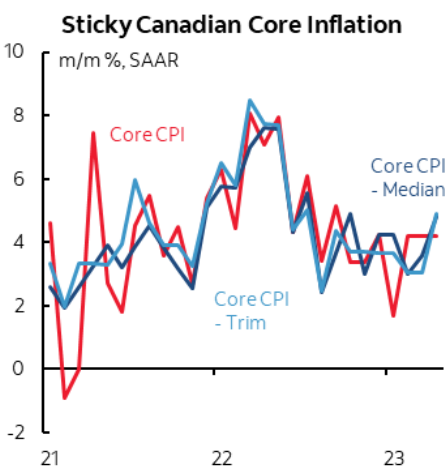


Contributors

Derek Holt

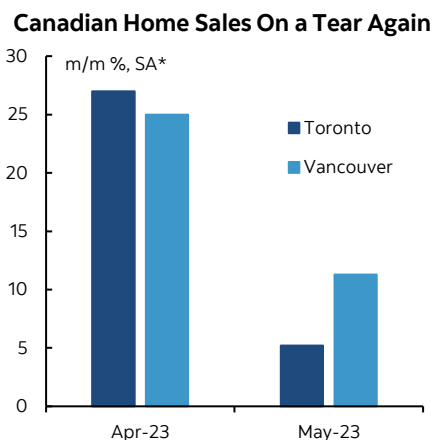
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Chart 1



Sources: Scotiabank Economics, Haver.

Chart 2



*Scotiabank Economics seasonally adjusted.
 Sources: Scotiabank Economics, TRREB, REBGV.

On Deck for Wednesday, June 7

Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
US	06-07	07:00	MBA Mortgage Applications (w/w)	Jun 02	--	--	-3.7
CA	06-07	08:30	Merchandise Trade Balance (C\$ bn)	Apr	--	--	1.0
CA	06-07	08:30	Productivity (q/q a.r.)	1Q	-0.4	--	-0.5
US	06-07	08:30	Trade Balance (US\$ bn)	Apr	-74.4	-75.4	-64.2
CA	06-07	10:00	BoC Interest Rate Announcement (%)	Jun 7	4.75	4.50	4.50
US	06-07	15:00	Consumer Credit (US\$ bn m/m)	Apr	--	22.0	26.5
CA	06-07	10:00	Bank of Canada Rate Decision				

KEY POINTS:

- Sovereign yields continue to grind higher
- If the BoC whiffs, then it could unwisely engineer cut pricing all over again
- The BoC hold-for-longer alternative...
- ...would mean having learned absolutely nothing about limits to forward guidance
- The case for a BoC hike has strengthened since they considered one in April
- Preserving optionality throughout Summer merits a BoC hike today
- Other overnight developments

The BoC will be the main focal point in a statement-only affair at 10amET. Other overnight developments were mild in nature with brief comments offered at the end of the note so we can quickly get to the BoC. Sovereign debt yields are under mild upward pressure across the world's main benchmarks again while the USD is broadly weaker, stocks are flat to a touch lower across N.A. and European benchmarks and volatile oil prices are up by under 1%.

The Bank of Canada is a statement-only affair (10amET) sans presser or forecasts. The BoC surprised markets in 3 out of 8 decisions last year and surprised the median consensus call on two of those occasions. Right now, markets are pricing about 50–50 odds of a rate hike today and fully pricing a 25bps hike in July and then much of another one thereafter. A minority of economists expect a hike today; who knows what many of them think about July but one thing I do know is that there are not 37 folks who suddenly know Canada in the consensus polls. That said, several Canadian banks are hedging their bets with competing calls. The goal of forecasting higher shorter-term market yields off of the March lows has been achieved and now we're into the finer strokes on the call.

What if they don't hike? The case for hiking is solid and laid out in multiple notes (like [here](#)) and calls but it's the alternative scenario of what would happen if they didn't hike that perversely provides additional logic for hiking.

If the BoC doesn't hike or provide very explicit guidance toward hiking more than once, then they'll have to explain why they chose to ease financial conditions relative to what's priced because that's likely what would occur. Markets would view Governor Macklem as having said all along that he was leaning toward hiking if the conditions got violated as laid out below and then falling short when they did. That would be taken as a clear signal that the next move is more likely to be lower and it would probably resurrect a swing in positioning toward a pile-on into the rallying front-end that the BoC cannot or shouldn't want to court at this point. Hike today and you preserve greater optionality over Summer.

This is also one reason why the alternative scenario of signalling a longer hold instead of hiking makes no sense and there are three other reasons to add to this:

- Markets don't believe central banks' longer-term forecasts at the best of times (or anyone else's...). Say all you want about next year and beyond and all markets will

June 7, 2023

hear is that you're not hiking now, so buy, buy, buy away and we're back to March with Macklem scratching his head over how that happened.

- Markets extra don't believe Macklem's longer-term forward guidance. Listen to the guy who reeled in leveraged suckers when he said he wouldn't hike for years and years in the depths of the pandemic?? Oh that's rich.... Surely we've learned something from the pandemic. Fool me once, shame on you, fool me twice, shame on me if folks believe the longer hold fairy tale again. The lesson is that longer-dated forward guidance doesn't work because central bankers can't forecast and shouldn't promise that they can.
- Time is of the essence here. With each passing month that households and businesses see persistent core inflation at well above target rates and surging housing markets it gets more and more difficult for the BoC to convince folks that it is serious about doing whatever is necessary to bring down inflation and preserve financial stability. Keeping rates at current levels for longer in future doesn't achieve the goal of intervening against such forces now.

So what has tipped the balance now versus when Macklem said they discussed a hike in April but held off to evaluate further evidence?

- GDP is materially beating the BoC's H1 expectations. 3.1 in Q1 versus 2.3 forecast, nowcast tracking 2 ½% in Q2 versus the BoC's 1% forecast.
- this means more excess demand than they had judged in April which is going in the opposite direction to what they deem to be necessary to ease inflationary pressures back to 2% in the medium term.
- April core inflation in May accelerated to 4%+ m/m SAAR using trimmed mean and weighted median and traditional core (chart 1). The only improvement was over 2022H1 and since then these readings have been remarkably sticky at rates well above the BoC's target.
- Housing is back on a tear again with surging home sales and prices across major markets (chart 2).
- The debt ceiling is predictably donezo.
- Regional bank hiccups have stabilized
- Wage settlements in the public sector and spillover effects into airlines have become amplified.

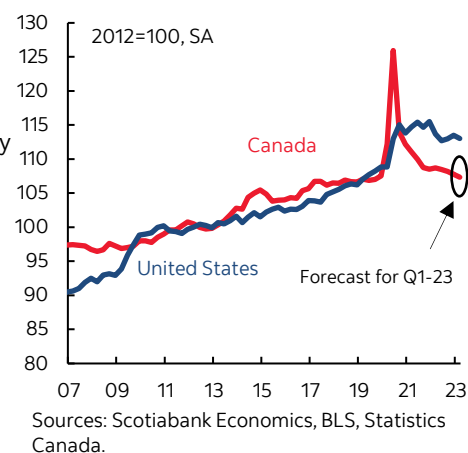
Other overnight developments are summarized as follows:

1. Chinese exports disappointed, with currency depreciation playing a significant role. In local currency terms, exports were down -0.8% y/y but in USD terms, exports fell by 7.5% y/y. Newswires only really reported the USD figure and missed the currency effect. The yuan fell by about 4% in y/y terms and has been depreciating since mid-April. Imports were up by 2.3% y/y in yuan-denominated terms but down 4.5% in USD terms.
2. German industrial output beat expectations on revisions. April's output was up by just 0.3% m/m (0.6% consensus) but the prior month's previously reported 3.4% drop was revised up to -2.1%. That's still clearly not great.
3. Australian GDP was a wash relative to expectations. Q1 missed a touch (0.2% q/q nonannualized, 0.3% consensus) but the prior quarter was revised up a tenth to 0.6%.
4. The OECD updates its projections this morning. They now see the world economy growing by 2.7% in 2023 and 2.9% in 2024. The US is projected to grow 1.6% and 1% in 2023 and 2024 respectively. Canada is forecast to grow by 1.4% in each year. In no major region is a full year contraction being forecast.

On tap into the N.A. session are a few distractions with the primary focus being the Bank of Canada's statement (10amET). Canadian labour productivity arrives just before that (8:30amET) and I'm expecting another dip of around -0.4% q/q nonannualized that would extend the miserable trend (chart 3). Canada also updates trade figures for April at the same time. The US updates trade figures as well but they only tack the services surplus onto the already known deterioration in the goods balance due to higher oil prices in April that then reversed in May.

Chart 3

Canada & US Labour Productivity



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.	4.51	4.48	4.40	3.84	3.81	3.76	3.68	3.66	3.65	3.85	3.85	3.86	Canada - BoC	4.50
CANADA	4.38	4.32	4.25	3.55	3.52	3.51	3.28	3.26	3.25	3.17	3.19	3.22	US - Fed	5.25
GERMANY	2.87	2.85	2.72	2.40	2.38	2.28	2.38	2.37	2.28	2.54	2.56	2.46	England - BoE	4.50
JAPAN	-0.06	-0.06	-0.05	0.09	0.09	0.10	0.43	0.43	0.44	1.27	1.27	1.26		
U.K.	4.49	4.48	4.34	4.18	4.18	4.10	4.20	4.21	4.18	4.46	4.47	4.52		
	Spreads vs. U.S. (bps):													
CANADA	-13	-16	-16	-29	-29	-25	-41	-40	-39	-68	-65	-64	Euro zone - ECB	3.75
GERMANY	-164	-163	-169	-144	-142	-148	-131	-129	-136	-131	-129	-140	Japan - BoJ	-0.10
JAPAN	-457	-454	-446	-375	-372	-366	-326	-324	-321	-259	-258	-260		
U.K.	-2	-0	-7	34	38	34	51	54	54	60	63	65	Mexico - Banxico	11.25
Equities	Level						% change:							
	Last			Change			1 Day	1-wk	1-mo			1-yr		
S&P/TSX	20056			124.0			0.6	1.6	-2.4			-4.2	Australia - RBA	4.10
Dow 30	33573			10.4			0.0	1.6	-0.3			1.2	New Zealand - RBNZ	5.50
S&P 500	4284			10.1			0.2	1.9	3.6			3.0		
Nasdaq	13276			47.0			0.4	2.0	8.5			9.0		
DAX	15964			-28.0			-0.2	1.9	0.0			9.7		
FTSE	7636			8.0			0.1	2.6	-1.8			0.5		
Nikkei	31914			-593.0			-1.8	3.3	9.5			14.2	Canada - BoC	Jun 07, 2023
Hang Seng	19252			152.7			0.8	5.6	-4.0			-10.6	US - Fed	Jun 14, 2023
CAC	7195			-14.4			-0.2	1.4	-3.2			10.7		
Commodities	Level						% change:							
WTI Crude	72.45			0.71			1.0	6.4	1.6			-39.3	England - BoE	Jun 22, 2023
Natural Gas	2.27			0.01			0.4	0.2	6.2			-75.6	Euro zone - ECB	Jun 15, 2023
Gold	1963.42			-0.10			-0.0	0.0	-2.6			6.0	Japan - BoJ	Jun 16, 2023
Silver	23.65			0.17			0.7	1.7	-8.5			6.2		
CRB Index	260.68			0.24			0.1	2.0	-0.4			-20.3		
Currencies	Level						% change:							
USDCAD	1.3385			-0.0018			-0.1	-1.4	0.1			6.8	Mexico - Banxico	Jun 22, 2023
EURUSD	1.0715			0.0022			0.2	0.2	-2.6			0.1	Australia - RBA	Jul 04, 2023
USDJPY	139.36			-0.2700			-0.2	0.0	3.2			5.1	New Zealand - RBNZ	Jul 11, 2023
AUDUSD	0.6701			0.0030			0.4	3.0	-1.2			-7.3		
GBPUSD	1.2454			0.0030			0.2	0.1	-1.3			-1.1		
USDCHF	0.9055			-0.0021			-0.2	-0.6	1.8			-6.9		

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