

There is not much terribly new information from this morning's US releases that were generally on the softer side. Analysis follows for inflation, consumption, incomes, the saving rate and ISM-manufacturing. I think ISM is settling into a path of more moderate growth that simply unwinds the overshoot provided by stimulus. There is a strong argument to be made for pent-up consumption demand through the saving rate evidence and the role played by harsher than usual weather and shutdown effects in temporarily depressing consumption.

At the margin, the data does nothing to further inform what is already an expected H1 pause and at this point is not inconsistent with our expectation for a return to Fed rate hikes later this year. After Q4 GDP growth that solidly beat expectations at 2.7%, a strong consumer sector remains a very decent base case to play a significant role in driving a return to hiking with modest upside pressure expected for inflation over H2-onward.

US Core PCE Unchanged, Saving Rate Points To Pent-Up Consumer Demand

United States, Personal Income / Consumption, % m/m, December:

Actual: 1.0 / -0.5

Consensus: 0.3 / -0.3

Scotia: 0.3 / -0.4

Prior: Unrevised from 0.2 / 0.4

United States, PCE / core PCE deflators, y/y % change, December:

Actual: 1.7 / 1.9

Consensus: 1.7 / 1.9

Scotia: 1.6 / 1.9

Prior: Unrevised from 1.8 / 1.9

- The broad outlines of this set of figures contained few surprises on balance. Weakness in consumption is explainable while the saving rate suggests pent-up spending demand and core inflation remained unchanged and near the Fed's 2% policy goal.
- Real consumption fell by 0.6% which matches expectations imputed from yesterday's GDP accounts such that there is no new information being revealed here. Nominal spending fell by 0.5% and so all of the decline was due to lower volumes.
- Because incomes were up by 1% m/m in December and consumption was soft, the saving rate shot much higher. All the way to 7.6% from 6.1% the prior month. Americans saving 7.6% of their paycheques??! The frugal American consumer? Imagine that. Sudden shocks to the saving rate like this one are almost always an indication of transitory factors that get unwound in subsequent periods. In this case I think that's weather and shutdown effects. The saving rate is almost four times higher than it bottomed at in 2005 when the cycle was getting to an end. There is nowhere near the same household finance dynamic this time around; in fact, it's the opposite with very strong financial conditions for households.

CONTACTS

Derek Holt, VP & Head of Capital Markets Economics

416.863.7707

Scotiabank Economics

derek.holt@scotiabank.com

- This release included income growth for January ahead of later consumption figures with the mismatch driven by the effects of the government shutdown on data collection and dissemination. January’s personal income dipped by 0.1% m/m which isn’t terribly surprising after the magnitude of the jump in December which was the largest gain since December 2012.
- Core PCE inflation bang on 1.9% unchanged while headline ticked down one move to 1.7% and by less than CPI drifted lower. The inflation figures matched expectations.

US ISM Disappoints But Still Signals Moderate Growth

ISM-manufacturing, February:

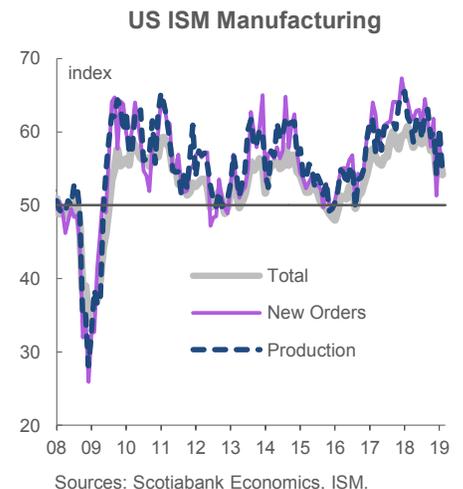
Actual: 54.2

Scotia: 55.0

Consensus: 55.8

Prior: 56.6

- ISM-manufacturing disappointed consensus expectations with softer growth being signalled. The underlying details broadly supported the softer headline.
- Overall, I think the likely path forward points toward continued moderate growth in the manufacturing sector after a temporary acceleration that began prior to the US election in November 2016 and was temporarily juiced by the Tax Cuts and Jobs Act of early last year and the US\$300 billion spending bill from just over one year ago. Reversing that temporary acceleration does not mean recession, versus a return to more normal growth. Potential upside could come as the global economy stabilizes and if a trade truce can be struck between the US and China.
- The headline reading is the lowest since November 2016—ironically the month of the US election as the rise has now been fully reversed.
- The new orders book decelerated to 55.5 from 58.2. This was driven by a softer domestic order book as new export orders picked up to 55.3 (53.8 prior).
- Employment decelerated to 52.3 (55.5 prior).
- Prices paid stabilized at 49.4 (49.6 prior).



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 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, Scotiabanc Inc.; Citadel Hill Advisors L.L.C.; The Bank of Nova Scotia Trust Company of New York; Scotiabank Europe plc; Scotiabank (Ireland) Limited; Scotiabank Inverlat S.A., Institución de Banca Múltiple, Scotia Inverlat Casa de Bolsa S.A. de C.V., 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 authorised 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 authorised 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., and Scotia 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.