ON DECK FOR FRIDAY, MAY 17

Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
US	05/17	10:00	Leading Indicators (m/m)	Apr	--	0.2	0.4
US	05/17	10:00	U. of Michigan Consumer Sentiment	May P	98	97	97
US	05/17	11:15	Fed's Williams Meets With Community Leaders	--	--	--	--

KEY POINTS:

- **Risk-off as China douses restarting negotiations**
- **China's government heats up rhetoric in clandestine fashion…**
- **…through a 'WeChat' social media account**
- **PBOC signals easing, targets yuan stability**
- **Trump launches auto talks, delays tariff decision by 180+ days**
- **BoC's Poloz interviews today**
- **Eurozone 'supercore' CPI on a rising trend**
- **US UofM sentiment: watch inflation expectations**
- **Fed-speak: Clarida, Williams**
- **Canada's bond market shuts early today**

INTERNATIONAL

Global markets are in gentle risk-off mode after aggressive trade rhetoric out of China overnight, albeit communicated in somewhat clandestine fashion. **Taoran Notes—an anonymous social media account on Tencent's WeChat service—issued commentary that doused prospects for restarting trade negotiations with the US.** No doubt Trump's Huawei ban yesterday helped to escalate the rhetoric. While obscure, Taoran Notes has recently generated a following because a) it is **thought to be controlled by the government** which is because b) it is one of the rare voices that has not been censored on Chinese social media, and c) because what it says tends to get re-printed by China's anything-but-free press such as the People's Daily that re-ran the post. Who authors the posts is unknown but it is clear that there is a high level government connection. The post said "If there is no real concrete action by the United States, it will be meaningless for you to come and talk" and "It is better to suspend the consultation completely and return to normal working track" and also noted that the US "keeps using petty tricks to destroy the atmosphere for talks." My personal view remains that the US poisoned the well in the talks more than it has let on by insisting upon maintaining tariffs even in the wake of an agreement like it did with steel and aluminum tariffs following the USMCA/CUSMA deal. Neither party is innocent, but retaining tariffs post-agreement is unprecedented and lessens market faith in what are the true goals of the Trump administration.

Comments from the PBOC set a ceiling on yuan depreciation amid limited appetite for policy easing (see below). **The White House announced this morning that USTR Lighthizer has been directed to launch auto sector trade negotiations** with the EU and Japan and report back in six months time while postponing a decision on tariffs until at least six months from now.

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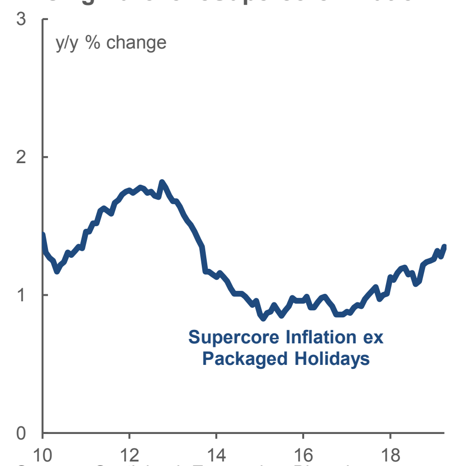
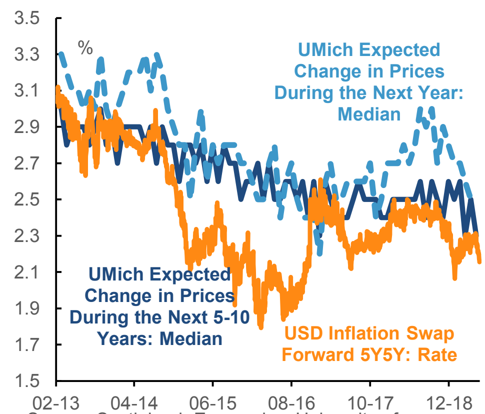
Rising EurozoneSupercore Inflation



Sources: Scotiabank Economics, Bloomberg.

Falling Inflation Expectations - But No Crisis Yet



Source: Scotiabank Economics, University of Michigan,Bloomberg.

Other developments are comparatively light including **higher Eurozone core and supercore inflation** (see below), **media interviews by Governor Poloz** (see below) and an update on **US consumer confidence including measures of inflation expectations that the Fed has indicated are among the gauges it is closely watching** (see below). Also be on guard for Trump's auto tariff decision which has to be delivered by Saturday at the latest even if he just confirms delaying it all.

- **Safe haven currencies are in vogue again.** The USD is gaining against most crosses and especially pound sterling (Brexit, what else), the rand (global trade concerns), and with the Mexican peso and CAD depreciating not that far behind despite higher oil prices. The yen is appreciating against all of them and the Swiss franc against most.

- **Sovereign bond yields are falling again.** The US 10 year note is now at 2.37%, down 2bps in a parallel downward shift across the curve. Canada's curve is performing similarly with the 10 year yield down 3bps to 1.65%. Fixed mortgage rate borrowers and the Spring Canadian and US housing markets are rejoicing. Even Italian debt is rallying! Gilts are outperforming all of them in a bull flattener that has the 10 year down 6bps to an even 1%.

- Oil prices are up by 30–50 cents on middle east tensions again.

- **US equity futures are selling off** by between ¾% and 1% across the exchanges. TSX futures are down by about ½%. European cash markets are down by between ½% and just over 1%. Asian equities were mixed. Anything with China in it sold off, including the Shanghai (-2.5%), Shenzhen (-3 ¼%) and HK (-1.2%) exchanges. But Tokyo was loving it with the Nikkei up by about 1% as Seoul fell ½% and the Sensex was up by 1½%.

The **People's Bank of China** delivered its quarterly report on Monetary Policy Implementation this morning and commented that it plans to deliver 'targeted' cuts to the required reserve ratio alongside yuan stability while maintaining 'prudent' monetary policy. This indicates limited appetite for policy easing and cognizance toward the risks of destabilizing the currency. This followed anonymous sources saying to Reuters that 7 is the magic number for the yuan-dollar cross in that the PBOC will intervene if the currency crosses this mark.

Eurozone core inflation was revised up a tick to 1.3% on the second pass at the figures, but more important is that we now have the detail necessary to strip out the reasons why. There had been the view that perhaps the shifting timing of the annual Easter holiday motivated stronger core prices this year versus prior years because Easter was later than usual this year. That would have pumped travel related categories like packaged holiday prices higher in year-ago terms during April of this year versus last year when Easter was earlier. That's not so much the case. There was a partial Easter effect, but even core CPI excluding packaged holiday prices picked up slightly again (see chart). This 'supercore' measure has been on an upswing since early 2017, but only from about 0.9% y/y then to 1.35% now. Still, **the trend is definitely showing progress toward the ECB's 'under 2%' inflation target.**

UNITED STATES

We'll get an update on US consumer confidence through the University of Michigan's widely followed consumer sentiment gauge for May (10amET). In the current Fed context that is focused upon measures of inflation expectations, **the 1 year and 5 year ahead measures may be worth peeking at**. In April, they were still riding at 2.5% and 2.3% respectively (see chart) but they've fallen over the long term and that's why Clarida said the Fed are watching them. As yet, however, both gauges remain over 2% and so the decline relative to the Fed's 2% target is not alarming as of yet alongside the decline in market-based measures like the 5y5y inflation swap also shown on the chart. Personally, I'm convinced that these measures are the bees knees as far as inflation gauges go; market-based measures tend to correlate with current spot oil prices versus saying much about what is truly expected to happen to inflation. It's also possible that consumer based expectations have fallen because they were simply ridiculously too high over many prior years and the way in which such views are communicated in surveys by consumers leaves an evidence-based approach somewhat wanting. Clarida will get a chance to possibly remark on this later in the day along with NY Fed President Williams who speaks twice at 11:15amET and 2pmET.

CANADA

BoC Governor Poloz is delivering media interviews today and his comments will appear in dribs and drabs until a full-on one-on-one interview is aired on BNN at 1pmET. Clips from interviews have been running on BNN/Bloomberg tv in which **Poloz said he would “frown upon” loosening mortgage rules including B20, that a 20% drop in home prices is “conceivable” and that he thinks homeowners are “mentally prepared” for this risk.** When combined with his remarks yesterday, he has nevertheless stated that **his base case view** is that froth is coming out of markets like Vancouver’s and that he remains of the view that housing and credit markets will return to growth over the year.

Canada’s bond market shuts at 1pmET ahead of the long weekend.

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.	2.17	2.19	2.27	2.15	2.17	2.26	2.37	2.40	2.47	2.81	2.83	2.89
CANADA	1.57	1.58	1.64	1.53	1.56	1.61	1.65	1.68	1.73	1.89	1.91	1.96
GERMANY	-0.65	-0.65	-0.62	-0.52	-0.51	-0.47	-0.12	-0.10	-0.05	0.53	0.54	0.61
JAPAN	-0.16	-0.16	-0.16	-0.16	-0.17	-0.16	-0.05	-0.06	-0.05	0.53	0.52	0.54
U.K.	0.68	0.72	0.74	0.78	0.82	0.86	1.02	1.07	1.14	1.57	1.62	1.68
	Spreads vs. U.S. (bps):											
CANADA	-60	-61	-63	-61	-61	-65	-72	-72	-74	-93	-92	-93
GERMANY	-282	-284	-288	-267	-268	-273	-249	-249	-251	-229	-229	-228
JAPAN	-233	-235	-243	-231	-234	-243	-242	-246	-252	-228	-232	-235
U.K.	-149	-147	-153	-137	-135	-140	-135	-132	-133	-124	-121	-121

Equities	Level		% change:			
	Last	Change	1 Day	1-wk	1-mo	1-yr
S&P/TSX	16444	125.7	0.8	0.7	-0.6	1.9
Dow 30	25863	214.7	0.8	0.1	-2.2	4.6
S&P 500	2876	25.4	0.9	0.2	-0.8	5.7
Nasdaq	7898	75.9	1.0	-0.2	-1.2	7.0
DAX	12156	-154.6	-1.3	0.8	0.0	-7.3
FTSE	7312	-41.1	-0.6	1.5	-2.1	-6.1
Nikkei	21250	187.1	0.9	-0.4	-4.6	-7.0
Hang Seng	27946	-328.6	-1.2	-1.3	-7.2	-9.7
CAC	5404	-44.4	-0.8	1.4	-2.9	-3.9
Commodities	Level		% change:			
WTI Crude	63.36	0.49	0.8	2.8	-0.6	-11.4
Natural Gas	2.65	0.01	0.5	1.3	5.4	-7.2
Gold	1283.85	-2.85	-0.2	-0.2	0.8	-0.5
Silver	14.80	-0.02	-0.1	-0.2	-1.0	-9.0
CRB Index	182.10	-0.23	-0.1	1.8	-2.4	-10.5
Currencies	Level		% change:			
USDCAD	1.3496	0.0036	0.3	0.6	1.2	5.4
EURUSD	1.1179	0.0005	0.0	-0.5	-1.0	-5.2
USDJPY	109.65	-0.2000	-0.2	-0.3	-2.2	-1.0
AUDUSD	0.6885	-0.0007	-0.1	-1.7	-4.1	-8.3
GBPUSD	1.2758	-0.0040	-0.3	-1.8	-2.2	-5.6
USDCHF	1.0102	0.0002	0.0	-0.2	-0.0	0.9

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	1.50
Next Meeting Date	
Canada - BoC	May 29, 2019
US - Fed	Jun 19, 2019
England - BoE	Jun 20, 2019
Euro zone - ECB	Jun 06, 2019
Japan - BoJ	Jun 20, 2019
Mexico - Banxico	Jun 27, 2019
Australia - RBA	Jun 04, 2019
New Zealand - RBNZ	Jun 25, 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.

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