

**ON DECK FOR MONDAY, SEPTEMBER 16**

| Country | Date  | Time  | Event  | Period | BNS | Consensus | Latest |
|---------|-------|-------|--|--------|-----|-----------|--------|
| CA      | 09/16 | 08:30 | International Securities Transactions (C\$ bn) | Jul    | --  | --        | -4.0   |
| US      | 09/16 | 08:30 | Empire State Manufacturing Index               | Sep    | --  | 4.0       | 4.8    |
| CA      | 09/16 | 09:00 | Existing Home Sales (m/m)                      | Aug    | --  | 1.3       | 3.5    |

**KEY POINTS:**

- Risk off driven by drones and China
- A massive shock to Saudi and world oil production...
- ...could face further market effects
- US release of strategic reserves has little effect
- Chinese retail & industrial figures slow...
- ...and could be slower than reported based on other readings...
- US Empire offers a soft start to another round of mfrg surveys
- CDN home resales remain on upward trend
- FOMC preview
- Global Week Ahead

Please see an FOMC Preview [here](#) ahead of Wednesday's communications. Please also see the Global Week Ahead [here](#) with key risks including the following but with the obvious addition of the weekend attacks on Saudi Arabia:

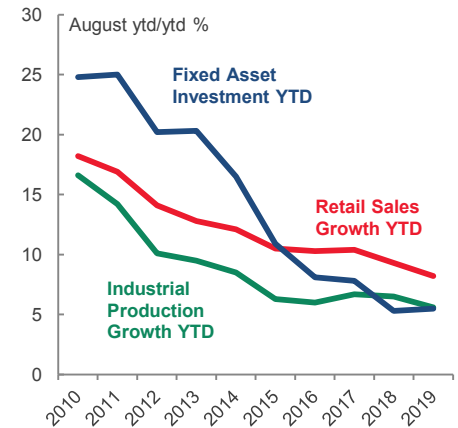
- CBs: Fed, BoJ, BoE...
- ...SNB, Norges, BCB...
- ...SARB, BI, CBCT
- UK Court ruling
- US-China trade
- CPI: UK, Canada
- China macro
- CDN mfrg, retail
- US macro
- Australian jobs
- GDP: NZ, Argentina
- US, CDN auctions

**INTERNATIONAL**

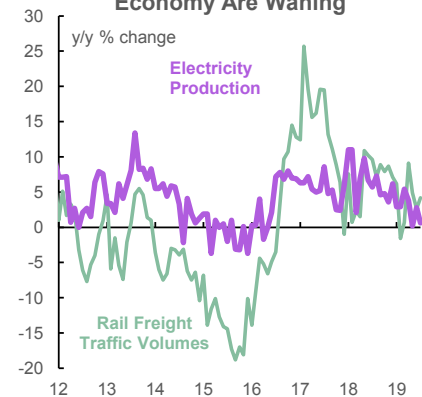
Global risk off drivers include the drone attacks on Saudi oil production and soft Chinese macro data. The weekend also brought a strike announcement by UAW against GM that will disrupt just under one-fifth of US auto production and cause weakness in September's industrial data but with the pre-market stock response dirtied by the impact of higher oil prices. The market implications stemming from the attacks on Saudi Arabia are impossible to treat fully in isolation of the focus upon soft Chinese macro data. Nevertheless, they could be the tip of the iceberg as finger pointing waits to be further informed along with the risk of escalation including Trump's itchy trigger finger.

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**China's Slowing Economy**


Sources: Scotiabank Economics, Bloomberg.

**Core Readings On China's Economy Are Waning**


Source: Scotiabank Economics, Bloomberg.

**Is China's Growth Momentum Waning Again?**


Sources: Scotiabank Economics, Bloomberg.

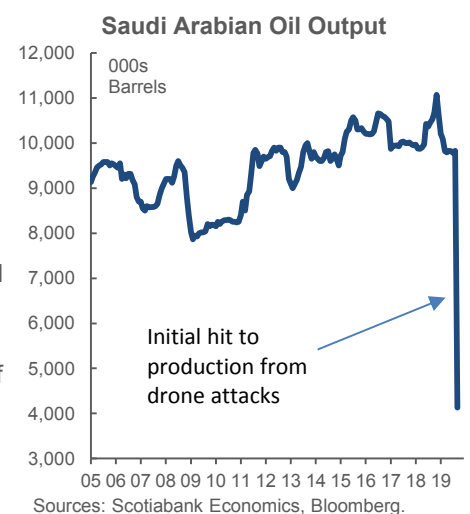
- Stocks are under almost universal downward pressure, aside from the more energy dependent markets. US equity futures are down by between ¼% and ½% with the tech-heavy Nasdaq leading decliners. TSX futures are flat with oil's outperformance helping given energy's 17% weight. European bourses are down by as little as 0.2% in London to ¾% in Italy and Madrid. Norway's exchanged is outperforming with a 1.4% rise on higher oil prices.
- Petro currencies are generally outperforming with CAD and the Norwegian krone leading the way. The Mexican peso is not participating in the rally.
- Sovereign bond yields are moving lower outside of Japan's shut market. US Treasury yields are down by 4–6bps across the curve with Canada's curve rallying by underperforming Treasuries partly given the differential impact of higher oil prices (the US is still a net importer). EGBs are rallying by about 3–4bps in 10s across most countries.
- Brent oil has scaled back just under half of the initial spike of nearly US\$12 when Asian market participants walked in and is presently up by over US\$6. WTI is slightly underperforming Brent but is still up by over US\$5½ with little offset from the announced release of US strategic reserves (see below). Gold is up US\$13½ to just over US\$1500 in the first bit of 'good' news following a \$65 drop from the peak earlier this month.
- Market-based measures of inflation expectations have increased. The 10 year TIPS breakeven, for instance, moved up 2bps to 1.7% and is about 19bps above the trough in early September to its highest since the end of July. It's early and these are distorted measures, but the Fed may be somewhat encouraged by the recent rise.

**The Chinese macro misses that were reported over the weekend had at least as much to do with overly optimistic expectations as slower growth than the prior month.** Chinese retail sales decelerated by a tick to 7.5% y/y, but missed consensus by four-tenths. Industrial output growth slowed by four tenths to 4.4%, but missed consensus by double that. The year-to-date growth rates in retail sales, industrial production and fixed asset investment are shown in chart 1 and all three measures have been decelerating for years but with **2019 setting new lows** across most of them. Year-to-date growth is a better way of looking at Chinese data that struggles with distortions such as the annual lunar new year effect. If anything, other readings suggest that the actual growth might be weaker yet. Chart 2 shows electricity production and rail freight traffic volumes and how much they've decelerated. These are inputs into the so-called Li Keqiang index, or at least Bloomberg's arbitrarily weighted proxy that is comprised of electricity output, rail freight and credit figures (chart 3). Premier Li once advised these are his preferred macro variables to watch as indicators of the industrial sector versus 'manmade' GDP.

**The magnitude of the hit on Saudi oil production cannot be overstated if it persists.** Chart 4 shows the recent trend in Saudi Arabia's oil production and what it would sink to if the disruption persisted for one month to help put the magnitude of the shock into perspective. Some of that production is already slated to come back on line within days, but Saudi Arabia is advising that 100% recovery could take weeks to months. Beyond the obvious motive being conflict between the Saudis and Iran is the added incentive to destabilize plans for Aramco's initial public offering and the wealth it could bring to the Saudi royal family, the state's budget and its regional influence. Analyst presentations were to occur on September 22<sup>nd</sup> ahead of the IPO that could happen in November.

If this were only about a transitory hit to Saudi production that can be repaired then by corollary the effects upon markets would be transitory. The uncertainty that will hang over markets is nevertheless likely to persist. We don't know with certainty who was behind the attacks. The Houthis in Yemen have drawn military support from Iran, Lebanon's Iranian-backed Hezbollah, but also North Korea. The US has made hasty and politically motivated claims about military threats and their origins before the pictures and quick remarks offered yesterday such as Bush's misleading WMDs. Therefore the knock-on effects that inform the risk of further escalation may be informed over time. Further, the vulnerability of global energy infrastructure, or infrastructure in general, is clear if it wasn't previously.

**Trump's announcement that the US would release its Strategic Petroleum Reserve is having little effect on WTI relative to Brent.** The reserves consist of about 650



million barrels of oil stored within a US government complex that consists of four sites in underground caves within salt domes along the Texas and Louisiana Gulf Coasts. The reserves have declined over the past couple of years by just under 50 million barrels and the storage facilities have capacity of 727 million barrels. Part of the reason for the fact that WTI is similarly impacted by the attacks as Brent's rise is that it's unclear how much of the reserves will be released and how soon. It takes time to release the reserves and in any event it is stockpiled production that is already at least partially priced into markets by way of the option to release.

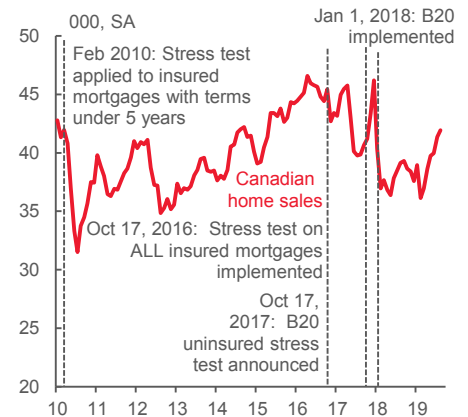
## CANADA

Canada updated existing home sales for August this morning and they were up 1.4% m/m. Sales have been on a tear of sorts over recent months with August's rise building upon the 3.5% m/m gain in July, flatness in June, a 1.9% increase in May and the 3.6% jump in April for a robust overall Spring and Summer season. Chart 5 shows the strong upward trend dating back to Spring. August, however, is often more about seasonal adjustments than underlying activity. Canada also updated securities transactions for July but it's of no use telling traders what went through their markets two months ago.

## UNITED STATES

The Fed's communications on Wednesday will obviously be the week's main event. The same factors cited above are dominating US markets. The Empire manufacturing gauge slipped a little to 2.0 (4.8 prior) which is a soft start to the fresh round of manufacturing surveys on the path to the next ISM print.

### Home Sales Are Regaining Momentum After B20's Effects



Sources: Scotiabank Economics, CREA.

| Fixed Income   | Government Yield Curves (%): |         |       |        |       |       |           |       |       |         |                    |              | Central Banks    |      |
|--|------------------------------|---------|-------|--------|-------|-------|-----------|-------|-------|---------|--------------------|--------------|------------------|------|
| U.S.<br>CANADA<br>GERMANY<br>JAPAN<br>U.K.<br><br>CANADA<br>GERMANY<br>JAPAN<br>U.K. | 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         |                  |      |
|  | 1.76                         | 1.80    | 1.59  | 1.71   | 1.75  | 1.50  | 1.85      | 1.90  | 1.64  | 2.32    | 2.37               | 2.13         | Canada - BoC     | 1.75 |
|  | 1.63                         | 1.64    | 1.55  | 1.49   | 1.51  | 1.38  | 1.48      | 1.51  | 1.35  | 1.68    | 1.71               | 1.55         | US - Fed         | 2.25 |
|  | -0.72                        | -0.71   | -0.86 | -0.72  | -0.70 | -0.85 | -0.48     | -0.45 | -0.59 | 0.09    | 0.13               | -0.00        | US - Fed         | 2.25 |
|  | -0.24                        | -0.24   | -0.31 | -0.25  | -0.25 | -0.34 | -0.15     | -0.15 | -0.25 | 0.34    | 0.34               | 0.24         | England - BoE    | 0.75 |
|  | 0.53                         | 0.57    | 0.44  | 0.50   | 0.56  | 0.39  | 0.71      | 0.76  | 0.59  | 1.17    | 1.23               | 1.10         | England - BoE    | 0.75 |
|  | Spreads vs. U.S. (bps):      |         |       |        |       |       |           |       |       |         |                    |              |                  |      |
|  | -13                          | -17     | -5    | -22    | -25   | -12   | -37       | -39   | -29   | -64     | -66                | -58          | Euro zone - ECB  | 0.00 |
| -248   | -251                         | -245    | -243  | -245   | -235  | -233  | -235      | -223  | -223  | -224    | -213               | Japan - BoJ  | -0.10            |      |
| -200   | -204                         | -190    | -196  | -200   | -184  | -200  | -205      | -190  | -197  | -203    | -189               | Japan - BoJ  | -0.10            |      |
| -123   | -123                         | -116    | -120  | -120   | -111  | -114  | -114      | -105  | -115  | -115    | -103               |              |                  |      |
| Equities   | Level                        |         |       |        |       |       | % change: |       |       |         |                    |              | Mexico - Banxico | 8.00 |
|  | Last                         | Change  |       |        |       |       | 1 Day     | 1-wk  | 1-mo  | 1-yr    |                    |              |                  |      |
| S&P/TSX  | 16682                        | 39.1    |       |        |       |       | 0.2       | 0.9   | 3.3   | 4.2     | Australia - RBA    | 1.00         |                  |      |
| Dow 30   | 27220                        | 37.1    |       |        |       |       | 0.1       | 1.6   | 5.2   | 4.1     |                    |              |                  |      |
| S&P 500  | 3007                         | -2.2    |       |        |       |       | -0.1      | 1.0   | 4.1   | 3.5     | New Zealand - RBNZ | 1.00         |                  |      |
| Nasdaq   | 8177                         | -17.8   |       |        |       |       | -0.2      | 0.9   | 3.6   | 2.1     |                    |              |                  |      |
| DAX  | 12405                        | -63.3   |       |        |       |       | -0.5      | 1.5   | 7.3   | 2.3     |                    |              |                  |      |
| FTSE   | 7350                         | -17.1   |       |        |       |       | -0.2      | 1.6   | 3.3   | 0.6     |                    |              |                  |      |
| Nikkei   | 21988                        | 228.7   |       |        |       |       | 1.1       | 3.7   | 7.7   | -4.8    | Canada - BoC       | Oct 30, 2019 |                  |      |
| Hang Seng  | 27125                        | -228.1  |       |        |       |       | -0.8      | 1.7   | 5.4   | -0.6    | US - Fed           | Sep 18, 2019 |                  |      |
| CAC  | 5623                         | -32.1   |       |        |       |       | -0.6      | 0.6   | 6.1   | 5.1     |                    |              |                  |      |
| Commodities  | Level                        |         |       |        |       |       | % change: |       |       |         |                    |              |                  |      |
| WTI Crude  | 60.32                        | 5.47    |       |        |       |       | 10.0      | 4.3   | 9.9   | -12.6   | England - BoE      | Sep 19, 2019 |                  |      |
| Natural Gas  | 2.67                         | 0.06    |       |        |       |       | 2.1       | 3.2   | 21.3  | -3.5    |                    |              |                  |      |
| Gold   | 1502.25                      | 13.60   |       |        |       |       | 0.9       | 0.2   | -0.7  | 25.9    | Euro zone - ECB    | Oct 24, 2019 |                  |      |
| Silver   | 18.15                        | -0.05   |       |        |       |       | -0.2      | 0.0   | 4.0   | 27.6    |                    |              |                  |      |
| CRB Index  | 181.04                       | 6.24    |       |        |       |       | 3.6       | 3.9   | 6.2   | -5.0    | Japan - BoJ        | Sep 19, 2019 |                  |      |
| Currencies   | Level                        |         |       |        |       |       | % change: |       |       |         |                    |              |                  |      |
| USDCAD   | 1.3239                       | -0.0049 |       |        |       |       | -0.4      | 0.5   | -0.2  | 1.5     | Mexico - Banxico   | Sep 26, 2019 |                  |      |
| EURUSD   | 1.1025                       | -0.0048 |       |        |       |       | -0.4      | -0.2  | -0.6  | -5.6    |                    |              |                  |      |
| USDJPY   | 107.86                       | -0.2300 |       |        |       |       | -0.2      | 0.6   | 1.4   | -3.6    | Australia - RBA    | Oct 01, 2019 |                  |      |
| AUDUSD   | 0.6862                       | -0.0017 |       |        |       |       | -0.2      | 0.0   | 1.2   | -4.5    |                    |              |                  |      |
| GBPUSD   | 1.2445                       | -0.0056 |       |        |       |       | -0.4      | 0.8   | 2.4   | -5.4    | New Zealand - RBNZ | Sep 24, 2019 |                  |      |
| USDCHF   | 0.9918                       | 0.0014  |       |        |       |       | 0.1       | -0.0  | 1.4   | 3.0     |                    |              |                  |      |

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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