BMO Capital Markets
We're here to help.™

BMO CAPITAL MARKETS ECONOMICS

Focus

A weekly financial digest

Douglas Porter, CFA, Chief Economist, BMO Financial Group

February 15, 2019

Feature Article
Page 7

The Watch that Ends the Tightening Cycle?

U.S./China Make Progress on Trade

U.S. Government Shutdown Averted... at a Cost

Global Equities Rally...

...Despite Disappointing Economic Data

BMO Capital Markets Economics
economics.bmocapitalmarkets.com • 1-800-613-0205
Please refer to page 14 for important disclosures

Somebody Call 9-1-1...

Douglas Porter, CFA
Chief Economist
douglas.porter@bmo.com
416-359-4887

...And, no, not because there is an emergency on the border—it's up to the reader to decide whether that's the case. And, no, not because markets are struggling mightily—it's quite the opposite, with stocks rolling higher yet again this week. Instead, it's because **the run of economic data globally has been so awful lately**. The dismal 1.2% decline in December U.S. retail sales almost made us long for the days of the data void. It also raises some serious doubts on arguably the last remaining stronghold for global growth—the U.S. consumer. At the same time, initial jobless claims have been quietly drifting higher, moving to a one-year high on the rolling average and raising a flicker of doubt on whether even the vaunted job market is still so healthy. Piling on, manufacturing production fell 0.9% in January, the second-largest monthly drop in the past five years.

Even Canada got into the act. Following the encouraging pop in January jobs, manufacturing sales volumes fell 1.2% in December, leaving them below year-ago levels for the first time since 2016. This drop comes on the heels of a 0.1% sag in November GDP, and raises the distinct possibility of a two-month setback—all just before Alberta's mandated oil production cuts began in January. The economy will do well to top 1% growth in both Q4 and Q1 given this lacklustre background.

The story hardly improves as we head overseas. Europe and Japan are slow, period. In a refreshing burst of clarity, the ECB's Coeure bluntly stated that *"the slowdown has been stronger and broader than we expected"*. This week's official Q4 GDP results were not bad, they just weren't good. Looking past the quarterly quirks, the best gauge is the annual trend, and on that measure, growth in the Euro Area is now just 1.2% y/y (and just 0.6% in Germany) and nil in Japan. It's little better in the U.K., where Brexit uncertainty seems to be finally weighing heavily on growth. While Q4 was no worse than expected (up 0.2% and 1.3% y/y), a deep drop in December GDP was a bad hand-off to 2019.

China had already sent up flares around a cooler economy, notably in some of the PMI figures. The key report this week was January's trade data, and they were better than anticipated, albeit with the usual caveats over any economic data and the timing of Lunar New Year. Exports did manage to pop 9% y/y, although imports are still down 1.5% y/y. Specifically, imports from the U.S. have plunged 41% y/y, down from double-digit advances as recently as mid-2018. (Curiously, imports from Canada have rocketed 37% y/y at the same time, a divergence previously unheard of, and a heavy hint that massive trade diversion is underway amid the U.S./China wrangling.)

Markets took most of the economic news in stride, aside from a brief shudder on the U.S. retail result. In part, the mild investor response was because softness was already known/suspected, or the weakness was suspect (e.g., retail sales). As well, this week brought a pair of non-negative events. A second U.S. government shutdown was averted (albeit at the price of a national emergency), and there actually did seem to be some bi-partisan cooperation on the spending agreement (votes in the House and Senate had strong majorities).

Next, **optimism continues to build on the U.S./China trade talks**, even with some stark warnings on structural issues. It seems quite likely that the March 1 deadline

will “slide” out a month or two. We have long railed that hopes for a quick, full-meal deal on IP protection and technology transfers are pie in the sky, but a partial deal on trade (with an agreement to keep negotiating on other issues) would be a reasonable outcome. This may not be a full win-win resolution, but it also is certainly not a lose-lose proposition, which a deepening of the trade battle would be.

With hope springing eternal among investors on the trade file, the soft economic data have had little lasting impact on markets. For example, despite this week’s run of disappointing figures, Treasury yields actually rose a tad on net, with 10s up 3 bps to 2.67% (not far from where they started the year) and 2s up 5 bps to 2.52%. Meantime, stocks had a solid week overall, with the S&P 500 up more than 2% and the Dow aiming for its eighth consecutive weekly advance. The U.S. dollar was slightly firmer on the week, despite the hit from the retail figure, although it held about steady against the Canadian dollar. The loonie benefited from a further recovery in oil prices, as fresh evidence that OPEC had indeed cut output meaningfully at the start of 2019 spurred WTI up 5% this week to over $55.

Next week should be much quieter on the economic front—a holiday-shortened affair with few major economic releases. However, we will hear from the Fed in the FOMC minutes for the sea-change January meeting, as well as from BoC Governor Poloz on Thursday. We doubt either will be declaring any emergency, but the tone is likely to take a much more cautious turn on both fronts, appropriately so.

The highlight economic report of the week was no doubt the stunning drop in U.S. retail sales for December. We won’t drag this result through the mire any further, as it’s amply covered off elsewhere. Instead, we will note that this (quite important) report had been delayed by more than four weeks by the 35-day government shutdown—and wouldn’t it have been oh-so-helpful to have had this crucial piece of data on hand when the Fed met in late January? But what really irks is that even with the said 35-day shutdown, the U.S. government still managed to get December retail sales out eight days BEFORE Statistics Canada will release its version of the shopping event (out next Friday). It remains baffling that it takes 53 days for StatsCan to produce an estimate of retail sales in this day of instant info, when the retailers likely know their sales tallies for a month when the clock strikes 12 the last day. Rant finished.

One Bad Week for the Economy (Likely) Does Not Make a Trend

Sal Guatieri
Senior Economist
sal.guatieri@bmo.com
416-359-5295

Those bullish on the U.S. economy (like the Administration’s economic advisors) probably wished the Commerce Department had stayed shut. **The release of some long-awaited reports was not a pretty sight**. Hopes were running high that **retail sales** would confirm a merry end to the holiday season given earlier data from chain stores, auto dealers, credit card companies and even Amazon. Instead, we got the symbolic equivalent of a lump of coal in our stockings. Although auto sales did not disappoint, just about everything else did. Most eye-popping (and suspicious) was the second-largest decline in online sales in 17 years, a category that has consistently grown about 15% y/y since the recession. Doubts about data quality aside, the broad

weakness across categories could not be ignored. The “core” measure of retail sales, which feeds into the BEA’s estimate of consumer spending, plunged 1.7%, the most in 18 years. While sales excluding gasoline stations were down a lesser 0.9%, this was still the most in 5 years. Spending at restaurants and bars fell for the fourth time in five months, as confidence was whacked by plunging equities and 800,000 federal workers wondering when they would get paid. The report lopped a prior upside risk from our 2.6% Q4 GDP estimate that arose from the surprising slide in the November trade deficit.

The **greater risk is to our Q1 GDP call of 1.6%**, which already includes a 0.3-ppts ding from the government shutdown. **Industrial production unexpectedly fell** in January, led by a 0.8% slide in manufacturing that fully retraced a prior strong gain. While a good chunk reflected a reversal in auto assemblies from two-year highs in December, broad weakness in other areas (materials, construction supplies and upward-trending business equipment) suggests factories are downshifting after cranking out 3.2% more output in 2018, the best year since 2010’s snapback from recession.

After climbing to record highs last summer on the back of tax reform and lighter regulations, **small business confidence has been coasting downhill** and now rests just modestly above long-run norms. While plans to hire and spend are largely intact, they are off their highs amid concerns about trade policies and political instability. This likely explains why **initial jobless claims** are quietly drifting off half-century lows, even with the federal government (and presumably federal private contractors) fully operational.

Piling on, the IRS reported that **tax refunds are down** 9% from last year. While it’s still early going in the refund season, the trend suggests a slight drag on growth this year rather than an assumed modest lift. The amount of taxes withheld from paycheques more than compensated for the tax cuts and reforms, providing an extra boost to spending last year at the expense of this year.

Despite these setbacks, **households should still propel the expansion forward**, albeit at a subdued pace. The latest jump in payrolls and partial rebound in equities will pad confidence, as suggested by the partial recovery in the University of Michigan’s measure in February. And note that, although real consumer spending likely fell 0.3% in December, earlier gains still indicate a third straight quarterly gain in excess of 3% annualized in Q4. While the warm glow from tax cuts is fading, shoppers aren’t about to go into hibernation. Interest rates have largely peaked, and the 30-year mortgage rate just hit one-year lows of 4.37%. Although fuel costs have stopped falling, earlier declines are supportive. Employment should continue to expand and wages are likely to pick up modestly due to worker shortages. **Although the economic risks are tilted to the downside, we still see 2.4% annual growth in 2019**, a tick below the consensus call.

Provincial Budget Season Preview

Robert Kavcic
Senior Economist
robert.kavcic@bmo.com
416-359-8329

The 2019 budget season begins next week when the **Province of British Columbia** tables its FY19/20 fiscal plan. This should be a relatively straightforward affair, with the Province looking at a continued string of surpluses, stable debt-to-GDP (capital spending has been hefty) and priority spending in areas such as clean energy, childcare and housing affordability. While B.C. has doggedly held its AAA credit rating, its peers have long left the scene. Aside from what will be a closely-watched federal pre-election budget, there should be some interesting developments at the provincial level, too.

Ontario will be closely watched given that the new government, despite two rounds of fiscal updates, has yet to give any guidance beyond the current fiscal year. That said, the initial $14.5 billion deficit assessment was clearly setting the bar low to begin with, and the Province has already trimmed that by $1 billion, with more improvement likely coming before the year is up. The medium-term fiscal plan will be key, including any guidance on the timing of promised tax relief—we suspect that will be a story for the second half of the current mandate. **Quebec's** recently-elected government already served up a budget-like fall fiscal update, with the recent fiscal strength in that province firmly in place.

Meantime, **Alberta** has quietly posted better-than-expected numbers this year despite the oil price drama. At last check, the Province was estimating a $7.5 billion deficit, $1.3 billion better than expected in the original budget plan. And, assuming WTI, the WCS differential, and the loonie hold around current levels through March, the Province could be looking at a further $1.5 billion of bottom-line improvement. Of course, the 2019 budget will be of the pre-election variety, and the incumbent NDP would surely like to publish an earlier return to balance, currently not planned until FY23/24. **Newfoundland & Labrador** and **Saskatchewan** have been more aggressive with their oil price assumptions, so they probably won't see as much momentum heading into 2019.

Finally, **the Maritimes** have quietly been riding a wave of stronger population and economic growth, with all three provinces running balanced budgets for the first time in more than a decade. **Nova Scotia's** net debt is down almost 4 percentage points from its recent high as a share of GDP. In fact, relative to Ontario, the net debt burden (5 ppts lower on average for the three provinces) is the most favourable on record going back to the late-1980s. That said, these Provinces are also aware that medium-term demographic trends are far less favourable, so we'll see if the group chooses to use the current strength to build fiscal capacity for down the road.

All told, the combined provincial deficit is currently on track to widen to $16.7 billion in FY18/19 (or 0.8% of GDP), twice year-ago levels. But, that is entirely Ontario-driven, as the ex-Ontario deficit has narrowed for a third straight year—the overall combined shortfall should begin to shrink again in FY19/20. Net debt could also edge down as a share of GDP, after rising to a record high in FY18/19, now matching the federal total for the first time on record. Rob K.

Priscilla Thiagamoorthy
Economic Analyst
priscilla.thiagamoorthy@bmo.com
416-359-6229

	Good News	Bad News
Canada ▪ Global investors unload Canadian bonds at a rapid pace	**Existing Home Sales** +3.6% (Jan.)	**Manufacturing Sales Volumes** -1.2% (Dec.) **Manufacturing New Orders** -0.8% (Dec.) **MLS Home Price Index** +0.8% y/y (Jan.) **New Housing Price Index** unch (Dec.) **New Motor Vehicle Sales** -7.5% y/y (Dec.) **Global Investors** sold a net $19.0 bln in Canadian securities (Dec.)—largest since Oct. ’07
United States ▪ Pres. Trump says trade talks with China going *“extremely well”* ▪ Lawmakers agree to keep government funded through September… ▪ …but Pres. Trump declares national emergency for wall funding	**Job Openings** 7,335k (Dec.)—record high **Empire State Manufacturing Survey** +0.6 pts to an ISM-adjusted 52.5 (Feb.) **U of M Consumer Sentiment** +4.3 pts to 95.5 (Feb. P) **Producer Prices** +2.0% y/y (Jan.) **Import Prices** -1.7% y/y (Jan.)	**Retail Sales** -1.2% (Dec.)—biggest drop since Sep. ’09 **Industrial Production** -0.6% (Jan.) **Core Consumer Prices** +2.2% y/y (Jan.) **Business Inventories** -0.1% (Nov.) **NFIB Small Business Optimism Index** -3.2 pts to 101.2 (Jan.) **Initial Claims** +4k to 239k (Feb. 9 week)
Japan ▪ BoJ Gov. Kuroda is looking carefully for side effects of ultra-easy policy	**Real GDP** +0.3% q/q (Q4 P)	**Machine Tool Orders** -18.8% y/y (Jan. P) **Tertiary Industry Index** -0.3% (Dec.) **Producer Prices** +0.6% y/y (Jan.)
Europe ▪ Germany narrowly avoids a recession ▪ PM May loses key parliamentary vote… again ▪ BoE Gov. Carney stresses the *“need for certainty”* as Brexit risks weigh on growth	**U.K.—Consumer Prices** slowed to +1.8% y/y; **Producer Prices** +2.1% y/y (Jan.) **U.K.—Trade Deficit** narrowed slightly to £12.1 bln (Dec.) **U.K.—Retail Sales (incl. Fuel)** +1.0% (Jan.)	**Euro Area—Industrial Production** -0.9% (Dec.) **Euro Area—Trade Surplus** narrowed to €15.6 bln (Dec.) **Germany—Real GDP** unch q/q (Q4 P) **U.K.—Real GDP** slowed to +0.2% q/q (Q4 P) **U.K.—Monthly Real GDP** -0.4% (Dec.)—**Services GDP** -0.2% **U.K.—Industrial Production** -0.5% (Dec.) **U.K.—RICS House Price Balance** -22% (Jan.)
Other ▪ China’s negotiating team heads to Washington next week ▪ RBNZ on hold and tilts dovish	**China—Exports** +9.1% y/y (Jan.) **Aggregate Yuan Financing** 4.64 trln (Jan.)—and **New Yuan Loans** 3.23 trln **M2 Money Supply** +8.4% y/y (Jan.) **China—Foreign Reserves** up slightly to $3.09 trln (Jan.) **Australia—Consumer Confidence** +4.3% (Feb.) **Australia—Business Confidence** +1 pt to 4 (Jan.)	**China—Imports** -1.5% y/y (Jan.) **Consumer Prices** slowed to +1.7% y/y; **Producer Prices** +0.1% y/y (Jan.) **China—Foreign Direct Investment** slowed to +4.8% y/y (Jan.)

Indications of stronger growth and a move toward price stability are good news for the economy.

The Watch that Ends the Tightening Cycle?

Douglas Porter, CFA, Chief Economist • douglas.porter@bmo.com • 416-359-4887

A question that we are hearing more and more frequently in recent days is: **What exactly has changed in the past few months to justify such a dramatic adjustment in the North American interest rate outlook?** After all, the spirited recovery in stocks over the past eight weeks has lifted the S&P 500 above its 200-day moving average and has essentially reversed the December slide. As well, the government shutdown is done, U.S./China trade talks have taken on a better tone, and employment gains just keep chugging along. Yet, in barely three months' time, the outlook on central bank policy has taken a 90 degree turn, and held it. Since the point at which most U.S. interest rates peaked in early November, market expectations for Fed rate hikes have receded by roughly 50 bps, a move that has been almost mirrored across the Treasury curve.

Note from *Table 1* how little most other major financial variables have shifted on net since the collapse in rate expectations since November; and, it's a broadly similar tale for key economic metrics such as jobless rates and inflation. With stocks basically reversing their late-2018 sag in short order, the complete reset in bond yields stands in stark contrast *(Chart 1)*. So, again, what precisely has changed to trigger such a sea-change in the central bank outlook?

First, **let's dispense with the theory that the Fed succumbed to political pressure.** For one, the most intense criticism from the President was unleashed just prior to the December rate hike. Next, note that both that meeting's decision, as well as the dramatically more dovish tone at the January FOMC, saw unanimous votes. It's pretty tough to believe that the entire Fed board was swayed by hectoring from on high. Finally, note that Canadian markets also had a similarly dramatic rethink on the BoC outlook late last year, without any political posturing getting in the way *(Chart 2)*. The difference is that the Canadian overnight rate at 1.75% is 50-75 bps below the Fed's target range; while the Fed may have paused at the cusp of being at neutral, the BoC is well shy of the mildest estimate of neutral.

Instead, something much more fundamental must have changed to prompt such a profound pivot in the central bank outlook. Fed Chair Powell identified four broad factors for the change in January: tighter financial conditions, policy uncertainty, lower inflation expectations, and slower global growth. As we have previously asserted, all of the first three could readily be reversed or have already done so—for example, the snap-back in stocks, the partial recovery in oil, the retreat in yields and corporate spreads have eased financial conditions and stabilized the inflation outlook. The

Table 1

What Has Changed?

(as of February 15, 2019, 11:00 am)

	Nov. 8, 2018	Now	Change (bps)
U.S. 2-year Yield	2.98	2.51	-47
U.S. 10-year Yield	3.24	2.67	-57
10-year Real Return	1.17	0.80	-37
Implied Inflation	2.07	1.87	-20
Canada 2-year Yield	2.36	1.77	-59
Canada 10-year Yield	2.54	1.90	-64
Germany 10-year Yield	0.46	0.10	-36
			(%)
S&P 500	2,806	2,767	-1.4
TSX	15,357	15,807	2.9
WTI	60.67	55.46	-8.6
C$/US$	1.316	1.328	0.9
US$/Euro	1.136	1.126	-0.8
CNY/US$	6.93	6.77	-2.3

Sources: BMO Economics, Haver Analytics

Chart 1

Split Decision

United States (as of February 15, 2019, 10:00 am)

¹ (lhs : 1941-43=10) ² (rhs : %)

Sources: BMO Economics, Haver Analytics

Chart 2

Rate Hike Expectations Crumble

Canada (as of February 15, 2019, 10:00 am)

¹ (%) ² (ppts)

Sources: BMO Economics, Haver Analytics

policy uncertainty is hardly a new development, and may soon see some resolution on a few key files (U.S./China trade and Brexit).

The strongest and most compelling answer for what has changed is **a weaker outlook for the global economy**. It likely is not a coincidence that both Germany and Japan reported negative quarterly GDP readings the very week after yields peaked last November. Real concerns about global growth re-emerged with force at that time, and have not let go. The IMF has since clipped its forecast, and almost certainly has not yet gone far enough to meet the dimmer reality for 2019 (we are looking at a 3.3% rise for global GDP versus their revised 3.5%). This week saw the OECD LEI drop for a 12th consecutive month, taking it to a near decade low *(Chart 3)*. Perhaps the most pronounced change has been seen in Europe, which is now being widely flagged as *"the most likely region to first sink into recession"*. Industrial production fell more than 4% y/y in December and Q4 GDP eked out a meagre 0.8% annualized rise, taking the annual gain down to just 1.2% y/y versus 2.7% just one year ago. Between budget wrangling in Italy, the Yellow Vest protests in France, Brexit, more political uncertainty in Spain, and Germany's auto sector difficulties, all major EU economies are facing challenges.

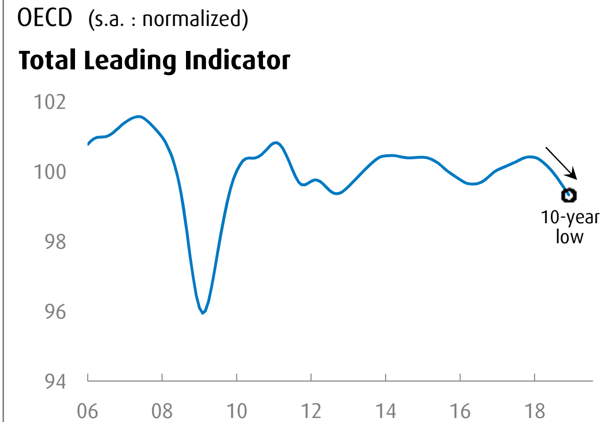
The cooldown is certainly not confined to Europe. Market volatility and policy uncertainty rattled U.S. consumer and business confidence, highlighted by the December dive in retail sales. After reaching a record high in August on the NFIB, and a 17-year high on the Conference Board's consumer survey, sentiment for both sectors has cascaded back to levels last seen in late 2016 *(Chart 4)*. While there are a whirlwind of factors at work here, intensifying trade conflicts may be the most corrosive underlying factor. Note the deepening slide in export sentiment in both Germany and the U.S., which began to really pick up steam after trade hostilities were cranked up last spring *(Chart 5)*.

If we can thus conclude that the primary and lasting reason for the Fed (and BoC) shift is a marked-down global outlook, the crucial next question is: **will slower global growth be enough to not just pause the rate hike cycle, but to end it?** The answer most likely depends on what unfolds for some of the many lingering policy uncertainties—especially on the trade front. Provided there are no big shocks, we suspect that the underlying bias to lift rates somewhat higher will re-emerge, and that there is as much upside risk to our call of one further rate hike as there is downside.

Bottom Line: Part of the abrupt reset in all interest rates can be justified by the combination of lower oil prices, a weaker global backdrop and trade uncertainty. Part, but not all. While both the Fed and the BoC have retracted their talons, we believe that this is a pause, and not an end, to the tightening cycle. We still lean to one more rate hike later this year by both, and hold on to the possibility of more in 2020 if some of biggest risk overhangs are resolved—U.S./China trade, Brexit, debt ceiling, etcetera, etcetera…

Chart 3

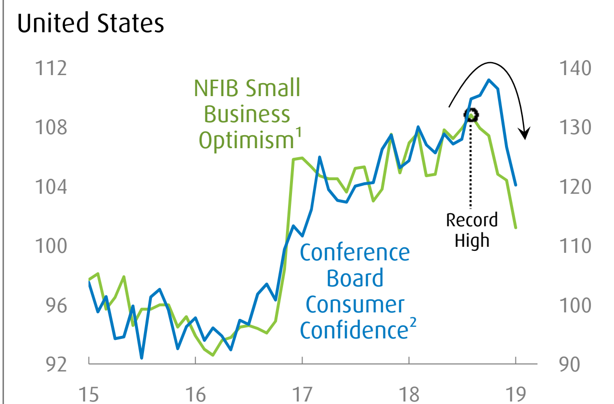
It's a Global Thing



Sources: BMO Economics, Haver Analytics

Chart 4

Sentiment Slumps for Consumers and Businesses...



¹ (lhs : 1986=100 : s.a.) ² (rhs : 1985 = 100 : s.a.)

Sources: BMO Economics, Haver Analytics

Chart 5

...and Exporters Especially

¹ manufacturers, next 3 months (lhs : 2015=100 : s.a.)

² (rhs : 50+ = expansion)

Sources: BMO Economics, Haver Analytics

Economic Forecast Summary for February 15, 2019

BMO Capital Markets Economic Research

	2018				2019				Annual		
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2017	2018	2019
CANADA											
Real GDP (q/q % chng : a.r.)	1.7	2.9	2.0	1.2	1.0	2.5	2.2	1.9	3.0	2.0	1.8
Consumer Price Index (y/y % chng)	2.1	2.3	2.7	2.0	1.5	1.8	1.7	2.0	1.6	2.3	1.8
Unemployment Rate (percent)	5.8	5.9	5.9	5.7	5.8	5.8	5.7	5.7	6.3	5.8	5.7
Housing Starts (000s : a.r.)	224	218	197	217	209	207	204	200	220	214	205
Current Account Balance ($blns : a.r.)	-69.3	-66.7	-41.4	-56.4	-55.8	-56.2	-57.5	-58.4	-60.1	-58.5	-57.0
Interest Rates	(average for the quarter : %)										
Overnight Rate	1.25	1.25	1.50	1.75	1.75	1.75	1.75	1.83	0.71	1.44	1.77
3-month Treasury Bill	1.14	1.21	1.47	1.66	1.65	1.65	1.65	1.85	0.69	1.37	1.70
10-year Bond	2.24	2.28	2.28	2.32	1.95	2.00	2.05	2.10	1.78	2.28	2.00
Canada-U.S. Interest Rate Spreads	(average for the quarter : bps)										
90-day	-44	-66	-61	-70	-77	-76	-76	-76	-26	-60	-76
10-year	-52	-64	-65	-72	-77	-76	-76	-75	-55	-63	-76
UNITED STATES											
Real GDP (q/q % chng : a.r.)	2.2	4.2	3.4	2.6	1.6	2.5	2.0	1.9	2.2	2.9	2.4
Consumer Price Index (y/y % chng)	2.2	2.7	2.6	2.2	1.6 ↓	1.7 ↓	1.7 ↓	1.9 ↓	2.1	2.4	1.7 ↓
Unemployment Rate (percent)	4.1	3.9	3.8	3.8	3.9	3.7	3.6	3.5	4.4	3.9	3.6
Housing Starts (mlns : a.r.)	1.32	1.26	1.23	1.24	1.26	1.24	1.23	1.21	1.21	1.26	1.24
Current Account Balance ($blns : a.r.)	-487	-405	-499	-490	-521	-535	-547	-557	-449	-470	-540
Interest Rates	(average for the quarter : %)										
Fed Funds Target Rate	1.46	1.71	1.96	2.21	2.38	2.38	2.38	2.46	1.00	1.83	2.40
3-month Treasury Bill	1.58	1.87	2.08	2.36	2.40	2.40	2.40	2.60	0.95	1.97	2.45
10-year Note	2.76	2.92	2.93	3.03	2.70	2.75	2.80	2.85	2.33	2.91	2.75
EXCHANGE RATES	(average for the quarter)										
US¢/C$	79.1	77.5	76.5	75.7	75.2	75.3	75.4	75.4	77.1	77.2	75.3
C$/US$	1.27	1.29	1.31	1.32	1.33	1.33	1.33	1.33	1.30	1.30	1.33
¥/US$	108	109	112	113	110 ↑	110 ↑	110	110	112	110	110 ↑
US$/Euro	1.23	1.19	1.16	1.14	1.14	1.15	1.16	1.17	1.13	1.18	1.15
US$/£	1.39	1.36	1.30	1.29	1.29 ↓	1.32	1.32	1.31	1.29	1.34	1.31

Blocked areas represent BMO Capital Markets forecasts

Up and down arrows indicate changes to the forecast ↑↓

Spreads may differ due to rounding

Canada

See Robert Kavcic's Thought on page 5.

Benjamin Reitzes
Canadian Rates & Macro Strategist
benjamin.reitzes@bmo.com
416-359-5628

British Columbia Budget
Tuesday

Retail Sales
Friday, 8:30 am

		Ex. Autos
Dec. (e)	**-0.1%**	**-0.3%**
Consensus	*unch*	*-0.5%*
Nov.	-0.9%	-0.6%

Retail sales likely slipped slightly to close 2018, but far from the deep downdraft seen in U.S. sales in December. Another sharp drop in gasoline prices is expected to weigh heavily on the report. Firmer auto sales look to provide a bit of offset, but not enough to keep the headline out of the red. Core sales (ex. autos & gas) are projected to climb modestly after November was much more subdued than we've seen over the past few years. Lastly, goods prices were down 0.2% in December, suggesting volumes will see a small positive in the month, enough to push the yearly change back above zero due to a favourable year-ago comparable.

United States

Michael Gregory, CFA
Deputy Chief Economist
michael.gregory@bmo.com
416-359-4747
Sal Guatieri
Senior Economist
sal.guatieri@bmo.com
416-359-5295

FOMC Minutes from January 29-30 meeting
Wednesday, 2:00 pm

The policy statement and Powell's press conference left little to the imagination, as both clearly argued the case for patience and flexibility before taking the next policy step, in either direction, not just forward. Due to *"muted inflation pressures"* and global *"cross-currents"*, the case for extending the tightening cycle—for both the policy rate and the balance sheet—is not as clear cut as when rates were far below neutral. And, this is despite continued *"strong"* job gains, *"low"* unemployment and *"solid"* economic growth; which, in the past, have tended to fan the inflation embers. The minutes are likely to reflect widespread support among policymakers—of every stripe—that an extended pause is the most prudent course of action until various headwinds fade or inflation pressures mount.

Durable Goods Orders
Thursday, 8:30 am

		Ex. Transport
Dec. (e)	**+1.0%**	**+0.4%**
Consensus	*+1.8%*	*+0.3%*
Nov.	+0.7%	-0.4%
	Nondef. Capital Goods ex. Air	
Dec. (e)	**+0.5%**	
Consensus	*+0.2%*	
Nov.	-0.6%	

Durable goods orders are expected to jump 1.0% in December, propelled by Boeing's bookings. Allowing for some braking in motor vehicle-related sales, total transportation orders likely rose 2.2%, though a lesser 0.4% excluding transportation. Nondefense capital goods orders excluding aircraft should rise 0.5%, supported by late-cycle capacity constraints and the drive to automate. However, there is little doubt that capex has downshifted in the face of trade and policy uncertainty. After growing at a 16.1% annualized rate in the four months to July due to tax reforms, the next four months saw core capital goods orders contract 2.6% annualized. Business investment is still expanding, though at a more moderate pace than earlier last year.

Existing Home Sales
Thursday, 10:00 am

Jan. (e)	**4.97 mln a.r. (-0.5%)**
Consensus	*5.00 mln a.r. (+0.2%)*
Dec.	4.99 mln a.r. (-6.4%)

Pending home sales fell in the final three months of 2018, suggesting contract closings began the New Year the same way they ended the old one, on a down note. As well, the Fed's recent survey of senior loan officers reported weaker housing demand, even as lending standards were little changed. Therefore, despite tumbling in December on widespread declines by segment and region, **existing home sales** are expected to slip another 0.5% to three-year lows of 4.97 million annualized in January. On a more positive note, new mortgage applications hit multi-year highs last month, while home-buying intentions in the Conference Board's consumer sentiment survey popped to 12-year highs. This suggests some near-term pickup in sales due to the recent drop in mortgage rates to a one-year low.

		Feb 15 [1]	Feb 8	Week Ago	4 Weeks Ago	Dec. 31, 2018
					(basis point change)	
Canadian Money Market	Call Money	1.75	1.75	0	0	0
	Prime Rate	3.95	3.95	0	0	0
U.S. Money Market	Fed Funds (effective)	2.50	2.50	0	0	0
	Prime Rate	5.50	5.50	0	0	0
3-Month Rates	Canada	1.68	1.65	3	6	4
	United States	2.42	2.41	1	3	7
	Japan	-0.22	-0.25	3	-1	-7
	Eurozone	-0.31	-0.31	0	0	0
	United Kingdom	0.87	0.88	-1	-6	-4
	Australia	1.97	2.01	-4	-10	-12
2-Year Bonds	Canada	1.78	1.77	1	-16	-8
	United States	2.50	2.47	4	-11	1
10-Year Bonds	Canada	1.90	1.88	3	-13	-6
	United States	2.67	2.64	3	-12	-2
	Japan	-0.03	-0.03	1	-4	-2
	Germany	0.10	0.09	2	-16	-14
	United Kingdom	1.16	1.15	1	-19	-12
	Australia	2.10	2.10	0	-22	-22
Risk Indicators	VIX	15.1	15.7	-0.7 pts	-2.7 pts	-10.4 pts
	TED Spread	26	29	-2	-11	-19
	Inv. Grade CDS Spread [2]	65	69	-4	-7	-23
	High Yield CDS Spread [2]	354	369	-15	-27	-96
					(percent change)	
Currencies	US¢/C$	75.30	75.31	0.0	-0.2	2.7
	C$/US$	1.328	1.328	—	—	—
	¥/US$	110.49	109.73	0.7	0.6	0.7
	US$/€	1.1263	1.1323	-0.5	-0.9	-1.8
	US$/£	1.283	1.294	-0.9	-0.3	0.6
	US¢/A$	71.20	70.88	0.5	-0.7	1.0
Commodities	CRB Futures Index	180.21	178.04	1.2	-1.1	6.1
	Oil (generic contract)	55.36	52.72	5.0	2.9	21.9
	Natural Gas (generic contract)	2.60	2.58	0.8	-25.2	-11.4
	Gold (spot price)	1,314.48	1,314.50	0.0	2.6	2.5
Equities	S&P/TSX Composite	15,838	15,633	1.3	3.5	10.6
	S&P 500	2,770	2,708	2.3	3.7	10.5
	Nasdaq	7,462	7,298	2.2	4.3	12.5
	Dow Jones Industrial	25,759	25,106	2.6	4.3	10.4
	Nikkei	20,901	20,333	2.8	1.1	4.4
	Frankfurt DAX	11,313	10,907	3.7	1.0	7.1
	London FT100	7,255	7,071	2.6	4.1	7.8
	France CAC40	5,163	4,962	4.1	5.9	9.1
	S&P ASX 200	6,066	6,071	-0.1	3.2	7.4

[1] = as of 10:50 am [2] = One day delay

Global Calendar
February 18 – February 22

BMO Capital Markets®

Japan

Monday February 18

Core Machine Orders

Dec. (e)	**-1.1%**	**+3.4% y/y**
Nov.	unch	+0.8% y/y

Department Store Sales [D]

Jan.	
Dec.	-0.7% y/y

Wednesday February 20

Trade Deficit

Jan. '19 (e)	**¥1.0 trln**
Jan. '18	¥1.0 trln

Thursday February 21

Manufacturing PMI

Feb. P	
Jan.	50.3

All-Industry Activity Index

Dec. (e)	**-0.2%**
Nov.	-0.3%

Machine Tool Orders

Jan. F (e)	**-18.8% y/y**
Dec.	-18.3% y/y

Friday February 22

	CPI	Core CPI
Jan. (e)	**+0.2% y/y**	**+0.8% y/y**
Dec.	+0.3% y/y	+0.7% y/y

CPI ex. Food & Energy

Jan. (e)	**+0.4% y/y**
Dec.	+0.3% y/y

Euro Area

Tuesday February 19

GERMANY

Zew Survey—Expectations

Feb. (e)	**-13.0**
Jan.	-15.0

ITALY

Industrial Orders

Dec.		
Nov.	-0.2%	-2.0% y/y

Wednesday February 20

EURO AREA

Consumer Confidence

Feb. A (e)	**-7.7**
Jan.	-7.9

GERMANY

Producer Price Index

Jan. (e)	**-0.2%**	**+2.2% y/y**
Dec.	-0.4%	+2.7% y/y

Thursday February 21

EURO AREA

Manufacturing PMI

Feb. P (e)	**50.3**
Jan.	50.5

Services PMI

Feb. P (e)	**51.3**
Jan.	51.2

Composite PMI

Feb. P (e)	**51.1**
Jan.	51.0

ECB Minutes from Jan. 24 meeting

GERMANY

Consumer Price Index

Jan. F (e)	**-1.0%**	**+1.7% y/y**
Dec.	+0.3%	+1.7% y/y

FRANCE

Consumer Price Index

Jan. F (e)	**-0.6%**	**+1.4% y/y**
Dec.	+0.1%	+1.9% y/y

ITALY

Consumer Price Index

Jan F. (e)	**-1.7%**	**+0.9% y/y**
Dec.	-0.1%	+1.2% y/y

Friday February 22

EURO AREA

Consumer Price Index

Jan. F (e)	**-1.1%**	**+1.4% y/y**
Dec.	unch	+1.6% y/y

Core CPI

Jan. F (e)	**+1.1% y/y**
Dec.	+1.0% y/y

GERMANY

Real GDP

Q4 F (e)	**unch**	**+0.6% y/y**
Q4 P	unch	+0.6% y/y
Q3	-0.2%	+1.1% y/y

Ifo Business Climate

Feb. (e)	**99.0**
Jan.	99.1

U.K.

Monday February 18

Rightmove House Prices

Feb.		
Jan.	+0.4%	+0.4% y/y

Tuesday February 19

Employment (3m/3m)

Dec. (e)	**+153,000**
Nov.	+141,000

Avg. Wkly Earnings Ex. Bonus (3 mma)

Dec. (e)	**+3.4% y/y**
Nov.	+3.3% y/y

Jobless Rate (3 mma)

Dec. (e)	**4.0%**
Nov.	4.0%

	Jobless Claims	Claimant Count Rate
Jan.		
Dec.	+20,800	2.8%

Other

Monday February 18

CHINA

U.S./China trade talks continue this week in Washington, D.C.

Tuesday February 19

AUSTRALIA

RBA Minutes from Feb. 5 meeting

Thursday February 21

AUSTRALIA

Employment

Jan. (e)	**+15,000**
Dec.	+21,600

Jobless Rate

Jan. (e)	**5.0%**
Dec.	5.0%

[D] = date approximate

Upcoming Policy Meetings | BoE: Mar. 21, May 2, June 20 | ECB: Mar. 7, Apr. 10, June 6

North American Calendar
February 18 – February 22

BMO Capital Markets

Monday February 18

Canada
Family Day (markets closed)

New date for previously delayed release:
Mar. 6: Merchandise Trade (Dec.)

United States
U.S./China trade talks continue this week in Washington, D.C.

President's Day (markets closed)

New dates for previously delayed releases:
- **Feb. 25:** Wholesale Trade (Dec.)
- **Feb. 26:** Housing Starts/Building Permits (Dec.)
- **Feb. 27:** Factory Orders; Advanced Indicators (Dec.)
- **Feb. 28:** Real GDP (Q4 A+P); Homeowner Vacancy Rate (Q4)
- **Mar. 1:** Personal Income & Spending (Dec.); Personal Income ex. Spending (Jan.)
- **Mar. 4:** Construction Spending (Dec.)
- **Mar. 5:** New Home Sales (Dec.), Budget Balance (Jan.)
- **Mar. 6:** Goods & Services Trade Deficit (Dec.)
- **Mar. 11:** Business Inventories (Dec.)
- **Mar. 21:** Services Survey (Q4)

Sunday February 17
President to receive Commerce Department recommendations on national security risk from auto imports

Tuesday February 19

Canada
British Columbia Budget

10:30 am — 3-, 6- & 12-month bill auction $12.0 bln (new cash $0.8 bln)

United States
10:00 am — NAHB Housing Index
Feb. (e)	**59**
Consensus	*59*
Jan.	58

Fed Speaker: Cleveland's Mester (8:50 am)

11:00 am — 4- & 8-week bill auction announcements

11:30 am — 13- & 26-week bill auction $84 bln

Wednesday February 20

Canada
Noon — 30-year real return bond auction $0.4 bln

United States
7:00 am — MBA Mortgage Apps
Feb. 15	
Feb. 8	-3.7%

2:00 pm — FOMC Minutes from January 29-30 meeting

11:30 am — 2[R]-year FRN auction $18 bln

Thursday February 21

Canada
8:30 am — Wholesale Trade
Dec. (e)	**-0.5%**
Nov.	-1.0%

8:30 am — ADP Employment Report
Jan.	
Dec.	-13,049

12:35 pm — BoC Governor Poloz speaks to the Montreal Chamber of Commerce

2-year bond auction announcement

United States
8:30 am — Initial Claims
Feb. 16 (e)	**229k (-10k)[C]**
Feb. 9	239k (+4k)

8:30 am — Continuing Claims
Feb. 9	
Feb. 2	1,773k (+37k)

8:30 am — Durable Goods
	Orders	Ex. Transport
Dec. (e)	**+1.0%**	**+0.4%**
Consensus	*+1.8%*	*+0.3%*
Nov.	+0.7%	-0.4%

8:30 am — Nondef. Capital Goods ex. Air
Dec. (e)	**+0.5%**
Consensus	*+0.2%*
Nov.	-0.6%

8:30 am — Real GDP by Industry (Q3)

8:30 am — Philly Fed Index
Feb. (e)	**14.0**
Consensus	*15.5*
Jan.	17.0

9:45 am — Markit PMI (Feb. P)

10:00 am — Existing Home Sales
Jan. (e)	**4.97 mln a.r. (-0.5%)**
Consensus	*5.00 mln a.r. (+0.2%)*
Dec.	4.99 mln a.r. (-6.4%)

10:00 am — Leading Indicator
Jan. (e)	**+0.1%**
Consensus	*+0.2%*
Dec.	-0.1%

Fed Speaker: Atlanta's Bostic (7:50 am)

11:00 am — 13-, 26- & 52-week bill, 2-, 5- & 7-year note auction announcements

11:30 am — 4- & 8-week bill auction

1:00 pm — 30-year TIPS auction $8 bln

Friday February 22

Canada
8:30 am — Retail Sales
	Retail Sales	Ex. Autos
Dec. (e)	**-0.1%**	**-0.3%**
Consensus	*unch*	*-0.5%*
Nov.	-0.9%	-0.6%

Ottawa's Budget Balance[D]
Dec. '18	
Dec. '17	+$565 mln

United States
11:00 am — Monetary Policy Report

Fed Speakers: Atlanta's Bostic (8:15 am); New York's Williams (10:15 am, 5:30 pm); Vice Chair Clarida (noon); St. Louis' Bullard (1:30 pm); Philadelphia's Harker (1:30 pm); Vice Chair for Supervision Quarles (1:30 pm)

[C] = consensus [D] = date approximate [R] = reopening

Upcoming Policy Meetings | Bank of Canada: Mar. 6, Apr. 24, May 29 | FOMC: Mar. 19-20, Apr. 30-May 1, June 18-19

General Disclosure

"BMO Capital Markets" is a trade name used by the BMO Financial Group for the wholesale banking businesses of Bank of Montreal and its subsidiaries BMO Nesbitt Burns Inc., BMO Capital Markets Limited in the U.K. and BMO Capital Markets Corp. in the U.S. BMO Nesbitt Burns Inc., BMO Capital Markets Limited and BMO Capital Markets Corp are affiliates. This document is issued and distributed in Hong Kong by Bank of Montreal ("BMO"). BMO is an authorized institution under the Banking Ordinance (Chapter 155 of the Laws of Hong Kong) and a registered institution with the Securities and Futures Commission (CE No. AAK809) under the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong). BMO does not represent that this document may be lawfully distributed, or that any financial products may be lawfully offered or dealt with, in compliance with any regulatory requirements in other jurisdictions, or pursuant to an exemption available thereunder. This document is directed only at entities or persons in jurisdictions or countries where access to and use of the information is not contrary to local laws or regulations. Their contents have not been reviewed by any regulatory authority. Bank of Montreal or its subsidiaries ("BMO Financial Group") has lending arrangements with, or provide other remunerated services to, many issuers covered by BMO Capital Markets. The opinions, estimates and projections contained in this report are those of BMO Capital Markets as of the date of this report and are subject to change without notice. BMO Capital Markets endeavours to ensure that the contents have been compiled or derived from sources that we believe are reliable and contain information and opinions that are accurate and complete. However, BMO Capital Markets makes no representation or warranty, express or implied, in respect thereof, takes no responsibility for any errors and omissions contained herein and accepts no liability whatsoever for any loss arising from any use of, or reliance on, this report or its contents. Information may be available to BMO Capital Markets or its affiliates that is not reflected in this report. The information in this report is not intended to be used as the primary basis of investment decisions, and because of individual client objectives, should not be construed as advice designed to meet the particular investment needs of any investor. This document is not to be construed as an offer to sell, a solicitation for or an offer to buy, any products or services referenced herein (including, without limitation, any commodities, securities or other financial instruments), nor shall such Information be considered as investment advice or as a recommendation to enter into any transaction. Each investor should consider obtaining independent advice before making any financial decisions. This document is provided for general information only and does not take into account any investor's particular needs, financial status or investment objectives. BMO Capital Markets or its affiliates will buy from or sell to customers the securities of issuers mentioned in this report on a principal basis. BMO Capital Markets or its affiliates, officers, directors or employees have a long or short position in many of the securities discussed herein, related securities or in options, futures or other derivative instruments based thereon. The reader should assume that BMO Capital Markets or its affiliates may have a conflict of interest and should not rely solely on this report in evaluating whether or not to buy or sell securities of issuers discussed herein.

Dissemination of Research

Our publications are disseminated via email and may also be available via our web site http://economics.bmocapitalmarkets.com. Please contact your BMO Financial Group Representative for more information.

Conflict Statement

A general description of how BMO Financial Group identifies and manages conflicts of interest is contained in our public facing policy for managing conflicts of interest in connection with investment research which is available at http://researchglobal.bmocapitalmarkets.com/Public/Conflict_Statement_Public.aspx.

ADDITIONAL INFORMATION IS AVAILABLE UPON REQUEST

BMO Financial Group (NYSE, TSX: BMO) is an integrated financial services provider offering a range of retail banking, wealth management, and investment and corporate banking products. BMO serves Canadian retail clients through BMO Bank of Montreal and BMO Nesbitt Burns. In the United States, personal and commercial banking clients are served by BMO Harris Bank N.A., Member FDIC. Investment and corporate banking services are provided in Canada and the US through BMO Capital Markets. BMO Capital Markets is a trade name used by BMO Financial Group for the wholesale banking businesses of Bank of Montreal, BMO Harris Bank N.A, BMO Ireland Plc, and Bank of Montreal (China) Co. Ltd. and the institutional broker dealer businesses of BMO Capital Markets Corp. (Member SIPC), BMO Nesbitt Burns Securities Limited (Member SIPC) in the U.S., BMO Nesbitt Burns Inc. (Member Canadian Investor Protection Fund) in Canada, Europe and Asia, BMO Capital Markets Limited in Europe, Asia and Australia and BMO Advisors Private Limited in India.

"Nesbitt Burns" is a registered trademark of BMO Nesbitt Burns Inc., used under license. "BMO Capital Markets" is a trademark of Bank of Montreal, used under license. "BMO (M-Bar roundel symbol)" is a registered trademark of Bank of Montreal, used under license.

® Registered trademark of Bank of Montreal in the United States, Canada and elsewhere.

™ Trademark Bank of Montreal in the United States and Canada.

© COPYRIGHT 2019 BMO CAPITAL MARKETS CORP.

A member of BMO Financial Group