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GLOBAL ECONOMICS

DAILY POINTS

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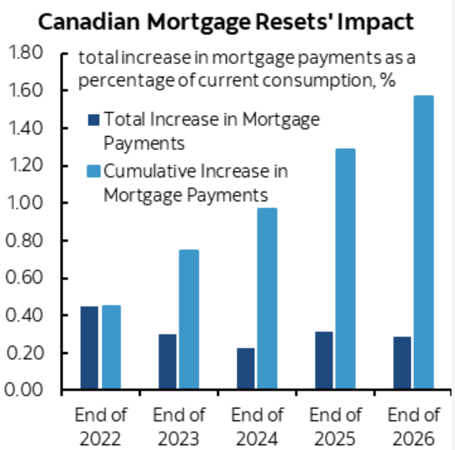
Chart 1



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

On Deck for Thursday, December 21

Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
CA	12-21	08:30	Retail Sales (m/m)	Oct	0.8	0.8	0.6
CA	12-21	08:30	Retail Sales ex. Autos (m/m)	Oct	--	0.5	0.2
US	12-21	08:30	GDP (q/q a.r.)	3Q T	5.3	5.2	5.2
US	12-21	08:30	GDP Deflator (q/q a.r.)	3Q T	--	3.6	3.6
US	12-21	08:30	Initial Jobless Claims (000s)	45276	220	215.0	202.0
US	12-21	08:30	Continuing Claims (000s)	45269	1875	1880.0	1876.0
US	12-21	08:30	Philadelphia Fed Index	Dec	--	-3.0	-5.9
US	12-21	10:00	Leading Indicators (m/m)	Nov	--	-0.5	-0.8

KEY POINTS:

- **U.S., Canadian data still poses risk as holidays approach**
- **BoC research poured cold water on mortgage reset hysteria**
- **Canadian retail sales probably posted a gain in October, November guidance key**
- **US GDP, core PCE revisions on tap**
- **Will US claims retain the prior dip?**
- **Bank Indonesia holds, pushes back against premature easing**
- **Turkey's central bank hikes, signals it's nearing terminal**

Expect a quiet session with the only main risk being any potential overreaction to minor revisions to US GDP and core PCE (8:30amET), modest Canadian data, and whether the US holds onto the dip in initial claims that fell to 202k the week before last (8:30amET).

The USD is mildly depreciating. There is a bias toward mild cheapening across sovereign bonds led by about a 2–3bps cheapening across US Ts. Equities are mixed with N.A. futures up by roughly ½% but European cash markets following yesterday afternoon's sell off in N.A.

Bank Indonesia held its 7-day reverse repo rate at 6% as widely expected. Governor Warjiyo said "we will not rush" to ease next year and that they may only have comfort in addressing risks to the stability of the rupiah by "the second half of 2024." There was little overall effect on the currency or rates.

Turkey's central bank hiked by another 250bps to a new one-week repo rate of 42.5% as expected. The statement said that "The Committee anticipates to complete the tightening cycle as soon as possible" and emphasized its data dependence in determining future actions.

Canada updates retail sales for October and offers a preliminary estimate for November this morning (8:30amET). Statcan had previously estimated retail sales were up 0.8% m/m in October but this number is subject to revision. The November reading will kick off holiday season tracking.

Canada's lagging payrolls report is also due out but it's for October (8:30amET). The US releases its payroll and household survey numbers simultaneously but Canada has a long lag. Tomorrow we'll get Canadian GDP and US PCE estimates to keep data risk alive.

CANADIAN MORTGAGE RESETS

The Bank of Canada has released a staff analytical note on the impact of mortgage resets (**here**). It's highly recommended reading for multiple audiences with any interest in Canada whatsoever, whether from a broad economy perspective or an interest in housing finance or the implications for the Bank of Canada's potential future policy actions.

The punchline is that under reasonable assumptions, they position the reset shock as a relatively small effect. Keys are the following:

- Absent any income growth over the years ahead, "the median borrower may need to dedicate up to 4% more of their pre-tax income to mortgage payments by the end of 2027" relative to what they were paying back in February 2022 just before the BoC began to raise its policy rate.
- By assuming income growth over 2024–27 at a pace equal to the average annual income gain over the past ten years, they whittle this estimate down further to a cumulative impact upon the mortgage debt service ratio of 1.5 percentage points starting from February 2022 through to the end of 2027.

Put another way, under their no income growth assumption, the average annual increase in debt payments as a share of pre-tax income for the median borrower is around 0.7 percentage points per year at a compounded rate. Under their scenario that assumes income growth, the average annual rise is about ¼% per year.

That's not nothing, but it's pretty darn close!

Also note that the income growth assumptions may be low. Income growth is currently proceeding at a considerably faster rate than the ten -year average as employment and wages both soared this year. I think it's fair to conclude that wages will continue to rise at an aggressive pace over the next 3+ years given what is being incorporated into long-term collective bargaining contracts.

They also do not assume any changes in borrower behaviour "such as making accelerated payments or switching to another mortgage product" and "Thus, our simulation results represent an upper-bound estimate."

You could add to that by noting they say nothing about other mitigating steps being taken by borrowers and lenders alike including adjusting amortization periods and backing into strong home equity gains since the start of the pandemic, not to mention shifts in household behaviour.

A don't have a problem with their assumptions on rates with the focus being upon fixed rates since variable rate mortgage resets are largely done. At about 3.2% right now, the Canada 5-year GoC yield may be rich in the short-term, but over the coming years it's probably in the ballpark of what is reasonable after tacking a modest term premium onto a reasonable range of neutral policy rate assumptions.

It's important to read their whole study and also important to note that while the math leans against resets being a big macroeconomic shock, the distributional effects will be important. For instance, lenders see only the indebted folks and not the 60% of Canadians who don't even have a mortgage.

How does their work compare to spit balled estimates on the street given that the BoC has access to more system-wide data and greater resources? It leans close to my earlier estimate that resets would take up about a cumulative 1% of total income over the years ahead as argued in **this** piece back in September. I had argued that the effect on consumption would be trivial (chart 1).

By contrast, the BoC's research makes a mockery of some of the rest of the street's shrill cries especially its loudest and most alarmist voices.

Now how did the BoC research get covered and did market participants even notice it? Instead of Bloomberg—that, recall, hyped the ridiculously alarmist estimate—flagging that the BoC came up with little by way of any macroeconomic shock from mortgage resets, they only flashed that "higher payments hit 45% of mortgages" according to BoC research. Alarmism over substance. Frankly that's appalling and it misinforms a considerable part of the world's market participants who stare at their screens treating its content as the divine truth.

I still contend that mortgage resets are like an economic mirage. From a distance it looks like a dark, ominous, shimmering danger. The closer you get to the shock period leaves you standing with mouth agape wondering where all the worries went.

For BoC watchers, the clear conclusion is that while staff research doesn't necessarily represent the opinions of Governing Council, it informs them and likely results in the following takeaways:

- The BoC is not going to ease just because of mortgage resets;
- As they have noted, resets are how monetary policy works in the first place;
- and the shock factor isn't anywhere close enough to something that could derail the outlook on its own.

On both counts, this further leans against premature rate cuts with markets overpricing easing too soon.

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.	4.36	4.33	4.39	3.86	3.84	3.91	3.86	3.85	3.92	4.00	3.99	4.04
CANADA	3.91	3.90	3.91	3.17	3.17	3.24	3.06	3.05	3.15	2.89	2.89	2.97
GERMANY	2.47	2.47	2.57	1.95	1.95	2.08	1.97	1.97	2.12	2.16	2.15	2.33
JAPAN	0.05	0.05	0.06	0.22	0.20	0.28	0.58	0.56	0.67	1.52	1.50	1.62
U.K.	4.12	4.12	4.36	3.52	3.51	3.82	3.54	3.53	3.79	4.08	4.07	4.29
	Spreads vs. U.S. (bps):											
CANADA	-45	-43	-48	-69	-67	-66	-81	-80	-77	-110	-109	-107
GERMANY	-189	-186	-182	-191	-189	-183	-189	-188	-180	-184	-183	-171
JAPAN	-430	-428	-433	-365	-365	-363	-328	-329	-325	-247	-249	-241
U.K.	-24	-22	-3	-34	-34	-9	-32	-32	-13	8	8	26

Equities	Level		% change:			
	Last	Change	1 Day	1-wk	1-mo	1-yr
S&P/TSX	20601	-238.8	-1.1	-0.1	2.4	5.3
Dow 30	37082	-475.9	-1.3	-0.0	5.7	11.1
S&P 500	4698	-70.0	-1.5	-0.2	3.5	21.1
Nasdaq	14778	-225.3	-1.5	0.3	4.1	38.0
DAX	16652	-81.2	-0.5	-0.6	4.7	18.1
FTSE	7670	-45.4	-0.6	0.3	2.5	2.3
Nikkei	33140	-535.5	-1.6	1.4	-0.9	25.0
Hang Seng	16621	7.3	0.0	1.3	-6.3	-15.5
CAC	7546	-37.0	-0.5	-0.4	4.4	14.7
Commodities	Level		% change:			
WTI Crude	73.47	-0.75	-1.0	2.6	-5.5	-6.2
Natural Gas	2.47	0.02	0.9	3.2	-13.2	-53.7
Gold	2037.76	6.38	0.3	0.1	2.0	12.3
Silver	23.97	0.06	0.3	5.5	2.5	1.0
CRB Index	266.39	-1.31	-0.5	2.8	-3.9	-3.6
Currencies	Level		% change:			
USDCAD	1.3353	-0.0016	-0.1	-0.4	-2.5	-1.9
EURUSD	1.0979	0.0037	0.3	-0.1	0.6	3.5
USDJPY	142.79	-0.7800	-0.5	0.6	-3.8	7.8
AUDUSD	0.6757	0.0027	0.4	0.9	3.1	0.7
GBPUSD	1.2656	0.0017	0.1	-0.9	0.9	4.8
USDCHF	0.8589	-0.0038	-0.4	-1.0	-2.8	-7.3

Central Banks	
Current Rate	
Canada - BoC	5.00
US - Fed	5.50
England - BoE	5.25
Euro zone - ECB	4.50
Japan - BoJ	-0.10
Mexico - Banxico	11.25
Australia - RBA	4.35
New Zealand - RBNZ	5.50
Next Meeting Date	
Canada - BoC	Jan 24, 2024
US - Fed	Jan 31, 2024
England - BoE	Feb 01, 2024
Euro zone - ECB	Jan 25, 2024
Japan - BoJ	Jan 23, 2024
Mexico - Banxico	Feb 08, 2024
Australia - RBA	Feb 05, 2024
New Zealand - RBNZ	Feb 27, 2024