

ON DECK FOR TUESDAY, MAY 28

Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
US	05/28	09:00	S&P/Case-Shiller Home Price Index (m/m)	Mar	0.4	0.5	0.2
US	05/28	09:00	S&P/Case-Shiller Home Price Index (y/y)	Mar	2.4	2.6	3.0
US	05/28	10:00	Consumer Confidence Index	May	129	130.0	129.2
US	05/28	10:30	Dallas Fed. Manufacturing Activity	May	--	5.8	2.0

KEY POINTS:

- Markets divided on Italy, Brexit and US protectionism
- Italian debt spreads continue to rise...
- ...as the bond market punishes militant fiscal talk...
- ...by the strengthened League
- Trump's voter support is waning again...
- ...but it's not yet moderating his protectionism
- Slightly improve Eurozone confidence is likely noise
- US: consumer confidence, home prices...
- ...and a good day to auction more debt
- Canada quiet

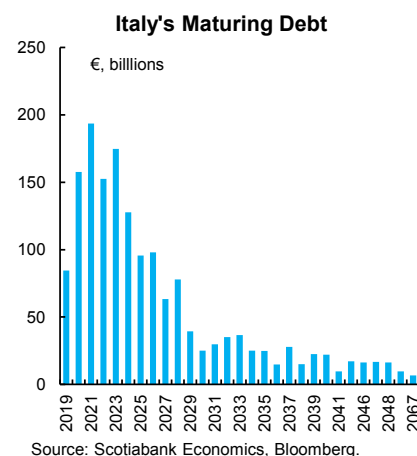
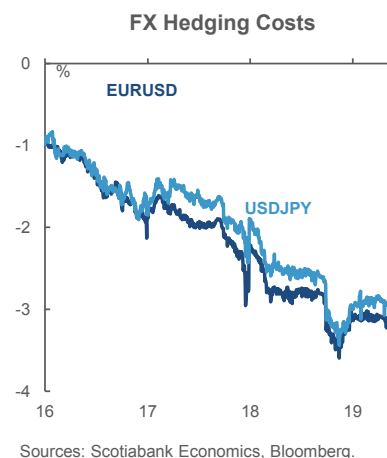
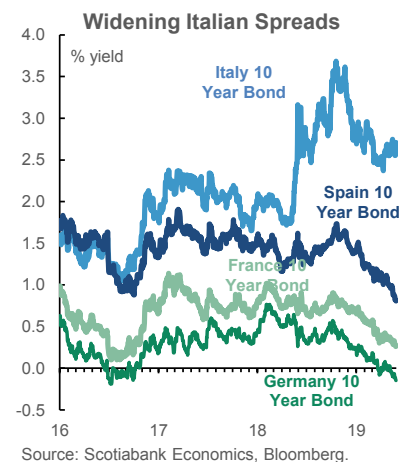
INTERNATIONAL

A mild risk-off session is underway across global markets as NY and London return to work. Pick your catalyst as each of the deterioration in US-China trade tensions, prolonged Brexit uncertainty and the return of Italian fiscal policy concerns are all plausible candidates (see below). Amidst the risk-off sentiment are automatic stabilizers such as the bond market effect in bringing the 30 year US mortgage rate down to its lowest since the start of last year (4%, from a peak of 4.8% last November). What little incremental risk lies on the formal calendars is focused upon the US today with some data risk and auctions (see below).

- Equity markets are mixed as American and British PMs return to work. European cash markets range from being flat in Paris and Frankfurt, up by about ¼% in London, and down by about ½% in Milan. Asian equities rallied overnight by between ¼% (Seoul) and ½% (Shenzhen). US and Canadian equity futures are roughly flat after clawing back mild earlier losses.
- Yields on US Treasuries and gilts are lower across the curves. Treasuries are marked by a mild bull flattener that has the 10 year yield down 3bps to 2.29% and well timed for the US Treasury to foist more of the stuff onto markets today. Canadas are underperforming but our traders note that this is because Canadas rallied yesterday when the Treasury market was shut. Italian debt spreads continue to widen over bunds with the 10 year Italian yield up 3bps to 2.70% and the 10 year bund unchanged at -15bps (see chart). That's the lowest 10 year bund yield since September 2016 and we used to use that as a gauge of Euro-centric risks including the extreme break-up concerns around the Greek crisis. Europe's challenges are dragging US Treasury yields lower through the attractive carry and modest improvement in FX hedging costs this year versus late last year (second chart).

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- Oil prices are mixed with Brent flat and WTI up 40 cents. We'll get private weekly US oil inventories this afternoon ahead of tomorrow's government report.
- The USD is flat on a DXY basis with little movement against the majors. The yen, A\$ and some scandies are a little firmer. CAD, the Mexican peso and rand are all depreciating. The euro and pound sterling are little changed.

Italian debt spreads over the rest of core Europe continue to widen (see chart 1 again) and escalating tensions between an emboldened Italian government and Brussels are responsible. The League Party (formerly "Northern League")—that has its roots in xenophobic policies—scored significant gains in the European parliamentary elections. The League's support increased to 34.4% and when combined with the Five Star's 17% support, the coalition government has the support of 51% of voters but the coalition has been weakened by speculation the League is seeking concessions if not early elections. Italy has a debt maturity profile that is skewed toward the near term (see chart 3) and therefore prolonged market uncertainty would cost its Treasury dearly in the nearer term. Hence it's an inopportune moment at which to see EC-Italian tensions escalate. An unnamed EC official has speculated upon whether billions in fines should be imposed for lack of progress toward fiscal targets, prompting Deputy PM Matteo Salvini to retort that "All of my energies will be devoted to changing these old and obsolete rules" and "the next index of well-being must be the unemployment rate." At over 10%, Italy's unemployment rate remains high and fiscal coffers would benefit from a lower rate, but the causes of Italy's structurally high unemployment rate have few economists recommending abandoning fiscal targets as a cure! For one thing, the bond market's reaction would probably leave Italy's workers worse off and this is something that continues to be lost on Italy's politicians.

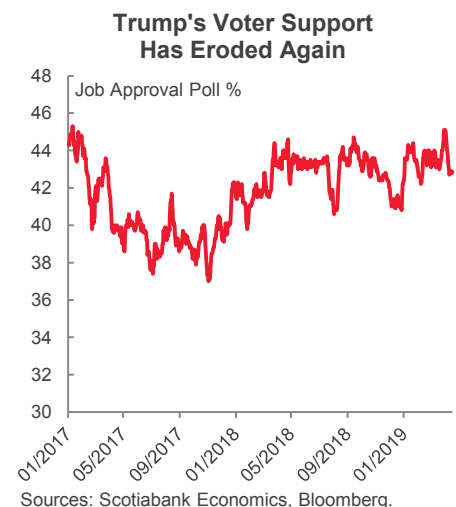
A batch of Eurozone confidence readings slightly improved. Readings for broad economic confidence, industrial confidence and services confidence improved after a year-long downward retreat. I'm inclined to treat the readings as noise in the face of ongoing tensions such as Brexit, Italian fiscal policy and US-centric protectionism.

UNITED STATES

US markets face an updated reading on **consumer confidence** from the Conference Board for May (10amET). **Repeat sale home prices** get updated for March (9amET) but usually carry little to no market consequences. **A pair of Treasury auctions** will be set against the backdrop of an ongoing rally; 2s get auctioned at 11:30amET and 5s at 1pmET.

Unstable thinking toward US-China trade tensions is also weighing upon markets. Trump's remarks yesterday continue to reverberate, including reference to the US not being ready for a deal, threatening that tariffs "could go up very, very substantially, very easily," and his claim that China badly wants a deal. While he has no credibility in centrist policy circles, Bannon's advice to seek further escalation including blocking Chinese companies from accessing US capital markets isn't helpful. While the Trump administration positions China as having changed the agreement at the last second in stealth fashion, it's also feasible that China did this because the US administration wasn't committing to dropping tariffs against China in the wake of an agreement. **Why would China agree to the same concessions if its assumption that the US tariffs would disappear is invalidated?** I find the US press and analysts are choosing to ignore this point versus more of an international audience. This bargaining in bad faith by the US administration was also done in NAFTA negotiations with metals tariffs only being eradicated last week.

What may come to bear upon Trump's attitudes is that after rising in the immediate aftermath of the escalation of trade tensions with China, **Trump's voter support has fallen again** (see chart 4). It is back to where it was in March of this year when a March 1st deadline to raise tariffs against Chinese imports into the US was postponed but Trump said tariffs would remain "for a substantial period of time." The message from voters and markets is clear in that US protectionism and scapegoating is fomenting instability in the world economy and markets. The S&P500 is off by 4% so far this month from its all-time high of just a few weeks ago.



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.	2.15	2.17	2.26	2.10	2.12	2.23	2.29	2.32	2.43	2.72	2.75	2.84	Canada - BoC	1.75
CANADA	1.54	1.55	1.68	1.48	1.48	1.65	1.59	1.60	1.76	1.84	1.85	1.97	US - Fed	2.50
GERMANY	-0.64	-0.65	-0.63	-0.54	-0.54	-0.49	-0.15	-0.14	-0.06	0.50	0.50	0.59	England - BoE	0.75
JAPAN	-0.16	-0.16	-0.15	-0.18	-0.17	-0.16	-0.07	-0.07	-0.05	0.49	0.51	0.54	Euro zone - ECB	0.00
U.K.	0.61	0.64	0.74	0.68	0.71	0.84	0.93	0.96	1.08	1.50	1.52	1.63	Japan - BoJ	-0.10
Spreads vs. U.S. (bps):														
CANADA	-61	-62	-57	-62	-64	-58	-71	-72	-67	-88	-90	-87	Mexico - Banxico	8.25
GERMANY	-279	-281	-288	-264	-266	-272	-244	-247	-249	-222	-225	-225	Australia - RBA	1.50
JAPAN	-231	-232	-241	-227	-229	-238	-236	-239	-247	-223	-224	-230	New Zealand - RBNZ	1.50
U.K.	-154	-152	-151	-142	-141	-139	-136	-137	-134	-122	-123	-122	Next Meeting Date	
Equities	Level			Change			% change:							
	Last	1-day	1-wk	1 Day	1-wk	1-mo	1 Day	1-wk	1-mo	1 Day	1-wk	1-mo		
S&P/TSX	16347			116.6			0.7	-0.3	-1.6				Canada - BoC	May 29, 2019
Dow 30	25586			95.2			0.4	-0.7	-3.6				US - Fed	Jun 19, 2019
S&P 500	2826			3.8			0.1	-1.2	-3.9				England - BoE	Jun 20, 2019
Nasdaq	7637			8.7			0.1	-2.3	-6.1				Euro zone - ECB	Jun 06, 2019
DAX	12073			2.1			0.0	-0.6	-2.0				Japan - BoJ	Jun 20, 2019
FTSE	7309			30.9			0.4	-0.0	-1.6				Mexico - Banxico	Jun 27, 2019
Nikkei	21260			77.6			0.4	-0.1	-4.5				Australia - RBA	Jun 04, 2019
Hang Seng	27391			102.7			0.4	-1.0	-7.5				New Zealand - RBNZ	Jun 25, 2019
CAC	5334			-1.8			-0.0	-0.9	-4.2					
Commodities	Level			Change			% change:							
	Last	1-day	1-wk	1 Day	1-wk	1-mo	1 Day	1-wk	1-mo	1 Day	1-wk	1-mo		
WTI Crude	59.20			0.57			1.0	-6.2	-6.5					
Natural Gas	2.55			-0.05			-2.0	-4.8	-0.8					
Gold	1277.89			-11.06			-0.9	0.3	-0.6					
Silver	14.55			0.07			0.5	0.5	-1.7					
CRB Index	179.80			1.17			0.7	-1.0	-2.6					
Currencies	Level			Change			% change:							
	Last	1-day	1-wk	1 Day	1-wk	1-mo	1 Day	1-wk	1-mo	1 Day	1-wk	1-mo		
USDCAD	1.3471			0.0027			0.2	0.5	0.1					
EURUSD	1.1186			-0.0008			-0.1	0.2	0.0					
USDJPY	109.52			0.0100			0.0	-0.9	-1.9					
AUDUSD	0.6922			0.0004			0.1	0.6	-1.9					
GBPUSD	1.2660			-0.0019			-0.1	-0.4	-2.1					
USDCHF	1.0060			0.0022			0.2	-0.5	-1.3					

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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