

ON DECK FOR WEDNESDAY, JULY 22

Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
US	07/22	07:00	MBA Mortgage Applications (w/w)	Jul 17	--	--	4.1
CA	07/22	08:30	Core CPI - Common (y/y)	Jun	1.3	1.4	1.5
CA	07/22	08:30	Core CPI - Median (y/y)	Jun	1.7	1.8	1.9
CA	07/22	08:30	Core CPI - Trim (y/y)	Jun	1.5	1.6	1.8
CA	07/22	08:30	CPI, All items (m/m)	Jun	0.3	0.4	0.8
CA	07/22	08:30	CPI, All items (y/y)	Jun	0.2	0.2	0.7
CA	07/22	08:30	CPI, All items (index)	Jun	--	136.6	137.2
US	07/22	10:00	Existing Home Sales (mn a.r.)	Jun	5.0	4.8	4.7
US	07/22	10:00	Existing Home Sales (m/m)	Jun	28	21.4	20.7

KEY POINTS:

- Equities slightly weaker on stalled US stimulus, China tensions
- US home resales soar, but fresher housing readings are ahead
- Canadian inflation firmer than expected...
- ...amid multiple reasons to ignore it
- Reaffirming the Canadian retail recovery
- Don't expect much out of next week's FOMC

INTERNATIONAL

Global markets are in mild risk-off mode so far. There may be two catalysts in addition to simple noise that defies the quest to always have an explanation at the ready.

US stocks began slipping into the close yesterday when more negative headlines began to hit on how US stimulus discussions were in disarray. Some of this renewed concern over US stimulus plans spilled over into the overnight Asian and European sessions including through US equity futures. Selling pressure recommenced in two bouts during the Asian overnight session and before the headlines hit on how the US apparently told China to shut its consulate in Houston "to protect American intellectual property and Americans' private information." The order followed mysterious fires to burn papers outside the consulate yesterday. China vows to retaliate but was silent on how and when.

I'd place the disarray that appears to govern the US fiscal stimulus plans as a more important driver of today's market movements. Maybe a WSJ piece on how the Fed might sit on its hands through the rest of the summer isn't helping either.

US home resales were strong, but reflect decisions made before rising covid cases in some parts of the US. Canadian CPI was a bit firmer than expected, but with little cause for paying much attention.

- Stocks are somewhat mixed. European equities are down by ½% to 1½%. They are probably catching up to the sell off in North American equities into the final hour yesterday when markets reined in assumptions about

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Chart 1


progress toward achieving another US fiscal stimulus bill. Ditto for Asian equities that saw HK down 2 ¼%, a mild decline in Tokyo and a mild gain across mainland China's exchanges. US and Canadian equities are little changed this morning.

- Sovereign curves are slightly bull flattening. Ten year yields are down by 2–6bps across The US, Canada and Europe with Italy continuing to lead the decline after the EU achieved its stimulus agreement.
- Oil prices are off by just over 1%.
- The USD is little changed on balance as the euro rises along with lesser appreciation in CAD and the A\$ versus flat sterling and mild depreciation in the yen.

UNITED STATES

US home resales climbed in line with expectations. Sales were up by +20.7% m/m (21.4% consensus). I was a little higher at 28% m/m. The uncertainty was over the exact distribution of the huge gain in pending home sales during May that close 1–3 months later. It will be the gift that keeps on giving next month when the rest of the sales close. Single family homes sold were up 20% m/m and multiples were up 29%. Months supply fell to 4 which is fairly tight.

How housing is holding up in the face of covid-19 cases will be better informed by Friday's new home sales. Contract signings, so fresher take on current sentiment rather than lags in when resales close months later. Next week we also get June pending home sales that will also be a bit fresher than what we got today.

[This](#) WSJ piece on the Fed may also be of interest. It basically says **not to expect any material changes at next week's FOMC meeting**. That includes no changes yet to forward guidance or alterations to purchase plans just yet versus potentially later in the year once the Fed has more evidence on the virus and the recovery. In other words, the Fed is like the rest of us in the markets! What's unwritten may also be that they want to see if Washington can pull a rabbit out of its hat with another stimulus bill that averts cliff effects.

CANADA

Canada registered a slightly firmer set of inflation readings than expected that were largely ignored. In one sense it's dicey to ignore fresh evidence, but in this case there may be legitimate reason for doing so as explained below. It is less legitimate to dismiss yesterday's massive strength in retail sales during May and June (recap [here](#)). We all know there are forward looking risks. But when the evidence points to a stronger and faster than expected recovery, it's called confirmation bias to reject it in favour of one's prior that it simply cannot happen.

Canada, CPI (m/m % NSA ; y/y % NSA), June:

Actual: 0.8 / 0.7

Scotia: 0.3 / +0.2

Consensus: +0.4 / +0.2

Prior: Unrevised from 0.3 / -0.4

Canada, Core Inflation, y/y %, June:

Average: 1.7 (prior 1.6)

Weighted Median: 1.8 (prior 1.9)

Common Component: 1.5 (prior 1.4)

Trimmed Mean: 1.8 (prior 1.6 revised from 1.7)

The C\$ and short-term market rates rightly ignored a modest upside to expectations for inflation readings for the month of June as the Bank of Canada is likely to do so as well and with considerable justification for doing so.

Headline inflation climbed by more than anticipated and core inflation edged up a tick to 1.7% from a slightly revised average of 1.6% in May (chart 1).

The main reason the BoC would ignore the release is that it's too soon to expect most of the adjustment lower in the core measures. As spare capacity has ballooned, more of this lagging effect is likely to come with a 3–5 quarter lag which is one reason behind why we expect the average 'core' measure to dip below 1% y/y toward year-end into early 2021. The BoC is likely to remain anchored to this longer run view and dismiss short-term readings. If we have firm—let alone higher—core inflation along that time frame then that would obviously be material information, but we don't have that today.

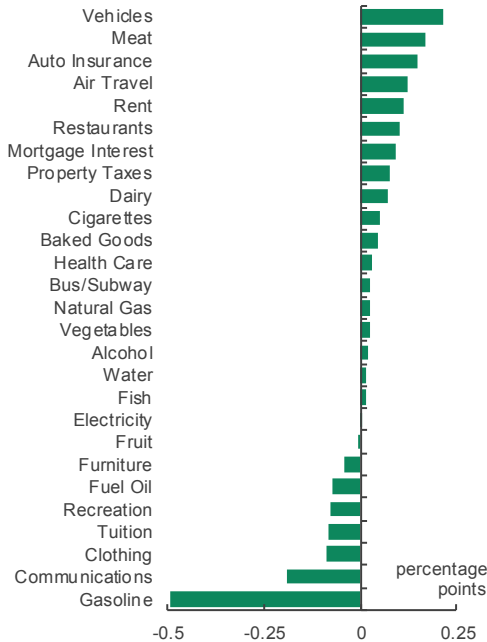
There also remain data quality issues that provide ongoing reason to be skeptical toward the exact estimates. For example, prices for suspended flights are still being excluded and replaced by imputed readings for some parts of the air transportation index. Alcohol prices are being imputed with several regions still restricting access (bars etc). Out-of-stock items continue to have their prices imputed. Prices at temporarily shut businesses continue to be imputed. This series of points isn't meant to imply that StatsCan isn't doing its best to adapt to unique challenges, but judgement in the face of such question marks surrounding data quality should lead markets to put a filter on the estimates.

With these caveats in mind, here were the drivers in the short-term:

- Charts 2 and 3 break down the weighted contributions to year-over-year and month-ago inflation to give a sense of where the pressures to the upside and downside are coming from.
- Electricity prices spiked higher because they increased by 17% y/y in Ontario for the biggest rise since May 2003 as a result of higher prices that were introduced on June 1st. In month-ago terms this driver should drop out in July but will continue to impact the year-over-year readings until June 2021 barring further policy changes. Chart 4 shows electricity price inflation along with what at times have been other transitory drivers. For instance, mortgage interest cost is finally turning lower and with more to come given the lags to policy rate and market rate changes.
- Gasoline prices rose in month-ago terms and fell at a slower pace in year-ago terms, in line with our tracking based upon market prices (chart 5).
- I'm a little surprised by auto prices and had not factored a mild positive contribution to higher inflation from that part of the basket. As chart 6 shows, auto prices should follow the currency with a lag over time and yet they increased this time. It's not an airtight relationship mind you. Strong sales momentum during May and June during the initial phase of the recovery was likely a driver of pricing power, but the relationship between sticker prices and USDCAD could reassert itself to the downside with a lag.
- Prices for clothing and accessories as well as the recreation/reading/education category posted less of a decline than previously.
- Chart 7 shows the breakdown of what got included in the trimmed mean CPI core measure in June. The biggest outlier moves were excluded such that components like gas and electricity prices did not impact the core measure.

Chart 2

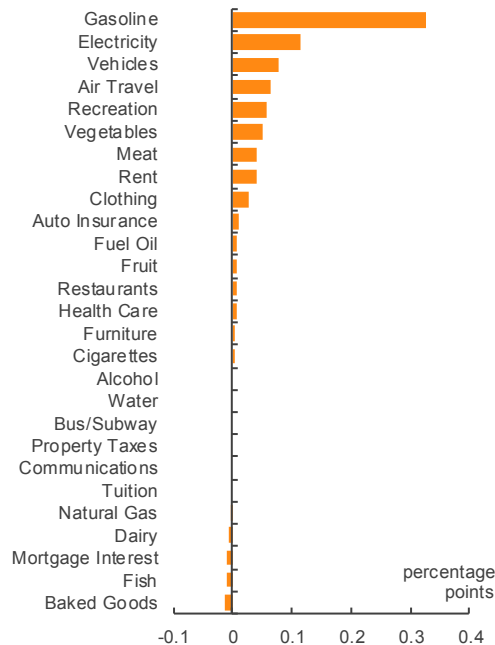
Weighted Contributions to June's 12-Month Change in Headline CPI



Source: Scotiabank Economics, Statistics Canada.

Chart 3

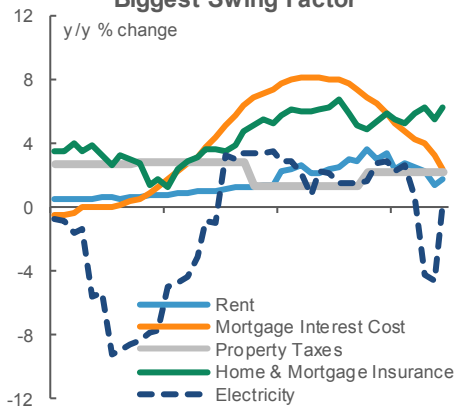
Weighted Contributions to June's Monthly Change in Headline CPI



Source: Scotiabank Economics, Statistics Canada.

Chart 4

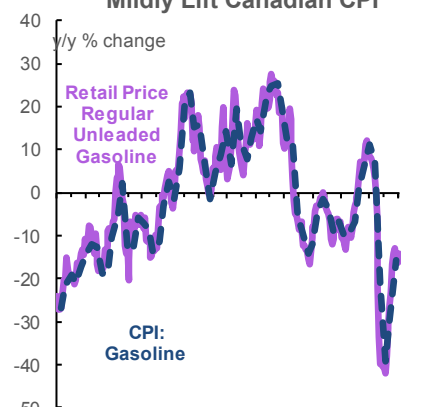
Electricity Prices Are The Biggest Swing Factor



Sources: Scotiabank Economics, Statistics Canada.

Chart 5

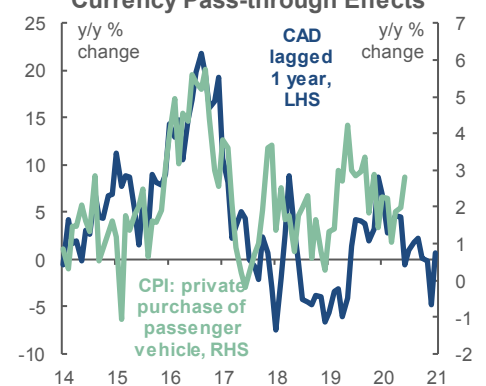
Gas Prices To Mildly Lift Canadian CPI



Sources: Scotiabank Economics, Statistics Canada, Natural Resources Canada.

Chart 6

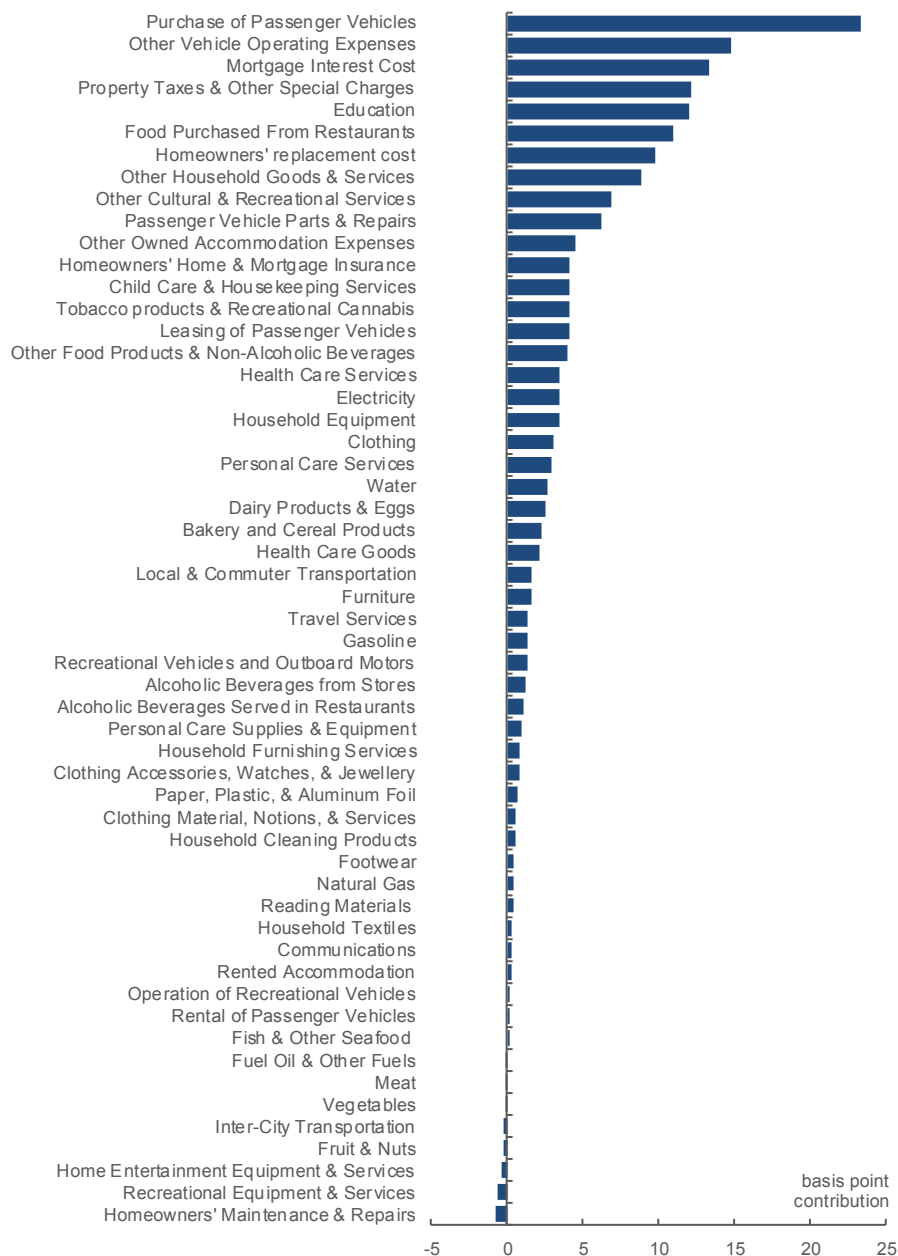
Auto Price Inflation Bottoming on Currency Pass-through Effects



Sources: Scotiabank Economics, Statistics Canada, Bank of Canada.

Chart 7

Weighted Component Contributions to the June CPI Trim Measure



Sources: Scotiabank Economics, Statistics Canada.

Fixed Income	Government Yield Curves (%):												Central Banks	
U.S. CANADA GERMANY JAPAN U.K. CANADA GERMANY JAPAN 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		
	0.14	0.14	0.16	0.26	0.27	0.29	0.59	0.60	0.63	1.28	1.31	1.33	Canada - BoC	0.25
	0.27	0.27	0.27	0.35	0.35	0.35	0.50	0.51	0.53	0.99	0.99	1.04	US - Fed	0.25
	-0.69	-0.67	-0.67	-0.69	-0.66	-0.65	-0.49	-0.46	-0.44	-0.06	-0.02	-0.02	England - BoE	0.10
	-0.13	-0.13	-0.13	-0.11	-0.11	-0.10	0.02	0.03	0.04	0.58	0.58	0.61		
	-0.11	-0.11	-0.08	-0.12	-0.10	-0.05	0.12	0.14	0.17	0.63	0.65	0.68		
	Spreads vs. U.S. (bps):													
	13	13	12	8	8	6	-8	-9	-10	-30	-32	-30	Euro zone - ECB	0.00
	-83	-81	-83	-95	-92	-93	-108	-106	-107	-135	-133	-136	Japan - BoJ	-0.10
-27	-27	-29	-37	-38	-38	-57	-58	-60	-71	-73	-72			
-25	-25	-24	-38	-36	-34	-47	-47	-46	-66	-66	-65			
Equities	Level						% change:						Mexico - Banxico	5.00
	Last	Change				1 Day	1-wk	1-mo	1-yr					
S&P/TSX	16158	-5.4				-0.0	0.6	4.1	-2.2			Australia - RBA	0.25	
Dow 30	26921	81.0				0.3	0.2	3.4	-0.9			New Zealand - RBNZ	0.25	
S&P 500	3258	0.4				0.0	1.0	4.5	9.1			Next Meeting Date		
Nasdaq	10666	-14.0				-0.1	1.1	6.1	30.0			Canada - BoC	Sep 09, 2020	
DAX	13085	-87.0				-0.7	1.2	6.7	6.5			US - Fed	Jul 29, 2020	
FTSE	6201	-68.4				-1.1	-1.5	-0.7	-17.5			England - BoE	Aug 06, 2020	
Nikkei	22752	-132.6				-0.6	-0.8	1.4	6.2			Euro zone - ECB	Sep 10, 2020	
Hang Seng	25058	-577.7				-2.3	-1.7	2.2	-11.7			Japan - BoJ	Sep 17, 2020	
CAC	5032	-71.9				-1.4	-1.5	1.7	-9.6			Mexico - Banxico	Aug 13, 2020	
Commodities	Level						% change:							
WTI Crude	41.51	-0.41				-1.0	0.8	2.6	-26.2			Australia - RBA	Aug 04, 2020	
Natural Gas	1.66	-0.02				-1.0	-6.7	-0.3	-28.2			New Zealand - RBNZ	Aug 11, 2020	
Gold	1859.32	17.41				0.9	2.7	6.0	30.5					
Silver	20.56	1.12				5.7	8.8	17.3	26.0					
CRB Index	142.48	-0.02				-0.0	0.9	2.5	-20.2					
Currencies	Level						% change:							
USDCAD	1.3414	-0.0045				-0.3	-0.7	-0.8	2.2					
EURUSD	1.1592	0.0065				0.6	1.6	2.9	3.4					
USDJPY	107.15	0.3500				0.3	0.2	0.2	-0.7					
AUDUSD	0.7145	0.0017				0.2	2.0	3.4	1.5					
GBPUSD	1.2732	0.0001				0.0	1.2	2.1	2.1					
USDCHF	0.9290	-0.0042				-0.5	-1.6	-2.0	-5.4					

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