Weekly Economic Watch

Economics and Strategy

NATIONAL BANK OF CANADA FINANCIAL MARKETS

February 15, 2019

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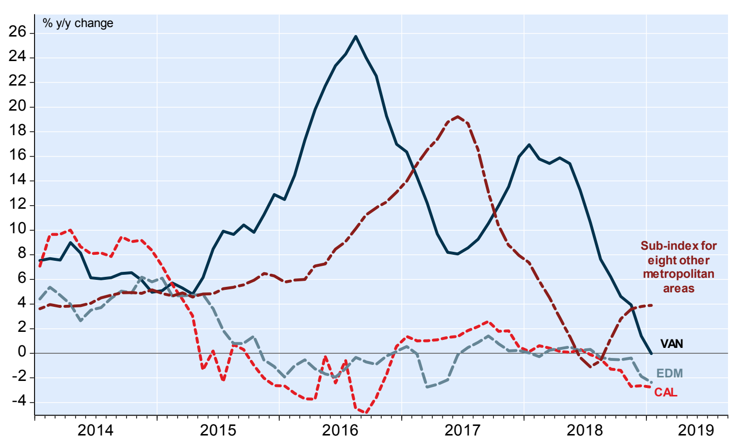
Week in review

CANADA: The **Teranet–National Bank Composite National House Price Index™** dipped 0.1% in January, marking a fifth consecutive month without an increase in prices. The retreat reflected weakness in Western Canada's three largest metropolitan areas: Edmonton (-0.8%), Calgary (-0.5%), and Vancouver (-0.3%). For Calgary, this marked a seventh consecutive monthly drop. In Edmonton and Vancouver, the negative streak stretched to six and five months, respectively. To add to the bad news, both Calgary and Edmonton were having to deal with an outsized number of vacant new dwellings, a matter that should continue to exert downward pressure on prices going forward. Looking back at the national picture, the Composite gauge rose 2.2% on a 12-month basis as gains in Ottawa-Gatineau (6.0%), Victoria (4.9%), Hamilton (4.6%), and Montreal (4.5%) were only partially offset by pullbacks in Calgary (-2.8%) and Edmonton (-2.4%). Prices in Vancouver, meanwhile, stayed flat year on year while Toronto saw its index climb 3.6%.

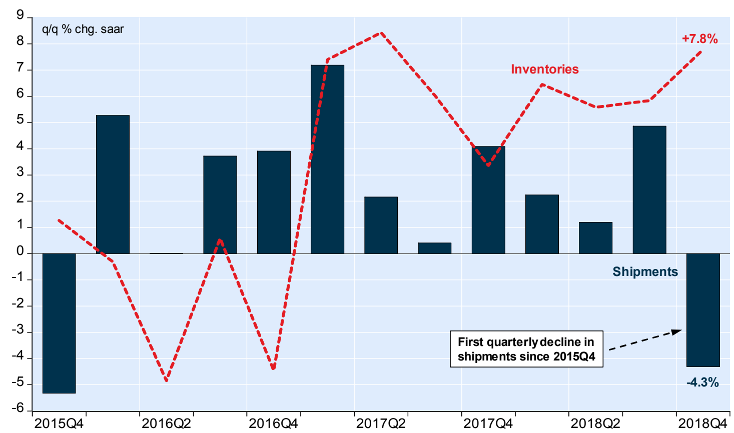
Home prices weaken further in Western Canada
HPI for Vancouver, Calgary and Edmonton vs. sub-index for eight other metropolitan areas



NBF Economics and Strategy (data via Teranet-National Bank House Price Index)

Manufacturing shipments fell 1.3% to C$56.4 billion in December after declining a downwardly revised 1.7% (instead of 1.4% as initially reported) the month before. Sales were down in 12 of the 21 broad industries and in 6 of the 10 provinces. As expected, shipments of petroleum and coal products (-10.4%), which suffered from lower prices and dwindling volumes in roughly equal measure, weighed on the headline figure. Even without this segment, however, sales still retreated 0.3% on declines for chemicals (-1.8%), food manufacturing (-2.3%) and machinery (-1.8%). With the price effect removed, total factory sales sank 1.2% m/m, while inventories sagged 0.2%. On a quarterly basis, real total shipments fell an annualized 4.3% in the fourth quarter, interrupting the longest streak of positive prints since data collection began in 2002 (11 straight quarters). Lower shipments should act as a drag on Q4 GDP but their effect may be softened by a 7.8% annualized increase in real inventories, their steepest jump since 2017Q2. However salutary this sharp upswing in inventory may prove for Q4 GDP, it could hinder production in 2019Q1 in the manufacturing sector. Indeed, the fact that the real inventory-to-sales ratio presently stands at its highest level since the recession does not exactly herald a ramp-up in production.

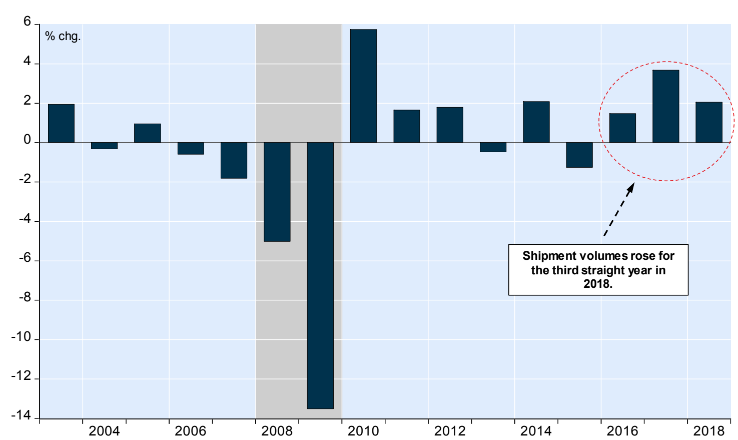
Canada: Shipments and inventories on different trajectories in Q4
Real manufacturing shipments and inventories



NBF Economics and Strategy (source: Statistics Canada)

Despite the poor showing in Q4, 2018 was a rather positive year for the manufacturing sector on the whole. Shipment volumes swelled 2.1%, marking a third straight annual increase. Inventories contributed to growth as well, surging a record 5.8%.

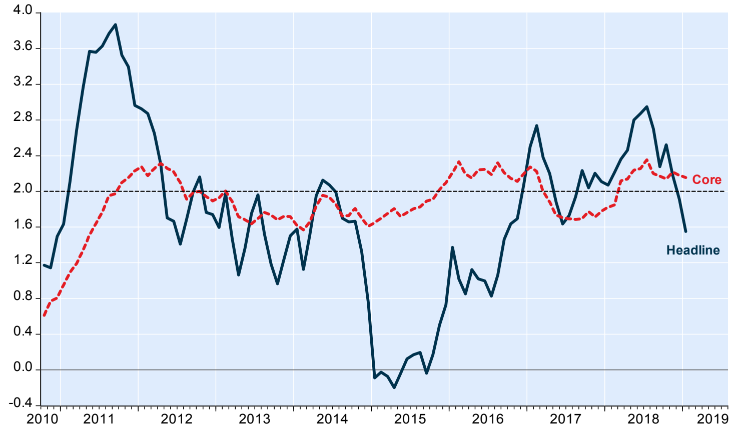
Canada: A decent year for the manufacturing sector in 2018
Real manufacturing shipments



NBF Economics and Strategy (source: Statistics Canada)

UNITED STATES: In January, the **consumer price index** remained unchanged from the previous month instead of increasing 0.1% as per expectations. Energy prices slid 3.1% (their steepest drop in 35 months), while food costs rose 0.2%. Excluding these two categories, the core CPI advanced a consensus-matching 0.2% on gains for both ex-energy goods (+0.4%) and ex-energy services (+0.2%). Year on year, the headline inflation gauge slipped three ticks to 1.6%, while the core index stayed put at 2.2%.

United States: Headline CPI pulled down by energy prices
CPI, headline and core (excluding food and energy)

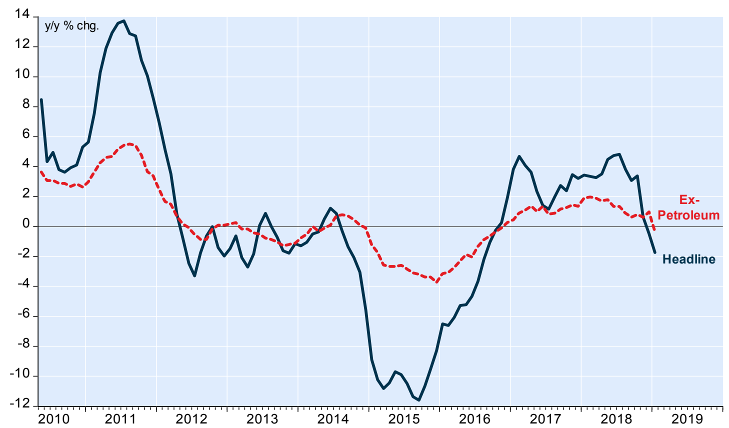


NBF Economics and Strategy (source: U.S. Labor Department via Refinitiv)

January's CPI report will probably reassure the Fed in its newly minted "wait-and-see" approach. Headline inflation continued to be depressed by slumping energy prices, which have now fallen 8.3% since October, their worst 3-month showing since early 2016. True, the core index came in stronger but this stemmed in part from a 1.1% monthly rise in the apparel category, which is likely to be reversed in next month's report. Still, the central bank will have to monitor price movements very carefully going forward. The U.S. economy remains relatively strong, as evidenced by yet another strong job report in January. Wages are trending upward and the greenback has now come down from its trade-weighted peak. These two factors, together with the stabilization of oil prices, could lend inflation some lift in the back end of 2019. Until then, though, the Fed should enjoy the luxury of staying on the sidelines.

Still in January, the **import price index** (IPI) registered a third sharp drop in a row, falling 0.5% m/m. Although prices for petroleum products (0.1%) once again weighed on the headline number, their impact was minimal. Prices for natural gas, on the other hand, acted as a major drag as it dropped no less than 44.2% following two steep increases in November and December (+60.1% and +26.5%, respectively). Still, even excluding fuels, a category which includes coal and natural gas, the IPI still retraced 0.2% in the month, signalling broad-based weakness across a variety of consumer and industrial goods. On an annual basis, the headline IPI sank from -0.5% to a 29-month low of -1.7%. The less volatile ex-petroleum gauge, for its part, tanked from 1.0% to -0.4%. The continued strength of the U.S. dollar (notwithstanding a slight depreciation of late) should continue to exert downward pressure on import prices going forward, as currency movements tend to impact import prices with a lag of several months. The energy sector, for its part, should be less of a drag in the future judging from the recent stabilization of oil prices.

U.S.: Strong USD continued to weigh on import prices in January
Import price index. Last observation: January 2019



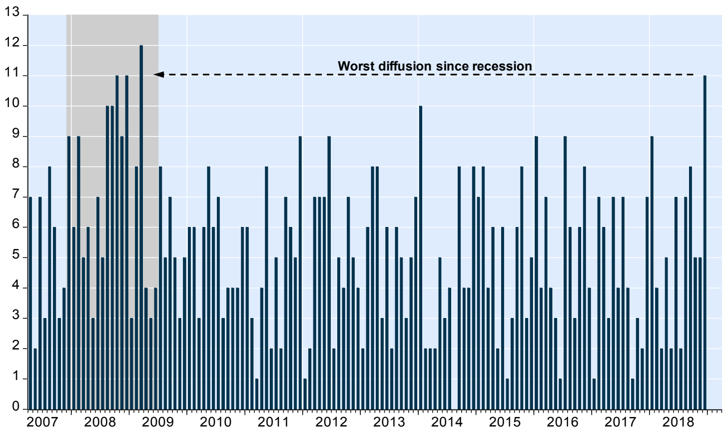
NBF Economics and Strategy (Source: U.S. Labor Department via Datastream)

Again in January, the **producer price index** (PPI) for final demand edged down 0.1% for a second month in a row. The decrease reflected lower prices for goods (-0.8%). The category was hampered by declines for both food (-1.7%) and energy (-3.8%). Alternatively, prices for services climbed a decent 0.3%. The core PPI, which excludes food and energy, rose 0.3%. Year over year, the headline PPI slid four ticks to 2.5%, its lowest level in 18 months. The index excluding food and energy, instead, slipped just one tick to 2.6%.

After seven consecutive months of expansion (the longest streak since 2010), **industrial production** fell 0.6% in January. Manufacturing output sank 0.9%, reflecting an 8.8% slump in the motor vehicles/parts segment, the worst monthly drop registered since May 2009. Should anybody be concerned by those numbers? We think not. Auto assembly tends to be a volatile component as evidenced by the 8.5% drop last May which was followed by a 7% increase the following month. It's also worth noting that auto production suffered from atypical plant shutdowns at GM and Fiat/Chrysler plants during the month. As such, we expect a factory rebound sooner rather than later. Output advanced 0.4% in the utilities segment and crept up 0.1% in mining. **Capacity utilization** in the industrial sector as a whole fell from 78.8% to 78.2%.

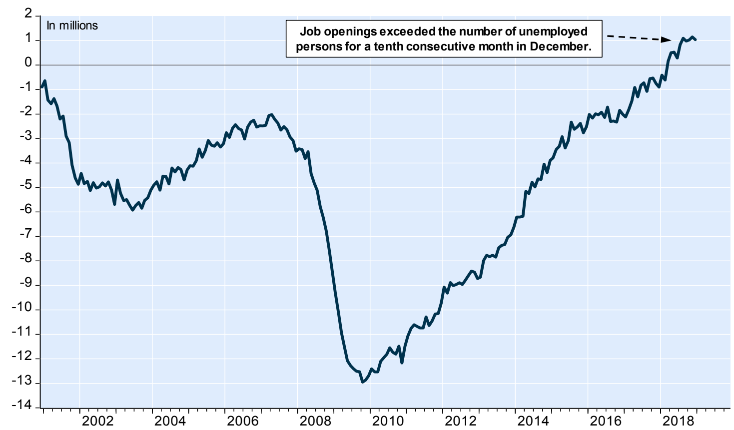
Retail sales tumbled 1.2% m/m in December, their sharpest pullback since September 2009. Surprising as it may seem, sales of motor vehicles actually advanced 1.0% m/m, which means that ex-auto sales had an even worse month, falling at their steepest pace since the recession (-1.8%). Several retail categories had their weakest showing in years, including non-store retailers (-3.9%, their worst since 2008M11), sporting goods/hobby (-4.9%, since 2008M09), and miscellaneous items (-4.1%, since 2015M09). Outlays at gasoline stations also slumped (-5.1%) but this was to be expected in a context of falling pump prices. In all, as many as 11 of the 13 categories surveyed experienced drawbacks, something that had not been seen in nearly 10 years.

United States: Broad-based slump in retail sales in December
Number of categories (out of 13) where sales declined from one month to next



NBF Economics and Strategy (source: U.S. Commerce Department via Refinitiv)

United States: Still more job openings than job searchers in December
Difference between job openings and unemployed persons. Last observation: December 2019



NBF Economics and Strategy (Source: National Federation of Independent Business via Refinitiv)

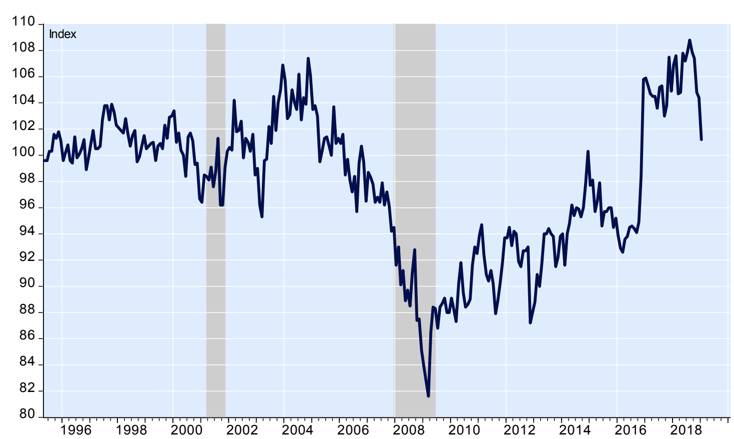
It is not clear what caused consumer outlays to plummet in December. While the government shutdown and stock market downturn may have played a part, it is difficult to reconcile this poor result with the vigour of the labour market. Unfortunately, January's data, too, could be distorted by the government shutdown, as well as by smaller-than-expected tax returns for U.S. consumers. In the meantime, we can take solace in the fact that core sales (i.e., excluding food services, auto dealers, building materials and gasoline stations) managed to expand an annualized 1.8% in Q4 as a whole, which suggests that consumption on goods might still have contributed to growth in the last quarter of the year.

The **Empire State Manufacturing Index** of general business conditions climbed from 3.9 in January to 8.8 in February. While the *new orders* (7.5 vs. 3.5) gauge improved, the *shipments* tracker fell 7.5 points to a 26-month low of 10.4. The *number of employees* sub-index (4.1 vs. 7.4), meanwhile, slid to its lowest level in a year-and-a-half, suggesting further moderation in job creation. The *prices paid* tracker (27.1 vs. 35.9) continued to fall, hinting at an easing of price pressures in the manufacturing sector. Finally, businesses' confidence for the next six months improved markedly (32.3 vs. 17.8), probably in response to the end of the government shutdown.

According to the **Job Openings and Labor Turnover Survey** (JOLTS), positions waiting to be filled in the United States rose from 7,166K in November to an all-time high of 7,335K in December. The result meant that, for a tenth consecutive month, job offers in the country exceeded the number of unemployed persons, a clear sign of tightness on the labour market. Openings reached all-time highs in several sectors, including construction, leisure/hospitality, accommodation/food services, and health care. Given the high number of vacancies, hires remained elevated across sectors at 5,907K, just short of the record number attained back in October (5,928K). The report also showed the quit rate stayed put at 2.3%, one tick shy of its cyclical high.

The **NFIB Small Business Optimism Index** fell for a fifth month in a row in January, dropping 3.2 points to 101.2, its lowest mark in 26 months. The decline, the steepest registered since June 2015, overshot the 1.4-point pullback expected by consensus. Forward-looking indicators in the survey fell in unison. For one, the net percentage of polled firms that expected the economic situation to improve fell from 16% to 6%, the lowest percentage observed since Donald Trump's election in late 2016. Survey respondents were also less bullish about future sales: A net 16% thought they would improve, the smallest such figure in 16 months. Against this less optimistic backdrop, a lower net proportion of businesses were planning to hire (18% vs. 23% the prior month) and expand (20% vs. 24%). Investment intentions, for their part, remained relatively healthy with 26% of respondents saying they were planning to increase capital spending in the next 3 to 6 months, compared with 25% the prior month.

United States: Small business confidence faded again in January
NFIB Small Business Optimism Index. Last observation: January 2019



NBF Economics and Strategy (Source: National Federation of Independent Business via Refinitiv)

The government shutdown no doubt had a negative impact on the January report of the NFIB, but it is hard to say to what extent. It will thus be interesting to see how the headline NFIB gauge reacts to the return to work of federal employees. Although a bounce-back seems likely in the short term, we doubt that the index will revisit its recent peak anytime soon in the context of a slowing world economy. That said, it is worth pointing out that the Small Business Confidence Index held above its historical average (approximately 98.0) and thus remained consistent with a decent level of confidence among small firms. The recent pullback may simply reflect a return to more normal levels of enthusiasm on the part of small businesses following a period of admittedly unsustainable optimism fueled by tax cuts and above-potential growth.

WORLD: The **Japanese economy** recouped some of the losses it suffered in Q3 as it expanded 1.4% in real annualized terms in the three months to December. Business investment was the biggest driver in the quarter, contributing 1.5 percentage points to the overall growth figure, though it had shaved 1.7 points from it the prior quarter. Consumption, residential investment and government added to growth as well, but to a smaller degree. Trade, on the other hand, suffered from a slowdown in international demand, particularly in China and the Eurozone, and thus weighed on growth for the third quarter running. With global economic momentum fading, domestic demand is likely to be the main driver of Japanese growth in the next few quarters. Unfortunately, the government intends to go ahead with its plan to increase the consumption tax from 8% to 10% as of October, a decision that is likely to bear down on consumption. A similar tax hike in 2014 had pushed the economy into recession. To avoid such an outcome this time, Prime Minister Shinzo Abe has promised to implement a wave of stimulus spending. We will have to wait to see whether these measures will be enough to keep the economy afloat.

Contributions to real GDP growth

	Q4 2018	Q3 2018
GDP	**1.4**	**-2.6**
Consumption	1.3	-0.5
Business Investment	1.5	-1.7
Residential Investment	0.1	0.1
Government	0.4	-0.2
Final Domestic Demand	**3.3**	**-2.3**
Exports	0.7	-1.0
Imports	-1.9	0.5
Trade	**-1.2**	**-0.6**
Inventories	-0.8	0.3

NBF Economics and Strategy (data via Datastream)

Jocelyn Paquet and al.

Jobs

	Unemployment rate		Employment change	
	Latest	12 months ago	Latest	12-month avg
Canada	5.8%	5.9%	66.8K	27.3K
Ontario	5.7%	5.6%	41.4K	14.2K
Quebec	5.4%	5.4%	16.4K	3.2K
British Columbia	4.7%	4.8%	8.7K	5.2K
Alberta	6.8%	7.0%	-15.5K	0.9K
United States	4.0%	4.1%	304.0K	233.9K
Eurozone	7.9%	8.6%	---	---
Japan	2.4%	2.7%	-450.0K	95.8K

Inflation

	Y/Y Latest	3-mth ann.	Y/Y 6 months ago	Y/Y 1 year ago
Canada				
Headline CPI	2.0%	1.5%	2.5%	1.9%
Average core	1.9%	---	1.9%	1.9%
United States				
Headline PCE	1.8%	1.5%	2.3%	1.9%
Core PCE	1.9%	1.7%	2.0%	1.6%
Eurozone				
Headline CPI	1.6%	---	2.0%	1.4%
Core CPI	1.0%	---	0.9%	0.9%
Japan				
Headline CPI	0.3%	-1.2%	0.7%	1.1%
Core CPI	0.7%	0.0%	0.8%	0.9%

Housing Market

	Median home price	Mort. payment share of income / 12 months ago	House prices Y/Y chg.	Housing starts 3-month avg. / 10yr avg
Canada	$572,214	50.4% / 47.3%	2.2%	215.4K / 195.8K
Toronto	$847,256	71.1% / 67.4%	3.6%	41.5K / 36.8K
Vancouver	$1,081,529	83.2% / 77.0%	0.0%	24.2K / 19.8K
Montreal	$340,985	33.7% / 30.7%	4.5%	27.9K / 20.5K
Calgary	$437,645	32.4% / 31.5%	-2.8%	8.4K / 11.3K
United States	---	---	5.2%	1236.7K / 916.1K

Manufacturing Sector

	Markit manufacturing PMI		Industrial production	
	Latest	6-month trend	3 mth ann chg	12-month chg
Canada	53.0	▼	-1.2%	1.9%
United States	54.9	▼	0.4%	3.8%
Eurozone	50.5	▼	-9.5%	-3.9%
Japan	50.3	▼	7.2%	-1.0%
China	48.3	▼	---	---

Central Banks

	Policy rate	12 months ago	Trend	Next announce
Bank of Canada	1.75%	1.25%	▲	03/06/2019
Fed Reserve (upper bound)	2.50%	1.50%	▲	03/20/2019

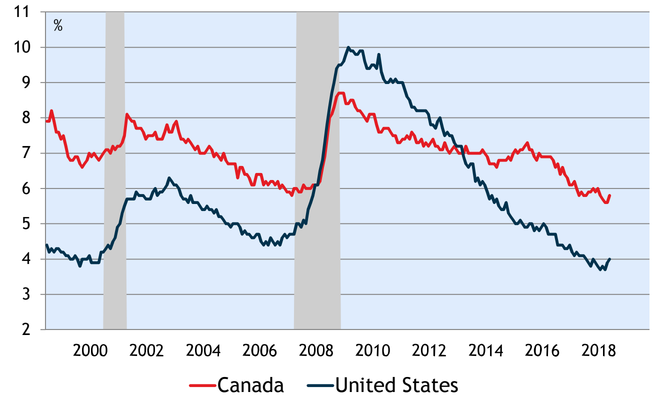
GDP Growth

	Q/Q ann Latest	Q/Q ann Previous	Y/Y Latest	Y/Y 6 months ago
Canada	2.0% (Q3)	2.9% (Q2)	2.1%	1.9%
United States	3.4% (Q3)	4.2% (Q2)	3.0%	2.9%
Eurozone	0.6% (Q4)	1.7% (Q3)	1.2%	1.6%
Japan	1.4% (Q4)	-2.6% (Q3)	0.0%	0.2%

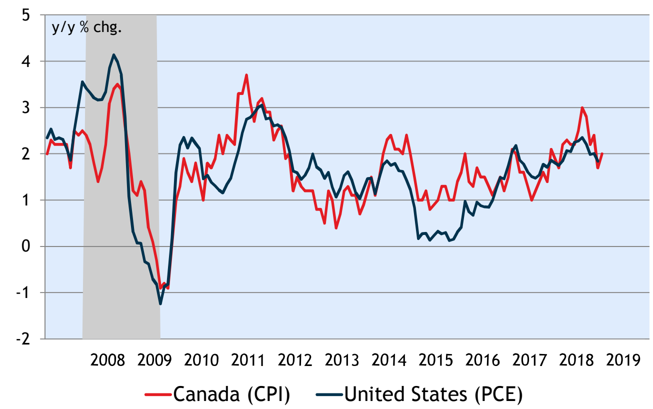
Contributions to real GDP growth - Canada

	Q3 2018	Q2 2018	Q1 2018	Q4 2017
GDP	**2.0**	**2.9**	**1.7**	**1.7**
Consumption	0.7	1.3	0.8	1.4
Business Investment	-0.8	0.1	1.5	0.7
Nonprofit Sector	0.0	0.1	0.0	0.0
Residential Investment	-0.5	0.0	-0.6	0.9
Government	0.5	0.3	0.6	1.5
Final Domestic Demand	**-0.1**	**1.8**	**2.3**	**4.3**
Exports	0.3	3.9	0.7	1.7
Imports	2.7	-2.0	-1.5	-2.5
Trade	**3.0**	**2.0**	**-0.8**	**-0.8**
Inventories	-1.3	-0.6	0.1	-1.7
Statistical discrepancy	0.3	-0.3	0.1	-0.2

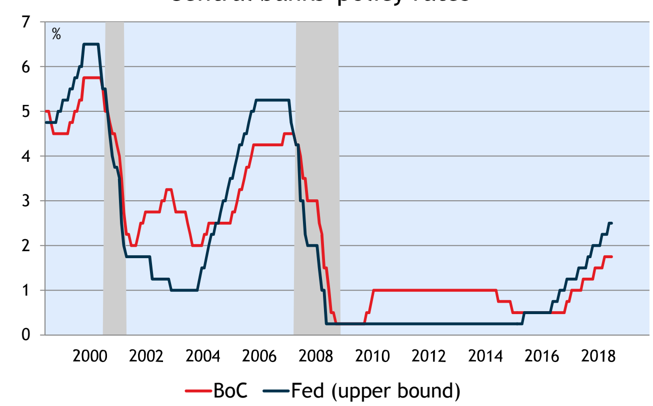
Unemployment rate



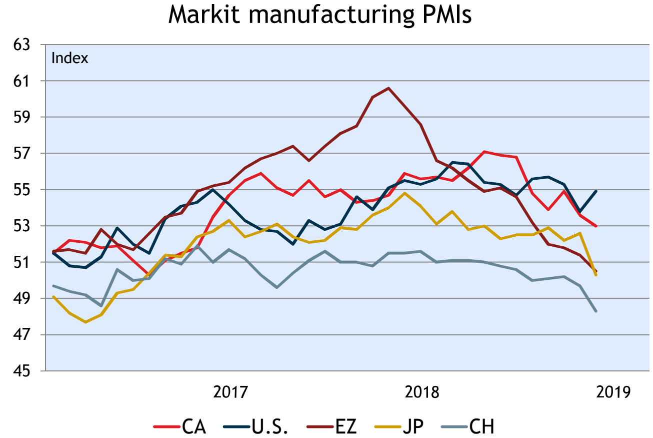
Headline inflation



Central banks' policy rates



Markit manufacturing PMIs

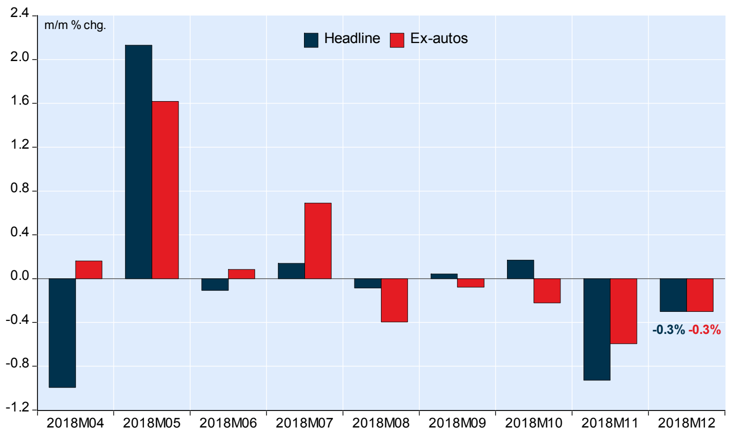


What we'll be watching

IN CANADA, the week will provide some valuable information about economic activity in December with the release of **retail sales**. We expect both headline and ex-auto sales to have retraced in the month, reflecting poor auto sales and a slump in gasoline prices which likely hit gasoline station receipts. We'll also keep an eye on the release of **wholesale trade sales** for December. A speech at the Chamber of Commerce of Metropolitan Montreal by **Bank of Canada Governor Stephen Poloz** is also scheduled on Thursday.

	Previous	NBF forecasts
Retail sales (December, m/m chg.)	-0.9%	**-0.3%**
Ex-autos retail sales (December, m/m chg.)	-0.6%	**-0.3%**

Canada: Retail sales likely retreated once more in December
Headline and ex-autos retail sales

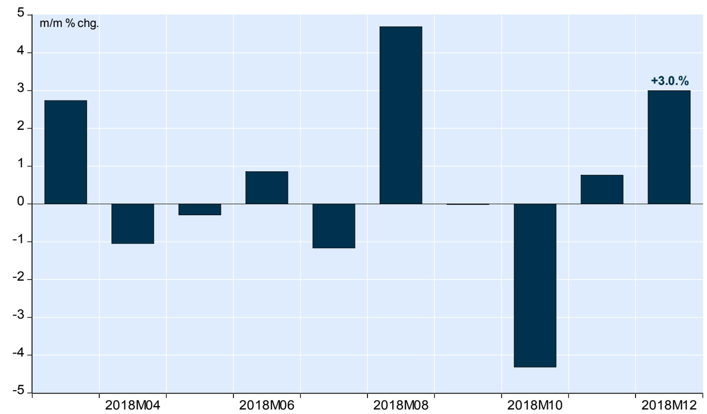


NBF Economics and Strategy (Source: Statistics Canada)

IN THE U.S., we'll get **durable goods orders** for December, with a healthy advance expected based on the jump observed in civilian plane orders. In other news, January's **existing home sales** data will be published, with a slight rebound expected on account of the fall in mortgage rates during the month. Markit will also publish its flash estimate of the **composite PMI** for February. Finally, the Fed will release the minutes of its January 30 meeting.

	Previous	NBF forecasts
Durable goods orders (December, m/m chg.)	0.7%	**3.0%**
Existing home sales (January, saar)	4990K	**5150K**

U.S.: Civilian airplanes may have boosted durable goods orders in December
Durable goods orders



NBF Economics and Strategy (Source: Refinitiv)

ELSEWHERE IN THE WORLD, **Markit's flash manufacturing PMI** will be available in both the Eurozone and Japan. Still in Japan, several important indicators for January will be released including **national CPI** and the **trade balance**.

NATIONAL BANK OF CANADA
FINANCIAL MARKETS

Economic Calendar – Canada & U.S

Economic releases & events

Day	Time	Country	Release	Period	Previous	Consensus Estimate	NBF Estimate
Monday Feb 18							
Tuesday Feb 19	10:00	US	NAHB Housing Market Index	Feb	58.0	59.0	
Wednesday Feb 20	7:00	US	MBA Mortgage Applications	Feb-15	-3.70%	--	
Thursday Feb 21	8:30	CA	Wholesale Trade Sales MoM	Dec	-1.00%	--	
	8:30	US	Initial Jobless Claims	Feb-16	239k	220k	
	8:30	US	Durable Goods Orders	Dec P	0.70%	1.80%	3.00%
	8:30	US	Durables Ex Transportation	Dec P	-0.40%	0.30%	0.30%
	9:45	US	Markit US Manufacturing PMI	Feb P	54.9	54.9	
	9:45	US	Markit US Services PMI	Feb P	54.2	--	
	10:00	US	Existing Home Sales	Jan	4.99m	5.00m	5.10m
	10:00	US	Existing Home Sales MoM	Jan	-6.40%	0.20%	2.20%
Friday Feb 22	8:30	CA	Retail Sales MoM	Dec	-0.90%	0.00%	-0.30%
	8:30	CA	Retail Sales Ex Auto MoM	Dec	-0.60%	-0.50%	-0.30%

Earnings announcements

Day	Company	Time	Qtr	Cons. EPS
Monday Feb 18				
Tuesday Feb 19	Capital Power Corp	Bef-mkt	Q4 18	0.44
	OceanaGold Corp	Bef-mkt	Q4 18	0.04
	Emera Inc	Bef-mkt	Q4 18	0.68
	Sienna Senior Living Inc	Aft-mkt	Q4 18	0.35
	Hudbay Minerals Inc	Aft-mkt	Q4 18	0.01
	Medtronic PLC	06:45	Q3 19	1.24
	Walmart Inc	07:00	Q4 19	1.34
	Ecolab Inc	08:30	Q4 18	1.54
	Concho Resources Inc	Aft-mkt	Q4 18	1.13
	Diamondback Energy Inc	Aft-mkt	Q4 18	1.61
	FirstEnergy Corp	Aft-mkt	Q4 18	0.47
	Verisk Analytics Inc	Aft-mkt	Q4 18	1.07
Wednesday Feb 20	Uni-Select Inc	06:00	Q4 18	0.19
	Bausch Health Cos Inc	Bef-mkt	Q4 18	0.84
	IAMGOLD Corp	Aft-mkt	Q4 18	-0.01
	Alamos Gold Inc	Aft-mkt	Q4 18	0.01
	Exchange Income Corp	Aft-mkt	Q4 18	0.71
	Pan American Silver Corp	Aft-mkt	Q4 18	0.05
	Osisko Gold Royalties Ltd	Aft-mkt	Q4 18	0.02
	CVS Health Corp	Bef-mkt	Q4 18	2.09
	Southern Co/The	07:00	Q4 18	0.23
	Analog Devices Inc	08:00	Q1 19	1.28
	Agilent Technologies Inc	16:00	Q1 19	0.73
	Realty Income Corp	16:00	Q4 18	0.74
Thursday Feb 21	TransAlta Renewables Inc	0:00	Q4 18	0.22
	Hydro One Ltd	Bef-mkt	Q4 18	0.28
	Gildan Activewear Inc	Bef-mkt	Q4 18	0.43
	Loblaw Cos Ltd	06:30	Q4 18	1.07
	Finning International Inc	09:00	Q4 18	0.48
	Northland Power Inc	Aft-mkt	Q4 18	0.28
	SSR Mining Inc	Aft-mkt	Q4 18	0.00
	Pembina Pipeline Corp	Aft-mkt	Q4 18	0.62
	Eldorado Gold Corp	Aft-mkt	Q4 18	-0.07
	Keyera Corp	Aft-mkt	Q4 18	0.37
	Altus Group Ltd/Canada	Aft-mkt	Q4 18	0.37
	Enerflex Ltd	Aft-mkt	Q4 18	0.28
Friday Feb 22	Winpak Ltd	0:00	Q4 18	0.45
	SNC-Lavalin Group Inc	0:00	Q4 18	-1.28
	Home Capital Group Inc	Bef-mkt	Q4 18	0.43
	Cott Corp	Bef-mkt	Q4 18	0.04
	SNC-Lavalin Group Inc	0:00	Y 18	0.83
	Enerplus Corp	Bef-mkt	Q4 18	0.33
	Magna International Inc	Bef-mkt	Q4 18	1.60
	Royal Bank of Canada	06:00	Q1 19	2.21
	Canfor Corp	Bef-mkt	Q4 18	-0.06
	Chorus Aviation Inc	Bef-mkt	Q4 18	0.24
	CCL Industries Inc	06:30	Q4 18	0.72
	Centerra Gold Inc	Aft-mkt	Q4 18	0.30

Source: Bloomberg

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