TD Economics

The Weekly Bottom Line

January 4, 2019

Highlights of the Week

United States

- The New Year came with baggage from the old for thousands of federal employees caught in the middle of a budget tug-of-war between Congress and the White House that has led to a partial government shutdown.
- The volatility in stock markets continued early in the week as a slew of weaker-than-expected economic data and signs of a slowing China roused investor concerns that global growth may be slowing faster than expected.
- Fortunately, a strong payrolls tally lifted investors' spirits by week's end. Employment rose 312k and the unemployment rate edged up to 3.9% as more people joined the workforce. Hourly earnings growth also topped 3% (year-on-year) for a third consecutive month.

Canada

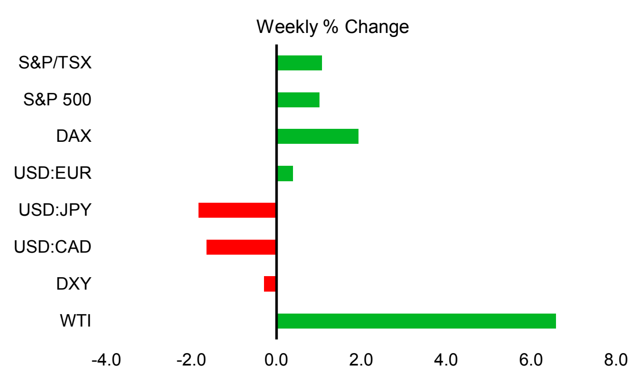
- A soft jobs report that left the unemployment rate at a historically-low 5.6% highlighted a light week for Canadian data.
- The S&P/TSX composite index is up modestly on the week, but global risk-off sentiment and a decline in energy prices have weighed heavily on the index in recent weeks.
- Oil prices enjoyed a strong run this week, with Brent rising around 9% and WTI up 6% as markets weigh recent data suggesting large Saudi production cuts against global growth concerns.

This Week in the Markets

	Current*	Week Ago	52-Week High	52-Week Low
Stock Market Indexes				
S&P 500	2517	2486	2931	2351
S&P/TSX Comp.	14383	14222	16567	13780
DAX	10766	10559	13560	10382
FTSE 100	6843	6734	7877	6585
Nikkei	19562	20015	24271	19156
Fixed Income Yields				
U.S. 10-yr Treasury	2.65	2.72	3.24	2.45
Canada 10-yr Bond	1.92	1.95	2.60	1.83
Germany 10-yr Bund	0.21	0.24	0.77	0.15
UK 10-yr Gilt	1.27	1.27	1.73	1.19
Japan 10-yr Bond	-0.04	0.00	0.16	-0.04
Foreign Exchange Cross Rates				
C$ (USD per CAD)	0.75	0.73	0.82	0.73
Euro (USD per EUR)	1.14	1.14	1.25	1.12
Pound (USD per GBP)	1.27	1.27	1.43	1.25
Yen (JPY per USD)	108.3	110.3	114.5	104.7
Commodity Spot Prices**				
Crude Oil ($US/bbl)	48.1	45.3	76.4	42.3
Natural Gas ($US/MMBtu)	2.72	3.25	5.46	2.52
Copper ($US/met. tonne)	5713.8	5987.0	7330.5	5713.8
Gold ($US/troy oz.)	1283.6	1281.1	1358.5	1174.2

*as of 11:28 am on Friday. **Oil-WTI, Cushing, Nat. Gas-Henry Hub, LA (Thursday close price), Copper-LME Grade A, Gold-London Gold Bullion; Source: Bloomberg.

WTI Jumps on Signs of Saudi Output Cuts



Note: Data as of 11:31 AM ET, January 4, 2019
Sources: Bloomberg, TD Economics

Global Official Policy Rate Targets

	Current Target
Federal Reserve (Fed Funds Rate)	2.25 - 2.50%
Bank of Canada (Overnight Rate)	1.75%
European Central Bank (Refi Rate)	0.00%
Bank of England (Repo Rate)	0.75%
Bank of Japan (Overnight Rate)	-0.10%

Source: Central Banks.

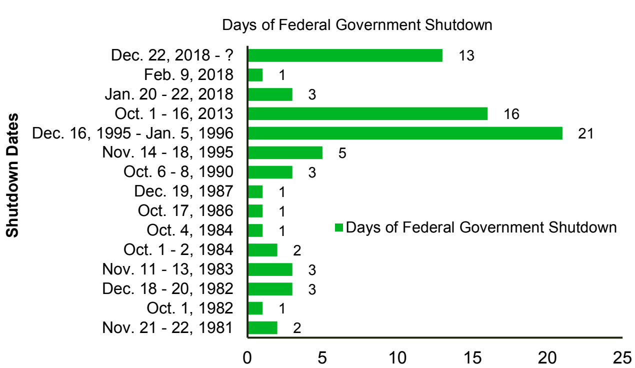
U.S. - The Shutdown Slowdown

Happy New… whatever. 2019 kicked off with a fizzle as a partial U.S. government shutdown that began in the old year limped into the new. President Trump and Congress are at a stalemate over discretionary funding for 25% of the Federal government, and a border wall with Mexico. The standoff meant a not-so-happy start to the New Year for over 800,000 federal employees who have been furloughed, or if considered "essential", had to work without pay.

Set to enter its third week, the shutdown is expected to negatively impact consumer spending and business activity. Assuming it ends soon, it is projected to lower first quarter GDP growth by 0.1 percentage points. Once resolved, federal employees will receive back pay, (though workers on contract will not), and this should boost economic activity in the second quarter. The question that remains is how long it will last. The longest government shutdown was for 21 days in 1995 (Chart 1), but workers and businesses who depend on their spending, are hopeful that such a scenario will not be repeated.

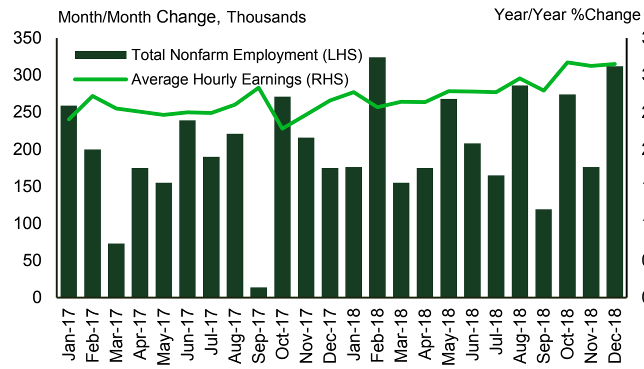
The stock market also rang in the New Year noticeably lower. Sentiment had been dragged down by a confluence of factors ranging from slowing global growth and uncertainty over the Fed's policy path to simmering trade tensions between the U.S. and China. A weaker-than-expected reading for December's ISM manufacturing index on top of an outright contraction in China's manufacturing activity, further fueled fears through the middle of the week. Though still technically in growth territory, the U.S.

Chart 1: As Federal Government Shutdown Continues, Workers Feel the Squeeze



Source: Congresional Research Service, TD Economics

Chart 2: Solid Labor Market Dynamics Places U.S. Consumer on Firm Footing



Source: Bureau of Labor Statistics, TD Economics

ISM index posted the slowest pace of expansion since November 2016, reflecting concerns of less robust demand and trade worries. The Trump administration has negotiated truces with multiple trading partners, however, many of these are set to expire in short order. Unless a long-term agreement can be reached, businesses may face renewed trade uncertainty as the year unfolds.

By the end of the week, a nod to "patience" by Fed Chair Powell and a strong December jobs report helped pull equity markets back into positive territory. Non-farm payrolls exceeded expectations, adding 312K jobs in December. This resulted in 99 straight months of expanding payrolls – the longest stretch on record. Even the uptick in the unemployment rate to 3.9% resulted from a labor force rising participation rate. Such dynamics suggest that even amid the tightest labor market in decades, the U.S. economy is still able to pull workers off the sideline and into the job mix. Wages also surprised to the upside, growing by 3.2% year-on-year (Chart 2) – the best full-year gain since 2008.

The employment data should serve to calm concerns that the American economy is quickly running out of steam. While growth in 2019 is projected to be lower (see forecast), we still expect it to remain above the economy's trend pace. All in all, government showdowns aside, consumers remain on firm footing, supported by the most favorable labor market in decades.

Shernette McLeod, Economist | 416-415-0413

Canada - An Uneventful Start to 2019

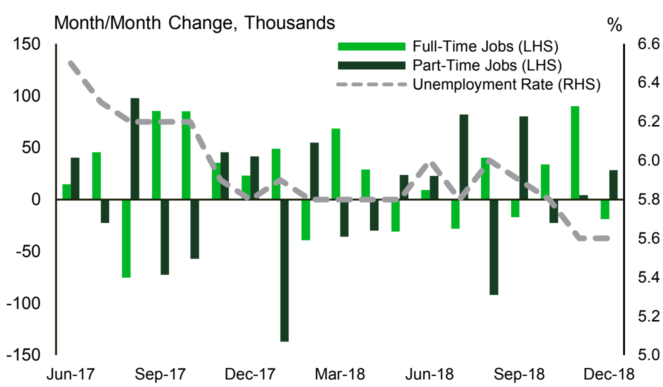
The last two weeks were relatively quiet on the Canadian economic data front. Today's labour force survey report was the highlight this week, but proved largely immaterial from a policymaker's standpoint. Financial and commodity price movements, however, remained the centre of attention again given the ongoing global risk-off sentiment amidst fears of a global economic slowdown.

Following November's blockbuster jobs report, December's less stellar report does not change the Canadian labour market narrative. Employment gains were modest at 9.3k, largely in line with consensus expectations. This was accompanied by an almost equal change in labour force growth (+9.6k) that together acted to hold the unemployment rate at a historically-low 5.6% (Chart 1).

The details of the report were less encouraging. Part-time jobs (+28.3k) drove the headline gain, with full-time employment falling on the month (-18.9k). Furthermore, job gains were concentrated in the self-employment category (+46.4k), the most volatile class of worker in the labour force survey. Still, these compositional changes are likely more noise than signal.

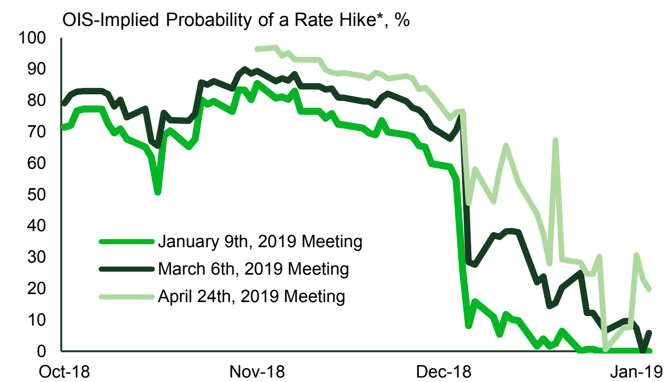
Meanwhile, the subdued trend in wage growth continues to be one of the more puzzling aspects of Canada's labour market. Coming in at 1.5% year-on year (y/y), the pace implies that Canada's labour market may not be as tight as one would expect given its record-low unemployment rate.

Chart 1: Part-time Jobs Drive Modest Gain, with the Unemployment Rate Still at Record Low



Source: Statistics Canada, TD Economics

Chart 2: The Market's Pricing of a Near-Term Rate Hike has Declined Remarkably since November



*As of January 4th, 2019. Source: Bloomberg, TD Economics

Combined with a moderation in other indicators and a struggling energy sector, the economic picture suggests that higher interest rates are not urgently needed. Indeed, odds of an upcoming rate hike for the next three Bank of Canada meetings as implied by the OIS curve have steadily declined since October. In fact, expectations of a rate hike by January have fallen to zero from roughly 80% in October, although ongoing global risk-off sentiment has likely contributed in part to this sudden re-pricing (Chart 2).

Following a December which saw markets mostly in the red, performance was slightly more positive this week, with the energy-heavy S&P/TSX composite posting a modest gain relative to last week at the time of writing. Just as encouraging was the strong run up in oil prices this week after dipping to lows not seen in more than a year. The WTI benchmark is up roughly 6%, and Brent crude is up an even more impressive 9%. Data suggesting Saudi output declines ahead of the OPEC+ cut implementation schedule contributed to the recent oil price rally. That said, prices are likely to remain volatile as markets weigh output cuts against evidence of slowing global growth.

In the meantime, higher world oil prices are a welcome development for Canada's ailing oil patch. Since early December, Alberta's output curtailment plan has sent heavy oil prices surging, narrowing the WCS benchmark's spread to WTI to below US$15.

Omar Abdelrahman, Economist | 416-734-2873

U.S.: Upcoming Key Economic Releases

U.S. CPI - December*

Release Date: January 11, 2019

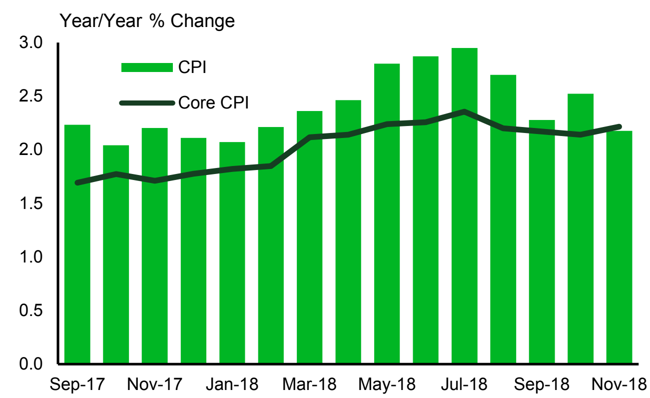
Previous: 0.0% m/m, 2.2% y/y

TD Forecast: -0.1% m/m, 1.9% y/y

Consensus: -0.1% m/m, 1.9% y/y

We expect another sharp retreat in oil prices to be reflected on a significant 8.4% m/m decline in the CPI's fuels category, more than offsetting an expected increase in food prices at 0.2% m/m. The notable decline in energy prices should have dragged down headline CPI inflation to a negative 0.1% m/m print for December, which should also be reflected on a softer 1.9% annual increase. On the back of another steady rise in its core services segment, we anticipate core CPI prices to have registered their third consecutive 0.2% m/m increase, maintaining annual core CPI inflation stable at 2.2%. Looking ahead, we expect headline CPI inflation to gradually rebound to above-2% levels as oil prices stabilize and core CPI inflation maintains its recent steady pace.

U.S. Consumer Price Index (CPI)



Source: Bureau of Labor Statistics, TD Economics

*Forecast by Rates and FX Strategy Group. For further information, contact TDRates&FXCommoditiesResearch@tdsecurities.com

Canada: Upcoming Key Economic Releases

Canadian International Trade - November*

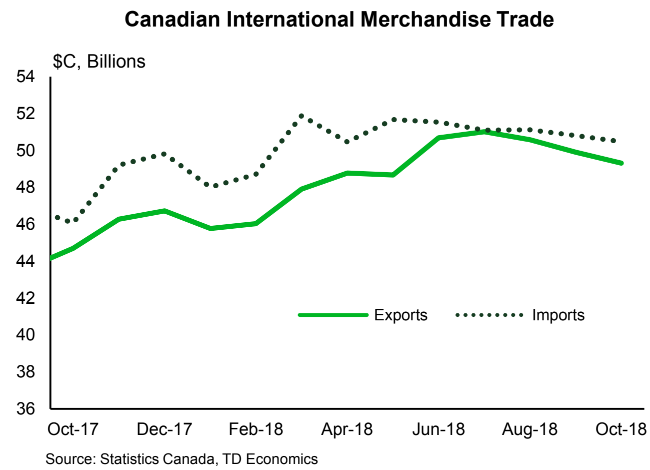
Release Date: January 8, 2019

Previous: -$1.2bn

TD Forecast: -$2.8bn

Consensus: -$1.93bn

TD looks for the international trade deficit to widen to $2.8bn in November on another outsized decline in energy exports, as a sharp pullback in crude oil prices is compounded by voluntary shut-ins throughout the oil sands. Motor vehicle exports unwind part of the 6% gain in October, contributing to a wider deficit, while nominal imports should see little change after posting four declines in the last five months. Aircraft imports have scope to recover on higher deliveries to Canadian airlines while imports of machinery & equipment will be closely watched as a barometer for a rebound for Q4 investment. The real trade balance is expected to post a more modest deterioration on lower commodity prices, allowing real exports to outperform the nominal decline, although the external sector should still be a drag on growth.



Canadian Housing Starts - December*

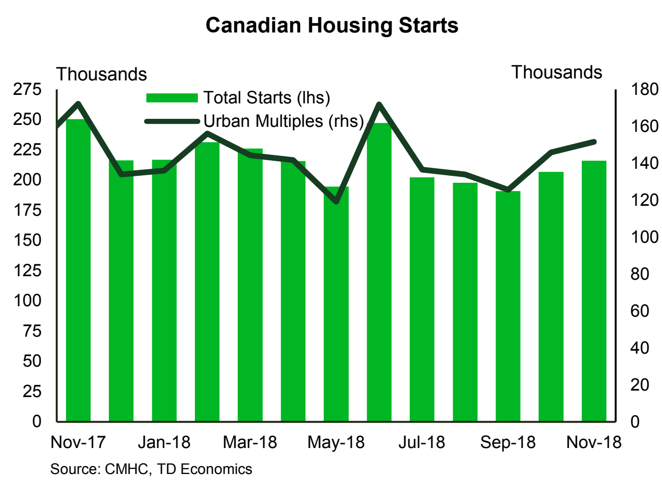
Release Date: January 9, 2019

Previous: 216k

TD Forecast: 205k

Consensus: 210k

Housing starts are forecast to slow to an annualized 205k in December. Weaker multi-unit construction in Toronto and Vancouver should provide the main catalyst following outsized gains the prior month, while single family construction should see little change. This will leave housing starts to tally roughly 213k for the year as a whole, only slightly below the 220k units created in 2017. However, our forecast is consistent with only 55k single-unit starts in urban areas, which is only slightly above the worst year on record from 1982.



Bank of Canada Rate Decision*

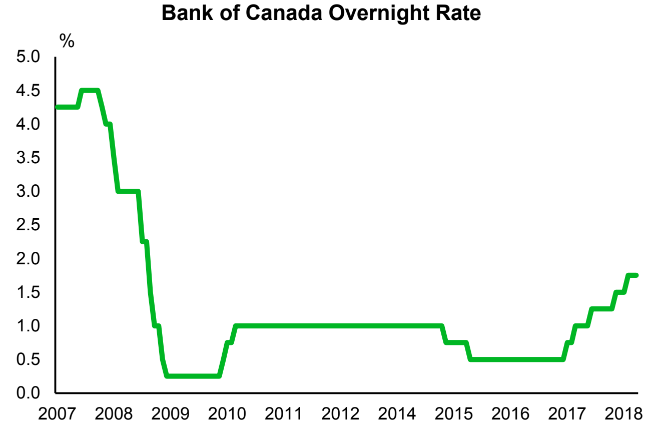
Release Date: January 9, 2019

Previous: 1.75%

TD Forecast: 1.75%

Consensus: 1.75%

We expect the Bank of Canada to hold the overnight rate steady at 1.75% next week, which is already fully priced into markets. The Bank will have to acknowledge recent developments in the energy sector and financial markets, but will try to strike a somewhat balanced tone as the longer term forecast is largely intact; we expect modest downward revisions to growth for 2019 (approximately 0.2 p.p.), but the 2020 growth estimate should be stable. Risks around international trade tensions and/or global growth may take a more prominent position in the hierarchy of risks, but we nonetheless look for Poloz to reiterate that the policy rate will need to move back to the neutral range while maintain the BoC's data dependence.



Source: Bank of Canada, TD Economics

*Forecast by Rates and FX Strategy Group. For further information, contact TDRates&FXCommoditiesResearch@tdsecurities.com

Release Date		Economic Indicator/Event	Data for Period	Units	Current	Prior
Recent Key Economic Indicators: Dec 24, 2018 - Jan 4, 2019						
United States						
Dec 26		S&P CoreLogic CS US HPI NSA	Oct	Y/Y % Chg.	5.48	5.5
Dec 27		New Home Sales	Nov	Thsd	568.0	544.0
Dec 27		Conf. Board Consumer Confidence	Dec	Index	128.1	136.4
Dec 28		Pending Home Sales	Nov	M/M % Chg.	-0.7	-2.6
Jan 02		Markit US Manufacturing PMI	Dec	Index	53.8	53.9
Jan 03		ADP Employment Change	Dec	Thsd	271.0	157.0
Jan 03		Initial Jobless Claims	Dec 29	Thsd	216.0	217.0
Jan 03		ISM Manufacturing	Dec	Index	54.1	59.3
Jan 03		ISM Employment	Dec	Index	56.2	58.4
Jan 03		Wards Total Vehicle Sales	Dec	Mlns	17.5	17.4
Jan 04		Change in Nonfarm Payrolls	Dec	Thsd	312.0	176.0
Jan 04		Unemployment Rate	Dec	%	3.9	3.7
Jan 04		Average Hourly Earnings	Dec	M/M % Chg.	0.4	0.2
Jan 04		Markit US Services PMI	Dec	Index	54.4	53.4
Canada						
Dec 27		CFIB Business Barometer	Dec	Index	53.6	61.2
Jan 02		MLI Leading Indicator	Nov	M/M % Chg.	-0.1	-0.2
Jan 02		Markit Canada Manufacturing PMI	Dec	Index	53.6	54.9
Jan 04		Hourly Wage Rate Permanent Employees	Dec	Y/Y % Chg.	1.5	1.5
Jan 04		Unemployment Rate	Dec	%	5.6	5.6
Jan 04		Net Change in Employment	Dec	Thsd	9.3	94.1
Jan 04		Industrial Product Price	Nov	M/M % Chg.	-0.8	0.2
International						
Dec 27	JN	Jobless Rate	Nov	%	2.5	2.4
Dec 27	JN	Retail Trade	Nov	Y/Y % Chg.	1.4	3.6
Jan 02	EZ	Markit Eurozone Manufacturing PMI	Dec	Index	51.4	51.4
Jan 02	UK	Markit UK PMI Manufacturing	Dec	Index	54.2	53.6
Jan 03	JN	Nikkei Japan PMI Manufacturing	Dec	Index	52.6	52.4
Jan 04	EZ	Consumer Price Index Core	Dec	Y/Y % Chg.	1.0	1.0
Jan 04	EZ	Producer Price Index	Nov	Y/Y % Chg.	4.0	4.9

Source: Bloomberg, TD Economics.

Release Date	Time*		Economic Indicator/Event	Data for Period	Units	Consensus Forecast	Last Period
			Upcoming Economic Releases and Events: Jan 7 - 11, 2019				
			United States				
Jan 07			Advance Goods Trade Balance	Nov	M/M % Chg.	-76.0	-77.2
Jan 07			New Home Sales	Nov	Thsd	568.0	544.0
Jan 07	10:00		Cap Goods Orders Nondef Ex Air	Nov	M/M % Chg.	-	-0.6
Jan 07	10:00		Durable Goods Orders	Nov	M/M % Chg.	-	0.8
Jan 07	10:00		Factory Orders	Nov	M/M % Chg.	0.3	-2.1
Jan 07	10:00		Factory Orders Ex Trans	Nov	M/M % Chg.	-	0.3
Jan 07	10:00		ISM Non-Manufacturing Index	Dec	M/M % Chg.	59.4	60.7
Jan 07	12:40		*Fed's Raphael Bostic speaks at the Rotary Club of Atlanta in Atlanta, GA*				
Jan 08	6:00		NFIB Small Business Optimism	Dec	Index	104.3	104.8
Jan 08	8:30		Trade Balance	Nov	Blns	-53.7	-55.5
Jan 09	8:20		*Fed's Raphael Bostic speaks the Chattanooga Chamber of Commerce in Chattanooga, TN*				
Jan 09	9:00		*Fed's Charles Evans speaks at the Discover Financial Services Company in Riverwoods, IL*				
Jan 09	11:30		*Fed's Eric Rosengren speaks at the Boston Economic Club in Boston, MA*				
Jan 09	14:00		FOMC Meeting Minutes	Dec 19			
Jan 10	8:30		Initial Jobless Claims	Jan 05	Thsd	-	231.0
Jan 10	8:35		*Fed's Tom Barkin speaks at the Raleigh Chamber of Commerce in Raleigh, NC*				
Jan 10	10:00		Wholesale Trade Sales	Nov	M/M % Chg.	-	-0.2
Jan 10	12:30		*Fed's James Bullard speaks at the Little Rock Chamber of Commerce in Little Rock, AR*				
Jan 10	13:00		*Fed's Charles Evans speaks at the Milwaukee Business Journal Economic Forecast in Milwaukee, WI*				
Jan 11	8:30		Consumer Price Index	Dec	M/M % Chg.	-0.1	0.0
Jan 11	8:30		Consumer Price Index	Dec	Y/Y % Chg.	1.9	2.2
Jan 11	8:30		Consumer Price Index Ex Food and Energy	Dec	M/M % Chg.	0.2	0.2
Jan 11	8:30		Consumer Price Index Ex Food and Energy	Dec	Y/Y % Chg.	2.1	2.2
			Canada				
Jan 08	8:30		Int'l Merchandise Trade	Nov	Blns	-1.9	-1.2
Jan 09	8:15		Housing Starts	Dec	Thsd	210.0	215.9
Jan 09	10:00		Bank of Canada Rate Decision	Jan 09	%	2.00	1.75
			International				
Jan 07	5:00	EZ	Retail Sales	Nov	Y/Y % Chg.	-	1.7
Jan 09	5:00	EZ	Unemployment Rate	Nov	%	-	8.1
Jan 09	20:30	CH	Consumer Price Index	Dec	Y/Y % Chg.	2.1	2.2
Jan 11	4:30	UK	Gross Domestic Product	Nov	M/M % Chg.	0.2	0.1
Jan 11	4:30	UK	Industrial Production	Nov	Y/Y % Chg.	-	-0.8

* Eastern Standard Time. Source: Bloomberg, TD Economics.

Disclaimer