ON DECK FOR FRIDAY, JANUARY 24

Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
CA	01/24	08:30	Retail Sales (m/m)	Nov	0.6	0.6	-1.2
CA	01/24	08:30	Retail Sales ex. Autos (m/m)	Nov	0.4	0.5	-0.5

KEY POINTS:

- **Markets settle down as China's markets shut for the Lunar New Year…**
- **...as coronavirus concerns will take weeks to evaluate**
- **Why the UK PMI improvement shouldn't negate BoE easing**
- **Eurozone composite PMI remains flat…**
- **…with manufacturing contracting at a slower pace…**
- **…while three-quarters of the economy decelerated**
- **CDN retail sales: would a rebound change anything for the BoC?**
- **Don't dismiss soft Canadian growth…**
- **…as just a function of strikes and weather**
- **US Markit PMIs on tap**
- **Japan CPI going nowhere slightly faster**
- **NZ CPI keeps pricing for the RBNZ on hold**

INTERNATIONAL

Calendar-based risk to global asset classes is focused upon a fresh batch of purchasing managers' indices from the Eurozone, UK and US. **Markets are in a better mood across most but not all asset classes**, and probably because a) China's markets were shut as the country goes into the Lunar New Year week that began Friday and so there was no further alarm stemming from a sell-off in Chinese assets, and b) a sense that China's aggressive actions against the coronavirus may be positive. It will probably take weeks to assess the latter bias and especially when the world's largest annual migration has Chinese workers returning to work after next week from elsewhere in the country and abroad.

UK PMI improved, but don't necessarily negate a BoE cut next week in my opinion. The Eurozone composite PMI was flat. RBNZ hold expectations firmed up in the wake of higher inflation. Canada digests retail sales as everything else performed poorly on the path to November GDP next week. The US faces just the Markit gauges.

- The USD is broadly gaining strength against a variety of major crosses. Sterling is depreciating by among the greatest degrees despite a positive surprise on PMIs. The euro is also slipping and the yen, Mexican peso, CAD and A$/NZ$ are on the slightly softer side with only the rand gaining.

- Sovereign bond curves are generally little changed with a very slight average cheapening bias. Canada's curve is dead flat ahead of retail sales.

- Oil prices are slightly lower with WTI around US$55.50 and Brent just under US$62. Western Canada Select—a proxy for Alberta's and Saskatchewan's heavy crude—sits at US$32.75 which is the lowest since the end of 2018.

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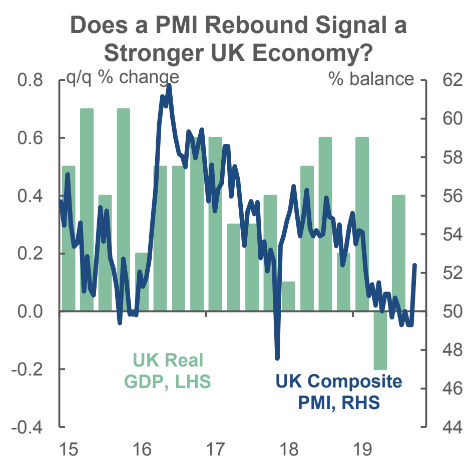
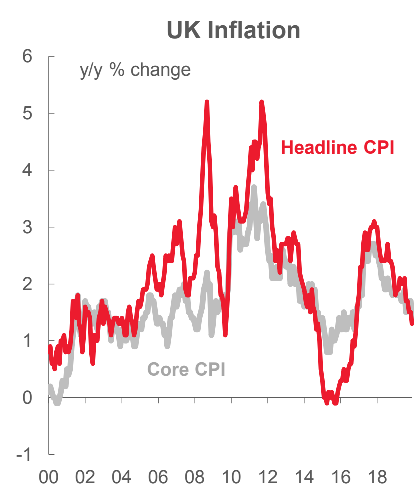


Sources: Scotiabank Economics, Markit, Bloomberg.



Sources: Scotiabank Economics, ONS.

- US equity futures are up by about 1/4% and so are TSX futures. European cash markets are up by around 1% or slightly more across all exchanges. Asian equities saw a small gain in Tokyo and Hong Kong. Each of mainland China's and Korea's stock markets were shut.

UK purchasing managers indices rose by much more than expected and that caused a minor cheapening of short-dated bonds while sterling nevertheless depreciated. The composite PMI increased to 52.4 which was a 3.1 point improvement over December. The new orders sub-index increased by 4.5 points to 50.9. The services PMI increased to 52.9 from 50 and the manufacturing PMI increased by 2.3 points to 49.8. A PMI gain of this magnitude may be indicative of considerably stronger GDP growth as chart 1 demonstrates. That's not always the case, however, such as in 2015Q3 when the composite PMI gained by more than it just did and yet that quarter's GDP growth decelerated before a later gain and then renewed disappointment. Or take 2017Q2 when the composite PMI gained by more than it just did and GDP growth went on a cooling trend for the next two quarters. These are useful, but rough and sentiment-based signals that can be noisy.

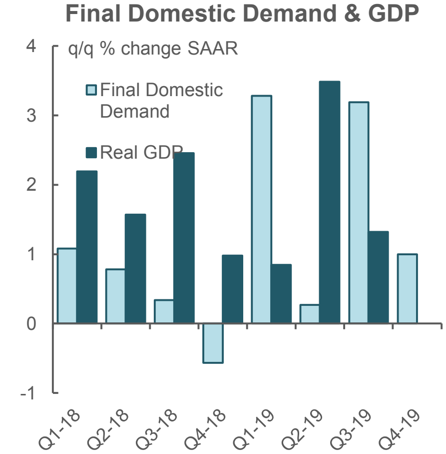
So the question now becomes this: does a one month PMI spike negate a BoE cut next week? It shouldn't. Will it? Not necessarily. The BoE's principal mandate is to target 2% inflation and inflation is falling (chart 2). Core inflation was 1.4% y/y in December which was down three-tenths from the prior month and the lowest reading since November 2016. Headline inflation is a touch cooler at 1.3% y/y which was also the lowest since November 2016. Easing doesn't necessarily mean higher inflation as the world has come to well understand by now. This observation has never stopped central banks mind you. Inaction when you are completely failing at your main goal would be tough to communicate to markets. Besides, step back from the wiggles and look at the bigger picture. Hard Brexit may be off the table, or just postponed, and we don't have a trade agreement with the EU and probably won't this year. Do you really think businesses are going to rip investment activity higher when they have no clue what the rules of the game might be going forward? Export growth and trend hiring needs investment to support it. Maybe sterling is the smartest currency in the room this morning.

An ancillary point to the UK data is that conditions took a turn for the worse across the channel and the feedback mechanism onto UK export prospects isn't looking so hot. Ditto for China's freshest challenges that, if like SARS, may knock around a full percentage point off the Chinese economy (here). The Eurozone's composite PMI was unchanged at 50.9 against expectations for a modest gain. The manufacturing PMI slightly improved by 1.5 points to 47.8 which was a full point higher than the consensus guesstimate, but the sector is still contracting. The patient is still spilling blood, just slightly less of it. The services sector PMI fell six-tenths to 52.2 (52.8 consensus). The service sector comprises about three-quarters of the Eurozone economy (here).

Guess what? Japanese inflation is low! OMG! Read all about it here! Boy, who saw that one coming. Headline edged up to 0.8% y/y (0.5% prior) and core edged up to 0.7% (0.5% prior) which remains about the Pacific Ocean's width away from the BoJ's 2% target. The yen ignored the reading.

The NZ$ rallied after CPI was released late yesterday but even though it is outperforming a number of other crosses, it's still just flat to the USD this morning. Headline inflation moved up to 1.9% y/y (1.5% prior, 1.8% consensus). The two-year bond yield inched up by about 2bps as already low market pricing for RBNZ policy moves at the February 12th and March 25th meetings basically went closer to zero.

Final Domestic Demand & GDP



Sources: Scotiabank Economics, Statistics Canada.

CANADA

Canada updates retail sales for November (8:30amET) that will complete the observable data inputs necessary to firm up expectations for next week's November GDP estimate. A partial rebound from the prior month's weakness is expected, but there is always as high risk into this report as there is into a jobs report. Right now, November GDP is tracking about as badly as the prior month's dip of 0.1% m/m. The lone bright spot was a 0.7% m/m rise in housing starts and a small 0.6% m/m rise in existing home sales that might have a small positive influence upon ancillary housing services (lawyers, agents, lenders etc) and both of those gains reversed the next month. Hours worked tanked by 0.9%

m/m in November and that alone doesn't bode well for GDP since GDP is an identity expressed as hours worked times labour productivity. Manufacturing shipment volumes fell 0.8% m/m. Wholesale trade volumes were down 0.9% m/m. Export volumes plunged by 2.7% m/m. Import volumes fell by 1.3%. As for the next month's GDP tracking in December, it's early in terms of data, but hours worked were flat, housing starts fell by 3.4% and existing home sales were down by 0.9% m/m, all seasonally adjusted.

Is all of this just distorted by weather, the CN rail strike, the GM strike in the US that impacted parts plants here and the price of cannabis on the moon? That's hard to swallow given how long this has been going on. The BoC sort of suggests as much but still says there is something else going on beneath it all. That might be the understatement of the year. More data will inform this, but take a minute to look at how long this has been going on.

1. GDP: Q4 growth is tracking around 0%. That would follow growth of 1.3% in Q3, 3.5% in Q2, 0.8% in Q1 and 1.0% in Q4. GDP growth has smelled like the Don River for four of the past five quarters. That's not just due to temporary distortions that suddenly began cropping up in October and November.

2. Final Domestic Demand: Some of this weak GDP is distorted by trade and inventory effects. Stripping those out results in the concept of Final Domestic Demand as a perhaps cleaner read on the domestic economy. FDD is tracking growth just over 1% in 2019Q4. It was 3.2% in Q3, 0.3% in Q2, 3.3% in Q1, -0.6% in 2018Q4, and 0.3–1.1% in each of the first three quarters of 2018. That's not transitory softness and it's not showing much at all by way of the resilience spin.

UNITED STATES

Calendar-based risk should be fairly low in the US today. The only focal point is on the Markit PMIs for January at 9:45amET. These are the less widely followed PMIs compared to the ISM gauges because a) the Fed tends to watch the ISM readings more closely, and b) the ISM manufacturing gauge is very well correlated with actual industrial production.

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.	1.52	1.51	1.56	1.55	1.55	1.62	1.74	1.73	1.82	2.18	2.18	2.28
CANADA	1.51	1.51	1.64	1.43	1.42	1.58	1.42	1.41	1.56	1.55	1.55	1.68
GERMANY	-0.60	-0.60	-0.59	-0.57	-0.57	-0.51	-0.30	-0.31	-0.22	0.22	0.21	0.30
JAPAN	-0.13	-0.12	-0.13	-0.12	-0.12	-0.10	-0.02	-0.02	0.00	0.41	0.42	0.46
U.K.	0.43	0.42	0.42	0.41	0.40	0.42	0.59	0.59	0.63	1.09	1.08	1.16
	Spreads vs. U.S. (bps):											
CANADA	-1	-0	8	-12	-12	-5	-32	-32	-26	-62	-63	-60
GERMANY	-212	-212	-215	-212	-212	-213	-204	-204	-204	-196	-197	-198
JAPAN	-165	-164	-169	-167	-167	-172	-176	-175	-182	-177	-176	-182
U.K.	-109	-109	-114	-114	-114	-120	-115	-114	-119	-109	-110	-112

Central Banks	
Current Rate	
Canada - BoC	**1.75**
US - Fed	**1.75**
England - BoE	**0.75**
Euro zone - ECB	**0.00**
Japan - BoJ	**-0.10**
Mexico - Banxico	**7.25**
Australia - RBA	**0.75**
New Zealand - RBNZ	**1.00**
Next Meeting Date	
Canada - BoC	**Mar 04, 2020**
US - Fed	**Jan 29, 2020**
England - BoE	**Jan 30, 2020**
Euro zone - ECB	**Mar 12, 2020**
Japan - BoJ	**Mar 19, 2020**
Mexico - Banxico	**Feb 13, 2020**
Australia - RBA	**Feb 03, 2020**
New Zealand - RBNZ	**Feb 11, 2020**

Equities	Level		% change:			
	Last	Change	1 Day	1-wk	1-mo	1-yr
S&P/TSX	17622	21.9	0.1	0.8	2.6	15.3
Dow 30	29160	-26.2	-0.1	0.4	2.3	18.8
S&P 500	3326	3.8	0.1	1.1	3.2	25.9
Nasdaq	9402	18.7	0.2	1.6	5.0	32.9
DAX	13596	207.7	1.6	0.5	2.2	22.2
FTSE	7633	125.2	1.7	-0.5	0.0	11.9
Nikkei	23827	31.7	0.1	-0.9	-0.0	15.8
Hang Seng	27950	40.5	0.1	-3.8	0.3	3.1
CAC	6036	64.1	1.1	-1.1	0.1	23.9

Commodities	Level		% change:			
WTI Crude	55.39	-0.20	-0.4	-5.3	-9.4	4.3
Natural Gas	1.88	-0.05	-2.5	-9.6	-13.5	-39.4
Gold	1558.32	-4.62	-0.3	0.1	3.9	21.6
Silver	17.60	-0.17	-1.0	-2.3	1.3	14.4
CRB Index	177.56	-0.96	-0.5	-2.6	-4.3	-0.9

Currencies	Level		% change:			
USDCAD	1.3139	0.0012	0.1	0.6	-0.2	-1.6
EURUSD	1.1027	-0.0028	-0.3	-0.6	-0.6	-2.5
USDJPY	109.62	0.1300	0.1	-0.5	0.2	-0.0
AUDUSD	0.6842	-0.0005	-0.1	-0.5	-1.2	-3.6
GBPUSD	1.3085	-0.0038	-0.3	0.5	1.1	0.1
USDCHF	0.9714	0.0025	0.3	0.4	-0.9	-2.5

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.