

#### Contributors

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Chart 1

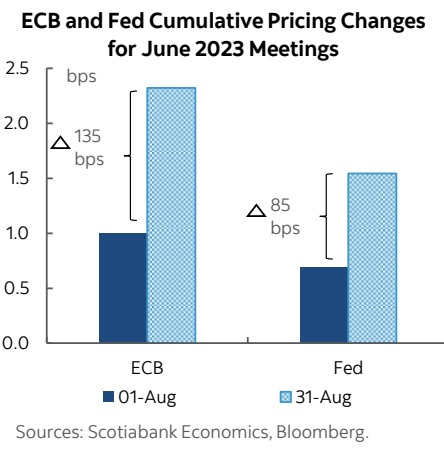
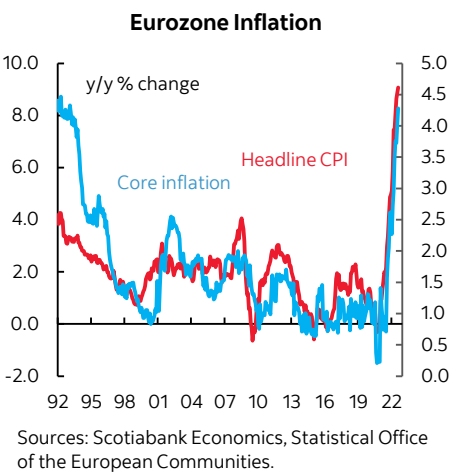


Chart 2



#### On Deck for Wednesday, August 31

Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
US	08-31	07:00	MBA Mortgage Applications (w/w)	Aug 26	--	--	-1.2
US	08-31	08:00	Fed's Mester Discusses Economic Outlook				
US	08-31	08:15	ADP Employment Change (m/m)	Aug	--	300.0	--
CA	08-31	08:30	Real GDP (m/m)	Jun	0.2	0.1	0.0
CA	08-31	08:30	Real GDP (q/q a.r.)	2Q	4.2	4.4	3.1
US	08-31	09:45	Chicago PMI	Aug	--	52.1	52.1
US	08-31	18:00	Dallas Fed Holds Event to Introduce New President Lorie Logan				
US	08-31	18:30	Fed's Bostic Speaks on Role of Fintech in Financial Inclusion				

#### KEY POINTS:

- **Bonds on the run as ECB bets intensify**
- **August's bond market was more about the ECB's later pivot than the Fed**
- **Eurozone inflation was stronger than expected...**
- **...prompting hawkish guidance and higher bond yields**
- **China's PMIs weakened again**
- **PBoC sets another higher fix in a losing battle**
- **Canadian GDP to inform cooling narrative**
- **Ignore US ADP payrolls**
- **The FOMC gets a new voice**
- **Otherwise mixed Asian macro readings**

Sovereign yields are on the march higher again this morning and primarily due to Eurozone inflation and ECB bets (see below). Italy's curve is leading the way with a bear flattener led by an 11bps rise in 2s, but significant increases are sweeping across EGBs. Yields on gilts are up another 10–11bps across the curve partly due to carry out of the Eurozone inflation readings and partly because the ONS stated that energy rebates won't factor into CPI calcs. Spillover effects through carry are driving US Treasury and Canadian government yields higher by about 3–4bps across maturities. That's hitting equities again although less so than earlier this morning perhaps given jawboning out of China (see below) with present European cash markets trading between little changed in Germany to down by as much as 1% in London. US and Canadian equity futures are performing a little better with Toronto flat while S&Ps are up by a mild ¼%. Oil is down another ~\$3. The USD is picking up some safehaven flows along with the yen.

Eurozone CPI surprised higher and markets reacted by leaning a little further toward pricing a 75bps hike next week and adding a few basis points to the cumulative path over coming months. In fact, the cumulative changes in market pricing for cumulative ECB rate increases between now and next June has gone up by much more over the month of August than has been the case for the Fed that pivoted earlier (chart 1). Heck, for that matter, while almost all global central banks woke up to rising inflation risk too late, the ECB slept in the latest. Headline CPI climbed two-tenths to 9.1% y/y (9% consensus) with prices up 0.5% m/m (0.4% consensus). Core CPI was up 4.3% y/y (4.1% consensus, 4% prior). Chart 2 shows the readings flying off the y-axis. The firmer than expected reading was primarily due to Italy's readings this morning. Italian CPI was up 0.8% m/m (0% consensus) and 9% y/y (8.2% consensus, 8.4% prior). France was a bit softer than expected at 0.4% m/m (0.6% consensus) and 6.5% y/y (6.7% consensus, 6.8% prior). This follows the other day's German and Spanish figures that were largely in line with expectations. Inflation expectations over the longer run are on or slightly above target

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which should counsel policy normalization instead of a policy rate around 0% if the central bank treats its inflation target with any seriousness (chart 3).

ECB Governing Council member and Bundesbank President Nagel was quick to react. He said that “There is an urgent....to act decisively at its next meeting to combat inflation. We need a strong rise in interest rates in September.”

European consumers are feeling the pinch effects with French real consumer spending down 0.8% m/m in July (-0.2% consensus) after a flat June and a string of generally weak readings back to last year

China’s PMIs weakened again in the August readings that came out overnight and mainland equities fell. The composite PMI slipped to 51.7 from 52.5 and confirms that the improvement in June was a transitory reopening effect after which this indication of growth in China’s economy fell for the next two months. The non-manufacturing PMI led the way lower (52.6, 53.8 prior) as the manufacturing PMI held steady and was slightly in contraction territory (49.4, 49 prior).

Cooling Chinese macro readings in a weak economy and relative PBoC-Fed bets forced the PBoC to set a stronger yuan fix for the 6<sup>th</sup> straight session. The effect of the fix was to set the yuan back to basically where it was at this time yesterday as it continues to hover around 6.9 and hence about 9% weaker over the past six months. We’re also seeing some jawboning out of China about vague plans to add stimulus measures.

Asian factories put in a mixed performance. Japanese industrial output was up by 1% (-0.5% consensus) and retail sales were also stronger than expected (+0.8% m/m, 0.3% consensus) although in both cases we’re getting significant lift effects from prices and partly due to yen weakness. South Korean industrial output, however, gave back most of the prior month’s gain and fell 1.3% m/m in July.

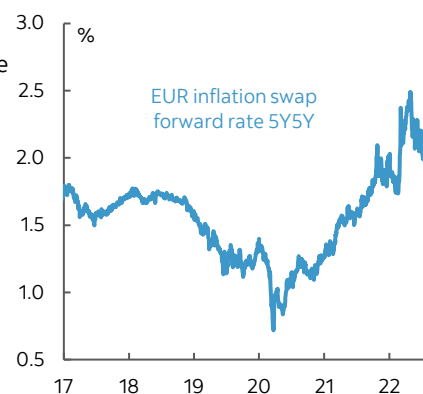
On tap for this morning is Canadian GDP (8:30amET). Watch for cooling momentum. Q2 should be strong (consensus 4.4% q/q SAAR, Scotia 4%), but the economy contracted in the month of May, likely squeezed out modest growth in June (consensus 0.1% m/m, Scotia 0.2%) as we get the more complete estimate, and then the first ‘flash’ reading for July probably faces downside risk. If so, then that sets up a weak Q3 with Canadian GDP growth having been brought forward into the H1 outperformance. That said, this is necessary with the economy having pushed further into excess demand in H1 so a lot more damage is likely required on the demand side going forward.

US ADP payrolls will be reintroduced after it was suspended in order to work on a new methodology. Again. Every time they do this it winds up being just as useless as before. Given that ADP has tracked private nonfarm payrolls very poorly over time it will take some time to assess whether the new methodology is of any use. Of course, like nonfarm, neither measure will capture what’s happening to most of the small business sector and so we still need to track the volatile household survey over time which has been the weakest of the bunch for several months now.

We might hear the new Dallas Fed President’s views that matter because she gets a vote when the calendar flips to 2023 and her views are not well known (6pmET). I’ve met her through meetings with the markets group at the NY Fed and she always struck me as thoughtful and measured. Cleveland Fed President Mester is also set to speak (8amET).

Chart 3

## Eurozone Inflation Expectations



Sources: Scotiabank Economics, Bloomberg.

Fixed Income	Government Yield Curves (%):												Central Banks	
	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		
U.S.	3.48	3.44	3.39	3.29	3.27	3.23	3.13	3.10	3.11	3.24	3.22	3.31	Canada - BoC	2.50
CANADA	3.67	3.63	3.51	3.30	3.26	3.23	3.11	3.07	3.10	3.03	2.99	3.07	US - Fed	2.50
GERMANY	1.18	1.15	0.92	1.37	1.34	1.16	1.53	1.51	1.37	1.60	1.60	1.50	England - BoE	1.75
JAPAN	-0.08	-0.09	-0.08	0.01	0.01	0.02	0.23	0.23	0.23	1.20	1.21	1.16		
U.K.	3.00	2.92	2.94	2.75	2.67	2.70	2.80	2.70	2.70	3.08	2.98	2.93		
	Spreads vs. U.S. (bps):													
CANADA	19	19	12	1	-1	-0	-2	-3	-1	-22	-23	-24	Euro zone - ECB	0.50
GERMANY	-230	-229	-247	-192	-193	-208	-160	-159	-174	-164	-162	-181	Japan - BoJ	-0.10
JAPAN	-356	-353	-347	-328	-325	-321	-290	-288	-288	-205	-201	-216		
U.K.	-48	-52	-45	-54	-60	-53	-34	-40	-41	-16	-24	-38	Mexico - Banxico	8.50
Equities	Level						% change:							
	Last	Change			1 Day	1-wk	1-mo	1-yr						
S&P/TSX	19513	-323.2			-1.6	-2.5	-0.9	-5.2					Australia - RBA	1.85
Dow 30	31791	-308.1			-1.0	-3.4	-3.2	-10.1					New Zealand - RBNZ	3.00
S&P 500	3986	-44.5			-1.1	-3.5	-3.5	-11.9						
Nasdaq	11883	-134.5			-1.1	-4.0	-4.1	-22.1						
DAX	12924	-37.3			-0.3	-2.2	-4.2	-18.4						
FTSE	7281	-80.4			-1.1	-2.8	-1.9	2.3						
Nikkei	28092	-104.1			-0.4	-0.8	0.4	-1.3					Canada - BoC	Sep 07, 2022
Hang Seng	19954	5.4			0.0	3.6	-1.0	-23.3					US - Fed	Sep 21, 2022
CAC	6173	-37.0			-0.6	-3.3	-4.3	-7.6						
Commodities	Level						% change:							
WTI Crude	89.00	-2.64			-2.9	-6.2	-9.8	29.9					England - BoE	Sep 15, 2022
Natural Gas	9.06	0.02			0.2	-2.9	10.1	107.0						
Gold	1716.12	-7.89			-0.5	-2.0	-2.8	-5.4					Euro zone - ECB	Sep 08, 2022
Silver	18.70	-0.52			-2.7	-1.6	-6.8	-20.8						
CRB Index	293.58	-8.18			-2.7	-0.9	0.5	34.6					Japan - BoJ	Sep 22, 2022
Currencies	Level						% change:							
USDCAD	1.3111	0.0018			0.1	1.1	2.1	3.9					Mexico - Banxico	Sep 29, 2022
EURUSD	0.9990	-0.0025			-0.2	0.2	-2.7	-15.4						
USDJPY	138.78	-0.0100			-0.0	1.2	5.4	26.1					Australia - RBA	Sep 06, 2022
AUDUSD	0.6855	0.0001			0.0	-0.8	-2.4	-6.3						
GBPUSD	1.1615	-0.0041			-0.4	-1.6	-5.2	-15.6					New Zealand - RBNZ	Oct 04, 2022
USDCHF	0.9806	0.0063			0.6	1.4	3.3	7.2						

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