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BMO CAPITAL MARKETS ECONOMICS

Focus

A weekly financial digest

Douglas Porter, CFA, Chief Economist, BMO Financial Group

May 10, 2019

Europe's Struggles Are Just Beginning

U.S. Hikes Tariffs on China to 25%

...Wall Street Sags

Canadian Jobs Gain Biggest in 43 Years

...But Trade Cuts Q1 GDP

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Tariff-ic

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Just when the clouds were parting for the U.S. economy in light of perkier productivity and equity markets, the threat of rising **trade protectionism** struck like a lightning bolt this week. After months of what seemed like constructive talks, the President said China *"broke the deal"*. Although talks continue, hopes of a quick settlement were dashed, and new 25% tariffs kicked in. So, after an eight-month ceasefire, it's time to sharpen our pencils again and tally the economic casualties from the trade war.

Let's start with the U.S. To be sure, estimates of tariff effects on GDP are fraught with uncertainty due to the many moving parts. To simplify the analysis, **we exclude currency effects**—the dollar is up 6% against the renminbi in the past year, allaying the loss of spending power though aggravating the effect of retaliatory actions on exports. We also **ignore policy responses** designed to cushion the blow—for instance, China has eased monetary and fiscal policies since the tariff tiff began last summer. **We focus on three channels**: the **loss of purchasing power** from higher-priced imports (with companies running at full tilt, imports will need to come from other countries or still from China, in both cases at higher cost); **China's retaliatory actions** to punish U.S. exporters; and, an **assumed adverse effect on business confidence and supply chains** that dampens investment. With that understood, the previous tariffs—25% on \$50 billion of China's goods effective July 6, 2018 and 10% on almost 6,000 items valued at \$200 billion effective September 24—are estimated to reduce U.S. GDP by about 0.2% over roughly a year. Friday's ratcheting of the latter duty to 25% and expected counter measures by China could hive off another 0.1%. And, if the President carries through with a repeated threat to impose a 25% duty on all other goods imports from China (about \$270 billion based on the 12-month tally to March), then another 0.3% will be added to the roster.

So, the total cost to the U.S. economy of the current trade tiff and threatened escalation with China could amount to 0.6%. Adding earlier tariffs on global imports of metals, solar panels and washing machines slices another 0.1%, while the looming threat of a duty on automobiles (excluding Canada and Mexico) could reduce activity by an additional 0.3% (we'll know next week as the President is expected to make an announcement by May 18).This implies around **1.0% of lost U.S. output (or 1½ million jobs) due to past and threatened protectionist actions**. No small potatoes.

China will suffer more than the U.S. While U.S. sales to China account for less than 1% of U.S. GDP, China's shipments to the U.S. make up over 3% of its economy. The earlier tariffs likely lower China's GDP by 0.5%, and the recent higher duty could strip off another 0.4%. The combined 0.9% impact could then nearly double to **1.7% if all of China's shipments to the U.S. are hit with a 25% tax**.

Bystander Canada gets off lighter than China and the U.S. but not unscathed. Watching your major trading partner and world's two largest commodity consumers slug it out on the battlefield doesn't exactly inspire confidence among businesses (though you wouldn't know if from the latest jobs report). The estimated 1.0% slowing in U.S. GDP due to current duties and possible further protectionist moves could translate into 0.5% less Canadian output, based on the estimated impact of a change in U.S. growth on Canada. Lower commodity prices won't help. Including earlier tariffs on steel, aluminum and retaliatory actions could cost the economy another 0.3%, putting the potential **hit from a global trade war at around 0.8%** (or 150,000 jobs) for Canada.

Apart from some firms in protected industries, there are few winners when countries start unfurling the protectionist banner. While the U.S. may extract concessions from China that eventually support its trade balance and economy, the casualties on the ground are starting to mount. It's a high-stakes game for both nations, which is at least one reason to believe that either side will fold and call a truce.

"Transitory" Still in Transit

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This week's U.S. CPI data were scoured for clues on whether the economy's turn-of-the-year disinflationary impulse was starting to stabilize or turn around. Consumers and businesses have already started unfastening the spending hatches that were originally battened down owing to the equity market scare, government shutdown and extreme weather. For example, real consumer spending jumped 0.7% in March after a -0.3% cumulative move over the previous three months. Core capital goods orders rose 1.4% in March after a cumulative 1.0% fall in the prior four months. What about prices?

The core CPI increased 0.1% in April, lifting the annual change a tenth to 2.1%. However, the shorter-term trends pointed to **no forward momentum**. The 6-month change slipped a tenth to 2.1% annualized, while the more volatile 3-month move dropped four tenths to 1.6% annualized. In April, shelter and medical care costs were the largest positive contributors (+0.4% and +0.3%, respectively). On the other side, driving the largest drop in core goods prices (-0.3%) in more than 12½ years (taken to two decimal places) were used vehicles (-1.3%). They are now down in four of the five past months for a cumulative decrease that matches the worst since the recession. Also, after posting their largest drop in 70 years owing to a methodological change, apparel prices fell again (-0.8%).

Of course, the Fed's operational target is the **core PCE price index**, not its CPI cousin. And, the latter suggests (via regression analysis) that the former could also rise 0.1%, but not enough to prevent the annual change from **dipping a tenth to 1.5%**… the likes of which we haven't seen since the summer of '17. At last month's post-FOMC presser, Fed Chair Powell employed the *"transitory"* or *"transient"* adjective often to describe the ebb in core inflation. It now looks like we'll have to wait until the May data (to be released in June) before potentially seeing any preliminary hint of stabilizing or turning around.

We agree that **most of core inflation's recent ebbing should prove to be temporary**. Since December, an unchanged trimmed-mean core PCE inflation rate (at 2.0% y/y) highlights that oversized individual price moves drove the disinflation, moves tied to the pullback in markets or caution in spending, and moves that should reverse course. However, we cautioned that **one shouldn't be completely dismissive of this year's disinflationary impulse**. This was because of the transitory nature of last year's inflationary impulse. Recall, a large dollop of fiscal stimulus was added to an economy already operating very close to full capacity. The consequent pickup in activity (4.2% annualized real GDP growth in 2018Q2) pushed the output gap into positive territory for the first time since before the Great Recession and stoked the embers of inflation. Core PCE inflation started 2018 at 1.6% and was hitting 2.0% during the spring months with the shorter-term metrics pointing to further acceleration into the 2.2%-to-2.3% range. But this didn't last. By the autumn, the shorter-term trends had cooled significantly (1.3%-to-1.6% range) and core inflation barely managed to hold on to 2.0%.

Given the obvious cyclical upward pressure on inflation—a late-cycle blast of fiscal stimulus—it must be that the secular forces of disinflation (such as automation, aging and digitalization) proved again to be dominant last year. And, they could still be dominant this year, which will act to rein in the anticipated rebound in core inflation and, thus, **keep the Fed's finger close to the easing trigger**. We could see some inflation push from the hike in tariffs on Chinese goods and, potentially, imported vehicles and parts, but the Fed will also be keeping its eye on the cost to growth. Indeed, given the failure so far to achieve the 2.0% inflation target in a symmetric fashion, we suspect the Fed will pay more attention to the growth consequences of tariffs' stagflationary impulses. MJG

Transitory Story Looking Good

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It was quite the week for Canada watchers as the data were solid almost across the board. After a rough start to 2019, it looks as if the economy ended Q1 in better shape and the initial Q2 data points were exceptionally solid. April **employment saw its best gain in 43 years** (and best in percentage terms since 1994), while housing starts surged 22% to 235k units annualized. Can't argue with that strength. However, those types of gains/levels are not sustainable, so next month will likely be much tamer. Indeed, there will be calls for some big-time payback in May employment; and, while that's a reasonable expectation (and the way I'd lean), it's important to note that similar expectations through the strong jobs run which started last summer would have been DEAD WRONG.

The bigger picture for Canada is that it **appears as though the economic weakness in Q4 and Q1 was transitory**. Unfortunately, we still need to finish off the Q1 data, with March/Q1 GDP not out until month-end. And, while the trade numbers were solid in March, the quarter was exceptionally weak and net exports look to have subtracted 3-to-4 percentage points from Q1 GDP. When the BoC released its April MPR forecast of just 0.3% growth in Q1, it seemed conservative. It now looks pretty good and **we've cut our forecast to a mere 0.2%**. That would mean there was pretty much zero growth in the past two quarters. So, while the March data will probably be decent, expect a dud of a quarterly report at month-end.

Key Takeaway: While the global headlines were less than encouraging this week, the domestic picture perked up and the BoC's transitory weakness thesis is looking pretty good. It's still really early with just a couple of Q2 data points; but, this backdrop suggests the BoC is a long way from contemplating rate cuts, while the wider output gap leaves potential hikes in the distant future (assuming all goes well). Barring a big shock, the **Bank could be on hold for some time**. *B.A.A.R.*

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	Good News	Bad News
Canada ▪ Growth forecasts slashed for Q1 following dismal trade data ▪ BoC Gov. Poloz expects housing market growth as GTA, GVA stabilize	**Employment** +106,500 (Apr.) **Jobless Rate** -0.1 ppts to 5.7% (Apr.) **Average Hourly Wages** +2.5% y/y (Apr.) **Merchandise Trade Deficit** narrowed to $3.2 bln (Mar.) **Housing Starts** +22.6% to 235,460 a.r. (Apr.) **Building Permits** +2.1% (Mar.) **Ivey PMI** +1.6 pts to 55.9 (Apr.)	**New Housing Price Index** unch (Mar.)
United States ▪ U.S. increases tariffs from 10% to 25% on Chinese imports… ▪ …stocks slide as truce ends	**Consumer Prices** +2.0% y/y (Apr.) **Producer Prices** +2.2% y/y (Apr.) **Job Openings** climbed to 7,488k (Mar.) **Initial Claims** -2k to 228k (May 4 week)	**Consumer Credit** slowed to +$10.28 bln (Mar.) **Goods & Services Trade Deficit** widened to $50.0 bln (Mar.) **Wholesale Inventories** revised down to -0.1% (Mar.)
Japan ▪ JPY strengthens amid flight to safety	**Household Spending** +2.1% y/y (Mar.) **Manufacturing PMI** revised up to 50.2 (Apr.) **Composite PMI** +0.4 pts to 50.8 (Apr.)	**Services PMI** -0.2 pts to 51.8 (Apr.) **Consumer Confidence** -0.1 pts to 40.4 (Apr.)
Europe ▪ U.K. Q1 growth supported by inventory stockpiling ahead of Brexit ▪ Norges Bank hawkish… looks for June hike	**Euro Area—Retail Sales** unch (Mar.) **Euro Area—Services PMI** revised up to 52.8; **Composite PMI** revised up to 51.5 (Apr.) **Germany—Industrial Production** +0.5% (Mar.) **Germany—Trade Surplus** widened to €20.0 bln (Mar.) **U.K.—Real GDP** +0.5% (Q1 P)—but boosted by Brexit preparations **U.K.—Industrial Production** +0.7% (Mar.) **U.K.—Trade Deficit** narrowed to £13.7 bln (Mar.)	**Germany—Factory Orders** +0.6% (Mar.) —below expected **France—Trade Deficit** widened to €5.3 bln (Mar.) **France—Industrial Production** -0.9% (Mar.) **Italy—Industrial Production** -0.9% (Mar.) **Italy—Retail Sales** -0.3% (Mar.) **U.K.—Monthly Real GDP** -0.1%; **Index of Services** -0.1% (Mar.)
Other ▪ U.S./China trade talks fail to meet deadline… China will retaliate ▪ RBA on hold… for now… cuts growth and inflation forecasts ▪ RBNZ cuts 25 bps to 1.50% ▪ Brazil on hold	**China—Imports** +4.0% y/y (Apr.) **China—Consumer Prices** +2.5% y/y; **Producer Prices** +0.9% y/y (Apr.) **China—Caixin Services PMI** +0.1 pts to 54.5 (Apr.) **Australia—Retail Sales** +0.3% (Mar.)	**China—Exports** -2.7% y/y (Apr.) **China—Aggregate Yuan Financing** slowed to 1.36 trln (Apr.)—and **New Yuan Loans** to 1.02 trln **China—M2 Money Supply** eased to +8.5% y/y (Apr.) **China—Caixin Composite PMI** -0.2 pts to 52.7 (Apr.) **China—Foreign Reserves** down slightly to $3.09 trln (Apr.) **Australia—Trade Surplus** narrowed to A$4.9 bln (Mar.)

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

Europe’s Struggles Are Just Beginning

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Perhaps the biggest downside surprise for the global economy in the past year has been Europe. While picking up somewhat in Q1, Euro Area GDP has risen just 1.2% y/y, half the pace of a year earlier. And, the euro is down 6%. Where next for the world’s largest trading bloc?

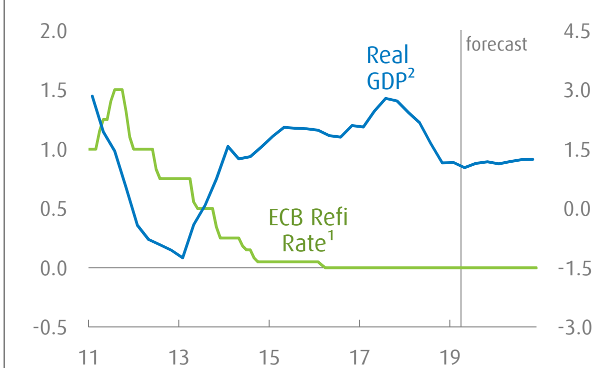
It has been nearly a year since the ECB signalled the end of quantitative easing, *“subject to incoming data”*, and that rates would stay at record lows *“at least through the summer of 2019”*. That declaration put the central bank firmly on the road to normalization. Over the following six months, as the economy slowed and the ECB trimmed the growth outlook, President Draghi defended the decision to remain on the path to end QE: *“We’re talking about weaker momentum, not a downturn.”* Besides, there were special factors at play, such as the implementation of new emissions-testing processes which stalled German car production, and political tensions which rippled through the Continent, including: Italy’s stand-off with Brussels over its national budget; Angela Merkel’s decision not to run for Chancellor again; and, the start of France’s Yellow Vest protests. All serious concerns, but the ECB could not be seen reacting to political developments. Plus, manufacturing and service PMIs had weakened, but Euro Area inflation was still on target, making it difficult to change course on the decision to stop asset purchases—lest it be accused of panicking. But, when QE ended in December, the ECB did not push the planned date for rate hikes far into the distance. Only in March did the central bank finally throw in the towel, not only changing the guidance to *“through the end of 2019”*, but introducing a new set of quarterly targeted longer-term refinancing operations, aka TLTRO-III, to keep credit flowing.

Trade War Looms

As the Euro Area economy continues to struggle, it now faces another large source of uncertainty: **the prospect of a trade war with the U.S.**, which is particularly worrying for **Germany**. The country is highly export-reliant (nearly 50% of GDP), and exports to the U.S. make up around 8.5% of the total (3% of GDP), mostly motor vehicles, machinery, pharmaceuticals, and computers/electronics. These cyclical industries are already feeling the effects of slower global demand, so potential U.S. tariffs on European cars would be another hit. (President Trump will make that decision by May 18th.) Germany is also under pressure from the rest of Europe to relax its fiscal rules and use some of its budget surplus for economic stimulus, but it is extremely reluctant to do so. No wonder German business executives are gloomy, as the latest Ifo survey showed. At least German domestic demand, though slowing, is 2% above year-ago levels, with record low joblessness underpinning consumer spending. In **France** and **Italy**, exports account for a smaller, but still significant, share of the economy (one-third), but other issues are

Chart 1
Flattish Growth

Euro Area

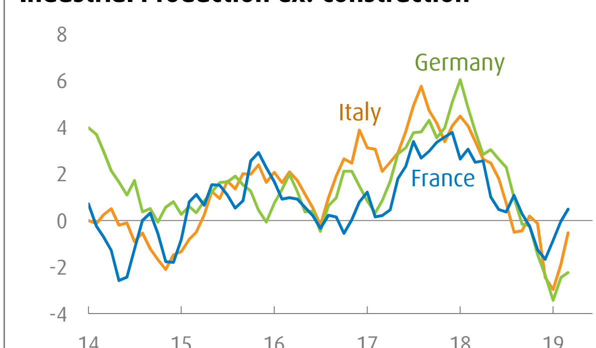


1 (lhs : %) 2 (rhs : y/y % chng)
Sources: BMO Economics, Haver Analytics

Chart 2
Production Declines Slow

(3-mnth m.a. : y/y % chng)

Industrial Production ex. Construction



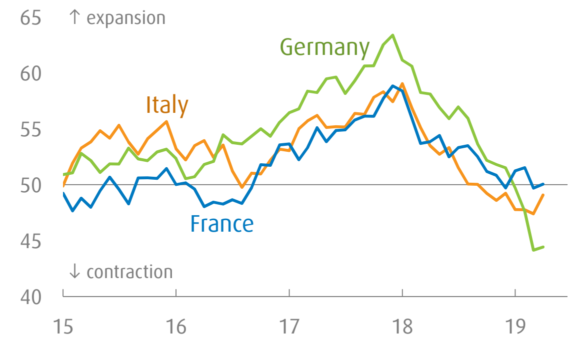
Sources: BMO Economics, Haver Analytics

weighing. In France, the Yellow Vest protests are hurting consumer spending; and, in Italy, growth is being held back by weak competitiveness (the country is ranked #31 of 140 countries in the World Economic Forum's Global Competitiveness Index, well behind the rest of the G7).

Chart 3
Manufacturing Hardest Hit

(s.a. : diffusion index)

Markit Manufacturing PMI

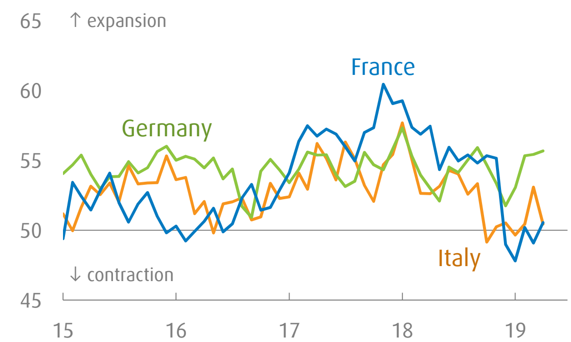


Sources: BMO Economics, Haver Analytics

Chart 4
Services Activity Less Weak

(s.a. : diffusion index)

Markit Services PMI



Sources: BMO Economics, Haver Analytics

Political Winds Blow

There is fear that there will be public backlash from years of fiscal austerity and structural reforms. Although these steps helped lift the Euro Area out of its debt crisis, it is **possible that the reform process could stall**, which is why the **upcoming May European Parliamentary elections are important to watch**. Newer political parties are capitalizing on public resentment after years of austerity and on controversial issues such as immigration. A softer economy simply compounds the situation. Nationalism has been rising throughout Europe (in fits and starts) and the influence of these newer parties, from all over the political spectrum, has grown. Adding to this volatile mix will be the presence of the U.K., and Nigel Farage's Brexit Party. And, candidates are faced with what is typically low voter turnout (1979: 62%, 2014: 42.6%). Also making this election important is that the top four jobs are up for grabs: Head of the European Commission (currently held by Jean-Claude Juncker), the European Council (Donald Tusk), the European Parliament (Antonio Tajani), and the ECB (Mario Draghi). All in, the populist parties could sway the vote enough to cost the mainstream European parties—centre-right EPP and centre-left S&D—their primacy and disrupt the legislature's normal business activities, such as determining the EU's budget.

Domestic politics are already reflecting these changes. In **Germany**, voters were angry over Angela Merkel's policies on migrants, costing the ruling CDU a large number of seats and Merkel's job as party leader, which she had held for 18 years. This has opened up the question of who will next lead Europe's largest economy, and the newest CDU leader must contend with more potential coalition partners than before. It is not just the Social Democrats, but the FDP, the Greens, and now, the far-right Alternative for Germany (AfD) are jockeying for position.

In **France**, President Emmanuel Macron's La République En Marche!, made up of individuals from the left and the right, has a vision for a more unified Europe while revving up the economy with business-friendly tax and fiscal policies. However, President Macron was forced to put aside his dreams of a *"European renaissance"* in order to deal with domestic unrest. Marine Le Pen's far-right National Rally party (formerly known as the National Front) took the opportunity to call out the government's policies and introduced a new 23-year old radical, Jordan Bardella, to appeal to the youth vote, while trying to win support from environmentalists on the left. And it is working; recent polls have the National Rally in the lead.

There has already been plenty of change in **Italy**. The centre-left Democrats were ousted last year and replaced by a coalition government made up of the anti-establishment Five-Star Movement and Northern League. Although the parties' leaders are often at odds, they are united when defending their fiscal plans to Brussels. And, though Italy fell into recession in the second half of 2019, the downturn has ended. Now, Matteo Salvini has been busily forming his own European party, with the European Alliance of Peoples and Nations made up of various politicians from the Continent, bound by some similar views; mainly, anti-immigration.

Finally, **Spain's** recent federal election saw Pedro Sanchez return as Prime Minister, but his left-wing Socialist party failed to win a majority and may need to lean on Catalonian separatists to govern. Meantime, the far-right VOX party entered Parliament for the first time since the country became a democracy.

Bottom Line: European economic growth remains weak at a time when the region is readying for a fight at the international level (trade) and battling it out within the Continent (populists). The ECB is unlikely to return to asset purchases but will likely commit to keeping rates lower for far longer than *"the end of 2019"*, which should put a lid on the euro. These more accommodative financial conditions will support GDP growth. But, with trade tensions building in the second half of this year and into 2020, we are not expecting much of a pickup beyond 1¼%.

View from our European Head of FX Strategy

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The EUR has already had a rough first half of the year, and our view is that risks facing the currency will remain biased to the downside, through the parliamentary elections in May and into the second half of 2019. The political fractures that will be made apparent in the elections should ultimately make the Eurozone more unwieldy to govern, leaving the bloc woefully exposed to the next global downturn, whenever that occurs. Brexit has a role to play as well, and not only because the risks of "no deal" are still lingering. Many voters will view the current Brexit impasse as another example of a bloc that is unattractive to remain a part of but also impossible to exit, and this strikes us as a recipe for a protracted period of political tension. We anticipate further dovish pivots from the ECB over the balance of the year, and short-EURUSD remains one of our preferred trades in FX, not least because it offers investors attractive carry. We in FX Strategy see the pair trading at 1.09 in 3M.

There is one upside risk to our bearish EUR call worth mentioning in the form of growth-positive fiscal policy. It is conceivable that at some point, an agreement amongst member states and the Eurogroup could be reached, aimed at relaxing the bloc's draconian fiscal rules. Such an agreement would be a significant short-run positive for the EUR that would probably allow the ECB to adopt a less "dovish" policy stance over time and possibly even allow ECB President Draghi to be replaced by a more "hawkish" successor, such as Jens Weidmann. At this stage, we assign this scenario a very low probability, but with so many moving parts in play, including international trade tensions, this is a risk worth monitoring.

Economic Forecast Summary for May 10, 2019

BMO Capital Markets Economic Research

	2018				2019				Annual		
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2018	2019	2020
CANADA											
Real GDP (q/q % chng : a.r.)	1.3	2.6	2.0	0.4	0.2 ↓	2.3	2.2	1.5	1.8	1.4 ↓	1.7
Consumer Price Index (y/y % chng)	2.1	2.3	2.7	2.0	1.6	2.0	1.9	2.2	2.3	1.9	2.1
Unemployment Rate (percent)	5.8	5.9	5.9	5.7	5.8	5.7	5.7	5.7	5.8	5.7	5.6
Housing Starts (000s : a.r.)	224	218	197	217	188	218 ↑	209 ↓	208	214	205	200
Current Account Balance ($blns : a.r.)	-69.0	-63.4	-40.4	-61.9	-72.9 ↓	-61.7 ↓	-61.8 ↓	-63.6 ↓	-58.7	-65.0 ↓	-61.0 ↓
Interest Rates	(average for the quarter : %)										
Overnight Rate	1.25	1.25	1.50	1.75	1.75	1.75	1.75	1.75	1.44	1.75	1.75
3-month Treasury Bill	1.14	1.21	1.47	1.66	1.65	1.65 ↓	1.65 ↓	1.65 ↓	1.37	1.65 ↓	1.65 ↓
10-year Bond	2.24	2.28	2.28	2.32	1.86	1.70 ↓	1.75 ↓	1.85	2.28	1.80	1.75
Canada-U.S. Interest Rate Spreads	(average for the quarter : bps)										
90-day	-44	-66	-61	-70	-79	-76 ↑	-76	-76	-60	-77	-73 ↓
10-year	-52	-64	-65	-72	-80	-78 ↑	-77 ↑	-76 ↑	-63	-78	-73 ↑
UNITED STATES											
Real GDP (q/q % chng : a.r.)	2.2	4.2	3.4	2.2	3.2	1.5	2.0	1.9	2.9	2.5	1.7
Consumer Price Index (y/y % chng)	2.2	2.7	2.6	2.2	1.6	2.0 ↓	2.1	2.3	2.4	2.0	2.2
Unemployment Rate (percent)	4.1	3.9	3.8	3.8	3.9	3.6	3.6	3.5	3.9	3.6	3.6
Housing Starts (mlns : a.r.)	1.32	1.26	1.23	1.19	1.19	1.22	1.24	1.22	1.25	1.22	1.23
Current Account Balance ($blns : a.r.)	-496	-414	-506	-538	-468	-483	-499	-512	-488	-490	-535
Interest Rates	(average for the quarter : %)										
Fed Funds Target Rate	1.46	1.71	1.96	2.21	2.38	2.38	2.38	2.38	1.83	2.38	2.38
3-month Treasury Bill	1.58	1.87	2.08	2.36	2.44	2.45	2.45	2.45	1.97	2.45	2.40
10-year Note	2.76	2.92	2.93	3.03	2.65	2.50 ↓	2.55 ↓	2.60	2.91	2.55 ↓	2.50
EXCHANGE RATES	(average for the quarter)										
US¢/C$	79.1	77.5	76.5	75.7	75.2	74.5	74.8	75.3	77.2	75.0	76.3
C$/US$	1.27	1.29	1.31	1.32	1.33	1.34	1.34	1.33	1.30	1.33	1.31
¥/US$	108	109	112	113	110	111	110 ↓	110	110	110 ↓	109
US$/Euro	1.23	1.19	1.16	1.14	1.14	1.12	1.12 ↓	1.12 ↓	1.18	1.12 ↓	1.13 ↓
US$/£	1.39	1.36	1.30	1.29	1.30	1.30	1.31	1.31	1.34	1.31	1.32 ↓

Blocked areas represent BMO Capital Markets forecasts
Up and down arrows indicate changes to the forecast ↑↓

Spreads may differ due to rounding

Canada

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Consumer Price Index
Wednesday, 8:30 am

Apr. (e)	**+0.4% (+0.1% sa)**	**+2.0% y/y**
Consensus	*%*	*% y/y*
Mar.	+0.7%	+1.9% y/y

Core CPI Measures (y/y)

	Trimmed Mean	**Weighted Median**	**Common Comp.**
Apr.			
Mar.	+2.1%	+2.0%	+1.8%

Canadian inflation is expected to rise solidly for a third consecutive month in April, though it won't be quite as strong as the prior two months. We're looking for a 0.4% increase, with another jump in gasoline prices the key driver. Pump prices likely climbed about 9% in April, which would put the three-month increase at nearly 22%. The strongest seasonal period for inflation has passed, but April and May are still among the stronger months. Beyond energy, shelter and household operations/furnishings are expected to lift inflation, while airfares and travel services reverse the March-break driven gain. Our call would push annual inflation up a tick to 2% for the first time since October.

Two of the Bank of Canada's core CPI measures, weighted median and trimmed mean, moved back to target in March. Look for those two to hold steady in April, with some upside risk for the weighted median. Meantime, the common component was steady last month at 1.8%, and that isn't expected to change this month.

Existing Home Sales, MLS Home Price Index
Wednesday, 9:00 (expected)

	Existing Home Sales	**Average Prices**
Apr. (e)	**+3.0% y/y**	**unch y/y**
Mar.	-4.6% y/y	-1.8% y/y

	MLS Home Price Index
Apr. (e)	**unch y/y**
Mar.	-0.5% y/y

Better weather drove better home sales after a challenging start to the year. We look for sales to climb 3% y/y in April, which translates to about a 2% m/m increase in seasonally-adjusted terms. The market remains localized, with different dynamics in different regions. Vancouver and B.C. generally remain weak as prices have further to fall after the multi-year sprint higher. However, sales appear to have bottomed (or at least are close to) as they sit near prior cycle lows. There are signs of life in Calgary and Edmonton, though sales are improving off very weak levels. Toronto sales surged double-digits (from the prior month and a year ago) as strong population growth, employment gains and better weather supported activity. And, Montreal remained a strong spot, while Ottawa cooled after a solid run. Broadly, the ~50-bp drop in mortgage rates since the start of the year is providing some support to the market; though given debt levels, don't expect housing to rebound strongly. Average prices look to be flat from a year ago (the first non-negative print in 7 months), while the quality-adjusted MLS HPI is also expected to be flat, an improvement from back-to-back negative prints.

United States

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Retail Sales
Wednesday, 8:30 am

		Ex. Autos
Apr. (e)	**+0.3%**	**+0.6%**
Consensus	*+0.2%*	*+0.7%*
Mar.	+1.6%	+1.2%

After the biggest surge in 1½ years, retail sales likely downshifted to a 0.3% pace in April on reversing autos. Offering support, however, will be stronger chain-store sales and higher gas-station receipts, lifting the ex-autos figure 0.6%. "Core" sales (excluding autos, fuel, building materials and food services) should rise 0.4%. The report could indicate flat real personal spending in the month, though March's strong 0.7% bounce looks to anchor a 2½% annualized advance in Q2, up from 1.2% in Q1. Spending last quarter was curbed by several one-off factors, such as bad weather and the government shutdown, and looks to remain the economy's big driver amid sturdy income support. Elevated confidence is also spurring discretionary purchases, such as restaurant outings and hobbies.

Industrial Production

Wednesday, 9:15 am

	Industrial Production	Capacity Utilization
Apr. (e)	**-0.1%**	**78.6%**
Consensus	*unch*	*78.7%*
Mar.	-0.1%	78.8%

Industrial production likely sagged again in April as the return of more seasonal weather led to less heating use. Moreover, manufacturing has stalled in part due to Mexican border snarls, as work hours were flat and the ISM index fell to 2½-year lows (52.8) in April. Providing some thrust, however, will be record oil output, which averaged 12 million bpd in the month. Lower industrial output will trim the capacity utilization rate for a fifth straight month to a 10-month low of 78.6%, implying little pressure on producer prices.

Housing Starts

Thursday, 8:30 (with revisions)

Apr. (e)	**1.192 mln a.r. (+4.7%)**
Consensus	*1.226 mln a.r. (+7.6%)*
Mar.	1.139 mln a.r. (-0.3%)

Housing starts should rebound in April, given the bloated backlog of blueprints waiting to begin. In both February and March, building permits hovered 13% above starts, sitting in the top 3% among all monthly ratios. The culprit for the backlog was the weather, which, unfortunately, still looks to dampen April's advance. Precipitation in the month was again elevated (recall this past winter was the wettest in history), sitting in the top 10% among all Aprils going back almost a century. Meanwhile, housing demand is stabilizing after sliding last year due to eroding affordability and less attractive tax treatment of mortgage payments. However, since November, 30-year mortgage rates have dropped about 85 bps, which, amid still-sturdy job and income growth, is strengthening demand. Importantly, this will occur amid lean inventories of unsold homes, which bodes well for new construction.

		May 10 [1]	May 3	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	1.67	1.67	0	-1	3
	United States	2.42	2.42	0	-1	6
	Japan	-0.17	-0.17	0	3	-2
	Eurozone	-0.31	-0.31	0	0	0
	United Kingdom	0.81	0.81	-1	-2	-11
	Australia	1.65	1.54	11	-5	-44
2-Year Bonds	Canada	1.61	1.64	-2	-2	-25
	United States	2.24	2.33	-9	-15	-25
10-Year Bonds	Canada	1.71	1.76	-6	-7	-26
	United States	2.44	2.53	-8	-12	-24
	Japan	-0.05	-0.05	-1	0	-5
	Germany	-0.04	0.02	-7	-10	-28
	United Kingdom	1.12	1.22	-10	-9	-15
	Australia	1.73	1.79	-6	-15	-59
Risk Indicators	VIX	19.2	12.9	6.3 pts	7.2 pts	-6.2 pts
	TED Spread	11	14	-3	-7	-34
	Inv. Grade CDS Spread [2]	63	58	5	6	-25
	High Yield CDS Spread [2]	346	324	22	20	-104
					(percent change)	
Currencies	US¢/C$	74.59	74.52	0.1	-0.6	1.7
	C$/US$	1.341	1.342	—	—	—
	¥/US$	109.62	111.10	-1.3	-2.1	-0.1
	US$/€	1.1245	1.1198	0.4	-0.5	-1.9
	US$/£	1.303	1.317	-1.1	-0.3	2.2
	US¢/A$	70.03	70.18	-0.2	-2.4	-0.7
Commodities	CRB Futures Index	178.98	181.77	-1.5	-5.0	5.4
	Oil (generic contract)	61.53	61.94	-0.7	-3.7	35.5
	Natural Gas (generic contract)	2.59	2.57	1.0	-2.5	-11.8
	Gold (spot price)	1,286.77	1,279.15	0.6	-0.3	0.3
Equities	S&P/TSX Composite	16,200	16,494	-1.8	-1.7	13.1
	S&P 500	2,844	2,946	-3.5	-2.2	13.4
	Nasdaq	7,826	8,164	-4.1	-2.0	17.9
	Dow Jones Industrial	25,604	26,505	-3.4	-3.1	9.8
	Nikkei	21,345	22,259	-4.1	-2.4	6.6
	Frankfurt DAX	12,041	12,413	-3.0	0.3	14.0
	London FT100	7,209	7,381	-2.3	-3.1	7.1
	France CAC40	5,324	5,549	-4.0	-3.2	12.5
	S&P ASX 200	6,311	6,336	-0.4	1.0	11.8

[1] = as of 10:30 am   [2] = One day delay

Global Calendar
May 13 – May 17

BMO Capital Markets

Japan

Tuesday May 14

Bank Lending Ex-Trusts

Apr.		
Mar.	+2.5% y/y	

Wednesday May 15

Machine Tool Orders

Apr. P		
Mar.	-28.5% y/y	

Thursday May 16

Producer Price Index

Apr. (e)	**+0.2%**	**+1.1% y/y**
Mar.	+0.3%	+1.3% y/y

Department Store Sales

Apr.		
Mar.	+0.1% y/y	

Friday May 17

Tertiary Industry Index

Mar. (e)	**+0.1%**	
Feb.	-0.6%	

Euro Area

Tuesday May 14

EURO AREA

Industrial Production

Mar. (e)	**-0.3%**	**-0.8% y/y**
Feb.	-0.2%	-0.3% y/y

GERMANY

Consumer Price Index

Apr. F (e)	**+1.0%**	**+2.1% y/y**
Mar.	+0.5%	+1.4% y/y

ZEW Survey—Expectations

May (e)	**2.5**	
Apr.	3.1	

Wednesday May 15

EURO AREA

Real GDP

Q1 P (e)	**+0.4%**	**+1.2% y/y**
Q1 A	+0.4%	+1.2% y/y
Q4	+0.2%	+1.2% y/y

GERMANY

Real GDP

Q1 P (e)	**+0.4%**	**+0.7% y/y**
Q4	unch	+0.6% y/y

FRANCE

Consumer Price Index

Apr. F (e)	**+0.3%**	**+1.4% y/y**
Mar.	+0.9%	+1.3% y/y

ITALY

Industrial Orders

Mar.		
Feb.	-2.7%	-2.9% y/y

Thursday May 16

EURO AREA

Trade Surplus

Mar. (e)	**€19.0 bln**	
Feb.	€19.5 bln	

ITALY

Consumer Price Index

Apr. F (e)	**+0.6%**	**+1.2% y/y**
Mar.	+2.3%	+1.1% y/y

Friday May 17

EURO AREA

Consumer Price Index

Apr. F (e)	**+0.7%**	**+1.7% y/y**
Mar.	+1.0%	+1.4% y/y

Core CPI

Apr. F (e)	**+1.2% y/y**	
Mar.	+0.8% y/y	

U.K.

Tuesday May 14

Employment (3m/3m)

Mar. (e)	**+141,000**	
Feb.	+179,000	

Avg. Wkly Earnings Ex. Bonus (3 mma)

Mar. (e)	**+3.3% y/y**	
Feb.	+3.4% y/y	

Jobless Rate (3 mma)

Mar. (e)	**3.9%**	
Feb.	3.9%	

	Jobless Claims	**Claimant Count Rate**
Apr.		
Mar.	+28,300	3.0%

Other

Monday May 13

CHINA

Foreign Direct Investment [D]

Apr.		
Mar.	+8.0% y/y	

Tuesday May 14

AUSTRALIA

NAB Business Confidence

Apr.		
Mar.	0	

Wednesday May 15

CHINA

Industrial Production (YTD)

Apr. (e)	**+6.5% y/y**	
Mar.	+6.5% y/y	

Retail Sales (YTD)

Apr. (e)	**+8.4% y/y**	
Mar.	+8.3% y/y	

Fixed Asset Investment (YTD)

Apr. (e)	**+6.4% y/y**	
Mar.	+6.3% y/y	

AUSTRALIA

Westpac Consumer Confidence

May		
Apr.	+1.9%	

Thursday May 16

AUSTRALIA

Employment

Apr. (e)	**+15,000**	
Mar.	+25,700	

Jobless Rate

Apr. (e)	**5.0%**	
Mar.	5.0%	

MEXICO

Central Bank of Mexico Monetary Policy Meeting

Friday May 17

AUSTRALIA

General Election (May 18)

[D] = date approximate

Upcoming Policy Meetings | BoE: June 20, Aug. 1, Sep. 19 | ECB: June 6, July 25, Sep. 12

North American Calendar
May 13 – May 17

BMO Capital Markets

Canada

Monday May 13

Tuesday May 14

8:30 am — **New Motor Vehicle Sales[D]**
Mar. (e) — **-2.1% y/y**
Feb. — -3.3% y/y

10:30 am — 3-, 6- & 12-month bill auction $13.5 bln (new cash $1.6 bln)

Wednesday May 15

8:30 am — **Consumer Price Index**
Apr. (e) — **+0.4%** | **+2.0% y/y** | **(+0.1% sa)**
Mar. — +0.7% | +1.9% y/y

8:30 am — **Trimmed Mean Core CPI**
Apr.
Mar. — +2.1% y/y

8:30 am — **Weighted Median Core CPI**
Apr.
Mar. — +2.0% y/y

8:30 am — **Common Component Core CPI**
Apr.
Mar. — +1.8% y/y

9:00 am — **Existing Home Sales[D]** | **Average Prices**
Apr. (e) — **+3.0% y/y** | **unch y/y**
Mar. — -4.6% y/y | -1.8% y/y

9:00 am — **MLS Home Price Index[D]**
Apr. (e) — **unch y/y**
Mar. — -0.5% y/y

Noon — 3-year bond auction $2.4 bln

Thursday May 16

8:30 am — **Mfg. Sales** | **Mfg. New Orders**
Mar. (e) — **+1.7%** | **+1.0%**
Feb. — -0.2% | +1.5%

8:30 am — **Int'l Securities Transactions** — **Inflows** | **Outflows**
Mar.
Feb. — $12.0 bln | $5.3 bln

8:30 am — **ADP Employment Report**
Apr.
Mar. — +13,227

10:30 am — **BoC Financial System Review; Press Conference at 11:15 am**

Newfoundland and Labrador Election

30-year real return bond auction announcement

Friday May 17

United States

Monday May 13

Fed Speakers: Vice Chair Clarida, Boston's Rosengren (9:05 am)

11:30 am — 13- & 26-week bill auction $75 bln

Tuesday May 14

6:00 am — **NFIB Small Business Economic Trends Survey**
Apr. (e) — **102.0**
Consensus — *102.0*
Mar. — 101.8

8:30 am — **Import Prices**
Apr. (e) — **+0.7%** | **+0.2% y/y**
Consensus — *+0.8%* | *+0.3% y/y*
Mar. — +0.6% | unch y/y

Fed Speakers: New York's Williams (3:15 am), Kansas City's George (12:45 pm)

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

Wednesday May 15

7:00 am — **MBA Mortgage Apps**
May 10
May 3 — +2.7%

8:30 am — **Retail Sales** | **Ex. Autos**
Apr. (e) — **+0.3%** | **+0.6%**
Consensus — *+0.2%* | *+0.7%*
Mar. — +1.6% | +1.2%

8:30 am — **Empire State Mfg. Survey**
May (e) — **9.0**
Consensus — *9.0*
Apr. — 10.1

9:15 am — **Ind. Prod.** | **Cap. Utilization**
Apr. (e) — **-0.1%** | **78.6%**
Consensus — *unch* | *78.7%*
Mar. — -0.1% | 78.8%

10:00 am — **NAHB Housing Market Index**
May (e) — **64**
Consensus — *64*
Apr. — 63

10:00 am — **Business Inventories**
Mar. (e) — **unch**
Consensus — *unch*
Feb. — +0.3%

4:00 pm — **Net TIC Flows** — **Total** | **Long Term**
Mar.
Feb. — -$21.6 bln | +$51.9 bln

Fed Speakers: Gov. Quarles (9:30 am), Richmond's Barkin (noon)

Thursday May 16

8:30 am — **Initial Claims**
May 11 (e) — **220k (-8k)[C]**
May 4 — 228k (-2k)

8:30 am — **Continuing Claims**
May 4
Apr. 27 — 1,684k (+13k)

8:30 am — **Housing Starts**
Apr. (e) — **1.192 mln a.r. (+4.7%)**
Consensus — *1.226 mln a.r. (+7.6%)*
Mar. — 1.139 mln a.r. (-0.3%)

8:30 am — **Building Permits**
Apr. (e) — **1.290 mln a.r. (+1.7%)[C]**
Mar. — 1.228 mln a.r. (-0.2%)

8:30 am — **Philadelphia Fed Index**
May (e) — **9.0**
Apr. — 8.5

Factory Orders revisions

Fed Speaker: Minneapolis' Kashkari (12:05 pm)

11:30 am — 4- & 8-week bill auction

11:00 am — 13-, 26- & 52-week bill, 10[R]-year TIPS auction announcements

Friday May 17

10:00 am — **Quarterly Services Survey (Q1 A)**

10:00 am — **University of Michigan Consumer Sentiment**
May P (e) — **97.5**
Consensus — *97.4*
Apr. — 97.2

10:00 am — **Leading Indicator**
Apr. (e) — **+0.3%**
Consensus — *+0.2%*
Mar. — +0.4%

Fed Speakers: New York's Williams (11:15 am, 2:00 pm), Vice Chair Clarida (1:40 pm)

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

Upcoming Policy Meetings | Bank of Canada: May 29, July 10, Sep. 4 | FOMC: June 18-19, July 30-31, Sep. 17-18

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