

ON DECK FOR THURSDAY, JULY 15

Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
US	07-15	08:30	Empire State Manufacturing Index	Jul	--	18.0	43.0
US	07-15	08:30	Export Prices (m/m)	Jun	--	1.4	1.2
US	07-15	08:30	Import Prices (m/m)	Jun	--	1.1	1.0
US	07-15	08:30	Initial Jobless Claims (000s)	Jul 10	360	350	360
US	07-15	08:30	Continuing Claims (000s)	Jul 3	3,300	3,300	3,241
US	07-15	08:30	Philadelphia Fed Index	Jul	--	28.0	21.9
CA	07-15	09:00	Existing Home Sales (m/m)	Jun	--	--	-8.4
US	07-15	09:15	Capacity Utilization (%)	Jun	75.7	75.6	75.4
US	07-15	09:15	Industrial Production (m/m)	Jun	0.7	0.6	0.4
US	07-13	09:30	Powell to Deliver Semi-Annual Testimony to Senate Banking Panel				
US	07-13	11:00	Fed's Evans Discusses the Economy				

KEY POINTS:

- Earlier flattening reverses on Fed comments
- Powell says tapering under “active consideration”
- What explains the market reaction to the BoC?
- Why the BoC may well turn more hawkish soon
- Hawkish BoE comments light up gilts, sterling...
- ...while jobs data was mixed ahead of the reopening experiment
- China's economic growth remains soft
- Canadian home sales dipped again under restrictions
- Mixed readings on the US industrial complex...
- ...indicate that a services and consumption rebound will be required to boost growth while supply chain issues get resolved
- Australia's job gain is a good sign for other countries about to pull back on job supports

INTERNATIONAL

Markets are in a bit of a risk-off frame of mind so far. Equities are soft with the S&P down ¼%, the TSX up ¼% and European cash markets all generally down by about 1%. The US curve was flattening but 10s are cheapening in the wake of comments by tFed Chair Powell that tapering is under “active consideration.” There is no follow-through on the Canadian curve to yesterday's BoC decisions. Gilts are underperforming especially at the front-end with the 2-year yield up 7bps on the day and 10s up 4bps as BoE comments added to exit bets. Most EGB 10s are flat except Italy's slight widening over bunds. Oil is down by about 1% across WTI and Brent.

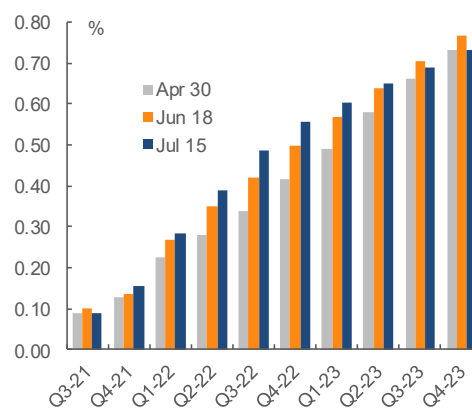
Take your pick of favourite theories for flattening. Mine remains debt ceiling related scarcity and liquidity issues combined with rising concern that the Fed is going to wait too long to tighten and ultimately risk tossing the economy into the recycling bin when it finally acts which would be a replay of multiple past policy errors. That's not a forgone conclusion, but risks continue to build imo. There is zero need for \$120B/month of Fed purchases. They should have already tapered which is where I side with Bullard's comments this morning. The problem is that cycle after cycle, the Fed waits too long to change its mind and by the time it achieves committee consensus it goes too far

CONTACTS

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

Chart 1

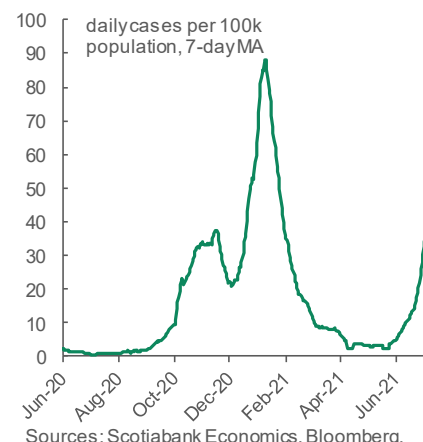
BoE Implied Policy Rate



Sources: Scotiabank Economics, Bloomberg.

Chart 2

UK COVID-19 Cases
Picking Up Again



Sources: Scotiabank Economics, Bloomberg.

in the opposite direction and both the economy pays a price. I like the outlook this year and next, but I worry that the biggest risk to the medium term picture is a presently very slow-footed Fed if it's not already getting too late.

Overnight developments were focused upon hawkish BoE talk, soft Chinese growth and encouraging Australian jobs. There should be little incremental calendar risk on tap today in the US and Canada.

Sterling and gilts have been on a bit of a wild ride this morning. First, mixed jobs data drove sterling a little softer when only 6k jobs were added in May over April and only 25k on the rolling 3 month ago convention (91k consensus). Chart 3 shows UK employment over time while chart 4 shows the composition of job changes over time. An offset was that jobless claims plunged by 115k in June and the prior month was revised to a bigger drop of 151k from -93k. I'd personally emphasize claims as the fresher data and they are falling by record amounts.

Earlier this morning BoE MPC member Michael Saunders rattled gilts and sterling with hawkish comments. He argued that if the economy and inflation continue to perform in line with recent trends and risks don't materially rise, then "options might include curtailing the current asset purchase program—ending it in the next month or two and before the full £150 billion has been purchased—and/or further monetary policy action next year." That follows yesterday's remarks by fellow MPC member Ramsden who said he leaned more strongly toward an inflationary scenario being sustained at levels below near-term peaks than the weight he places on a more disinflationary scenario. Chart 1 on the front page shows the evolution of the implied rate path.

Personally, I'd be more comfortable with where the BoE may head after seeing some evidence on how the UK handles blowing the barn doors open on restrictions after tomorrow in the context of soaring Delta variant cases (chart 2, front page).

Australia gained another 29.1k jobs in June following the prior month's surge of 115.2k. Given statistical noise, that about matches expectations for 20k. All of it was full-time(+51.6k) as part-time jobs fell. There was little incremental effect on the A\$ or curve. Still, this is encouraging for other countries like the US, UK and Canada as they move toward withdrawing labour supports in a couple of months, since Australia's decision to end Job Keeper wage subsidies had driven a drop in jobs during April from which it has mightily recovered.

Chinese GDP growth remains disappointingly weak. Q2 grew only slightly beat expectations because of rare downward revisions to the prior quarter. China usually gets its GDP figures out with remarkable speed and equally remarkable is the fact it almost never revises them! Q2 growth landed at 5.3% q/q annualized after Q1 grew by just 1.6%. Forget about year-over-year growth rates (7.9%, prior 18.3%) given pandemic distortions as it's the weak momentum in 2021's quarter-on-quarter rates that informs growth tracking at the margin. Few other major economies focus upon growth in year-over-year terms anyway. June data was a little better than expected, however, which suggests stronger hand-off momentum into Q3. Retail sales were up 12.1% y/y (10.8% consensus) and industrial output climbed 8.3% (7.9% consensus). Here too, however, we're dealing with year-ago distortions.

CANADA

There is nothing material on tap in Canada today with just existing home sales for June to consider. Sales fell 8.4% m/m in June. Wait another month for reopening effects. June's drop follows a -12.5% decline in April and a -7.4% drop in May, all of which happened during lockdowns and tightened restrictions including banned open houses in parts of the country like Ontario. In addition, there is a lag between relaxed restrictions and the ability to go out and kick some tires with secured pre-approvals. Listings fell in June which indicates soft supply which is probably consistent with not being able to list in the first place! I'd expect a Q3 rebound of sorts but we're kind of in the seasonal dead zone now for the Canadian housing market. We'll have to wait a while for the next big test in the classic spring market which hopefully won't be torpedoed by covid waves and restrictions. For now, fade

Chart 3

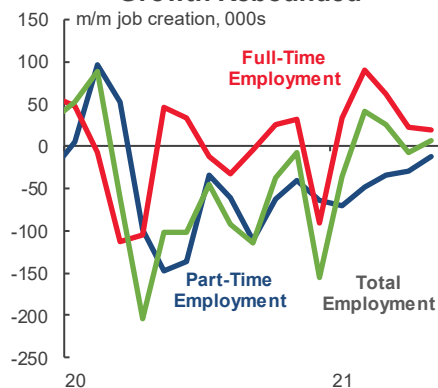
The UK Is a Long Way from a Jobs Recovery



Sources: Scotiabank Economics, ONS.

Chart 4

UK Monthly Job Growth Rebounded



Sources: Scotiabank Economics, Bloomberg.

the evidence as explainable and economic growth will have to rely more upon reopening services, broad consumption and transitioning toward better exports and investment.

As a reminder, please see yesterday's recap of what the Bank of Canada did [here](#).

So why did the market react the way it did as yields dropped and CAD slipped post-communications despite the BoC doing exactly what Scotia Economics expected? The BoC tapered purchases by \$1B to \$2B as we expected well ahead of consensus months ago. The base case was for the BoC to leave its output gap framework broadly unchanged which is what they did while not triggering what I had flagged as a risk to this base case that could have involved pulling it forward either now, or in October. Well, October it is likely to be as the higher forecast level of GDP only marginally impacted their output gap framework. Hikes continue to be guided for mid-2022. In all, this was very much in keeping with BoC's 'gradual and measured' (a euphemism for slow-footed?) policy guidance that didn't rock the boat.

In terms of market reactions, I think a swift reversal of pre-communications positioning is one factor to consider but that shouldn't be confused with markets thinking the BoC was dovish per se. Canada 10s were cheapening through Tuesday and particularly Wednesday morning ahead of the BoC perhaps on bets that the BoC would come off sounding more hawkish than it did. That doesn't mean they were dovish, just less hawkish than immediately preceding events might have had market participants expecting. It just means that the BoC didn't follow the RBNZ's abrupt ending of purchases and come off sounding more abruptly hawkish themselves especially in the wake of another US inflation surprise the day before. When the BoC didn't turn incrementally hawkish, position squaring ensued, and then global market factors took over.

But I still think yesterday was just a placeholder and October will probably pose greater risk with the BoC getting behind the curve here. By then, several things may change:

- **The BoC was forecasting inflation using old inflation statistics that are about to be redefined higher** by Statistics Canada with pandemic-era spending weights when June CPI comes out.
- **We're just transitioning toward a reopening economy and the BoC probably and reasonably wants to see some hard evidence on how this develops** in relation to their 7.3% q/q Q3 forecast and through a few jobs reports to test their expectations for a strong rebound.
- **Canada is also on the cusp of achieving herd immunity either later this month or by early August such that by October the double vaccination rate should be well over 75%** of adults 12+ with kids pending vaccine trials. By then, getting COVID-19 is much more likely to be a choice, much like how shooting yourself in the foot is a personal choice.
- **An election call likely stands in the way and we need to see platforms and who wins by how much before judging fiscal and political risk.** Current polls point to a majority for the Liberals which likely means more spending impulses.
- **Then there is the Fed and if the FOMC is closer to tapering and having an open, earnest dialogue about doing so by the October MPR with the US debt ceiling hopefully addressed then the BoC should have more cover for turning incrementally hawkish.** They met our expectations yesterday as market expectations got ahead of themselves, but October could be a different matter.

UNITED STATES

US data releases were relatively minor this morning and focused upon the industrial complex.

US industrial output advanced by 0.4% m/m (0.6% consensus, 0.7% Scotia) which was a little shy of expectations but I'm more concerned about the soft details. Utilities were up 2.7% m/m with mining up 1.4% while manufacturing was little changed at -0.1% m/m. Generally speaking, most manufacturing data is showcasing the supply chain challenges. If one believes this to be a transitory factor from an inflation standpoint, then one should also argue that it's a transitory weight on growth that will pick up as supply chains eventually sort themselves out. **Instead, some commentary tries to have its cake and eat it too by saying transitory effects on inflation will dissipate and we'll still get crappy growth in the aftermath which seems implausible.**

That followed a pair of regional Fed manufacturing gauges that offer mixed interpretations of where the next ISM-manufacturing report may land. The Philly Fed's metric fell by about nine points to 21.9, but the NY Fed's Empire gauge ([here](#)) soared to 43 from 17.4. Philly fell as new orders cooled (17 from 22.2), so did shipments (24.6 from 27.2) and so did unfilled orders (19 from 22.5) while employment was little changed (29.2 from 30.7). Prices paid are still soaring but at a slower pace in the Philly gauge (69.7 from 80.7). That returns us to the April signals for prices after June's peak. As for the Empire measure, prices paid were a less dovish signal as they only slipped to 76.8 from 79.8 and remain elevated. New orders soared to 33.2 from 16.3, shipments soared to 43.8 from 14.2 and hiring picked up (20.6 from 12.3). Prices paid in the Empire gauge were unchanged at a strongly rising pace (64.6 versus 64 prior).

All of which probably means that services reopening will be relied upon to carry the ball forward as goods sector supply chain issues gradually sort themselves out. Those supply chain bottlenecks are fundamentally caused by excess stimulus that drove a massive demand surge that damaged supply chains were not prepared to handle. The Fed poured kerosene onto the picture and has been surprised by the resulting inflation.

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		
	0.23	0.22	0.20	0.81	0.80	0.74	1.34	1.35	1.29	1.97	1.97	1.93	Canada - BoC	0.25
	0.46	0.45	0.48	0.91	0.91	0.90	1.30	1.29	1.26	1.81	1.80	1.74	US - Fed	0.25
	-0.67	-0.68	-0.68	-0.62	-0.62	-0.60	-0.32	-0.32	-0.31	0.16	0.18	0.18	England - BoE	0.10
	-0.12	-0.12	-0.11	-0.12	-0.12	-0.12	0.01	0.02	0.03	0.64	0.67	0.66		
	0.15	0.08	0.09	0.37	0.30	0.26	0.67	0.63	0.61	1.15	1.10	1.13		
	Spreads vs. U.S. (bps):													
	23	23	29	11	11	15	-5	-6	-3	-16	-17	-18	Euro zone - ECB	0.00
	-90	-90	-88	-142	-141	-135	-167	-167	-160	-181	-180	-175	Japan - BoJ	-0.10
-35	-35	-31	-93	-92	-86	-133	-133	-127	-133	-130	-127			
-7	-14	-11	-44	-50	-48	-67	-72	-68	-81	-87	-80			
Equities	Level						% change:						Mexico - Banxico	4.25
S&P/TSX Dow 30 S&P 500 Nasdaq DAX FTSE Nikkei Hang Seng CAC	Last	Change					1 Day	1-wk	1-mo	1-yr				
	20162	15.2					0.1	0.5	-0.3	25.5	Australia - RBA	0.10		
	34922	-11.1					-0.0	1.5	1.8	30.0	New Zealand - RBNZ	0.25		
	4363	-11.0					-0.3	1.0	2.7	35.2				
	14544	-100.5					-0.7	-0.1	3.4	37.9				
	15631	-157.5					-1.0	1.4	-0.6	20.9				
	7037	-54.6					-0.8	0.1	-1.9	11.8				
	28279	-329.4					-1.2	0.6	-3.5	24.2				
	27996	208.8					0.8	3.1	-1.5	12.1				
	6493	-65.8					-1.0	1.5	-2.2	27.1				
Commodities	Level						% change:						Next Meeting Date	
WTI Crude Natural Gas Gold Silver CRB Index	72.23	-0.90					-1.2	-1.0	0.2	75.3	Canada - BoC	Sep 08, 2021		
	3.62	-0.04					-1.0	-1.8	11.8	103.8	US - Fed	Jul 28, 2021		
	1821.63	-5.90					-0.3	1.0	-2.0	0.6	England - BoE	Aug 05, 2021		
	26.17	0.07					0.2	-0.8	-5.6	38.5	Euro zone - ECB	Jul 22, 2021		
	212.71	-0.67					-0.3	1.5	1.2	50.6	Japan - BoJ	Jul 16, 2021		
Currencies	Level						% change:							
USDCAD EURUSD USDJPY AUDUSD GBPUSD USDCHF	1.2545	0.0036					0.3	0.1	3.0	-7.1	Mexico - Banxico	Aug 12, 2021		
	1.1813	-0.0024					-0.2	-0.3	-2.6	3.5	Australia - RBA	Aug 03, 2021		
	110.02	0.0500					0.0	0.3	-0.1	2.9	New Zealand - RBNZ	Aug 17, 2021		
	0.7436	-0.0045					-0.6	0.1	-3.3	6.1				
	1.3851	-0.0009					-0.1	0.5	-1.6	10.0				
0.9180	0.0027					0.3	0.3	2.2	-2.8					

This report has been prepared by Scotiabank Economics as a resource for the clients of Scotiabank. Opinions, estimates and projections contained herein are our own as of the date hereof and are subject to change without notice. The information and opinions contained herein have been compiled or arrived at from sources believed reliable but no representation or warranty, express or implied, is made as to their accuracy or completeness. Neither Scotiabank nor any of its officers, directors, partners, employees or affiliates accepts any liability whatsoever for any direct or consequential loss arising from any use of this report or its contents.

These reports are provided to you for informational purposes only. This report is not, and is not constructed as, an offer to sell or solicitation of any offer to buy any financial instrument, nor shall this report be construed as an opinion as to whether you should enter into any swap or trading strategy involving a swap or any other transaction. The information contained in this report is not intended to be, and does not constitute, a recommendation of a swap or trading strategy involving a swap within the meaning of U.S. Commodity Futures Trading Commission Regulation 23.434 and Appendix A thereto. This material is not intended to be individually tailored to your needs or characteristics and should not be viewed as a "call to action" or suggestion that you enter into a swap or trading strategy involving a swap or any other transaction. Scotiabank may engage in transactions in a manner inconsistent with the views discussed in this report and may have positions, or be in the process of acquiring or disposing of positions, referred to in this report.

Scotiabank, its affiliates and any of their respective officers, directors and employees may from time to time take positions in currencies, act as managers, co-managers or underwriters of a public offering or act as principals or agents, deal in, own or act as market makers or advisors, brokers or commercial and/or investment bankers in relation to securities or related derivatives. As a result of these actions, Scotiabank may receive remuneration. All Scotiabank products and services are subject to the terms of applicable agreements and local regulations. Officers, directors and employees of Scotiabank and its affiliates may serve as directors of corporations.

Any securities discussed in this report may not be suitable for all investors. Scotiabank recommends that investors independently evaluate any issuer and security discussed in this report, and consult with any advisors they deem necessary prior to making any investment.

This report and all information, opinions and conclusions contained in it are protected by copyright. This information may not be reproduced without the prior express written consent of Scotiabank.

™ Trademark of The Bank of Nova Scotia. Used under license, where applicable.

Scotiabank, together with "Global Banking and Markets", is a marketing name for the global corporate and investment banking and capital markets businesses of The Bank of Nova Scotia and certain of its affiliates in the countries where they operate, including; Scotiabank Europe plc; Scotiabank (Ireland) Designated Activity Company; Scotiabank Inverlat S.A., Institución de Banca Múltiple, Grupo Financiero Scotiabank Inverlat, Scotia Inverlat Casa de Bolsa, S.A. de C.V., Grupo Financiero Scotiabank Inverlat, Scotia Inverlat Derivados S.A. de C.V. – all members of the Scotiabank group and authorized users of the Scotiabank mark. The Bank of Nova Scotia is incorporated in Canada with limited liability and is authorised and regulated by the Office of the Superintendent of Financial Institutions Canada. The Bank of Nova Scotia is authorized by the UK Prudential Regulation Authority and is subject to regulation by the UK Financial Conduct Authority and limited regulation by the UK Prudential Regulation Authority. Details about the extent of The Bank of Nova Scotia's regulation by the UK Prudential Regulation Authority are available from us on request. Scotiabank Europe plc is authorized by the UK Prudential Regulation Authority and regulated by the UK Financial Conduct Authority and the UK Prudential Regulation Authority.

Scotiabank Inverlat, S.A., Scotia Inverlat Casa de Bolsa, S.A. de C.V., Grupo Financiero Scotiabank Inverlat, and Scotia Inverlat Derivados, S.A. de C.V., are each authorized and regulated by the Mexican financial authorities.

Not all products and services are offered in all jurisdictions. Services described are available in jurisdictions where permitted by law.