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BMO CAPITAL MARKETS ECONOMICS

Focus

A weekly financial digest

Douglas Porter, CFA, Chief Economist, BMO Financial Group

May 17, 2019

Feature Article
Page 8

Running the Economy Hot for the Less-schooled Lot

China Strikes with Retaliatory Tariffs

...And Talks Tough on Trade

China's Spat with Canada also Flares

USMCA Partners Reach Deal to Lift Metals Tariffs

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Goodbye Yellow Brick (Belt and) Road

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A further escalation of the U.S./China trade hostilities was the dominant item this week and has leapt back to the top of the list of single-biggest threats to the global economic outlook. Financial markets are clearly struggling with how to play this new, dangerous turn; uncertain both of the odds of an eventual agreement, and just how deep the damage will be in the absence of a deal. Rapidly ping-ponging between fear and relief over the past two weeks, markets swung back into neutral mode by week's end on China's lack of interest in further talks until the U.S. shows "substantial sincerity". In honour of the upcoming biopic "Rocket Man", we turn to Sir Elton John for some words of wisdom:

Don't Go Breakin' My Deal: We have long been sceptical that the U.S./China tussle was headed anywhere positive, and had been pleasantly surprised/amazed that the talks seemed to be going reasonably well—until two weeks ago. At this point, we would counsel caution, especially given the fact that there is **no clear route for both sides to de-escalate in a face-saving manner** (see Michael's Thought for details). We would simply repeat, yet again, that it took 14 months of extremely hard bargaining to pound out the USMCA, and that was between three friendly nations, with a perfectly good existing deal in place. The U.S./China talks are, frankly, between two adversaries, with no existing deal, and where one side is asking the other to fundamentally change the way it conducts business. That can't happen overnight, and the only surprise was how smoothly things seemed to be progressing… until they weren't.

I'm Still Standing: Despite the mounting risks around a deepening trade war, equities have held up reasonably well. Prior to Friday, and the latest volley from China, the S&P 500 was down little more than 2% from its all-time high—hit less than three weeks ago. (The TSX was off just 1.4% from its record.) Some of that resilience reflected hope springing eternal that a deal can ultimately be reached, some on the decision by the Trump Administration to delay auto tariffs for six months, and some on hopes for stimulus from China (and possibly, the Fed itself).

Someone Saved My Loon Tonight: The renewed trade war has not been kind to currencies. With China letting the yuan slide nearly 3% (to 6.91/US$) in the past two weeks, the U.S. dollar has risen against almost all major currencies (save the super-safe yen and Swiss franc). Emerging market currencies have been caught in the crossfire, with Brazil's real notably weak (down 4% in May). The Australian dollar has also been walloped, dropping below 69 cents(US), with tomorrow's election an added source of uncertainty. The Canadian dollar has softened to a three-week low; but, at just above 74 cents (or $1.345/US$) it has actually held up better than most, with some support from firm oil prices and recent robust domestic economic data. As well, the currency got a boost when a deal to end the steel and aluminum tariffs was reached on Friday, and that is a necessary step on the long road to getting the USMCA approved. (Okay, the title to this section is a stretch, but I had to reference that great song—which may be the only pop song ever to mention *"stocks and bonds"*.)

Don't Let the Yield Go Down On Me: While most markets are struggling with the trade war, bonds are absolutely thriving. Yields have plunged anew since hostilities renewed, with 5-year Treasuries leading at down 17 bps in just two weeks. This has been like pushing on a rock that was already rolling downhill on sagging core inflation trends, taking almost all Treasury yields to their lowest ebb in a year. And, everything from the 2-year space out to 10s is now at, or below, the Fed's mid-point target rate (i.e., inverted curve, again). The rally in Canadian bonds has been a little less forceful, again partly on a wave of decent domestic data, but also on the simple fact that GoCs were already scraping along at incredibly low levels to begin with. Ten-years have still managed to drop nearly 10 bps in the past two weeks; and, at less than 1.7%, they are tucked neatly below core inflation.

Saturday Night's Alright For Fighting: In fact, no night is good for fighting on this front. But with no official talks currently planned—and even that's a point of dispute at this stage—the next big event looks to be the G20 summit in Japan, ending on Saturday June 29.

Rocket Man: While the U.S./China tussle dominated headlines this week, not to be overlooked are many other swirling geopolitical risks. North Korea has been making mischief again, while the U.S. and Iran have been openly hurling threats at each other. President Trump suggested that he *"hoped"* the two wouldn't go to war, which passes for good news these days. The recent bellicosity, as well as attacks on Saudi tankers and oil facilities, has kept oil prices fired up even in the face of fading global growth. WTI rose almost 3% this week to more than $63/barrel. Notably, gold prices have benefitted little on net from the mounting geopolitical tensions, still holding close to $1280 on a firm U.S. dollar and mild global inflation trends.

Tiny Dancer: As it is so wont to do, the Canadian economy is doing its own thing amid the global turmoil. Almost since the day that the Bank of Canada's MPR came out three weeks ago with a surprisingly downbeat economic forecast, growth has suddenly been on wheels. To wit, April alone saw the biggest monthly jobs gain on record (largely confirmed by this week's ADP release), a snap-back in housing starts, and clear signs that home sales are recovering (outside of British Columbia). We also know that inflation is now remarkably close to "home", with headline CPI bang on the 2% target, and core just one tick below. And, of course, oil prices have fully rebounded from last year's nastiness, especially so for Canadian prices (WCS is back above $50), while the loonie is lagging. Under normal circumstances, this backdrop would augur for eventual rate hikes by the Bank… but these are not normal times. Instead, markets are still priced for a reasonable chance of a rate cut over the next year (which could be interpreted as a small chance of something going seriously awry).

Stephen and the Frets: As if to reinforce the market's view, the Bank's latest Financial System Review—now produced annually—opined that the risk of a severe recession is *"elevated and rising"*, citing *"uncertainty and tensions around global trade arrangements"*. The Bank also raised climate change as a potential risk to the financial system for the first time, albeit with few details. Yet, despite the warnings, the Bank's core view is that a recession is not on the horizon. In a recent interview with Maclean's magazine, Mr. Poloz concluded that the Bank is expecting smooth sailing until the end of his mandate in June 2020. Oh, and that a fortune cookie told him that he is "independent politically", and he keeps that message in his wallet. (All true.) DoPoPo

Tit for Tat and All That

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China retaliated on Monday for last week's increase in U.S. tariffs on $200 billion of Chinese goods. The U.S. tariff rate rose to 25% from 10%, and China reacted by raising its tariff rates on $60 billion of U.S. goods to a range of 5%-to-25% from 5%-to-10%. Then, on Wednesday, the U.S. Bureau of Industry and Security (BIS) announced that Huawei Technologies and its affiliates would be added to its "Entity List". This means that the sale or transfer of American technology to Huawei would require a BIS-issued license that could be denied if the transaction is deemed harmful to U.S. national security or foreign policy interests.

Then, to strike where this escalating trade war is arguably hitting America the hardest—the agriculture sector—it was announced on Thursday that Chinese buyers cancelled orders for 3,247 metric tonnes of U.S. pork. China and Hong Kong are the second largest market for U.S. pork exports. Finally, on Friday, China ramped up its rhetoric, with the state-run media stating that, if Washington *"keeps using petty tricks to destroy the atmosphere for talks"*, then there's no point in talking further.

Since President Trump first tweeted about reactivating plans for the 25% tariff rate on May 5th, after learning that Beijing was demanding major rewrites in already agreed to (but still tentative) trade deal text, the U.S./China trade war has steadily escalated. This worrisome state stands in stark contrast to where things were a couple weeks ago, when the stock market was hitting new record highs on the buzz about a soon-to-be-reached trade deal.

We were always sceptical about an expeditious U.S./China trade deal, given that formal talks only began in January and given the experience in renegotiating the NAFTA. Recall that it took 14 months to come up with the USMCA (CUSMA in Canada, T-MEC in Mexico). The three economic partners began with an existing deal on the table (NAFTA) and most of what America wanted in the new deal the three had already agreed to as part of the Trans Pacific Partnership. There were, of course, major "new" new parts (e.g., increased North American and minimum wage rate content rules for the automotive industry) that chewed up big chunks of negotiating time, but the bottom line is that it took well over a year to conclude. On the other hand, China is America's economic adversary not its "amigo", there is no existing bilateral trade deal to build upon so the parties are starting from scratch, and the U.S. regularly accuses China of trading unfairly.

However, the Administration appears to want to get a win here, heading into the 2020 elections. The USMCA is bogged down in Congress, particularly in the House as Democrats demand some changes and/or greater scrutiny over Mexican compliance. Interestingly, this week, some "un-bogging" seems to be happening with the announced lifting of steel and aluminum tariffs off Canada and Mexico—tariffs that stood in the way of both Canadian and Mexican ratification let alone U.S. Senate approval.

Importantly for the Administration, any U.S./China trade deal does not have to be ratified by Congress because trade talks are being conducted under the auspices of Section 301 of the Trade Act of 1974, which gives the President complete control. There even appears to be an effort to clear the deck to focus solely on a China deal, in pushing back tariffs on imported vehicles and parts by six months, and keeping potential tariffs on the remaining $272 billion (Census basis) of Chinese imported goods hanging like a guillotine over negotiations.

We judge a deal will eventually get done in time for 2020 campaigning but we doubt it will be as comprehensive as promised at the outset of talks. In the meantime, current tariffs and other trade restrictions will probably remain in place, if not escalate further. We reckon once a deal is crafted, tariffs are unlikely to be rolled back aggressively, at first reflecting U.S. concerns over Chinese compliance. This means that these reciprocal tariffs and other trade restrictions will drag on U.S., Chinese and global economic growth well past the end of this year. MJG

U.S. Economy: Don't Hit the Panic Button

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Investors are getting antsy again about a slowing U.S. economy. It didn't help that **two of the three key releases this week backfired**, with both retail sales and industrial production falling in April. The latter setback, especially the clear downtrend in manufacturing this year, could partly reflect the need to unwind an inventory bulge which was partly caused by temporary factors (bad weather, federal shutdown, equity rout, delayed tax refunds) that slowed consumer spending at the turn of the year. Harder to explain, however, is the misfire in retail sales, despite solid consumer fundamentals. The "control" measure that feeds into the BEA's estimate of personal spending (retail sales excluding cars, gas, building materials and food services) was flat in the month (or to get really picky, down 0.03%). The silver lining, however, is that this measure is **still up strongly since the start of the year**, and the payback from March's outsized gain (1.1%, revised up a tenth) was both limited and well within historic norms. Going back to 1992, the average change following a 1% increase or more is +0.1% (followed by a 0.4% advance the subsequent month).

Virtually all other indicators this week actually surprised to the upside. The NFIB small business index rose for a third straight month, initial jobless claims fell sharply in the survey period for nonfarm payrolls (flagging another solid jobs report), and the Philadelphia Fed manufacturing index popped to multi-month highs (foreshadowing a likely bounce in nationwide output in May). Consumers have never been this optimistic in 15 years finds the University of Michigan survey. Moreover, housing markets are clearly in a rebuilding phase, with starts jumping 5.7% to three-month peaks in April and the NAHB homebuilder index (a good leading indicator of construction) forging seven-month highs in May.

The upshot is that, sure, **the economy is slowing in response to waning stimulus, but it's far from spinning in reverse**. We have not lowered our already-light 1.5% call for Q2 GDP growth, with the downshift from 3.2% in Q1 reflecting some payback from outsized moves in inventories and imports, offset partly by a likely pickup in domestic spending. Real GDP appears to be cruising somewhere between long-run potential (1.9% thinks the Fed) and post-recession norms (2.3%). Barring a nastier turn in the trade war or equity markets, we still expect 2.1% growth on a Q4/Q4 basis this year and 2.5% on an annual basis. Sal

Blue Crush

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The provincial political map is now set ahead of the federal election later this year, and it's hard not to notice the blue wave sweeping across most of the country. For Conservative observers, it has been more like set after set of glassy delight (i.e., very, very good in surfing parlance) given the multiple wins for that party. Consider that at this time in 2015, just ahead of the federal election that saw the Liberals sweep to power, there was just one conservative government (Saskatchewan) in power on the provincial landscape. Since then, and most decisively within the past year, each of Alberta, Manitoba, Ontario, Quebec, New Brunswick and PEI have shifted from Liberal or NDP, to Conservative, or conservative. (B.C. was the notable exception that proved the rule, swinging to the NDP, with Green support.) Last night's Newfoundland & Labrador vote just missed a clean sweep, but even there the governing Liberals were reduced to minority status, and coalition talk has already begun. As it stands now, fully 7 of 10 provinces are coloured with conservative blue.

The obvious question is: **Will this have federal election implications?** It's hard to ignore, and the latest polls suggest that change is indeed in the air, with the Conservatives polling ahead of the Liberals since March. And, current seat projections peg roughly 70% odds of the Conservatives forming a government. But, it's very early days still, and historically (with 2015 an obvious exception), there's not a lot to suggest that provincial voting habits translate to the federal level with any consistency (some might argue just the opposite).

As for implications, Conservative leader Andrew Scheer spoke on economic policy this week. While he delivered only broad strokes at this point, the main pledges included a more pro-energy and pipeline stance, scrapping of the carbon tax, maintaining the Canada Child Benefit and more (but not aggressive) fiscal restraint that would put a balanced budget on the fiscal timeline. Provincially, it's still early in the proceedings with some new right-leaning governments not even one budget into their mandate yet, but we're already seeing signs that priorities are shifting. Alberta is pledging aggressive corporate tax relief; Manitoba will cut the sales tax in July; Ontario is clamping down on program spending with visions of more aggressive tax relief ahead; and Quebec has continued to reduce the tax burden and pay down debt. The big message here is that, after a prolonged period where government program spending was flowing relatively freely at the provincial level (19% of GDP last fiscal year, up from 18% in 2014 and less than 16% at the start of the 2000s) and tax burdens were drifting up, we're seeing early signs that policy is moving back in the other direction. Whether or not voters want to double down on such change at the federal level remains to be seen… Rob K.

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	Good News	Bad News
Canada ▪ Soybean exports to China nosedive amid political spat ▪ BoC Gov. Poloz would *"frown upon"* any easing of B-20 mortgage rules ▪ BoC sees fragile corporate debt as an emerging vulnerability to the financial system	**Consumer Prices** +2.0% y/y (Apr.) **Manufacturing Sales Volumes** +1.6% (Mar.) **Manufacturing New Orders** +1.5% (Mar.) **Existing Home Sales** +3.6% (Apr.) **ADP Employment** +61,729 (Apr.)	**MLS Home Prices** -0.3% y/y (Apr.) **New Motor Vehicle Sales** -2.0% y/y (Mar.) **Global Investors** sold a net $1.5 bln in Canadian securities (Mar.)
United States ▪ Trade talks with China in limbo ▪ Washington strikes deal with Canada and Mexico to lift metals tariffs ▪ Decision on auto tariffs pushed back for 6 months	**Housing Starts** +5.7% to 1.235 mln a.r. (Apr.) **Building Permits** +0.6% to 1.296 mln a.r. (Apr.) **Business Inventories** unch (Mar.) **Import Prices** +0.2% (Apr.) **Leading Indicator** +0.2% (Apr.) **U of M Consumer Sentiment** +5.2 pts to 102.4 (May P)—15-yr high **Philly Fed Index** +0.5 pts to an ISM-adjusted 54.6 (May) **NAHB Housing Market Index** +3 pts to 66 (May) **NFIB Small Business Optimism** +1.7 pts to 103.5 (Apr.) **Initial Claims** -16k to 212k (May 11 week)	**Retail Sales** -0.2% (Apr.) **Industrial Production** -0.5% (Apr.)—and **Capacity Utilization** -0.6 ppts to 77.9% **Empire State Manufacturing Survey** -1.6 pts to an ISM-adjusted 52.7 (May) **Mortgage Delinquencies** +0.36 ppts to 4.42% (Q1) **Global investors** sold a net $30.3 bln in U.S. securities (Mar.)
Japan ▪ Restrictions on U.S. beef imports lifted after 15 years ▪ Weakening economy could delay sales tax hike yet again	**Bank Lending Ex-Trusts** +2.5% y/y (Apr.) **Producer Prices** +1.2% y/y (Apr.)	**Machine Tool Orders** -33.4% y/y (Apr. P) **Tertiary Industry Index** -0.4% (Mar.)
Europe ▪ EU Parliamentary elections on deck next week ▪ PM May set to bring Brexit deal for early-June parliamentary vote… ▪ …but regardless of outcome, agrees to set a timeline for resignation	**Euro Area—Core CPI** revised up to +1.3% y/y (Apr.) **Germany—Real GDP** +0.4% q/q (Q1 P) **France—Consumer Prices** revised up to +1.5% y/y (Apr.) **Italy—Industrial Orders** +2.2% (Mar.) **U.K.—Jobless Rate** -0.1 ppts to 3.8% (3 mths to Mar.)—45-yr low **U.K.—Average Weekly Earnings (ex. Bonus)** +3.3% y/y (3 mths to Mar.)	**Euro Area—Industrial Production** -0.3% (Mar.) **Euro Area—Trade Surplus** narrowed to €17.9 bln (Mar.) **Germany—ZEW Survey** -5.2 pts to -2.1 (May) **U.K.—Employment** +99,000 (3 mths to Mar.)—below expected
Other ▪ China signals no interest in resuming trade talks with the U.S. and announces retaliatory tariffs starting June 1 ▪ Central Bank of Mexico on hold	**Australia—Employment** +28,400 (Apr.)—but all part-time **Australia—Westpac Consumer Confidence** +0.6% (May) **Australia—NAB Business Confidence** +1 pt to 0 (Apr.)	**China—Industrial Production** slowed to +6.2% y/y (Jan.-to-Apr.) **China—Retail Sales** eased to +8.0% y/y (Jan.-to-Apr.) **China—Fixed Asset Investment** slowed to +6.1% y/y (Jan.-to-Apr.) **China—Foreign Direct Investment** slowed to +6.3% y/y (Apr.) **Australia—Jobless Rate** +0.1 ppts to 5.2% (Apr.)

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

Running the Economy Hot for the Less-schooled Lot

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"I strongly believe policies that bring prime-age workers into productive employment, particularly those who may have been left behind because of low skills or educational attainment, could bring great benefits both to those workers and to our economy."

—**Fed Chair Jerome Powell**, speech on February 28, 2019

Apart from a cooler economy and lower inflation, one reason central bankers are treading lightly on the tightening path is that running the economy flat out could improve the job prospects of less educated persons and expand the economy's capacity to grow. With advanced automation threatening to displace more low-skilled work while restraining inflation, this approach seems timely. In this note, we assess **whether persons at the lower end of the education ladder are finally thriving in this long-running expansion**.

By our estimates, the U.S. labour market has been running at full employment for two years.[1] In response, **persons lacking an advanced education have rarely faced better job markets**. After falling in the recession, the employment rate for those aged 25 and older with less than a high school diploma is at record highs near 44% (*Chart 1*). That's despite no net increase in jobs (*Chart 2*), as this group has shrunk due to rising college enrolment in past decades.[2,3] The jobs rate for those graduating from high school has also turned higher (56%) amid sturdy gains in recent years. By contrast, the rate for post-secondary graduates has fallen steadily to 72% from above 76% before the recession, though it remains high with job growth averaging more than 3% in the past eight years.

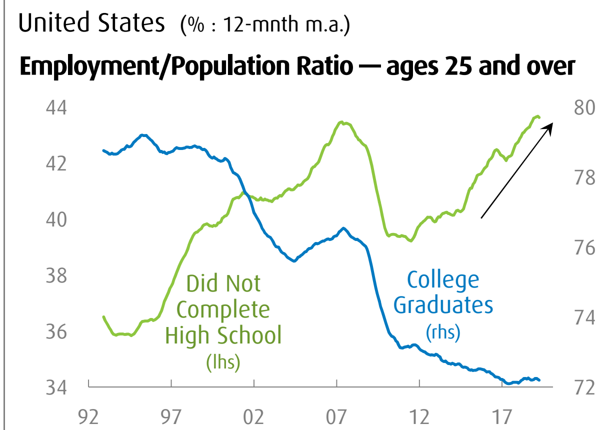
As in past cycles, **a shortage of workers is drawing the least schooled back to the workforce**. The participation rate of persons lacking a high school diploma turned up in 2014, while that of college grads merely stopped falling (*Chart 3*). A steady decline in discouraged workers (those wanting a job but not actively seeking one) has led to more participation among prime-age workers (between 25 and 54 years of age), providing a wellspring for companies trying to fill record openings.

[1] Our summary measure of 16 labour market indicators surpassed historical benchmarks of long-run sustainable employment in March 2017.

[2] After trending higher since at least the mid-1950s, college enrollment (as a share of total school enrollment as well as the population age 16 and older) peaked in 2010, but has subsequently declined.

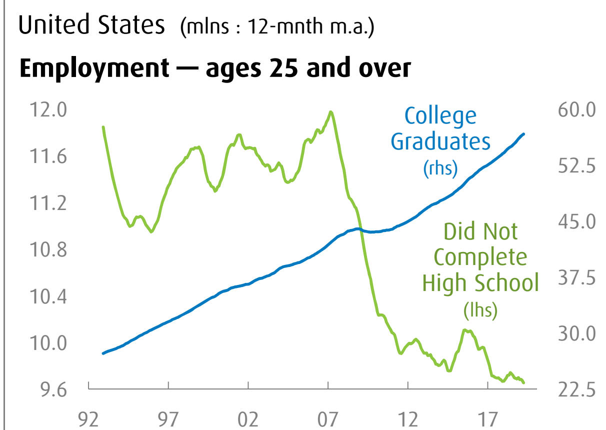
[3] The share of Americans aged 25 to 34 years with a post-secondary credential rose to 48% in 2017 from 40% in 2007 and 36% in 1997. It is above the OECD mean (44%), but well behind Canada (61%) and leader South Korea (70%). https://data.oecd.org/eduatt/population-with-tertiary-education.htm

Chart 1
No Degree, No Problem



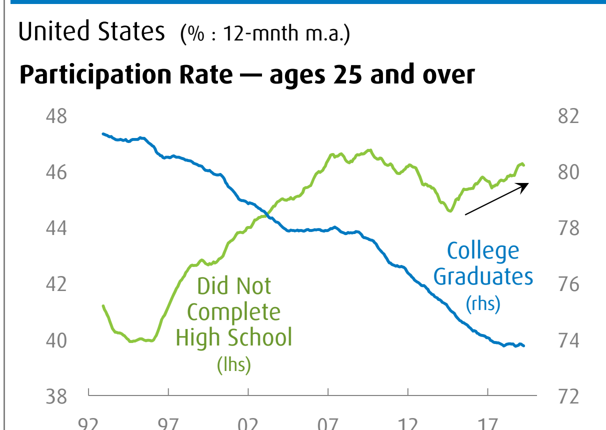
Sources: BMO Economics, Haver Analytics

Chart 2
Smarter Workforce



Sources: BMO Economics, Haver Analytics

Chart 3
Class Participation



Sources: BMO Economics, Haver Analytics

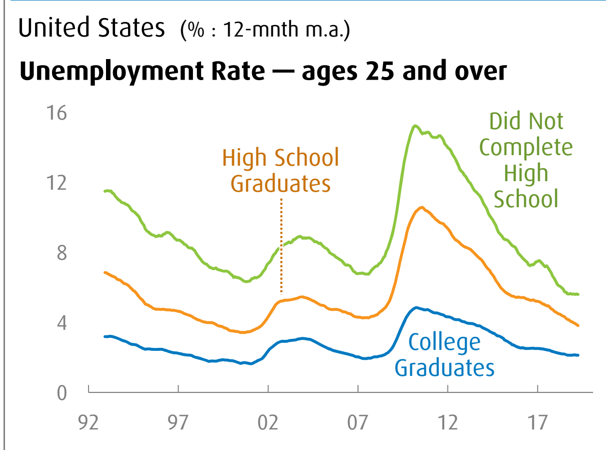
The **least schooled are enjoying the best job prospects in a quarter century**. After surging to almost 2 million in the recession, the number of unemployed who have not completed high school fell to almost half a million, the fewest since at least 1992. This sliced their jobless rate to 5.4% in April from nearly 16% in 2010 (*Chart 4*). Though still well above the 2.1% rate for college grads, the **gap in jobless rates between the two groups has never been smaller**.

Worker shortages are lifting wages of the least schooled. Median wage growth of persons with at most a high school diploma has approached that of college grads for the first time since before the recession (*Chart 5*). This is partly due to higher minimum wages in many states and cities. However, it also reflects faster wage gains in sectors that tend to hire persons with less formal education, such as manufacturing, transportation, construction and mining. As well, people age 25 and over with at most a high school diploma (who held 32% of jobs in 2016-17) dominate skilled trades such as engineering technicians, maintenance workers, auto mechanics, nursing aids and home healthcare workers. While wages continue to rise faster for high-skill jobs (3.7% y/y in April) than low-skill work (3.2%), pay for mid-skill positions, which includes many people with less formal education, is rising nearly as fast (3.5%).[4]

Of course, just because growth in wages for workers with different educations is narrowing doesn't mean the vast wedge in earnings is. The median income of households headed by someone with less than a Grade-9 education was still less than $27,000 (in 2017, the last year of available data) compared with $100,000 for households headed by someone with a bachelor's degree or higher. However, **as the labour market began to tighten in 2016 and 2017, incomes rose somewhat faster for persons without a high school diploma** and it will be noteworthy if this trend continued last year. Still, this group stands a one-in-four chance of poverty versus one-in-fifteen for college-degree holders.

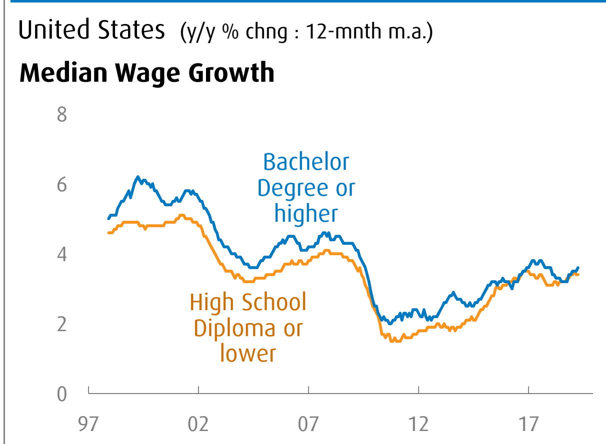
Bottom Line: While the Fed is not mandated to reduce income disparity, it does strive for full employment. And, the data suggest the hot job market has paid off for less-educated persons, many of whom are seeing pay increases despite the threat of advanced automation. Companies desperate to fill positions are reducing educational requirements. Of course, running the economy too-hot could backfire if it fans inflation and triggers a downturn. As well, it could discourage some people from pursuing higher education, leaving them vulnerable to the next downturn. That's why policies that support skills training are smart regardless of how well the economy is doing.

Chart 4
(All) Workers Wanted



Sources: BMO Economics, Haver Analytics

Chart 5
Earning More



Sources: BMO Economics, Haver Analytics

Canada

The situation is less clear in the Canadian labour market. It has been running near full employment since early 2018 when the jobless rate slipped below 6%, though milder wage gains and fewer job openings (per unemployed) than in the U.S. suggest the market is at lower risk of overheating. In contrast to the U.S., rates of employment and participation for persons with no more than a high school diploma have fallen in recent years, while the jobless rate for persons with a high school diploma has only tracked the aggregate lower since 2014 rather than outperformed.

https://www150.statcan.gc.ca/t1/tbl1/en/tv.action?pid=1410002001

4 High-skill jobs include managers, professionals and technicians; mid-skill jobs include office and administration, operators, production and sales; low-skill jobs include food preparation and serving, cleaning, personal care services and protective services.

Economic Forecast Summary for May 17, 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	2.2 ↑	2.0 ↑	2.3 ↑	2.3	2.0 ↑	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 ($blns : a.r.)	-69.0	-63.4	-40.4	-61.9	-72.9	-61.7	-61.8	-63.6	-58.7	-65.0	-61.0
Interest Rates	(average for the quarter : %)										
Overnight Rate	1.25	1.25	1.50	1.75	1.75	1.75	1.75	1.75	1.44	1.75	1.75
3-month Treasury Bill	1.14	1.21	1.47	1.66	1.65	1.70 ↑	1.70 ↑	1.70 ↑	1.37	1.65	1.70 ↑
10-year Bond	2.24	2.28	2.28	2.32	1.86	1.70	1.75	1.85	2.28	1.80	1.75
Canada-U.S. Interest Rate Spreads	(average for the quarter : bps)										
90-day	-44	-66	-61	-70	-79	-75 ↑	-74 ↑	-74 ↑	-60	-76 ↑	-72 ↑
10-year	-52	-64	-65	-72	-80	-77 ↑	-75 ↑	-74 ↑	-63	-76 ↑	-73
UNITED STATES											
Real GDP (q/q % chng : a.r.)	2.2	4.2	3.4	2.2	3.2	1.5	2.0	1.9	2.9	2.5	1.7
Consumer Price Index (y/y % chng)	2.2	2.7	2.6	2.2	1.6	2.0	2.1	2.3	2.4	2.0	2.2
Unemployment Rate (percent)	4.1	3.9	3.8	3.8	3.9	3.6	3.6	3.5	3.9	3.6	3.6
Housing Starts (mlns : a.r.)	1.32	1.26	1.23	1.19	1.20	1.23 ↑	1.24	1.22	1.25	1.22	1.23
Current Account Balance ($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	2.40 ↓	2.40 ↓	2.40 ↓	1.97	2.45	2.40
10-year Note	2.76	2.92	2.93	3.03	2.65	2.45 ↓	2.50 ↓	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	110 ↓	109 ↓	108 ↓	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	1.30 ↓	1.31	1.34	1.30 ↓	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

Retail Sales
Wednesday, 8:30 am

		Ex. Autos
Mar. (e)	**+0.9%**	**+0.9%**
Consensus	*+1.2%*	*+1.0%*
Feb.	+0.8%	+0.6%

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The surge in gasoline prices will likely be the big story in March retail sales. Pump prices rose over 10% in seasonally-adjusted terms, which will lift the headline by about 0.6 ppts. However, all that extra money spent on fuelling up tends to mean less spending elsewhere. Indeed, we're looking for core spending (ex. autos & gas) to be only slightly higher, despite an anticipated 0.9% headline increase. Auto sales look to be a positive as they were reported higher for a second-straight month after struggling through most of 2018. Ex- auto sales are expected to climb 0.9%, with gasoline the key contributor. Despite the expected big headline, volumes will likely be on the soft side as goods prices were up 0.8% in March. Even so, March GDP looks to bounce back from February's decline.

United States

Existing Home Sales
Tuesday, 10:00 am

Apr. (e)	**5.40 mln a.r.**	**(+3.6%)**
Consensus	*5.34 mln a.r.*	*(+2.6%)*
Mar.	5.21 mln a.r.	(-4.9%)

New Home Sales
Thursday, 10:00 am

Apr. (e)	**692,000 a.r.**	**(unch)**
Consensus	*677,000 a.r.*	*(-2.2%)*
Mar.	692,000 a.r.	(+4.5%)

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Total home sales continue to rebound after a weak 2018 and rough start to 2019. Last year's narrative was all about deteriorating affordability topped with tax changes that reduced the tax-attractiveness of mortgage interest payments. After 30-year mortgage interest rates peaked at 7¾-year highs in November and started falling, the sales rebound was initially checked by the stock market scare, wicked weather and government shutdown. Total home sales hit a cycle high in November 2017 (at 6.35 mln), and reached their nadir in January 2018 (down nearly 13% over 14 months to 5.56 mln). Since then, total sales are up 6.3% to 5.90 mln and look to build to around 6.1 mln in April, as the number of mortgage applications for purchases averaged their highest level since October 2009.

On the existing homes side, we look for a 3.6% increase to 5.40 mln in April, with pending home sales up comparably in the month (3.8%). In the new homes segment (less than 12% of the total), homebuilders' perceptions of current sales activity continued to improve in April and May, with the Housing Market Index's component now sitting at 72. This is the highest level since things started heading south after last October. However, new home sales data are notoriously volatile; and, after posting a 23% cumulative increase in Q1, one can't help think that some payback could be in store despite sturdy housing demand fundamentals (job growth, mortgage rates down more than 85 bps). We're pencilling in a flat figure for April.

FOMC Minutes from April 30-May 1 meeting
Wednesday, 2:00 pm

Every-meeting pressers have stolen some of the thunder from the FOMC Minutes, particularly for those confabs without fresh economic projections. We'll be searching for clues on the Committee's willingness to wait out the current "*temporary*" bout of core disinflation. And also, on how sensitive the Committee could be to further deterioration on the "*global economic and financial developments*" front. At the time of the meeting (April 30-May 1), the stock market had set a record high with a widespread belief that a U.S./China trade deal was close at hand. However, as the month unfolded, hopes were dashed by tit-for-tat tariffs. In turn, stocks sold off and the yield curve (10 yr-3 mo) inverted again. Finally, further stealing the thunder, Fed Chair Powell will be a keynote speaker at the Atlanta Fed's financial markets conference on Monday.

Durable Goods Orders

Friday, 8:30 am

		Ex. Transport
Apr. (e)	**-1.3%**	**+0.2%**
Consensus	*-2.0%*	*+0.2%*
Mar.	+2.8%	+0.2%

	Nondef. Capital Goods ex. Air
Apr. (e)	**unch**
Consensus	*-0.3%*
Mar.	+1.0%

Durable goods orders will probably drop 1.3% in April, owing to a pullback in Boeing's bookings (to 4 from 44 in March). Aircraft orders are volatile and April is among the most seasonally-weak months, but Boeing's new orders are likely also being dampened by reduced demand for its still-grounded 737 MAX model. Elsewhere, unchanged core capital goods orders should consolidate a recent positive trend as labour shortages continue to stir investment intentions.

Elections

Australia General Elections

Saturday

India General Election Results

Thursday

European Parliamentary Elections

Thursday

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Although **Australia's general elections** are on Saturday, markets may not know the results right away. It took over a week to hold recounts in key seats during the 2016 election. Although there are 54 parties running, the latest polls have Bill Shorten's Labor Party just ahead of the current centre-right Liberal-National Coalition government, led by PM Scott Morrison. Both parties are addressing the slowing economy with tax reform: Labor supports higher taxes for the *"top end of town"*, while the Coalition proposes corporate and personal tax cuts. However, environmental concerns are the top priority of voters, and Labor is vowing to cut carbon emissions, which is likely why they're ahead in the polls. BMO's Global Head of FX Strategy, Greg Anderson, assigns a 30% probability to a Labor-led minority, and expects the AUD to rally, as the minority status would keep the party in check.

The results of **India's** month-long general election will come out on Thursday, which will have a significant bearing on the direction of policymaking, particularly structural economic reforms. Another term for Prime Minister Narendra Modi's pro-business National Democratic Alliance is viewed to be the more positive market outcome as he is expected to continue pushing for business/growth-friendly reforms to enhance the country's economic competitiveness. In contrast, there are concerns that a return of a government led by the Indian National Congress could lead to the introduction of more populist welfare policies and curtail the prospect of business-friendly reforms being implemented.

The **European Parliamentary elections** will start on Thursday and run over the weekend, with results expected Sunday night for the 751 seats. The U.K. will be participating as well, with the Brexit Party poised to win the majority of the country's seats. The centre-right EPP (currently holds 217 seats) and the centre-left S&D (now at 186) are widely expected to lose their combined majority to anti-EU populist parties such as Matteo Salvini's European Alliance of Peoples and Nations. Their presence in Parliament and growing influence will certainly disrupt the legislature's decision-making process, such as approving laws and determining the EU's budget. Note that the top four jobs are also up for grabs: head of the European Commission, the European Council, the European Parliament and the ECB.

		May 17 [1]	May 10	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	1.68	-1	0	3
	United States	2.38	2.42	-4	-4	2
	Japan	-0.16	-0.17	1	3	0
	Eurozone	-0.31	-0.31	0	0	0
	United Kingdom	0.80	0.81	0	-2	-11
	Australia	1.55	1.65	-10	-14	-54
2-Year Bonds	Canada	1.60	1.64	-4	-2	-26
	United States	2.17	2.27	-10	-21	-32
10-Year Bonds	Canada	1.68	1.73	-5	-8	-28
	United States	2.37	2.47	-10	-19	-31
	Japan	-0.06	-0.06	0	-2	-5
	Germany	-0.10	-0.05	-6	-13	-34
	United Kingdom	1.02	1.13	-11	-18	-25
	Australia	1.64	1.73	-9	-31	-68
Risk Indicators	VIX	15.9	16.0	-0.1 pts	3.9 pts	-9.5 pts
	TED Spread	15	11	4	-2	-31
	Inv. Grade CDS Spread [2]	62	63	-1	5	-26
	High Yield CDS Spread [2]	347	347	0	22	-103
					(percent change)	
Currencies	US¢/C$	74.19	74.53	-0.5	-0.6	1.2
	C$/US$	1.348	1.342	—	—	—
	¥/US$	109.85	109.95	-0.1	-1.8	0.1
	US$/€	1.1162	1.1233	-0.6	-0.7	-2.7
	US$/£	1.274	1.300	-2.0	-1.9	-0.1
	US¢/A$	68.77	70.02	-1.8	-3.8	-2.4
Commodities	CRB Futures Index	181.53	178.95	1.4	-3.0	6.9
	Oil (generic contract)	63.06	61.66	2.3	-1.5	38.9
	Natural Gas (generic contract)	2.63	2.62	0.5	5.7	-10.5
	Gold (spot price)	1,278.93	1,286.05	-0.6	0.3	-0.3
Equities	S&P/TSX Composite	16,402	16,298	0.6	-1.3	14.5
	S&P 500	2,859	2,881	-0.8	-1.6	14.0
	Nasdaq	7,868	7,917	-0.6	-1.6	18.6
	Dow Jones Industrial	25,820	25,942	-0.5	-2.8	10.7
	Nikkei	21,250	21,345	-0.4	-4.3	6.2
	Frankfurt DAX	12,183	12,060	1.0	-0.3	15.4
	London FT100	7,325	7,203	1.7	-1.8	8.9
	France CAC40	5,416	5,327	1.7	-2.9	14.5
	S&P ASX 200	6,365	6,311	0.9	1.7	12.7

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

Global Calendar
May 20 – May 24

BMO Capital Markets®

	Monday May 20	Tuesday May 21	Wednesday May 22	Thursday May 23	Friday May 24
Japan	**Real GDP** **Q1 P (e) -0.1% +0.3% y/y** Q4 +0.2% +0.3% y/y **Industrial Production** **Mar. F (e) -0.9% -4.6% y/y** Feb. +0.7% -1.1% y/y	**Department Store Sales** **Apr.** Mar. +0.1% y/y	**Trade Surplus** **Apr. '19 (e) ¥229.5 bln** Apr. '18 ¥621.0 bln **Core Machine Orders** **Mar. (e) unch -3.5% y/y** Feb. +1.8% -5.5% y/y	**Manufacturing PMI** **May P** Apr. 50.2 **Machine Tool Orders** **Apr. F (e) -33.4% y/y** Mar. -28.5% y/y	**CPI / Core CPI** **Apr. (e) +0.9% y/y +0.9% y/y** Mar. +0.5% y/y +0.8% y/y **CPI ex. Food & Energy** **Apr. (e) +0.6% y/y** Mar. +0.4% y/y
Euro Area	**GERMANY** **Producer Price Index** **Apr. (e) +0.4% +2.4% y/y** Mar. -0.1% +2.4% y/y	**EURO AREA** **Consumer Confidence** **May A (e) -7.6** Apr. -7.9		**EURO AREA** **Manufacturing PMI** **May P (e) 48.1** Apr. 47.9 **Services PMI** **May P (e) 53.0** Apr. 52.8 **Composite PMI** **May P (e) 51.7** Apr. 51.5 **ECB Minutes** **European Parliamentary Elections** **GERMANY** **Real GDP** **Q1 F (e) +0.4% +0.7% y/y** Q1 P +0.4% +0.7% y/y Q4 unch +0.6% y/y **ifo Business Climate** **May (e) 99.2** Apr. 99.2 **FRANCE** **Business Confidence** **May (e) 105** Apr. 105	
U.K.	**Rightmove House Prices** **May** Apr. +1.1% -0.1% y/y		**Consumer Price Index** **Apr. (e) +0.7% +2.2% y/y** Mar. +0.2% +1.9% y/y **Core CPI** **Apr. (e) +2.0% y/y** Mar. +1.8% y/y **Producer Price Index (Output)** **Apr. (e) +0.3% +2.3% y/y** Mar. +0.3% +2.4% y/y		**Retail Sales (Incl. Fuel)** **Apr. (e) -0.4% +4.5% y/y** Mar. +1.1% +6.7% y/y
Other	**AUSTRALIA** **General Elections (May 18)**	**AUSTRALIA** **RBA Minutes from May 7 meeting**		**INDIA** **General Election Results**	**MEXICO** **Real GDP** **Q1 F (e) -0.2% +1.3% y/y** Q4 +0.3% +1.7% y/y

D = date approximate

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

North American Calendar
May 20 – May 24

BMO Capital Markets®

Canada

Monday May 20

Victoria Day (markets closed)

Tuesday May 21

Wednesday May 22

	Retail Sales	Ex. Autos
8:30 am		
Mar. (e)	**+0.9%**	**+0.9%**
Consensus	*+1.2%*	*+1.0%*
Feb.	+0.8%	+0.6%

Noon — 30-year real return bond auction $0.7 bln

Thursday May 23

	Wholesale Trade
8:30 am	
Mar. (e)	**+0.8%**
Feb.	+0.3%

Friday May 24

United States

Monday May 20

8:30 am — Chicago Fed National Activity Index

Apr. (e)	**-0.05**
Mar.	-0.15

7:00 pm — Fed Chair Powell makes a keynote speech at the 2019 Financial Markets Conference at Amelia Island, FL

Fed Speakers: Philadelphia's Harker (9:30 am); Vice Chair Clarida, New York's Williams (1:00 pm)

11:30 am — 13- & 26-week bill auction $72 bln

Saturday May 18

Fed Speaker: Dallas' Kaplan (2:05 pm)

Tuesday May 21

10:00 am — Existing Home Sales

Apr. (e)	**5.40 mln a.r. (+3.6%)**
Consensus	*5.34 mln a.r. (+2.6%)*
Mar.	5.21 mln a.r. (-4.9%)

Fed Speakers: Chicago's Evans (10:45 am); Boston's Rosengren (noon)

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

11:30 am — 52-week bill auction $26 bln

Wednesday May 22

7:00 am — MBA Mortgage Apps

May 17	
May 10	-0.6%

2:00 pm — FOMC Minutes from Apr. 30-May 1 meeting

Fed Speakers: St. Louis' Bullard (1:00 am); New York's Williams (10:00 am); Atlanta's Bostic (10:10 am)

Thursday May 23

8:30 am — Initial Claims

May 18 (e)	**215k (+3k)**[c]
May 11	212k (-16k)

8:30 am — Continuing Claims

May 11	
May 4	1,660k (-28k)

9:45 am — Markit PMI (May P)

10:00 am — New Home Sales

Apr. (e)	**692,000 a.r. (unch)**
Consensus	*677,000 a.r. (-2.2%)*
Mar.	692,000 a.r. (+4.5%)

11:00 am — Kansas City Fed Manufacturing Activity

May (e)	**6**
Apr.	5

Fed Speakers: Dallas' Kaplan, San Francisco's Daly, Atlanta's Bostic, Richmond's Barkin (1:00 pm)

11:00 am — 13- & 26-week bill, 2-, 5- & 7-year note, 2[R]-year FRN auction announcements

11:30 am — 4- & 8-week bill auction

1:00 pm — 10[R]-year TIPS auction $11 bln

Friday May 24

	Durable Goods Orders	Ex. Transport
8:30 am		
Apr. (e)	**-1.3%**	**+0.2%**
Consensus	*-2.0%*	*+0.2%*
Mar.	+2.8%	+0.2%

	Nondef. Capital Goods ex. Air
8:30 am	
Apr. (e)	**unch**
Consensus	*-0.3%*
Mar.	+1.0%

[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