ON DECK FOR WEDNESDAY, JULY 3

Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
US	07/03	07:00	MBA Mortgage Applications (w/w)	JUN 28	--	--	1.3
US	07/03	08:15	ADP Employment Report (000s m/m)	Jun	100	140.0	27.4
CA	07/03	08:30	Merchandise Trade Balance (C$ bn)	May	-2.0	-1.7	-1.0
US	07/03	08:30	Trade Balance (US$ bn)	May	-53.6	-54.0	-50.8
US	07/03	10:00	Factory Orders (m/m)	May	-0.4	-0.6	-0.8
US	07/03	10:00	ISM Non-Manufacturing Composite	Jun	55.9	56.0	56.9

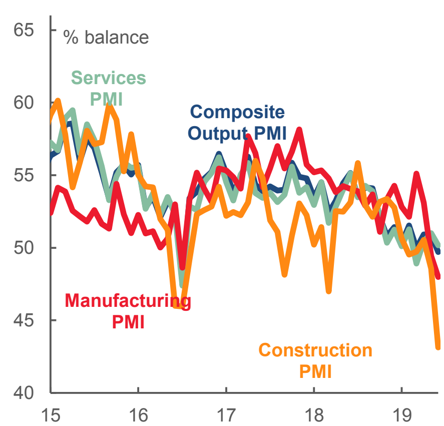
CONTACTS

Derek Holt, VP & Head of Capital Markets Economics
416.863.7707
Scotiabank Economics
derek.holt@scotiabank.com

KEY POINTS:

- **Dovish central bank nominations drive richer bonds and stocks**
- **Merit again loses to politics in key central bank nominations…**
- **…as both the Fed and ECB face intensifying politicization**
- **Will US ADP rebound as a warm-up to nonfarm?**
- **US markets shut early today ahead of Independence Day**
- **US: ISM-services, factory orders, trade, oil inventories**
- **UK PMIs show economy slipping into contraction…**
- **….as BoE risks remain geared to hold with material cut risk**
- **Canada's trade figures could be a grab bag of idiosyncratic factors**
- **Sweden's Riksbank holds, repeats unchanged hike guidance**
- **Overnight Chinese, Eurozone PMIs offered little new information**

UK PMIs



Sources: Scotiabank Economics, Haver Analytics, Markit.

Dovish and highly political central bank appointments at the ECB and Fed (see below) are driving sovereign bond yields lower and stocks higher with intensified focus upon the next round of US labour market readings. Could ADP repeat? Recall that the weak report in May (+27k) was the precursor to the weak US nonfarm payrolls reading for the same month. Another weak reading is significantly priced into nearer term fed fund futures contracts that are pricing a cut this month while the larger market risk lies in terms of an upside surprise that could lean against July cut pricing. US ISM non-manufacturing is expected to soften. Canadian trade figures could unwind unusual idiosyncratic drivers of export and import gains the prior month and more materially inform trade sector risks to GDP growth. Also note that that final batch of UK PMIs showed the economy contracting last month and Sweden's Riksbank stayed on hold with unchanged rate guidance.

- The USD is very little changed on a DXY basis this morning. Pound sterling is slightly depreciating (weak PMIs, see below), the Euro is little changed as dovish and highly politicized Fed and ECB nominations cancel out influences on the dollar cross (see below), and CAD is little changed ahead of trade figures (see below).

- Sovereign bond yields continue to plumb new depths. US Treasury yields are down by 1–2bps across the curve and Canada is being dragged along. Gilts are richer with yields down 2–4bps in a bull flattener move. Italian spreads over bunds are pulling in sharply (-16bps in 10s) in ongoing follow-through to its revised deficit targets and as EGBs in general enjoy a Lagarde premium this morning.

- Oil prices are higher partly on lower private US oil inventories ahead of the US government's tally today. WTI is up half a buck and Brent is up by a little more.
- US equity futures are up by about ¼% and TSX futures are slightly firmer. European cash markets are rallying by between ¾% (London, Paris, Frankfurt) to 1% (Madrid) and as much as 1¾% (Milan). Asian equities fell across most major exchanges and by up to 1.2% in the case of Seoul and Shenzhen. Maybe Asia didn't catch the premium through perceived dovishness to ECB and Fed appointments.

At least two out of three appointments at the Fed and ECB yesterday further illustrated that merit plays second fiddle to politics and circumstances across central banks and perhaps more generally in today's labour market. Christine Lagarde's appointment to head the ECB brings a bright, solid communicator and by most public accounts a good manager with prior private sector success to a challenging position that must navigate complex politics. There are many demanding roles for which her unique skillset would be suitable. But Lagarde's appointment also brings to the role someone who never studied economics, has zero experience as a central banker, has never been involved in making a monetary policy decision, possesses no direct experience in financial markets, who is a lawyer by training, and who has essentially been a politician since 2005 whether in her role as French finance minister or head of the so-past-its-prime IMF. How did she get the job? Because Merkel's pick for head of the EU crumbled, French President Macron rescued her with support for an alternative German pick (Ursula von der Leyen) that stoked controversy toward her own qualifications, but then Macron demanded a French person to be head of the ECB in return. You scratch my back and I'll scratch yours. Lagarde has risen to the occasion multiple times in her star studded career and may well do it again with the help of strong technical policy guidance across ECB staffers and on the Governing Council. But is a fragile moment in the world economy the right time to experiment with an unorthodox appointment? **It's probably fairly clear to markets that Lagarde is a dovish choice**. Hence, she will likely continue to advocate policies that interfere with market mechanisms in such fashion as to remove market discipline, thereby further lessening the odds of structural reforms to the benefit of medium- to longer-term growth and by quite possibly enabling protectionist forces in the world economy by tossing a security blanket over them.

Enter the Fed. You mean to say that with all of the bright minds out there, the best that we can do is to come up with a pick that is obviously partisan through her ties to the White House and the 2016 Trump campaign, supports the gold standard, doesn't believe in the Fed's Congressional dual mandate, thinks the Philips curve is totally dead and not dormant or a more muted relationship today, apparently shares the President's views toward simplistic zero-sum currency war and trade policy perspectives, did her schooling at some place in Utah and apparently thinks the Fed should be run by whatever markets fancy at a particularly moment? Oh, and she has a non-zero chance she could be Chair one day. Enter one Judy Shelton. I have less of an issue with Trump's other pick—Christopher Waller—who has a solid background in economics and in a research role at the St. Louis Fed, though he possesses no direct decision-making experience and has expressed a degree of one-sided certainty in his views that is perhaps too strong for a permanent voting member of the FOMC.

UK data continues to sour. This morning's composite PMI for June slipped into contraction territory with a 49.7 reading (50.9 prior, 51.0 consensus) as the services gauge fell to 50.2 (51.0 prior and consensus). See chart. This adds to earlier evidence that the manufacturing and construction sectors sank further into contraction in June. First, some of this is not surprising since it's the unwinding of the Brexit-related stocking that was occurring earlier in the year when a deadline was thought to be, well, a deadline for a decision. Second, however, is that the PMIs are weaker than just this effect alone would suggest as the composite tally is the lowest since July 2016. Global trade headlines are likely to blame for at least some of this. As I wrote in the Global Week Ahead, however, deteriorating domestic data could well weaken Boris Johnson's Brexit hand when he marches off demanding a new deal from the EU ahead of the Halloween deadline. In any event, Carney was never going to hike with Brexit looming so I don't understand views that express amazement over tamped down expectations in some quarters. The BoE is on hold with cut risk into and out of Brexit and nothing has changed in this regard.

Overnight PMIs carried little new information out of China and the Eurozone. China's private PMIs slipped by somewhat more than the earlier state PMIs did. The Caixin composite PMI fell to 50.6 (51.5) which signals little growth in the economy as the Caixin manufacturing PMI slipped below the critical 50 line (49.4) and the services PMI also fell to 52 (52.7 prior). The Eurozone composite PMI was revised up a tick to 52.2 in the final June estimate.

Sweden's Riksbank met expectations for no change in its repo rate (-0.25%) and the statement (here) generally repeated guidance for a rate hike later this year with no changes to the published forecast for the repo rate compared to the April projections subject to "risks concerning international developments."

UNITED STATES

Best wishes on Independence Day to our American friends and colleagues! Just get through to the early market closures and onto tomorrow's Fourth of July celebrations. That's today's market mantra. Bonds shut at 2pmET and stock markets close at 1pmET. The only thing that actually matters this week anyway is Friday's nonfarm payrolls, so heck, take the whole day, trade it for a few minutes Friday, and split for a slightly interrupted long weekend. Here's a brief rundown of the day's expectations:

- **ADP (8:15amET):** June's reading will be watched more closely than a normal ADP report given that the prior one nailed expectations for the disappointment in May's nonfarm reading. The consensus guesstimate is 140k (27k prior) which would be a mild rebound. Perhaps May was distorted and pent-up hiring demand will be unleashed. Or perhaps June's reading will face downside risk given the reference period that is the pay period that includes the 12th of the month may have been marked by dampened hiring confidence over the first half of June given Trump's Mexican stand-off and the deterioration in US-China relations. Weekly jobless claims (8:30amET) are nevertheless expected to remain around the 225k mark. See the Global Week Ahead (here) for a further discussion of the statistical odds for nonfarm following a disappointing reading like May's (here).

- **Trade (8:30amET):** A deterioration in the monthly trade deficit is all but assured for May's reading. We already know that the advance merchandise deficit widened by over US$2 billion per month that month. Tack on a reasonably stable monthly services surplus and an all-in trade deficit around US$53–54 billion is likely.

- **Factory orders (8:30amET):** May's estimate should follow lower the already known 1.3% m/m drop in durable goods orders but with an expected rise in nondurable goods orders tacked on. Durables are roughly half of total factory orders.

- **ISM non-manufacturing (10amET):** It's not just ISM-manufacturing that has been declining, although it has declined more sharply than the non-manufacturing gauged since late last summer. The ISM-services measure has declined from a peak of 60.8 last September to just under 57 in April amid expectations for a modest further deceleration. Overall, the two ISM readings indicate cooler but still modest growth in the US economy and within each of the manufacturing and non-manufacturing sectors of the economy.

- **DOE crude oil inventories (10:30amET):** The massive draw down two weeks was the biggest since the first week of July last year. Consensus is chasing the trend and expects another draw down, but a milder one this time. Yesterday's private industry tally supported that view as API inventories fell by 5 million barrels last week, but is it all priced in ahead of the DOE figures?

CANADA

Canada updates trade figures for May (8:30amET) before trading basically grinds lower as US accounts head for the exits until at least a few minutes around nonfarm on Friday. A wider deficit is expected, but anything goes with trade figures that often surprise not least of which because key parts like the energy balance are often inferred from incomplete surveys.

Idiosyncratic factors distorted both sides of the trade ledger the prior month and how they shake out is a key uncertainty this morning. Oil prices and non-energy commodity prices both fell over the month as trade tensions rose and this should weigh down the value of exports. Export volumes had been strong during the prior month of April (+2.0% m/m), but higher gold exports via the banking sector to Hong Kong and the UK played a significant role and one that is likely to drop out in the May figures. Import volumes were also distorted in April given a large decline in aircraft imports (-83% m/m) and a 3.6% drop in imports of autos and parts, both of which are likely to rebound.

Fixed Income — Government Yield Curves (%):

	2-YEAR Last	2-YEAR 1-day	2-YEAR 1-wk	5-YEAR Last	5-YEAR 1-day	5-YEAR 1-wk	10-YEAR Last	10-YEAR 1-day	10-YEAR 1-wk	30-YEAR Last	30-YEAR 1-day	30-YEAR 1-wk
U.S.	1.75	1.76	1.77	1.73	1.74	1.80	1.96	1.97	2.05	2.49	2.50	2.57
CANADA	1.48	1.48	1.46	1.40	1.40	1.40	1.45	1.47	1.50	1.66	1.68	1.73
GERMANY	-0.76	-0.76	-0.73	-0.65	-0.69	-0.63	-0.39	-0.37	-0.30	0.21	0.25	0.27
JAPAN	-0.22	-0.21	-0.21	-0.25	-0.24	-0.25	-0.15	-0.15	-0.14	0.35	0.38	0.38
U.K.	0.50	0.53	0.61	0.49	0.53	0.63	0.69	0.72	0.83	1.31	1.36	1.46

Spreads vs. U.S. (bps):

	2-YEAR Last	2-YEAR 1-day	2-YEAR 1-wk	5-YEAR Last	5-YEAR 1-day	5-YEAR 1-wk	10-YEAR Last	10-YEAR 1-day	10-YEAR 1-wk	30-YEAR Last	30-YEAR 1-day	30-YEAR 1-wk
CANADA	-28	-28	-31	-33	-34	-40	-50	-51	-55	-83	-83	-84
GERMANY	-251	-252	-250	-238	-244	-243	-234	-234	-235	-228	-225	-230
JAPAN	-197	-198	-198	-198	-198	-204	-211	-212	-218	-214	-212	-219
U.K.	-125	-124	-116	-124	-122	-117	-127	-125	-122	-118	-115	-111

Equities

	Level: Last	Level: Change	% change: 1 Day	% change: 1-wk	% change: 1-mo	% change: 1-yr
S&P/TSX	16471	89.1	0.5	-0.3	2.8	1.3
Dow 30	26787	69.3	0.3	0.9	7.9	10.8
S&P 500	2973	8.7	0.3	1.9	8.3	9.6
Nasdaq	8109	17.9	0.2	2.8	10.6	8.1
DAX	12605	78.7	0.6	2.9	6.9	2.1
FTSE	7614	55.2	0.7	2.7	6.0	0.3
Nikkei	21638	-116.1	-0.5	2.6	6.0	-0.7
Hang Seng	28855	-20.4	-0.1	2.4	7.3	1.1
CAC	5609	32.5	0.6	2.0	7.0	5.5

Commodities

	Level: Last	Level: Change	% change: 1 Day	% change: 1-wk	% change: 1-mo	% change: 1-yr
WTI Crude	56.72	0.47	0.8	-4.5	6.5	-23.5
Natural Gas	2.27	0.03	1.5	-0.8	-5.4	-20.8
Gold	1417.51	-1.14	-0.1	0.6	7.0	13.2
Silver	15.17	-0.09	-0.6	-1.5	4.8	-5.1
CRB Index	178.81	0.97	0.5	-1.9	2.3	-9.5

Currencies

	Level: Last	Level: Change	% change: 1 Day	% change: 1-wk	% change: 1-mo	% change: 1-yr
USDCAD	1.3101	-0.0007	-0.1	-0.2	-2.5	-0.3
EURUSD	1.1291	0.0006	0.1	-0.7	0.4	-3.1
USDJPY	107.72	-0.1600	-0.1	-0.1	-0.3	-2.6
AUDUSD	0.7018	0.0024	0.3	0.5	0.6	-5.0
GBPUSD	1.2576	-0.0017	-0.1	-0.9	-0.7	-4.7
USDCHF	0.9844	-0.0019	-0.2	0.7	-0.8	-0.8

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	**1.00**
New Zealand - RBNZ	**1.50**

Next Meeting Date	
Canada - BoC	**Jul 10, 2019**
US - Fed	**Jul 31, 2019**
England - BoE	**Aug 01, 2019**
Euro zone - ECB	**Jul 25, 2019**
Japan - BoJ	**Jul 30, 2019**
Mexico - Banxico	**Aug 15, 2019**
Australia - RBA	**Aug 06, 2019**
New Zealand - RBNZ	**Aug 06, 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.