ON DECK FOR MONDAY, FEBRUARY 4

Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
US	02/04	10:00	Durable Goods Orders (m/m)	Nov F	--	1.5	0.8
US	02/04	10:00	Durable Goods Orders ex. Trans. (m/m)	Nov F	--	0.1	-0.3
US	02/04	10:00	Factory Orders (m/m)	Nov	0.5	0.3	-2.1
US	**02/04**	**19:30**	**Fed's Mester Discusses Economic Outlook and Monetary Policy**				

KEY POINTS:

- **Global markets off to a light start**
- **UK construction PMI falls more than expected**
- **China private composite PMI creeps closer to no growth**
- **Italian inflation weighing down Eurozone CPI**
- **US factory orders should post a small rise…**
- **…but this week's release schedule is very light…**
- **…while markets await release dates for GDP, PCE**
- **RBA under no pressure to signal action tonight**
- **Canada's household debt burden in seven charts**
- **Global Week Ahead**

Please see the Global Week Ahead — Trump & May Need A Little Help from Cupid (here). Key risks this week include:

- **POTUS's SOTUS**
- **CBs: BoE, RBA, RBI, Russia…**
- **…Banxico, Brazil, Peru, Philippines, Thailand**
- **Lunar New Year**
- **CPI: Italy, Russia, Turkey…**
- **…Mexico, Brazil, Colombia, Chile**
- **US funding talks**
- **Fed-speak**
- **CDN jobs, housing starts**
- **BoC's Lane**
- **US macro**
- **UK PMIs**
- **German macro**
- **Asian macro**
- **Earnings continued**
- **Debt auctions in US, Canada**

INTERNATIONAL

The trading week is off to a very quiet start with little by way of major market moves or calendar-based developments to consider. **That will heat up quickly**, not least of which because nine global central banks issue decisions and guidance this week while seven countries update CPI. **Stalemated Brexit negotiations** offer little hope of any sudden deal that achieves a more

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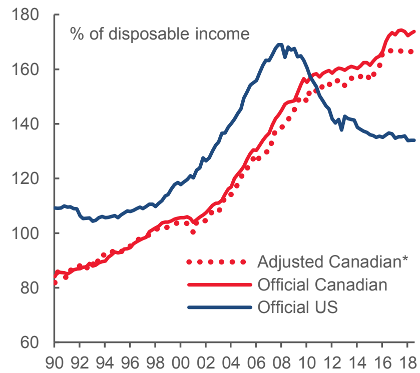
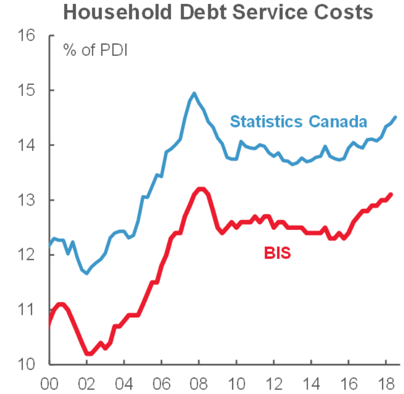
Household Debt



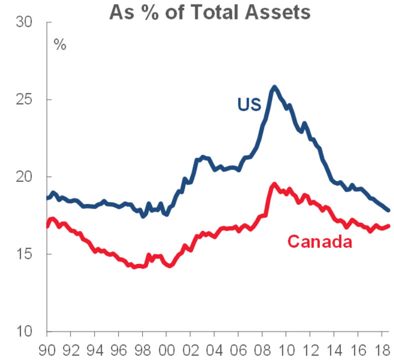
* Adjusted for US concepts and definitions.
Sources: Scotiabank Economics, BEA, Federal Reserve Board, Statistics Canada.

Household Debt Service Costs



Sources: Scotiabank Economics, BIS, Statistics Canada.

Total Household Liabilities As % of Total Assets



Sources: Scotiabank Economics, Federal Reserve Board, Statistics Canada.

satisfactory solution to the Irish border and will focus more upon exactly what to vote upon on Valentine's Day. Will Powell acknowledge improved markets plus positive data such as ISM-manufacturing and nonfarm when he speaks on Wednesday? **Trump;s SOTUS** will outline the usually heavily rhetorical wish list of remote prospects, most of which is to be ignored, but guidance regarding prospects for another shutdown at the end of next week may be material. **China goes quiet for the week** because of the Lunar New Year and with that we won't hear more about trade negotiations until next week's US high level entourage goes to China. **Canada should be mostly quiet until Friday's jobs report** but with a 2s auction, Lane and housing starts being modest highlights. Macro data is very light this morning. The Global Week Ahead is highlighted below.

- The USD is a touch stronger on a DXY basis, but the euro and CAD are slightly outperforming other crosses. The weakest crosses are the real, rand, A$ (ahead of RBA tonight, see below), some Scandies and yen.
- Sovereign bond yields are generally little changed with a mild cheapening bias. US Treasury yields are up by 1–2 bps across the curve. Canada's curve is flat. European bond yields are marked by slight spread widening in Italian and peripheral debt to bunds.
- US and Canadian equity futures are flat. European equities have a mild negative bias with ¼% to 1% declines in the Dax, CAC40, Spain and Italy while London is up by under ¼%. Asian equities saw the Nikkei rally ½%, HK up ¼%, but mainland China shut for the week and Seoul shut for much of the week for its own Lunar new year (Seollal).
- Oil prices are slightly lower by up to half a buck in the case of WTI.

The RBA is expected to hold its cash target rate at 1.5% tonight (10:30pmET). Neither headline inflation at 1.8% y/y nor the weighted median metric (1.7%) are pressuring the 2–3% inflation target range. Spillover effects from uncertainty through US-China trade negotiations also merit caution as do capital flow implications through currency connections to the Fed's 'patient' stance. Roughly one-third of economists including Scotia expect the RBA to raise rates this year.

The second of the monthly batch of UK purchasing managers indices further demonstrated softening growth momentum in the UK economy. The construction PMI fell to 50.6 (52.8 prior, 52.5 consensus) which is essentially on the bubble between expansion and contraction. This follows the greater than expected decline in the manufacturing PMI last Friday. Tomorrow's services PMI will round out the sector tracking with implications for GDP prospects but the last reading was barely above 50. Pound sterling largely shook it off as it had been depreciating into the figures on a morning of broad based dollar strength.

China's private PMIs signal an economy that is barely eking out growth and in contrast to GDP and alternative signals. The broad composite PMI fell to 50.9 (52.2 prior) and hence is barely above the 50 dividing line. The services PMI slipped a little but the contraction signal in the previously released manufacturing PMI is what weakened the composite reading.

Italian CPI fell to 0.9% y/y (1.2% prior). That reinforces the Eurozone estimate of 1.4% y/y released on Friday as Italy's recession is dragging down composite price pressures. By contrast to Italy, Germany and France are running at 1.4% y/y and Spain is at 1%.

UNITED STATES

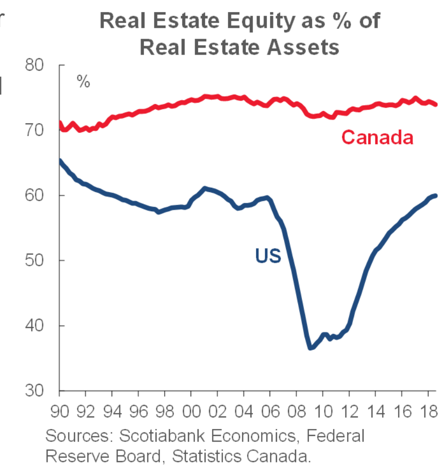
The US calendar is only focused upon factory orders for November today (10amET). Because we already know half of the report via the 0.8% jump in durables, we should see total orders expand at a soft pace upon inclusion of nondurable goods.

CANADA

Canada will be quiet pretty much until Friday's jobs report. Employment has been very strong and not only over the past four months during which 167,000 jobs were created, outshining the G10. In fact, since an inflection point in mid-2016 after which trend job growth accelerated, Canada has created a whopping 762,000 jobs and the trend is not slowing down.

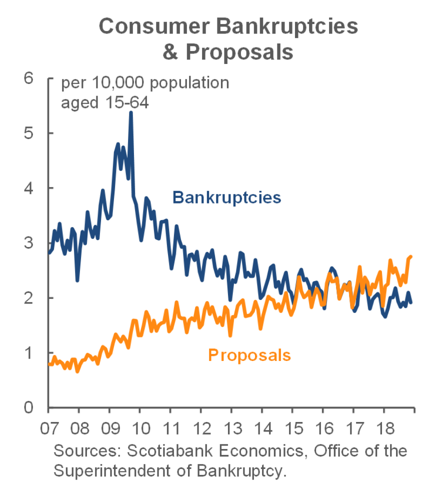
Which begs a few points about household finances that repeat the narrative I've offered for ages and that use the accompanying seven charts to do so. The broad conclusion to what follows is that emphasis upon risks is important, but the risks are often grossly exaggerated and at times through serious errors in the supporting facts.

- the first chart on page 1 shows a comparison of the US and Canadian household debt to income ratios when properly constructed. Statistics Canada makes comparability adjustments to the different ways in which the US and Canada measure not only debts but also incomes. A full explanation is available here. The result is the comparison between the red dotted line for Canada after comparability adjustments in order to make it methodologically similar to the US measurement. Canada's debt to income ratio remains a little below the US pre-crisis peak but elevated. It is certainly not leaps and bounds higher than the US peak as some would have one believe. In my view, it's a weak measure anyway that compares a stock of debt financed over much of one's lifetime to a flow of one year's income. There is nothing magical about a particular level of the debt-to-income ratio on its own that portends worries ahead versus many other considerations. Among those other considerations is how the broader financial heaps leverage through off balance sheet conduits (Canada does little of that) and how it funds the book (through generally more stable sources in Canada). Other considerations entail considering other measures below.



Sources: Scotiabank Economics, Federal Reserve Board, Statistics Canada.

- the second chart compares the debt service burden defined as debt payments including interest and principal as a share of disposable income. It's a better measure in that it compares flow to flow, ie: what's coming in through incomes versus what's going out through debt payments within an identical period. Two measures are shown, one being StatsCan's and the other being the Bank for International Settlements' metric that is part of a global data set made to be international comparable, or reasonably so. A glass half empty approach would involve flagging the upward trend over the past couple of years partly as rates have pushed higher. The glass half full approach would look at the scale and see it as an almost trivial movement.



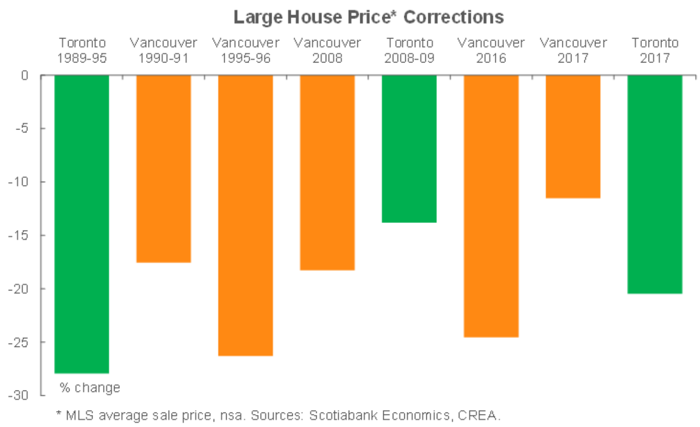
Sources: Scotiabank Economics, Office of the Superintendent of Bankruptcy.

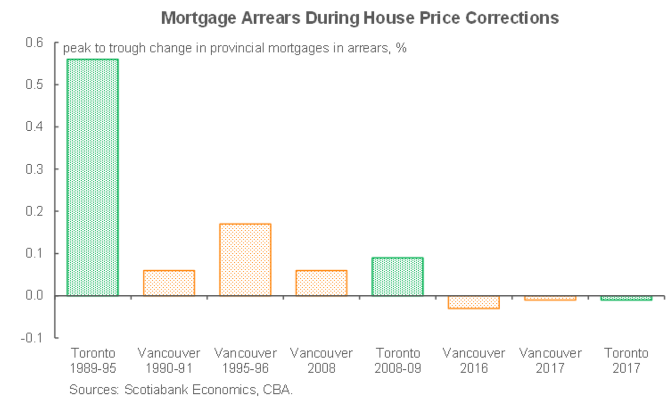
- The third chart shows debt as a percentage of assets. Canada's household balance sheet leverages up assets slightly less than the US now and much less than the US did at the peak of the US cycle. Part of the reason is that Canada generally doesn't offer mortgage interest deductibility that has long induced American households to vastly over-leverage on the back of the US Treasury (ie: other taxpayers).

- The fourth chart expands on this latter point by showing the massively higher home equity position of Canadian households. At the peak of the US cycle, US households had home equity equal to just over one-third of real estate assets they owned versus Canada that has been steady around three quarters on average. Clearly averages mask tails, but Canada's tails have also been generally better behaved than the US. In any event, it's hard to get a crisis when overall home equity is about double in Canada where it troughed in the US and considerably higher than where the US was before the crisis and hence around the mid-2000s.

- The fifth chart shows consumer bankruptcies versus proposals. Bankruptcies—whether in absolute terms or scaled to the population as the chart does—are at record lows. There has been a lot of erroneous commentary on this point with some pointing to rising insolvencies that include bankrupcies and proposals (more here). Proposals to restructure debt payments have been rising, but doing so for a long time even over periods when rates were falling. I believe proposals reflect the strength of the Canadian banking system in terms of averaging profitability over the full cycle. Strategic defaults and walking away or banks pulling the plug en masse generally haven't happened in Canada. The share of the population engaging in such proposals remains very low at 2–3 per 10,000 working age people, but swapping, say, a longer amortization for, say, lower payments is one way in which proposals for qualifying individuals can work out challenges.

- The sixth and seventh charts remind readers what happened during large house price declines in Toronto and Vancouver in the past. Even during large house price declines, like Toronto where prices fell by about one-third from 1989–1995, the 90 day mortgage delinquency rate popped higher by a relatively small 60bps. That's a fraction of what happened to the US in the GFC. Recall that everything that could go wrong went wrong in Canada and particularly Ontario during the early 1990s including recession, sky high rates, fiscal contraction, the FTA/NAFTA adjustments, mass job losses etc etc. Today's debt to income ratio is much higher than back then, but other leverage measures are not, and the broad macro backdrop remains night-and-day apart from the early 1990s conditions.





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.	2.52	2.50	2.59	2.52	2.50	2.58	2.70	2.69	2.75	3.04	3.03	3.07
CANADA	1.83	1.83	1.87	1.86	1.86	1.88	1.96	1.96	1.96	2.19	2.18	2.18
GERMANY	-0.57	-0.58	-0.58	-0.31	-0.32	-0.29	0.17	0.17	0.21	0.77	0.78	0.80
JAPAN	-0.17	-0.17	-0.16	-0.17	-0.17	-0.16	-0.01	-0.01	0.00	0.61	0.61	0.65
U.K.	0.78	0.77	0.77	0.90	0.89	0.91	1.26	1.25	1.27	1.76	1.75	1.75
	Spreads vs. U.S. (bps):											
CANADA	-69	-67	-72	-66	-65	-70	-74	-73	-78	-85	-84	-89
GERMANY	-309	-309	-317	-283	-282	-287	-253	-252	-254	-227	-225	-226
JAPAN	-269	-268	-275	-269	-268	-274	-271	-270	-274	-243	-242	-241
U.K.	-174	-173	-182	-162	-161	-167	-145	-144	-148	-128	-128	-132

Equities	Level		% change:			
	Last	Change	1 Day	1-wk	1-mo	1-yr
S&P/TSX	15506	-34.3	-0.2	0.9	7.5	-0.6
Dow 30	25064	64.2	0.3	1.3	7.0	-1.8
S&P 500	2707	2.4	0.1	1.6	6.9	-2.0
Nasdaq	7264	-17.9	-0.2	1.4	7.8	0.3
DAX	11147	-33.6	-0.3	-0.6	3.5	-12.8
FTSE	7034	13.8	0.2	4.3	2.9	-5.5
Nikkei	20884	95.4	0.5	1.1	6.8	-10.3
Hang Seng	27990	59.5	0.2	1.5	9.2	-14.1
CAC	4987	-32.6	-0.6	2.0	5.3	-7.1
Commodities	Level		% change:			
WTI Crude	54.76	-0.50	-0.9	5.3	14.2	-16.3
Natural Gas	2.69	-0.04	-1.6	-7.6	-11.6	-5.4
Gold	1311.53	-6.12	-0.5	0.6	2.1	-1.6
Silver	16.01	-0.07	-0.4	4.1	3.5	-6.9
CRB Index	179.68	-0.87	-0.5	1.2	3.7	-9.0
Currencies	Level		% change:			
USDCAD	1.3117	0.0015	0.1	-1.1	-1.9	4.6
EURUSD	1.1448	-0.0008	-0.1	0.2	0.5	-7.4
USDJPY	109.95	0.4500	0.4	0.5	1.3	0.8
AUDUSD	0.7219	-0.0031	-0.4	0.7	1.5	-8.4
GBPUSD	1.3054	-0.0025	-0.2	-0.8	2.6	-6.5
USDCHF	0.9975	0.0019	0.2	0.6	1.0	7.1

Central Banks	
Current Rate	
Canada - BoC	1.75
US - Fed	2.50
England - BoE	0.75
Euro zone - ECB	0.00
Japan - BoJ	-0.10
Mexico - Banxico	8.25
Australia - RBA	1.50
New Zealand - RBNZ	1.75
Next Meeting Date	
Canada - BoC	Mar 06, 2019
US - Fed	Mar 20, 2019
England - BoE	Feb 07, 2019
Euro zone - ECB	Mar 07, 2019
Japan - BoJ	Mar 15, 2019
Mexico - Banxico	Feb 07, 2019
Australia - RBA	Feb 04, 2019
New Zealand - RBNZ	Feb 12, 2019

Source: Bloomberg. All quotes reflect Bloomberg data as at the time of publishing. While this source is believed to be reliable, Scotiabank cannot guarantee its accuracy.