TD Economics

The Weekly Bottom Line

January 25, 2019

Highlights of the Week

United States

- Global equity markets are up on the week, despite some negative economic news, and continued dysfunction in Washington. The ECB characterized the economic risks as to the downside, and will be more cautious removing stimulus.
- Amidst the U.S. partial government shutdown there was little data to unpack. Home sales showed a sour end to 2018 for real estate. Negotiations in Congress continue, but there is no clear end to the impasse at time of writing.
- Next week we get some key events - an FOMC rate decision with a press conference, and a payrolls report. Furloughed federal workers are expected to lift the unemployment rate, but should not affect the payrolls tally.

Canada

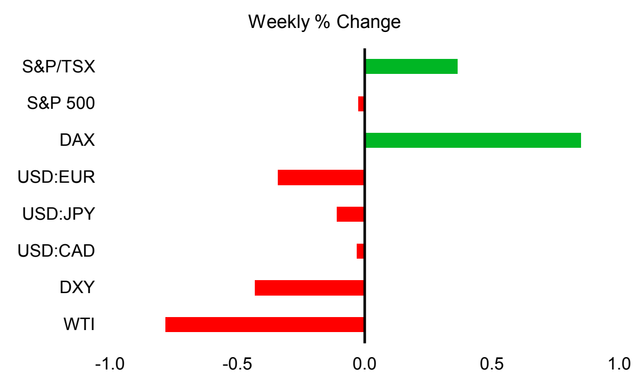
- The TSX and Canadian dollar traded sideways this week, hanging onto recent gains. Still, the WCS heavy oil price pushed higher and is up markedly compared to its November trough – a good news story for the beleaguered oil sector.
- Economic data released this week reinforced the slowing growth narrative, with wholesale activity, manufacturing sales and retail spending falling in November. The disappointing reports also caused us to shave our Q4 growth forecast. This softer economic backdrop should keep the Bank of Canada on hold at least until July.

This Week in the Markets

	Current*	Week Ago	52-Week High	52-Week Low
Stock Market Indexes				
S&P 500	2669	2671	2931	2351
S&P/TSX Comp.	15324	15304	16567	13780
DAX	11305	11206	13340	10382
FTSE 100	6827	6968	7877	6585
Nikkei	20774	20666	24271	19156
Fixed Income Yields				
U.S. 10-yr Treasury	2.75	2.78	3.24	2.55
Canada 10-yr Bond	1.97	2.04	2.60	1.83
Germany 10-yr Bund	0.20	0.26	0.77	0.15
UK 10-yr Gilt	1.31	1.35	1.73	1.19
Japan 10-yr Bond	0.00	0.02	0.16	-0.04
Foreign Exchange Cross Rates				
C$ (USD per CAD)	0.75	0.75	0.82	0.73
Euro (USD per EUR)	1.14	1.14	1.25	1.12
Pound (USD per GBP)	1.32	1.29	1.43	1.25
Yen (JPY per USD)	109.6	109.8	114.5	104.7
Commodity Spot Prices**				
Crude Oil ($US/bbl)	53.0	53.8	76.4	42.3
Natural Gas ($US/MMBtu)	3.16	3.43	4.80	2.52
Copper ($US/met. tonne)	5894.0	6029.5	7330.5	5713.8
Gold ($US/troy oz.)	1297.5	1281.8	1353.7	1174.2

*as of 10:56 am on Friday. **Oil-WTI, Cushing, Nat. Gas-Henry Hub, LA (Thursday close price), Copper-LME Grade A, Gold-London Gold Bullion; Source: Bloomberg.

Markets Mixed as Shutdown Drags On



Note: Data as of 11:11 AM ET, January 25, 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. - Markets Up Despite Lack of Good News on the Economy

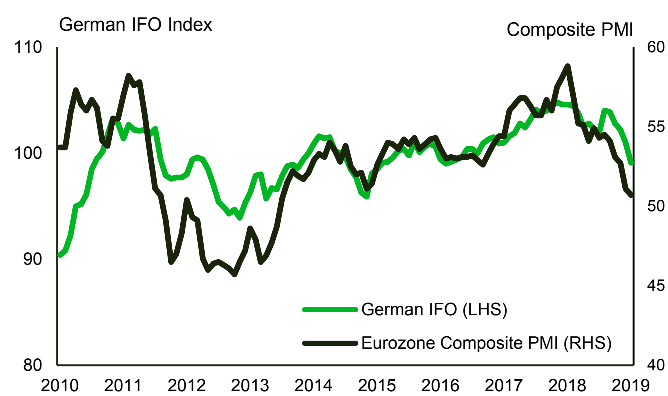
Global equity markets are up on the week, despite some negative economic news, and continued dysfunction in Washington. Most notably, Mario Draghi said that the risks to growth have moved to the downside, and the ECB will be even more cautious withdrawing stimulus. This more cautious view was supported by recent data, which showed worsening sentiment in the manufacturing sector, and in its leading economy (Chart 1).

We also got confirmation that China's economy slowed dramatically in the second half of 2018 (Chart2). The rebalancing of China's economy towards domestic consumption is underway, but the downward pressure from weaker construction and infrastructure investment on headline growth is being exacerbated by unanticipated declines in consumer and business sentiment resulting from trade tensions with the U.S.. So far the data remains consistent with our December forecast that calls for Chinese economic growth to slow further to 6.2% in 2019.

With the U.S. partial government shutdown affecting some government statistical agencies, there was little economic data this week. We did see that the resale housing market ended 2018 on a weak note, but we don't know what the housing starts or permit picture looked like.

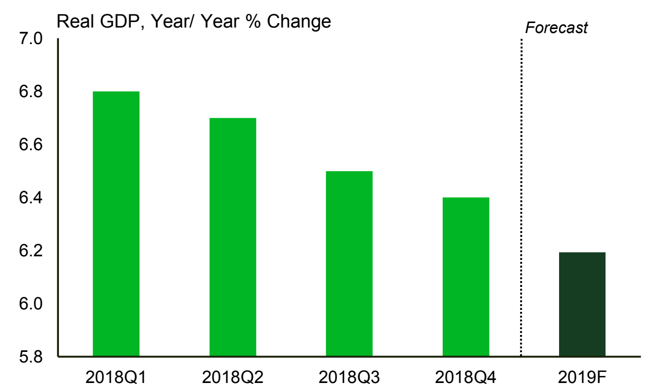
Looking ahead to next week, the closely watched advance release of Q4 real GDP growth is likely to be delayed. The incomplete picture of the U.S. economy is coming at an inconvenient time. Economists are trying to determine if the weakness in financial markets in the fourth quarter, which

Chart 1: European Business Confidence Deteriorates



Source: JP Morgan and Markit via Bloomberg, TD Economics

Chart 2: Chinese Growth Slowing as Expected



Source: China National Bureau of Statistics, Forecast by TD Economics as of December

has already contributed to dampened consumer and business sentiment in survey data, is also showing up in real measures of spending and activity.

The Federal Reserve will still meet next week amidst the shutdown. We will get to hear from Chair Powell at a post-meeting press conference, as the Fed moves to holding a press conference at every meeting. The Fed is widely expected to keep rates steady, consistent with recent speeches, which emphasized the ability to be patient to see how the economy fares in the wake of slower global growth and the deterioration in sentiment.

Fortunately, we are not in a total data vacuum. Next week, the BLS will release employment data, where we will see if the blistering hiring activity in December carried over into January. As legislation has been passed guaranteeing furloughed federal workers back pay to cover the shutdown, these workers will not dampen the payrolls tally. However, they are still likely to boost the unemployment rate. The reference week for the Household survey was January 6-12th, and furloughed federal employees (0.2% of the labor force) would be classified as unemployed. Assuming federal workers are appropriately sampled in the survey, this could result in a 0.2 percentage point boost to the January unemployment rate. Meanwhile, the economic hit from the shutdown continues to mount. Growth in the first quarter is looking soft at 1.4% (annualized), assuming a 0.2%-pt direct hit from the shutdown if it lasts to the end of January.

Leslie Preston, Senior Economist

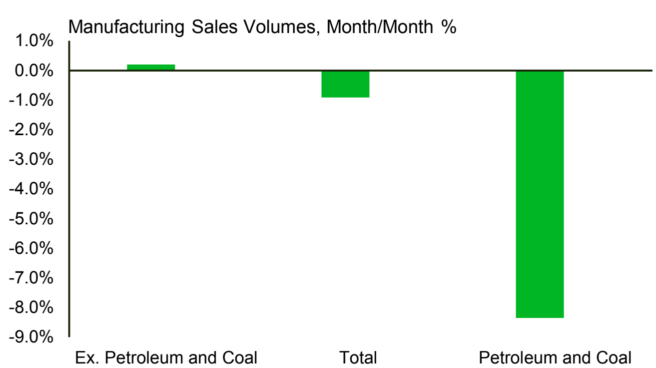
Canada - Data Confirms Slowing Growth Narrative

The TSX and Canadian dollar traded sideways this week, hanging on to recent gains. Still, the trend remains a friend, with both asset classes significantly off the lows seen late last month. Meanwhile, the price of WCS oil pushed higher during the week and is up over 200% compared to its November trough – a good news story for the beleaguered oil sector. On the data front, the news was less encouraging as economy watchers were delivered a trio of disappointing reports. Wholesale activity, manufacturing sales, and retail spending all declined in November, consistent with the softer economic backdrop expected by the Bank of Canada and prompting a modest downward revision to our fourth quarter growth forecast.

Manufacturing activity came in shy of expectations, with volumes dropping 0.9%. The petroleum and coal sector was the chief culprit (Chart 1), with maintenance and turnaround work contributing to an outsized decline in sales. The immediate outlook for this sector is no brighter, with Alberta's oil production curtailment plan commencing on January 1st (see report).

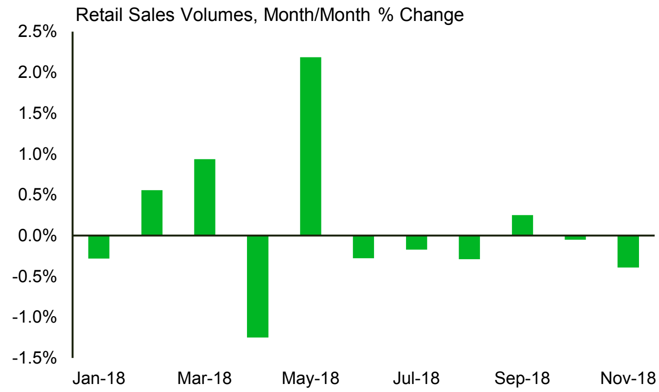
Stripping out the petroleum and coal sector, the picture was a little bit brighter, with manufacturing sales edging 0.2% higher. Peering ahead, manufacturing should find support from still-solid U.S. demand and a low-flying loonie, giving aid to the much needed rotation from consumer spending to investment and export-led growth. However, the aforementioned oil production cuts will exert a significant near-term drag on manufacturing output and overall GDP growth.

Chart 1: Petroleum and Coal Products Exert a Major Drag on November Manufacturing Sales



Source: Statistics Canada, TD Economics

Chart 2: A Tough Second Half of 2018 for Retailers



Source: Statistics Canada, TD Economics

November was another weak month for retail spending (Chart 2). With households feeling the pinch of rising interest rates, retail volumes dropped 0.4% during the month, weighed down by falling motor vehicle and parts sales. Sales in this rate-sensitive sector are now tracking a modest year-to-date drop through November, a marked change from the 6% gain averaged the prior three years. The impact of rising borrowing costs is also being felt at retailers tied to housing markets. Volumes at building material and garden equipment supplies stores dropped for the fifth straight month in November. Sales of these items are now down 3.9% compared to a year ago, the worst performance since 2013. Not to be outdone, sales at furniture and home furnishing stores were also significantly lower year-on-year in November. Going forward, household spending will likely remain muted through 2019, as debt burdened households contend with rising borrowing costs.

Putting it all together, the dataflow suggests that overall economic activity likely pulled back in November, and for fourth quarter as a whole will come in softer than previously anticipated. We now expect growth closer to the 1% mark, not far off the Bank of Canada's estimate of 1.3%. This softer economic backdrop combined with well contained inflation should keep a patient Bank of Canada in wait-and-see mode for some time yet.

Rishi Sondhi, Economist | 416-983-8806

U.S.: Upcoming Key Economic Releases

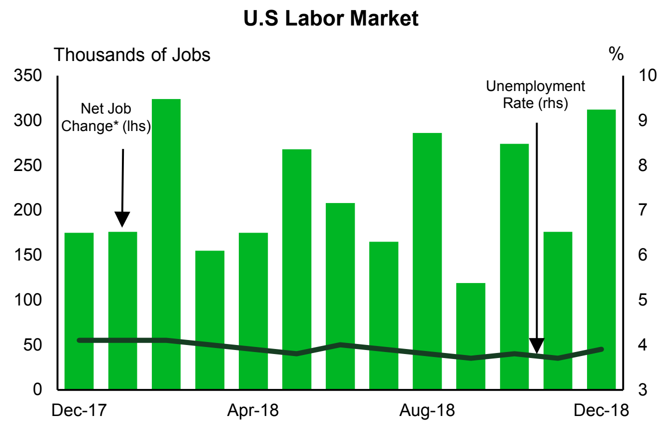
U.S. Employment - January*

Release Date: February 1, 2019

Previous: 312k, unemployment rate: 3.9%

TD Forecast: 150k, unemployment rate: 4.0%

Consensus: 160k, unemployment rate: 3.9%



Seasonally-Adjusted Data; * Change in Non-Farm Payrolls
Source: U.S. Department of Labor, TD Economics

TD expects payrolls to mean-revert to 150k in January following the eye-popping jump to 312k in December. In effect, we expect some of last month's unexpected gains in employment to be given back in January. In particular, we see scope for softness in the manufacturing sector after three consecutive months of solid payroll gains and as supported by the regional Fed surveys, which point to some weakness in the sector. In addition, employment in the retail sector may also revert back following a strong hiring streak during the holiday season (November-December). Weaker employment signal may also be exhibited in the household survey as a consequence of furloughed federal employees due to the ongoing government shutdown. Indeed, we anticipate the unemployment rate to reflect this by a tick up to 4.0% in January, and we see further risks to the upside. Lastly, we expect wages to keep their momentum and rise 0.3% m/m, maintaining the annual print unchanged at 3.2% in January.

U.S. ISM Manufacturing – January*

Release Date: February 1, 2019

Previous: 54.1

TD Forecast: 53.3

Consensus: 54.3

Source: Institute for Supply Management, TD Economics

ISM-adjusted regional surveys suggest the manufacturing ISM likely fell further in January following the sharp 5.2 decline in December. In particular, both the adjusted Empire and the Philly Fed manufacturing surveys pointed to further softness at the start of the year. Although our forecast currently stands below consensus expectations, we note that at that level the ISM index would remain in expansionary territory that still suggests above-trend GDP growth. Based on the surveys, we expect the inventory and employment components to lead the decline, while new orders has the potential to stabilize following its large decline in December.

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

Canada: Upcoming Key Economic Releases

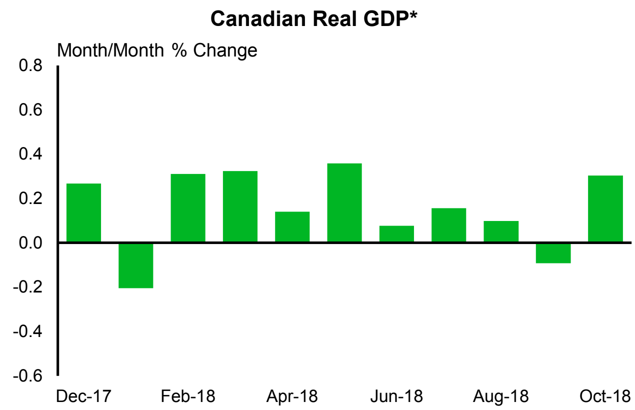
Canadian Real GDP - November*

Release Date: January 31, 2019

Previous: 0.3%

TD Forecast: -0.1%

Consensus: N/A



*Real GDP at Basic Prices in 2007 Chained Dollars
Source: Statistics Canada, Haver Analytics, TD Economics

The Canadian economy is projected to take a step backward in November with a 0.1% decline in industry-level GDP. Early signs are pointing towards a broad slowdown in activity as headwinds emerge across both goods and services. Energy will be an acute source of pain, reflecting voluntary shut-ins across the oil sands as producers grappled with blowout spreads on Canadian crude oil. Weaker construction and manufacturing activity will weigh further on output from the goods-producing sector while services will contend with a pullback in real retail and wholesale sales alongside ongoing softness in existing home sales. Given uncertainty around the impact of crude oil shut-downs we view risks as tilted to the downside, although the 0.3% increase from October will help blunt the impact on Q4 growth. The BoC has already set a relatively low bar at 1.3%, but a 0.1% decline would likely imply a growth tracking closer to the 1% mark.

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

Recent Key Economic Indicators: Jan 21 - 25, 2019						
Release Date		Economic Indicator/Event	Data for Period	Units	Current	Prior
United States						
Jan 22		Existing Home Sales	Dec	Mlns	5.0	5.3
Jan 24		Initial Jobless Claims	Jan 19	Thsd	213.0	212.0
Jan 24		Markit US Manufacturing PMI	Jan	Index	54.9	53.8
Jan 24		Markit US Services PMI	Jan	Index	54.2	54.4
Canada						
Jan 22		Manufacturing Sales	Nov	M/M % Chg.	-1.4	-0.1
Jan 22		Wholesale Trade Sales	Nov	M/M % Chg.	-1.0	0.7
Jan 23		Retail Sales Ex Auto	Nov	M/M % Chg.	-0.6	-0.2
Jan 23		Retail Sales	Nov	M/M % Chg.	-0.9	0.2
International						
Jan 22	UK	ILO Unemployment Rate 3Mths	Nov	%	4.0	4.1
Jan 23	JN	Nikkei Japan PMI Manufacturing	Jan	Index	50.0	52.6
Jan 24	EZ	Markit Eurozone Manufacturing PMI	Jan	Index	50.5	51.4

Source: Bloomberg, TD Economics.

Upcoming Economic Releases and Events: Jan 28 - Feb 1, 2019						
Release Date	Time*	Economic Indicator/Event	Data for Period	Units	Consensus Forecast	Last Period
		United States				
Jan 29	8:30	Retail Inventories	Dec	M/M % Chg.	-	-
Jan 29	8:30	Advance Goods Trade Balance	Dec	USD, Blns	-	-
Jan 29	9:00	S&P CoreLogic CS US HPI NSA	Nov	Y/Y % Chg.	-	5.5
Jan 29	10:00	Conf. Board Consumer Confidence	Jan	Index	126.0	128.1
Jan 30	8:15	ADP Employment Change	Jan	Thsd	165.0	271.0
Jan 30	8:30	Personal Consumption	4Q	Q/Q % Chg.	-	3.5
Jan 30	8:30	Core Personal Consumption Expenditure	4Q	Q/Q % Chg.	-	1.6
Jan 30	8:30	Gross Domestic Product Annualized	4Q	Q/Q % Chg.	2.6	3.4
Jan 30	10:00	Pending Home Sales	Dec	M/M % Chg.	1.0	-0.7
Jan 30	14:00	Interest Rate on Excess Reserves	Jan 31	%	-	2.4
Jan 30	14:00	FOMC Rate Decision (Upper Bound)	Jan 30	%	2.50	2.50
Jan 31	8:30	Personal Income	Dec	M/M % Chg.	0.5	0.2
Jan 31	8:30	Real Personal Spending	Dec	M/M % Chg.	-	0.3
Jan 31	8:30	Employment Cost Index	4Q	Index	0.7	0.8
Jan 31	8:30	Personal Consumption Expenditure Core	Dec	Y/Y % Chg.	-	1.9
Jan 31	8:30	Initial Jobless Claims	Jan 26	Thsd	-	199.0
Jan 31	8:30	Personal Consumption Expenditure Deflator	Dec	Y/Y % Chg.	-	1.8
Jan 31		Wholesale Trade Sales	Nov	M/M % Chg.	-	-0.2
Feb 01	8:30	Average Hourly Earnings	Jan	M/M % Chg.	0.3	0.4
Feb 01	8:30	Unemployment Rate	Jan	%	3.8	3.9
Feb 01	8:30	Change in Nonfarm Payrolls	Jan	Thsd	160.0	312.0
Feb 01	10:00	ISM Employment	Jan	Index	-	56.2
Feb 01	10:00	ISM Manufacturing	Jan	Index	54.1	54.1
Feb 01	17:00	Wards Total Vehicle Sales	Jan	Mlns	17.2	17.5
		Canada				
Jan 31	8:30	Gross Domestic Product	Nov	M/M % Chg.	-	0.3
Jan 31	8:30	Industrial Product Price	Dec	M/M % Chg.	-	-0.8
Jan 31	10:00	CFIB Business Barometer	Jan	Index	-	53.6
Jan 31	12:45	*BoC's Carolyn A. Wilkins speaks at the Toronto Region Board of Trade*				
Feb 01	8:30	MLI Leading Indicator	Dec	M/M % Chg.	-	-0.1
Feb 01	9:30	Markit Canada Manufacturing PMI	Jan	Index	-	53.6
		International				
Jan 29	18:50 JN	Retail Sales	Dec	M/M % Chg.	0.3	-1.1
Jan 30	20:00 CH	Manufacturing PMI	Jan	Y/Y % Chg.	-	49.4
Jan 31	5:00 EZ	Unemployment Rate	Dec	%	-	7.9
Jan 31	19:30 JN	Nikkei Japan PMI Mfg	Jan	Index	-	50.0
Feb 01	4:00 EZ	Markit Eurozone Manufacturing PMI	Jan	Index	-	50.5
Feb 01	4:30 UK	Markit UK PMI Manufacturing SA	Jan	Y/Y % Chg.	-	54.2
Feb 01	5:00 EZ	Gross Domestic Product SA	4Q	Y/Y % Chg.	-	1.6
Feb 01	5:00 EZ	Consumer Price Index Core	Jan	Y/Y % Chg.	-	1.0

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

Note: Some data releases may be impacted by the current U.S. partial government shutdown.

Disclaimer