession? What would gush in on one side of the trade ledger would go out on the other side and therefore quite possibly cancel out the effects on the trade balance. Theoretically the effects are ambiguous and so Trump won't like that; it's not simple and straightforward enough to allow him to claim a victory on narrowing the trade deficit notwithstanding that I don't buy his logic and concerns in that regard in the first place.

Second, Trump says he needs nothing out of Canada. That's just nonsense of course, but he's intent on developing US energy independence by producing more domestically. He wants US energy independence. A swap that leaves the US net status on oil unchanged wouldn't be compatible with this quest.

Third, this proposal could increase US processing costs in parts of the oil supply chain. If it's heavy oil that Canada would export more of to the US, then that's more expensive to process than light sweet oil and involves higher transportation costs from northern Alberta and Saskatchewan. Hence the discount that flares at various times but is, say, in a $10–15 per barrel range when stable (chart 1). Processing costs for US needs would go up under this scenario in which the US economy relies more on heavy oil while sending light sweet oil abroad that is cheaper to process. Would the parts of the US energy supply chain that would have to pay those higher processing costs be equipped to do so, and willing to do so? Doubt it. Who would bear the costs?

Chart 1



Sources: Scotiabank Economics, Bloomberg.

Fourth, how would you export so much more oil to the US without more infrastructure that would take years and many headaches to put in place when there is no present appetite for doing so? Again, the tariff threat is now, not in the 2030s…

Fifth, exporting a lot more oil from Canada might lift CAD—all else equal—and stick the rest of Canadian industry—including within the energy provinces—with the competitiveness consequences at a fragile point for trade tensions.

Now, if Canada wants to export more oil, then great, there are ways to do it. Stop being our own worst enemy would be a start. Yesterday's signal that the Union of BC Indian Chiefs is reversing opposition to the Northern Gateway pipeline might be a start toward exporting more oil from the west coast to Asia and lessening dependence on the US, but it needs a lot of other steps to fall into place across other interest groups, governments and the private sector and would take years. Years, when the tariff threat is now. In the meantime, I guess the thank you note for the $35 billion taxpayer price tag for Trans Mountain got lost in the mail.

IT'S IN CANADA'S INTERESTS TO DIG IN AGAINST EARLY CUSMA NEGOTIATIONS

Recent reports seem to indicate that the Trump administration's plan is to impose tariffs on Canada up front, forcing the country into an early renegotiation of the CUSMA/NAFTA 2.0/USMCA trade deal before the middle of next year (**here**). The idea posits that tariffs will force Canada to bend to US demands, cry uncle, say sorry for ever thinking of standing up for Canadian interests, and hand over the keys to its automotive sector with unfavourable changes to the agreement.

Good luck, US politicians. For several reasons.

First, I would think we should expect a replay of the Canadian approach in NAFTA 2.0. During that round, Canada dug in against pressure to sign a potentially bad deal it would be stuck with for years or perhaps decades. It was perfectly willing to accept the short-term costs of greater tensions and uncertainty in favour of securing better longer-run terms. In the end, the strategy worked, and Trump caved by signing the best trade deal ever—that changed hardly anything from a Canadian standpoint. Canada has tools to leverage against the US if tariffs are applied and shouldn't be afraid of using them.

Second, politics might be in Canada's favour. That might sound tough to believe right now, but give it a bit of time and the shoe will be on the other foot. Ontario sounds like it's gearing up for an election call that could be held in February and which—if the polling is on the mark—could give Ontario Premier Ford another four years in office. A Canadian federal election seems likely in May and in my opinion is more uncertain than the current polls indicate, but either way there will be a fresh government. Whether it's a majority or a solid minority or a fragile minority is unclear as I always view polls as largely useless, but a period of political stability is likely to persist for some time. These two developments could lend more political patience to the negotiations on the Canadian side of the border than in the US that faces midterm elections next year for which campaigning will consume much of 2026.

Third, the starting US position that seeks freer and fairer automotive trade would be laughed at north of the border. Southern states siphoned off auto investment from the northern states and Canada through billions in subsidies to attract automotive plants over the years. Biden's electric vehicle subsidies threw billions at the sector, forcing Canada to spend billions of taxpayer money to counter. There is no trust toward US goals within a highly distorted playing field.

Fourth, autos mean Ontario. There are bits here and there elsewhere including feeder industries, but it's overwhelmingly an Ontario-based industry. There is no way the province gives that up or accepts a material dent without digging in for a protracted fight for the longer time. Autos and parts are Canada's second biggest export. In Ontario, autos are about 30% of all exports. The multiplier effects on related manufacturing activity takes the true dependency much higher. Premier Ford and the Feds have a lot of tools in their own toolkit and are sure to use them if things get nasty.

All of Trump's incoming cabinet will need to learn the lesson noted in the first point above from scratch all over again. Ask Lighthizer and Co. They'll remind you of how Canada sent Trump packing the first time. Dig in through to midterm campaigning and set the bar equally high against signing a bad deal for a long time. That could make it ugly in the short-term, but the bigger issue is how ugly you're comfortable with making it for the very long-term.

Fixed Income	Government Yield Curves (%):											
	2-YEAR			5-YEAR			10-YEAR			30-YEAR		
	Last	1-day	1-wk	Last	1-day	1-wk	Last	1-day	1-wk	Last	1-day	1-wk
U.S.	4.27	4.28	4.27	4.39	4.40	4.45	4.57	4.58	4.65	4.79	4.81	4.88
CANADA	2.93	2.93	3.03	2.99	2.99	3.14	3.26	3.26	3.42	3.39	3.39	3.53
GERMANY	2.21	2.22	2.26	2.31	2.32	2.37	2.50	2.51	2.56	2.73	2.73	2.79
JAPAN	0.70	0.68	0.71	0.88	0.86	0.90	1.20	1.19	1.26	2.26	2.27	2.36
U.K.	4.33	4.33	4.47	4.32	4.34	4.47	4.59	4.59	4.73	5.14	5.15	5.30
	Spreads vs. U.S. (bps):											
CANADA	-134	-135	-124	-140	-141	-131	-131	-131	-124	-140	-142	-135
GERMANY	-206	-206	-201	-208	-208	-208	-207	-207	-209	-206	-208	-209
JAPAN	-357	-360	-356	-351	-354	-355	-337	-338	-340	-253	-254	-252
U.K.	6	6	20	-7	-6	2	2	1	8	35	34	42

Equities	Level		% change:			
	Last	Change	1 Day	1-wk	1-mo	1-yr
S&P/TSX	25282	110.1	0.4	2.8	2.8	20.8
Dow 30	44026	538.0	1.2	4.1	2.8	15.9
S&P 500	6049	52.6	0.9	3.6	2.0	24.7
Nasdaq	19757	126.6	0.6	3.5	0.9	28.6
DAX	21301	259.2	1.2	3.5	7.1	27.7
FTSE	8566	17.9	0.2	3.2	6.0	14.4
Nikkei	39646	618.3	1.6	3.1	1.2	8.6
Hang Seng	19779	-327.8	-1.6	2.6	-0.5	28.8
CAC	7847	76.2	1.0	5.0	7.9	5.9

Commodities	Level		% change:			
WTI Crude	75.78	-0.05	-0.1	-2.2	9.1	0.8
Natural Gas	3.75	-0.00	-0.1	-5.4	0.1	55.1
Gold	2759.71	14.91	0.5	2.4	23.8	36.5
Silver	30.49	0.23	0.8	2.5	5.9	33.7
CRB Index	308.87	-2.21	-0.7	-0.0	5.7	15.7

Currencies	Level		% change:			
USDCAD	1.4342	0.0020	0.1	0.0	-0.2	6.4
EURUSD	1.0438	0.0010	0.1	1.4	0.3	-4.1
USDJPY	155.82	0.3000	0.2	-0.4	-0.9	5.2
AUDUSD	0.6286	0.0012	0.2	0.9	0.6	-4.3
GBPUSD	1.2356	0.0006	0.0	0.9	-1.4	-2.8
USDCHF	0.9049	-0.0011	-0.1	-0.8	0.7	4.1

Central Banks	
Current Rate	
Canada - BoC	3.25
US - Fed	4.50
England - BoE	4.75
Euro zone - ECB	3.15
Japan - BoJ	-0.10
Mexico - Banxico	10.00
Australia - RBA	4.35
New Zealand - RBNZ	4.25
Next Meeting Date	
Canada - BoC	Jan 29, 2025
US - Fed	Jan 29, 2025
England - BoE	Feb 06, 2025
Euro zone - ECB	Jan 30, 2025
Japan - BoJ	Dec 19, 2024
Mexico - Banxico	Feb 06, 2025
Australia - RBA	Feb 17, 2025
New Zealand - RBNZ	Feb 18, 2025