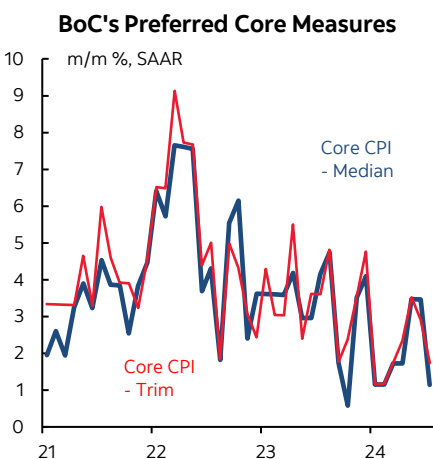


Contributors

Derek Holt

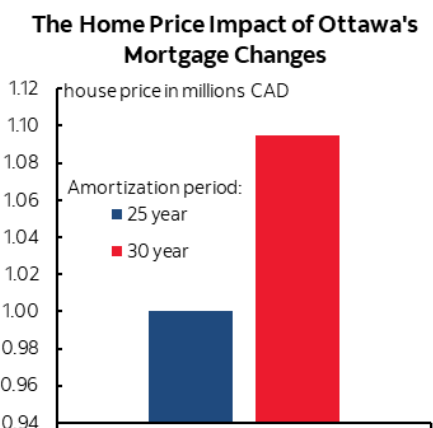
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Chart 1



Sources: Scotiabank Economics, Statistics Canada.

Chart 2



* Assuming a 5-year fixed term rate at about 4.6% from ratehub.ca - offers from the biggest banks.
 Sources: Scotiabank Economics, Ratehub.ca

On Deck for Tuesday, September 17

Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
CA	09-17	08:15	Housing Starts (000s a.r.)	Aug	245	250.0	279.5
CA	09-17	08:30	Core CPI - Median (y/y)	Aug	--	2.2	2.4
CA	09-17	08:30	Core CPI - Trim (y/y)	Aug	--	2.5	2.7
CA	09-17	08:30	CPI, All items (m/m)	Aug	0.0	0.0	0.4
CA	09-17	08:30	CPI, All items (y/y)	Aug	2.0	2.1	2.5
CA	09-17	08:30	CPI, All items (index)	Aug	--	162.1	162.1
US	09-17	08:30	Retail Sales (m/m)	Aug	-0.2	-0.2	1.0
US	09-17	08:30	Retail Sales ex. Autos (m/m)	Aug	0.2	0.2	0.4
US	09-17	09:15	Capacity Utilization (%)	Aug	77.7	77.9	77.8
US	09-17	09:15	Industrial Production (m/m)	Aug	0.0	0.2	-0.6
US	09-17	10:00	Business Inventories (m/m)	Jul	--	0.3	0.3
US	09-17	10:00	NAHB Housing Market Index	Sep	--	41.0	39.0
CA	09-17	08:30	Core CPI - Common (y/y)	Aug	--	--	2.2
CA	09-17	08:30	CPI SA, All items (m/m)	Aug	--	--	0.3

KEY POINTS:

- **Data to pass the time before tomorrow's FOMC decisions**
- **US retail sales: soft headline, stronger core?**
- **Canadian core CPI will help to inform the trend...**
- **...and whether July's cooling after three hot months was an aberration...**
- **...but it's just a placeholder as one of two CPIs before the BoC's October decision**
- **US IP, homebuilder confidence also on tap**
- **BoC's Rogers to weigh in post-CPI**
- **Gauging the effects of Canada's mortgage stimulus**
- **Canada's Liberals lost both by-elections despite attempting to buy them**

Canadian CPI and US retail sales will compete for attention at the same time this morning. Overnight developments were light. Canada's ruling Liberals lost both by-elections last night. I've summarized some views on the impact of Canada's announced changes to mortgage rules.

CANADIAN CPI IS JUST A PLACEHOLDER FOR NOW

Canada updates CPI for August this morning (8:30amET) after housing starts for the same month get refreshed (8:15amET). This is just one of two CPI reports before the October BoC decision. It may motivate market volatility, but it won't singlehandedly determine the BoC's likely action and forecasts. Still, core readings will help to inform the m/m trend.

There will be multiple opportunities for BoC officials to react starting today when Senior Deputy Governor Rogers participates in a fireside chat in Toronto (6pmET). Rogers is not a trained economist but may reflect upon the house view.

I've estimated a flat headline reading in m/m seasonally unadjusted terms as per the polling convention that would mean a rise of 0.3% m/m SA. That translates into 2.1% y/y, down from 2.5% the prior month and down from a peak of 8.1% in June 2022. Traditional core CPI excluding food and energy prices is also estimated at 0% m/m NSA that could mean 0.2% m/m SA.

Key, however, will be the trimmed mean and weighted median measures in m/m SAAR terms. No one can forecast those and they're misleading you if they say they can. The August readings will help to determine whether July's deceleration to 1.7% m/m SAAR was an aberration after a hotter pattern from April to June (chart 1).

As for a few details:

- Gasoline prices are estimated to drag less than a tenth off of m/m NSA CPI.
- Food prices probably offered an immaterial weighted contribution to m/m CPI.
- Rent may cool again based on nationwide price indices that fell -0.6% m/m NSA. A reduction in the international student population may be a contributing factor at the start of a new school year.
- The overall shelter category could also be soft because of housing's replacement cost captured in the new house price index that is elevated but trending sideways to the latest reading in July.
- mortgage interest cost has begun to edge lower in response to BoC rate cuts but carries a tiny weight in CPI and has never been included in the preferred core inflation readings throughout the pandemic era and even leading up to it.
- I'm expecting the two-month SA decline in the recreation and education category to edge upward as the prior steep declines in travel tours ebbs.
- Canada's aborted rail strike may still impact prices because of advance preparations to curtail rail transport and the very short duration of the strike. Also watch for any potential effects of Statcan's methodological changes to how it captures cellular service prices this time given that category's rapid increase in seasonally adjusted month-ago terms.

US MACRO READINGS ON TAP

US retail sales for August (8:30amET) are expected to dip given what we know about auto sales, but key will be core sales ex-autos and ex-autos-and-gas that are expected to post a mild gain. Also watch US industrial production (9:15amET) for August and homebuilder confidence for September (10amET) with the latter including model home foot traffic as a leading indicator of new home sales.

THE LIBERALS' ATTEMPT TO BUY BY-ELECTIONS FAILED

Canada's Liberals attempted to buy the outcome of two federal by-elections with yesterday's announcement on easier mortgage rules and it didn't work as they lost both. The Liberals lost the Montreal seat to the BQ, a regional Quebec-based party. This follows the summertime loss of a by-election in another Liberal stronghold in Toronto. The NDP won the Winnipeg seat, but by a much tighter margin over the Conservatives than previously in what is typically a stronghold for the NDP. Thus, both the Liberal and NDP leaders fared poorly and the pressure on the PM is likely to further intensify.

EASIER MORTGAGE RULES WILL WORSEN HOUSING AFFORDABILITY

As for those mortgage changes, Canada, you just never learn. The motives are clear in that we should expect more and more of this kind of desperate policy easing by the federal Liberal government into an election year and this one was announced on a day when the Libs were hoping it would buy them the Montreal by-election. Whoops. Expect more goodies to be thrown at a naive electorate in the Fall fiscal and economic update and then a winter budget which has been a core part of my narrative for a while. Monetary easing plus regulatory easing plus fiscal easing are among the multiple drivers that make it premature to discount inflation risk.

Recall that the changes include raising the house price ceiling for insured mortgages to \$1.5 million from \$1 million, raising amortization periods from 25- to 30-years for all first-time insured homebuyers in both the resale and new build markets as opposed to just new builds in the changes that took effect this past August, and allowing 30-year insured mortgages for all buyers of new builds (not just first-timers). The changes add to another change that was introduced in August that allows participants in the Home Buyers Plan to withdraw more from their RRSPs to finance a home purchase (from \$35k to \$60k) and then applying leverage to that amount.

But what effect will the changes have?

- They will add more demand pressure into supply challenged markets and thus drive a further deterioration of housing affordability that will make it tougher for all homebuyers. I can't see how that ultimately benefits young homebuyers which is the government's stated goal, though there may be a first-mover advantage before the market adjusts.
- House prices will ultimately rise through two effects. One effect is that allowing a higher ceiling for insured mortgages will put extra demand into the \$1-1.5 million price category with possible spillover effects above that threshold.

- Another effect on house prices is shown in chart 2. It shows the estimated impact of the increase from 25- to a 30-year amortization period for insured mortgages. At a 4.6% 5-year mortgage rate being quoted at ratehub.ca for the big banks, buyers who could afford the payments for a \$1 million mortgage will now be able to afford a \$1.1 million mortgage assuming 20% down which is probably high for this category of insured mortgage borrowers.
- If, by contrast, folks decide to stick to the same house price target then chart 3 shows the potential impact on lower bi-weekly mortgage payments. Is this realistic? Ha! That would be against the steady pattern of buying as much home as you can to the limits of affordability.
- Housing may be a dead zone until the December 15th implementation of the rule changes.
- Taxpayers face a larger potential liability stemming from the changes to insured mortgages and moral hazard and adverse incentive problems will increase in the mortgage market.
- Incidence effects will have various stakeholders capturing some of the effects for themselves.
- This is yet another signal that Canada has absolutely no policy desire to focus on lame productivity whatsoever. These announcements further emphasize the government’s policy bias toward maintaining—in fact, growing—the share of the economy that is represented by here-today-gone-tomorrow short-term spending activity. Chart 4 shows that almost 86% of GDP is tied up in consumer spending, residential investment and short-term government program spending which remains around the highest levels since the late 1980s. These forms of economic activity are sucking in resources from other forms of economic activity.

Overall, I’m expecting an accelerating housing market into an election year and beyond and this thesis will be tested next year once the latest changes take effect on December 15th into the mortgage pre-approvals environment ahead of the key Spring housing market. Everything is lining up robustly for housing which is good for growth including the spillover effects on complementary forms of consumer spending. Immigration has added a massive population shock that raised population by 3 million since 2020, 2.5 million since 2021, and all of that within a modestly sized population of about 41 million at present. Buying intention surveys are indicating robust appetite for housing over the coming year including the BoC’s measure within its consumer survey. The government keeps adding politically driven demand stimulus. The government’s supply side goals are predestined to fail as there is no way they come close to the homebuilding targets they have laid out over the rest of the decade. The Bank of Canada is cutting rates and Governor Macklem is on a pre-committed straight-line path to cutting further. The full pass through into fixed mortgage rates is likely to intensify in terms of the rally in 5-year GoC bonds down to 2.67% and 1.75 percentage points lower than the peak of about a year ago. Wage gains remain strong and disconnected from weak labour productivity.

Overall, the changes add to my bias that is more upbeat than consensus on growth including via the household sector, more concerned about the resurrection of inflation risk, and that the market is overpricing BoC cuts including through the belly of the Canada curve.

Chart 3

The Payments Impact of Ottawa's Mortgage Changes

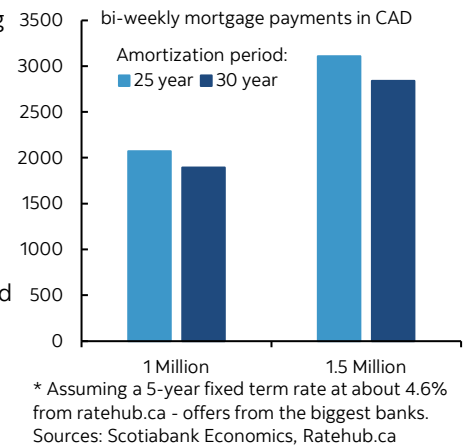
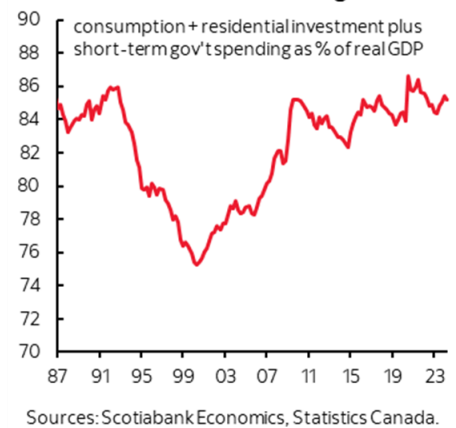


Chart 4

Here Today, Gone Tomorrow - The '80s Are Calling



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.	3.56	3.55	3.60	3.40	3.40	3.42	3.61	3.62	3.64	3.91	3.93	3.96	Canada - BoC	4.25
CANADA	2.88	2.88	2.99	2.67	2.68	2.72	2.86	2.87	2.89	3.04	3.06	3.06	US - Fed	5.50
GERMANY	2.19	2.18	2.18	1.99	2.00	1.99	2.10	2.12	2.13	2.37	2.40	2.41	England - BoE	5.00
JAPAN	0.39	0.39	0.40	0.49	0.51	0.53	0.83	0.85	0.90	1.99	2.02	2.08		
U.K.	3.79	3.79	3.86	3.60	3.61	3.69	3.74	3.76	3.82	4.33	4.35	4.40		
	Spreads vs. U.S. (bps):													
CANADA	-69	-67	-61	-73	-73	-70	-75	-75	-75	-87	-87	-91	Euro zone - ECB	3.65
GERMANY	-138	-137	-142	-141	-141	-143	-150	-150	-151	-154	-153	-156	Japan - BoJ	-0.10
JAPAN	-317	-316	-320	-291	-290	-289	-278	-277	-274	-192	-191	-189		
U.K.	23	24	26	20	21	26	13	14	17	42	42	43	Mexico - Banxico	10.75
Equities	Level						% change:							
	Last		Change		1 Day		1-wk		1-mo		1-yr			
S&P/TSX	23702		133.4		0.6		2.9		2.8		14.9		Australia - RBA	4.35
Dow 30	41622		228.3		0.6		1.9		2.4		20.2		New Zealand - RBNZ	5.25
S&P 500	5633		7.1		0.1		3.0		1.4		26.6			
Nasdaq	17592		-91.8		-0.5		4.2		-0.2		28.3			
DAX	18750		116.9		0.6		2.7		2.3		18.0			
FTSE	8333		54.7		0.7		1.5		0.3		8.1			
Nikkei	36203		-378.5		-1.0		-0.0		-4.9		8.0		Canada - BoC	Oct 23, 2024
Hang Seng	17660		237.9		1.4		2.5		1.3		-1.5		US - Fed	Sep 18, 2024
CAC	7494		44.4		0.6		1.2		0.6		1.6			
Commodities	Level						% change:							
WTI Crude	70.34		0.25		0.4		7.0		-8.2		-22.5		England - BoE	Sep 19, 2024
Natural Gas	2.40		0.02		1.0		7.4		12.9		-9.3		Euro zone - ECB	Oct 17, 2024
Gold	2580.51		-1.94		-0.1		2.5		15.7		34.1		Japan - BoJ	June 14, 2024
Silver	30.91		0.95		3.2		9.9		9.9		34.0			
CRB Index	276.86		3.02		1.1		2.7		0.5		-4.4			
Currencies	Level						% change:							
USDCAD	1.3584		-0.0003		-0.0		-0.2		-0.4		0.7		Mexico - Banxico	Sep 26, 2024
EURUSD	1.1138		0.0005		0.0		1.1		0.5		4.2			
USDJPY	140.61		-0.0100		-0.0		-1.3		-4.1		-4.7		Australia - RBA	Sep 24, 2024
AUDUSD	0.6763		0.0011		0.2		1.7		0.5		5.1			
GBPUSD	1.3221		0.0005		0.0		1.1		1.8		6.8		New Zealand - RBNZ	Oct 08, 2024
USDCHF	0.8443		-0.0005		-0.1		-0.3		-2.1		-5.9			

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