

**ON DECK FOR FRIDAY, MARCH 29**

Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
CA	03/29	08:30	IPPI (m/m)	Feb	--	--	-0.3
CA	03/29	08:30	Raw Materials Price Index (m/m)	Feb	--	--	3.8
CA	03/29	08:30	Real GDP (m/m)	Jan	0.2	0.1	-0.1
US	03/29	08:30	PCE Deflator (m/m)	Jan	0.0	0.0	0.1
US	03/29	08:30	PCE Deflator (y/y)	Jan	1.4	1.4	1.7
US	03/29	08:30	PCE ex. Food & Energy (m/m)	Jan	0.2	0.2	0.2
US	03/29	08:30	PCE ex. Food & Energy (y/y)	Jan	1.9	1.9	1.9
US	03/29	08:30	Personal Spending (m/m)	Feb	0.3	0.3	-0.5
US	03/29	08:30	Personal Income (m/m)	Feb	0.3	0.3	-0.1
US	03/29	10:00	New Home Sales (000s a.r.)	Feb	625	619.5	607.0
US	03/29	10:00	U. of Michigan Consumer Sentiment	Mar F	--	97.8	97.8
US	03/29	12:45	Fed's Quarles Speaks in New York				

**CONTACTS**

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

**KEY POINTS:**

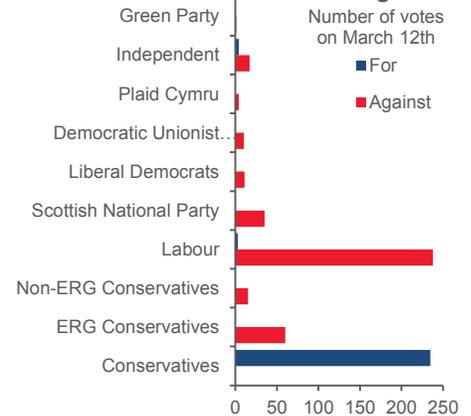
- Risk-on to end the week, but ahead of key US data
- US and China fine-tuning a trade agreement?
- Fed-speak pours cold water on 'premature' cuts...
- ...while laying out the conditionality
- Brexit vote appears doomed to fail. Again!
- Canadian GDP on tap
- US core PCE inflation still resilient?
- US consumption set to rise into the new year?
- French, Italian CPI point to softer headline Eurozone inflation
- Chile's CB expected to stay on hold
- US new home sales poised to rebound?
- German consumers roaring back in Q1

**INTERNATIONAL**

It's risk-on across global markets so far this morning but ahead of key US and Canadian macro data. Evidence that **US and Chinese negotiators are pouring over the details of an emerging trade agreement** was welcomed by Chinese equity markets with spillover effects elsewhere. **Today's Brexit vote (see below) is expected to fail again.** The Fed's preferred inflation gauge as well as consumer spending and incomes are on tap for updates. How **Canada's economy** entered 2019 will be informed by GDP for January. Also pay key attention to **efforts by voting FOMC members to push back on rate cut talk** and lay out the conditional nature of such expectations while inferring that such conditions have as yet not been achieved (see below).

- The USD is little changed but slightly depreciating this morning. Pound sterling is among the leading appreciating crosses along with the A\$/NZ\$ and some Scandies. CAD is appreciating a little ahead of GDP while the Euro is little changed but up and the yen is depreciating a touch.

**May's Brexit 3.0 Needs More Than The ERG To Swing**



Sources: Scotiabank Economics.

- Sovereign curves are cheaper across the major markets. US Treasury yields are up by 2–3bps from 2s through 10s and a little less at the long end. Canada's curve is up by about 2bps across maturities. Gilts, bunds and French bonds are comparably cheaper.
- Oil prices are up by about 75 cents in terms of WTI (just over US\$60) and Brent (US\$68 ½). Western Canada Select was US\$50.05 yesterday and may face upside in line with global benchmarks this morning.
- Stocks are higher everywhere. US equity futures are up by about ½% and TSX futures are up by about ¼%. European cash markets are up by about ¾%. Mainland China ripped higher with stocks up by over 3% while the Nikkei gained about ¾%, Seoul was up 0.6% and the Hang Seng was up by 1%.

**The vote on just the withdrawal portion of PM May's Brexit agreement will occur at about 10:30amET.** Speaker John Bercow rejected the three proposed amendments so this one will be a clean and relatively quick vote. If the vote passes, then the Brexit deadline is delayed until May 22<sup>nd</sup> and they would then have to vote on what's next after exit (the other part of May's agreement with the EU that is being temporarily shelved today). If it fails—which seems likely given opposition from Labour and the DUP and waffling among ERG members—then some alternative must be explored possibly including a long delay or hard Brexit. See the repeated chart for the breakdown of the last vote on May's agreement for purposes of illustrating the formidable math that today's vote is up against. Throughout it all, a Conservative leadership contest and possible general election loom such that the fun may only just be beginning.

Tangential matters to trade talks, Brexit and top shelf US and Canadian releases include the following:

- an **expected hold by Chile's central bank** after the NA market close (5pmET);
- a wave of Japanese indicators that signaled strong industrial output growth (+1.4% m/m in February) and softer than expected retail sales (+0.2%).
- German consumers posted a second consecutive strong gain in retail sales volumes that were up 0.9% in February after a 2.8% rise in January which combines to recover the 3% loss in December.
- French consumers, however, retrenched by 0.4% in February but in that case it followed a large upwardly revised 1.4% rise the prior month.
- Eurozone CPI will be released on Monday, but softer Italian and French figures reinforce softer headline inflation out of Germany the other day by contrast to a rise in Spain.

## UNITED STATES

**Fed officials are laying out the criteria for a rate cut and generally indicating they have not been met as of yet.** We heard some of that from speakers like Dallas Fed President Kaplan the other day and more of it since then. In particular, St. Louis Fed President Bullard (voting 2019) said the following last evening:

“It would be premature to contemplate a rate cut here. You do want to watch the data closely. Most likely the economy will be stronger in the second quarter. You won't know that until the July time frame. I would expect faster growth in the second half of 2019. I still think we are in reasonably good shape.”

On the yield curve, Bullard went on to say:

“I think you would have to get a wider variety of spreads inverted, the 2-year/10-year particularly, and it would have to stay inverted awhile to send a negative signal.”

This follows on the heels of a speech by the Fed's #2, Richard Clarida, yesterday morning ([here](#)). In that speech, Clarida basically laid out the criteria for a rate cut as driven by an external shock but without concluding that such criteria have been achieved. He noted that the Fed has eased—one way or another—during many past externally driven shocks to the global economy and

markets such as the Tequila Crisis in 94–95, the Russian default and collapse of LTCM in 1998, the Eurozone recession in 2011–13 and China's blundered devaluation in 2015. The way he ended his speech was to offer the strong inference that if current global risks evolve negatively, the Fed will likely have to ease again. In fact, his conclusion is the clearest wording yet on the Fed's focus upon global risks that are—in my opinion—still best treated as binary in nature. In fact, you could narrow his three down to two things on their minds since slower global growth in no small part reflects uncertainty surrounding the other two (Brexit, trade tensions).

"Let me conclude with some remarks on recent developments. U.S. and other financial markets are attuned to a number of prominent downside global risks, which include Brexit, a sharp slowdown in global growth prospects, and trade tensions. Even though the Fed has been and is committed to a dual mandate to achieve maximum employment and price stability, in today's world, U.S. policymakers can hardly ignore these risks, and three of our most recent FOMC statements have highlighted concerns about global economic and financial developments. In addition, in our policy statements, as well as in other communications, we have indicated that, in the presence of these risks and with inflation pressures muted, we can afford to be patient and data dependent as we assess in future meetings what adjustments in our policy rate might be necessary to sustain growth, employment, and price stability in the U.S. economy."

Some of this quote is somewhat charitable to the Fed. It's not as if the Brexit deadline hasn't been known for ages or the US-China trade tiff hasn't been evolving for about a year or that the US debt ceiling would be reinstated at the beginning of this month. The Fed knew all of that information on risks and yet kept hiking right up to December and with Chair Powell's references last Fall to still being a long way from neutral with the balance sheet on auto-pilot. Let's not practice revisionism toward the sudden shift in the Fed's reaction function here!

Nevertheless, the point to Clarida's speech in my opinion was to appropriately flag the external criteria for easing and saying they haven't been achieved. In my opinion, the market has gone to a very dark place in pricing fed funds futures with half a cut priced by late Summer and three quarters of a cut by year-end. The fed funds futures market and Treasury curve is saying they know with abject certainty that the risks to the global economy will turn out negatively in destabilizing fashion. We don't know that. Brexit could still go either direction with the likely scenario being prolonged uncertainty or a state of purgatory over a big bang. Trade talks with China could well evolve constructively whatever the wishes of USTR Lighthizer and Navarro as the President faces a re-election bid and one doesn't one elections pursuing policies that trash the stock market and economy. We saw this President essentially cave in NAFTA and KORUS talks. Ditto for the debt ceiling as the surest way to lose an election is to risk default.

In all, the rate cut pricing in markets has been assuming one side of that distribution of binary risks without a whole lot of obvious evidence to go by. It's the most crowded trade in markets these days with global bond PMs all sheepishly piling into the front-end. Yes economists have been known to be wrong—but assuming markets are right is often sheer folly. In any event, the Fed has already arguably provided policy accommodation through removing a hike from its dot plot this year and padding the balance sheet to a greater extent than arguably required in shift toward a risk management approach that has superseded what should still be fair debate over how to optimize normalization.

The US updates several key readings on inflation and activity measures this morning. They include:

- **PCE inflation:** Headline inflation is expected to pull back in sympathy to what we already learned in the previously released CPI figure on March 12<sup>th</sup>. My estimate matches consensus at 1.4% y/y (1.7% prior);
- **Core PCE inflation:** The Fed wouldn't care about a deceleration in headline PCE if core PCE is resilient. That's the expectation for today with consensus at 1.9% y/y and unchanged from the prior month. Bear in mind, however, that core CPI slipped a tick to 2.1% (2.2% prior) but also bear in mind the large differences in methodology between CPI and PCE.
- **Consumption:** a decent rise of 0.3% m/m is expected after a large 0.5% drop in December. We already know that retail sales grew by a fairly mild 0.2% in January but what matters in the retail report for purposes of estimating total consumption is not the headline but rather the control group reading which was up strongly in January (+1.1%).
- **US new home sales** (10amET) are expected to rebound but in large part only because they tanked by 6.9% m/m in January.

**CANADA**

**Canada releases January GDP this morning (8:30amET).** Estimates are all over the map on this one with a median expectation for a 0.1% m/m rise. At the consensus low-end is a -0.2% contraction and at the high end is a 0.3% gain. I'm at 0.2%. The economy slipped by -0.1% in December and this offers an easier jumping off point for growth. I run a simple regression model against the higher frequency readings we have to date and if I let it speak unfiltered then it spits out 0.3% growth. That was tamped down a bit in the final estimate because of the effects of considerations such as Alberta's mandated oil production cuts. Among the mixed drivers are a 1.4% rise in manufacturing shipment volumes, a 0.7% lift to wholesale volumes, and a strong gain in imports that may signal domestic strengths. To the downside were a decline in housing starts (-2.8%), a drop in hours worked (-0.3%) and flat retail volumes. There were other considerations as well that are not as easily measured such as how it may be unlikely to see continued retrenchment in utilities output after a large 2% decline in December.

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.	2.26	2.24	2.32	2.24	2.22	2.24	2.42	2.40	2.44	2.83	2.82	2.87	Canada - BoC	1.75
CANADA	1.51	1.49	1.53	1.49	1.46	1.48	1.58	1.56	1.60	1.88	1.86	1.89	US - Fed	2.50
GERMANY	-0.59	-0.59	-0.57	-0.43	-0.44	-0.40	-0.05	-0.07	-0.02	0.58	0.55	0.60	England - BoE	0.75
JAPAN	-0.17	-0.18	-0.17	-0.20	-0.19	-0.19	-0.08	-0.09	-0.07	0.51	0.50	0.53		
U.K.	0.67	0.66	0.66	0.79	0.77	0.78	1.02	1.00	1.01	1.56	1.54	1.49		
	Spreads vs. U.S. (bps):													
CANADA	-76	-75	-79	-76	-76	-76	-84	-84	-85	-96	-97	-98	Euro zone - ECB	0.00
GERMANY	-286	-283	-288	-267	-265	-264	-248	-247	-246	-226	-227	-227	Japan - BoJ	-0.10
JAPAN	-243	-241	-249	-244	-241	-243	-250	-249	-251	-233	-233	-235		
U.K.	-159	-158	-166	-145	-144	-146	-140	-140	-143	-128	-129	-139	Mexico - Banxico	8.25
Equities	Level		Change		1 Day		1-wk		1-mo		1-yr			
S&P/TSX	16155		23.0		0.1	-0.5	1.0	5.1					Australia - RBA	1.50
Dow 30	25717		91.9		0.4	-0.9	-0.8	6.7					New Zealand - RBNZ	1.75
S&P 500	2815		10.1		0.4	-1.4	1.1	6.6						
Nasdaq	7669		25.8		0.3	-2.2	1.8	8.6						
DAX	11534		105.6		0.9	1.5	0.2	-4.7						
FTSE	7261		26.9		0.4	0.7	2.6	2.9						
Nikkei	21206		172.1		0.8	-1.9	-0.8	0.2					Canada - BoC	Apr 24, 2019
Hang Seng	29051		276.2		1.0	-0.2	1.5	-3.5					US - Fed	May 01, 2019
CAC	5344		47.6		0.9	1.4	2.0	3.4						
Commodities	Level		Change		1 Day		1-wk		1-mo		1-yr			
WTI Crude	60.15		0.85		1.4	1.9	5.1	-7.4					England - BoE	May 02, 2019
Natural Gas	2.70		-0.01		-0.4	-1.9	-3.9	-1.2					Euro zone - ECB	Apr 10, 2019
Gold	1293.82		3.40		0.3	-1.5	-1.5	-2.4					Japan - BoJ	Apr 25, 2019
Silver	15.20		-0.21		-1.3	-2.2	-3.9	-7.7						
CRB Index	184.54		1.21		0.7	0.2	1.0	-5.5						
Currencies	Level		Change		1 Day		1-wk		1-mo		1-yr			
USDCAD	1.3413		-0.0025		-0.2	-0.1	1.8	4.1					Mexico - Banxico	May 16, 2019
EURUSD	1.1231		0.0010		0.1	-0.6	-1.2	-8.7					Australia - RBA	Apr 01, 2019
USDJPY	110.75		0.1200		0.1	0.8	-0.6	4.1						
AUDUSD	0.7094		0.0020		0.3	0.2	0.0	-7.6						
GBPUSD	1.3107		0.0063		0.5	-0.8	-1.2	-6.5					New Zealand - RBNZ	May 07, 2019
USDCHF	0.9958		0.0002		0.0	0.2	-0.2	4.1						

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.

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