NATIONAL BANK OF CANADA
FINANCIAL MARKETS

Top News

Research Services

October 18, 2023

U.S. EQUITY FUTURES	LAST	CHANGE	%CHG
Dow Jones MINI futures	34,051.00	-93.00	-0.27%
S&P500 MINI futures	4,378.75	-23.00	-0.52%
NASDAQ MINI futures	15,132.25	-108.50	-0.71%
CANADA EQUITY MARKET	**LAST**	**CHANGE**	**%CHG**
S&P/TSX 60 futures	1,181.60	-4.90	-0.41%
OVERSEAS MARKETS	**LAST**	**CHANGE**	**%CHG**
DJ EURO STOXX 50	4,121.11	-31.21	-0.75%
FTSE 100 INDEX	7,618.91	-56.30	-0.73%
DAX GERMANY	15,147.83	-103.86	-0.68%
CAC 40 Index	6,983.98	-45.72	-0.65%
NIKKEI 225 INDEX	32,042.25	1.96	0.01%
HANG SENG INDEX	17,732.52	-40.82	-0.23%
SHANGHAI COMPOSITE INDEX	3,058.71	-24.79	-0.80%

COMMODITIES/ FX		LAST	CHANGE
CRUDE OIL WTI		$88.12	$1.46
NATURAL GAS		$3.13	$0.05
GOLD		$1,947.69	$24.62
COPPER		$3.61	$0.03
CAD / USD		$0.7323	-$0.0003
CAD / EUR		€ 0.6933	€ 0.0008
USD / EUR		€ 0.9468	€ 0.0015
USD / JPY		¥149.74	-¥0.06
GOVERNMENT BONDS	**2YR**	**5YR**	**10YR**
CANADA (YLD%)	4.91%	4.31%	4.10%
U.S. (YLD%)	5.20%	4.87%	4.86%

Source: Refinitiv

Morning News

Canadian housing starts unexpectedly rose in September, climbing 8% compared with the previous month, as groundbreaking increased on multi-unit and single-family-detached projects. Data from the national housing agency showed that the seasonally adjusted annualized rate of housing starts rose to 270,466 units from a revised 250,383 units in August. Economists had expected starts to fall to 240,000. Canada's main stock index futures edged lower today, as fears of the escalated conflict in the Middle East weighed on global investor sentiment. Both materials and energy sectors are expected to rise as gold and oil soared following the huge explosion at a Gaza hospital killed hundreds of Palestinians, wrecking a diplomatic mission by U.S. President Joe Biden, who arrived in Israel today but was snubbed by Arab leaders who called off an emergency summit. Copper rose on hopes of improved demand following better-than-expected economic data from China. The world's second-biggest economy grew at a faster-than-expected clip in the third quarter, while consumption and industrial activity in September also surprised on the upside, suggesting the recent flurry of policy measures is helping to bolster a tentative recovery. Gross domestic product (GDP) grew 4.9% in July-September from the year earlier, data released by the National Bureau of Statistics showed, versus analysts' expectations in a Reuters poll for a 4.4% increase but slower than the 6.3% expansion in the second quarter. On a quarter-by-quarter basis, GDP grew 1.3% in the third quarter, accelerating from a revised 0.5% in the second quarter and above the forecast for growth of 1.0%.The government is walking a tight rope as it tries to restore economic equilibrium, with policymakers having to navigate a domestic property crisis, high youth unemployment, depressed private sector confidence, a slowdown in global growth and Sino-U.S. tensions over trade, technology and geopolitics. In the U.S., stock index futures also dipped this morning as growing tensions in the Middle East spurred demand for safe-haven assets. Investors will also be looking at EV maker Tesla and streaming services company Netflix, both scheduled to report quarterly results after market close today. In other corporate news, Nvidia dropped on lingering concerns over the Biden administration's plans to halt shipments of more advanced AI chips designed by the company and others to China. Several Federal Reserve officials, including New York's John Williams and Board Governors Christopher Waller and Michelle Bowman will speak later in the day, ahead of Chair Jerome Powell's remarks on Thursday. Philadelphia Fed president Patrick Harker said in an interview with the Wall Street Journal that the U.S. central bank should extend its pause on interest-rate increases. On the economic front, U.S. single-family homebuilding rebounded sharply in September, boosted by demand for new construction amid a dearth of previously owned homes. Single-family housing starts, which account for the bulk of homebuilding, increased 3.2% to a seasonally adjusted annual rate of 963,000 units last month. Overall housing starts accelerated 7.0% to a rate of 1.358 million units in September. Permits for future construction of single-family homes rose 1.8% in September to a rate of 965,000 units.

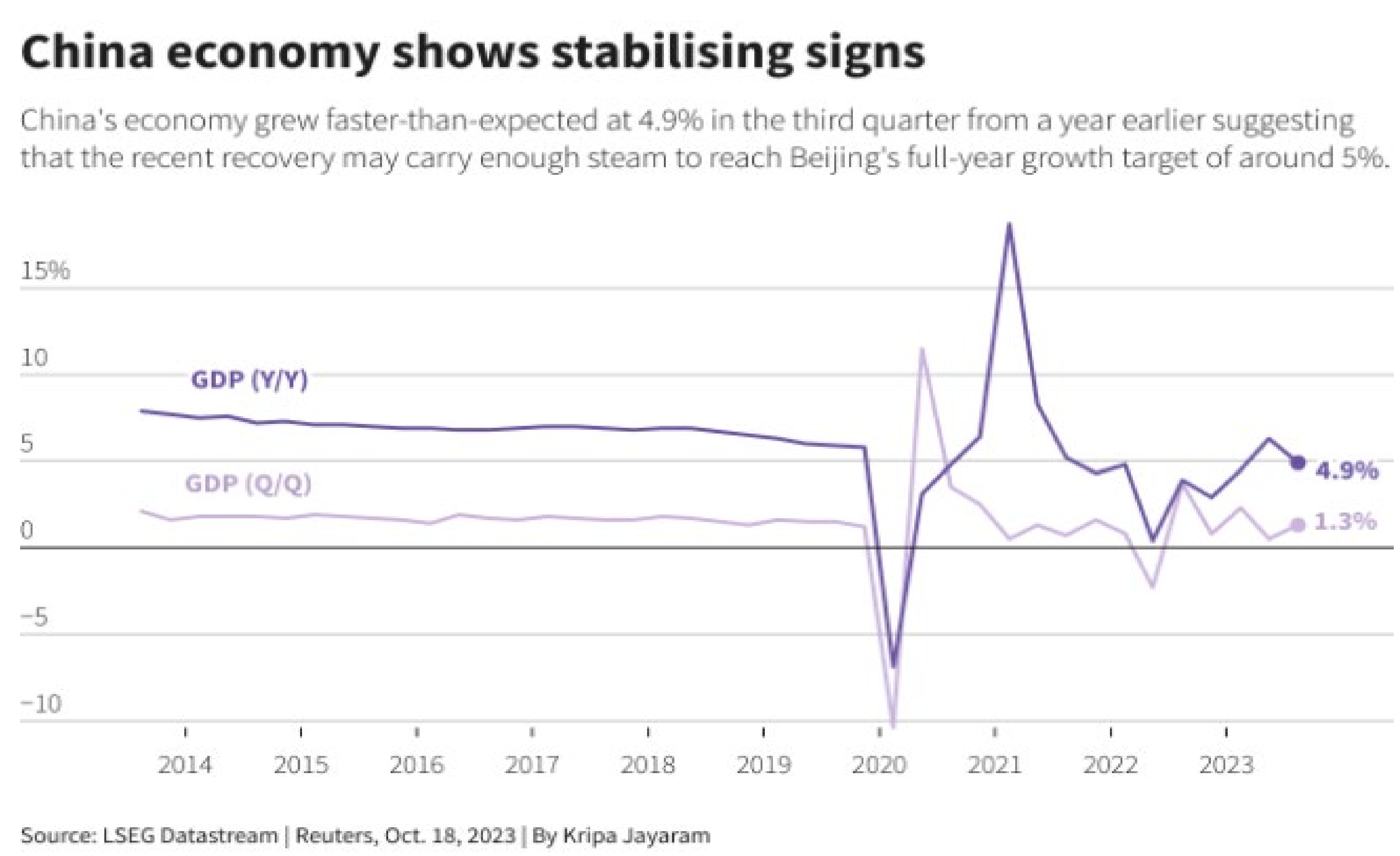
U.S Economic Calendar

Time	Indicator Name	Period	Consensus	Actual	Prior	Revised
07:00	MBA Mortgage Applications	13 Oct, w/e		-6.9%	0.6%	
07:00	MBA 30-Yr Mortgage Rate	13 Oct, w/e		7.70%	7.67%	
08:30	Building Permits: Number	Sep	1.450M	1.473M	1.541M	
08:30	Build Permits: Change MM	Sep		-4.4%	6.8%	
08:30	Housing Starts Number	Sep	1.380M	1.358M	1.283M	1.269M
08:30	House Starts MM: Change	Sep		7.0%	-11.3%	-12.5%

Canadian Economic Calendar

Time	Indicator Name	Period	Consensus	Actual	Prior	Revised
08:15	House Starts, Annualized	Sep	240.0k	270.5k	252.8k	250.4k

Chart of the day



Top News

Canadian Stocks

NATIONAL BANK OF CANADA FINANCIAL MARKETS

Morning news

A&W Revenue Royalties Income Fund: A&W Revenue Royalties Income Fund says it earned $10.6 million in net income in its third quarter up from $9.6 million a year earlier. The fast food income fund says the increase for the quarter ended Sept. 10 came as royalty income rose to $13.7 million compared with $13.2 million in the same quarter last year. The fund, which earns royalties on the gross sales of restaurants in a royalty pool, says gross sales reported by A&W restaurants in the pool totalled $456.8 million, up from $440.0 million a year earlier. The number of restaurants in the pool rose to 1,037 compared with 1,015 in the same quarter last year. Meanwhile, the royalty pool same-store sales growth was 1.1 per cent for the quarter. The fund's payout ratio for the quarter was 81.3 per cent compared with 80.3 per cent for the same quarter in 2022.

BlackBerry Ltd: The head of BlackBerry Ltd. says he's hoping for June timing on the initial public offering the company has planned for its Internet of Things business. The forthcoming IPO will carve BlackBerry into two business units, dividing its cybersecurity operations from its internet of things offerings. The Waterloo, Ont.-based technology company has been evaluating a range of strategic alternatives to enhance shareholder value since May. Speaking at an investors briefing, John Chen said he was aiming for June because he wants to avoid a summer IPO, when people are on holidays. He also wants to steer clear of September, which he considers a bad month for the stock market because people are coming back from vacation with a different mindset

NBF Research

RATING AND TARGET PRICE CHANGES

Parkland Corporation - Q3 2023 Preview: Strong EBITDA growth expected across all segments; Target: C$45 (Was C$43)
Real Matters Inc. - Extended Mortgage Lull; Target: C$7 (Was C$8.50); Rating: Sector Perform (Was OP)

DAILY BULLETIN HIGHLIGHTS

PARKLAND CORPORATION: Q3 2023 Preview: Strong EBITDA growth expected across all segments

PKI (TSX)	**C$41.04**
Target:	**C$45.00**
	(Was C$43.00)
Stock Rating:	**Outperform**
	(Unchanged)
Est. Total Return:	**13.0%**

Event: PKI reports Q3/23 results on November 1, 2023, after market close.

Key Takeaways: (1) We project Q3/23 EBITDA to be higher by 62% y/y, largely reflecting higher volumes in Canada and International, higher fuel margins, a higher crack spread, non-recurrence of losses in the USA segment, consolidation of non-controlling interest in SOL, acquisition contribution and favourable FX, partly offset by lower volume in the USA segment. (2) Recall, management expects growth in retail and commercial operations to outpace refinery. Since 2018, we calculate that PKI's marketing business will deliver an EBITDA CAGR of 21.0%, above refining at 3.8% (adjusted). (3) Maintain Outperform rating; price target is $45 from $43.

REAL MATTERS INC.: Extended Mortgage Lull; Downgrading to Sector Perform

REAL (TSX)	**C$5.69**
Target:	**C$7.00**
	(Was C$8.50)
Stock Rating:	**Sector Perform**
	(Was Outperform)
Est. Total Return:	**23.0%**

Event: Mortgage Bankers Association Event Takeaways

Key Takeaways: We had the opportunity to attend a reception (Solidifi Extraordinary Reception) hosted by Real Matters at the annual Mortgage Bankers Association (MBA) Conference earlier this week. The reception provided the opportunity to speak with some of Real Matters' customers, partners (appraisers) in addition to Brian Lang (CEO), Ryan Smith (CTO) and Lyne Beauregard (VP of IR and Corporate Communications). Overall, customer and partner sentiment around Real Matters Solidifi brand remained positive. That said, and not surprisingly, the overall mood from customers and partners was one of caution for near-term mortgage origination volumes that have extended beyond our expectations. Given the +36% increase in REAL's stock price YTD, the name is looking reasonably valued against that elongated turn. As such, we're downgrading the name to Sector Perform (from Outperform).

Top News
Canadian Stocks

RESEARCH FLASHES

Airlines - Airfares down y/y in September; but up 10.8% relative to 2019
Lundin Mining Corporation - Lundin Announces Certain Items Impacting Q3 Results
Tricon Residential Inc. - Activist unveils itself: Land & Buildings announces long position in TCN

MORNING HIGHLIGHTS

BROOKFIELD INFRASTRUCTURE PARTNERS L.P.: Super-cycle just getting started… upgrading to Outperform

BIP / BIP.UN (NYSE; TSX) : US$25.69; C$35.01

Stock Rating:	**Outperform**
	(Was Sector Perform)
Target:	**US$33.00**
	(Was US$38.00)
Est. Total Return:	**34.4%**

Event: For Q3/23, we forecast FFO of US$553 mln (US$0.72; Street: US$0.75), ~5% above Q3/22 levels, while the company reiterated its 12%+ FFO/unit CAGR outlook over the next one to three years.

Key Takeaways: BIP's growth strategy has tilted towards investing in platforms with highly executable organic growth backlogs (~80% contracted; inflation indexed), namely the generational investment cycle into data centres, with long-term capital appreciation expected to more than offset lower going in yields, supporting IRRs above its 12-15% target range. Elsewhere, BIP is boosting margins through organizational optimization techniques, including the introduction of AI. Overall, incorporating our Economics & Strategy Group's revised long-term GCAN assumption of 3.5% (was 3.0%) into our cost of capital assumption, our target moves down to US$33 (was US$38). That said, with the stock down ~30% since mid-summer following recent delays in commissioning HPC and the closing of the Triton acquisition (issuing 21 mln BIPC shares), combined with BIP now trading at a ~20% discount to our SOTP valuation of US$31, we are upgrading the name to OP (from SP).

MORNING COMMENTS

Brookfield Infrastructure Partners L.P. - Super-cycle just getting…; Rating: Outperform (Was SP); Target: US$33 (Was US$38)

MORNING FLASHES

Park Lawn Corporation - Divestiture of legacy lower margin assets yields $70 million - a little deleveraging and a little dilution

ETF RESEARCH & STRATEGY

ETF Industry News Update: New providers, new Buffer and Accelerator ETFs; other launches, filings and delistings

Canadian stocks ratings and target changes across the street

AGF Management Ltd AGFb.TO: TD Securities cuts target price to C$9.50 from C$10
Algonquin Power & Utilities Corp AQN.N: TD Securities cuts target price to US$6 from US$*
BCE Inc BCE.TO: JP Morgan cuts target price to C$59 from C$62
BCE Inc BCE.TO: RBC cuts target price to C$59 from C$63
BlackBerry Ltd BB.N: CIBC cuts target price to US$4.75 from US$5.50
Boralex Inc BLX.TO: BMO cuts target price to C$40 from C$42
Brookfield Infrastructure Partners LP BIP.N: National Bank of Canada raises to outperform from sector perform
Brookfield Infrastructure Partners LP BIP.N: National Bank of Canada cuts target price to US$33 from US$38
CI Financial Corp CIX.TO: TD Securities cuts target price to C$18 from C$20
Cogeco Communications Inc CCA.TO: RBC cuts target price to C$84 from C$93
Enbridge Inc ENB.TO: Barclays cuts target price to C$48 from C$54
Fiera Capital Corp FSZ.TO: TD Securities cuts target price to C$6 from C$7.50
High Tide Inc HITI.V: Eight Capital initiates coverage with buy rating and C$5 target price

Top News
Canadian Stocks

IGM Financial Inc IGM.TO: TD Securities cuts target price to C$38 from C$46
Labrador Iron Ore Royalty Corp LIF.TO: BMO cuts target price to C$30 from C$32
Largo Inc LGO.TO: CIBC cuts target price to C$8.25 from C$10
Nutrien Ltd NTR.N: BMO cuts target price to US$86 from US$90
Onex Corp ONEX.TO: TD Securities raises target price to C$105 from C$100
Parkland Corp PKI.TO: National Bank of Canada raises target price to C$45 from C$43
Pason Systems Inc PSI.TO: Barclays raises to equal weight from underweight; raises target price to C$15 from C$12
Peyto Exploration & Development Corp PEY.TO: BMO raises target price to C$16 form C$13.50
Quebecor Inc QBRb.TO: RBC cuts target price to C$36 from C$38
Real Matters Inc REAL.TO: National Bank of Canada cuts to sector perform from outperform; cuts target to C$7 from C$8.5
RF Capital Group RCG.TO: Cormark Securities cuts target price to C$18.25 from C$20.25
Rogers Communications Inc RCIb.TO: RBC cuts target price to C$69 from C$72
Sigma Lithium Corp SGML.O: BMO cuts target price to US$44 from US$48
Sprott Inc SII.TO: TD Securities cuts target price to C$49 from C$51
Stingray Group Inc RAYa.TO: Canaccord Genuity cuts target price to C$8 from C$8.50
TC Energy TRP.TO: Barclays cuts target price to C$50 from C$51
Telus Corp T.TO: RBC cuts target price to C$29 from C$31

S&P/TSX Earnings Calendar

Company	Symbol	Time	Consensus EPS Estimate
Winpak Ltd	WPK.TO	NTS	0.55

Source: Refinitiv

Top News
U.S. Stocks

ASML Holding NV: The semiconductor equipment maker reported lower-than-expected orders and warned of flat sales next year as customers conserve cash against an uncertain economic backdrop, hitting its shares. Europe's largest technology firm said the semiconductor industry was probably near a trough but that "customers continue to be uncertain about the shape of the demand recovery ... we therefore expect 2024 to be a transition year".

Elevance Health Inc: The company reported a nearly $700 million charge due to job cuts and write-offs from some technology assets after a strategic review in the third quarter to shield itself against several hits to its business next year. Net income attributable to non-controlling interests fell to $1.29 billion, or $5.45 per share in the quarter ended Sept. 30, from $1.60 billion, or $6.62 per share, a year earlier. Excluding items, the company made a profit of $8.99 per share, above analysts' estimates of $8.44 per share, according to LSEG data. Elevance's medical loss ratio, the percentage of claims paid to premiums collected, was 86.8% for the third quarter compared with 86.4% in the previous quarter. On an adjusted basis, the company now expects full-year profit of more than $33 per share, compared with its previous forecast of over $32.85 per share.

J B Hunt Transport Services Inc: The company on Tuesday missed profit estimates for the third quarter, as the logistics provider grapples with a drop in e-commerce volumes and elevated costs. The company's net profit dropped 30% to $1.80 per share for the quarter ended Sept. 30, from a year ago. Analysts on average had estimated earnings per share of $1.83, as per LSEG data. J.B. Hunt's revenue fell 18% to $3.16 billion, nearly in line with analysts' estimate of $3.18 billion.

Omnicom Group Inc: The company beat Wall Street targets for third-quarter results on Tuesday as demand for its marketing services jumped ahead of the all-important holiday shopping season. Omnicom's revenue grew nearly 4% to $3.58 billion in the quarter ended Sept. 30, compared with a consensus estimate of $3.55 billion from six analysts polled by LSEG. Its net income grew 2% to $371.9 million. Excluding items, the company earned $1.86 per share, compared with expectations of $1.84.

Procter & Gamble Co: The company's quarterly sales topped market expectations, helped by steady demand for its personal care products and cleaning supplies despite price hikes. The Pantene shampoo maker saw overall prices jump 7% in the first quarter, while total sales volume dropped 1%, consistent with the levels seen in the prior quarter. P&G said it now expected sales growth to be in the range of 2%-4% for fiscal 2024, compared to its prior estimate of a 3%-4% rise. Net sales at the consumer goods giant rose to $21.87 billion in the fiscal first quarter, from $20.61 billion a year earlier, and compared to analysts' average estimate of $21.58 billion.

Travelers Companies Inc: The company reported a 14% fall in quarterly profit, as severe wind and hail storms in parts of the United States drove up catastrophe losses for the insurer. Core income of the New York-based company, often seen as a bellwether for the insurance sector as it typically reports results before peers, fell to $454 million, or $1.95 per share, in the third quarter ended Sept. 30, from $526 million, or $2.20 per share, a year earlier.

United Airlines Holdings Inc: The company forecast weaker fourth-quarter earnings due to higher costs, sending its shares down. The Chicago-based carrier estimated an adjusted profit of $1.50-$1.80 per share in the quarter through December, below the $2.06 expected by analysts in a LSEG survey and lower than $2.46 per share a year ago. A jump in fuel prices since July is pressuring profits at U.S. carriers. United has said its fuel costs have climbed over 20% since mid-July. The company's average fuel bill is projected to increase by 11% in the quarter through December from the last quarter. Adjusted profit for the third quarter came in at $3.65 per share, higher than the $3.35 estimated by Wall Street analysts.

S&P500 Earnings Calendar

Company	Symbol	Time	Consensus EPS Estimate
Abbott Laboratories	ABT	BMO	1.10
Citizens Financial Group Inc	CFG	BMO	0.91
Crown Castle Inc	CCI	AMC	0.77
Discover Financial Services	DFS	AMC	3.19
Elevance Health Inc	ELV	06:00	8.43
Equifax Inc	EFX	AMC	1.78
Kinder Morgan Inc	KMI	AMC	0.26
Lam Research Corp	LRCX	AMC	6.12
Las Vegas Sands Corp	LVS	AMC	0.55
M&T Bank Corp	MTB	BMO	3.91

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U.S. Stocks

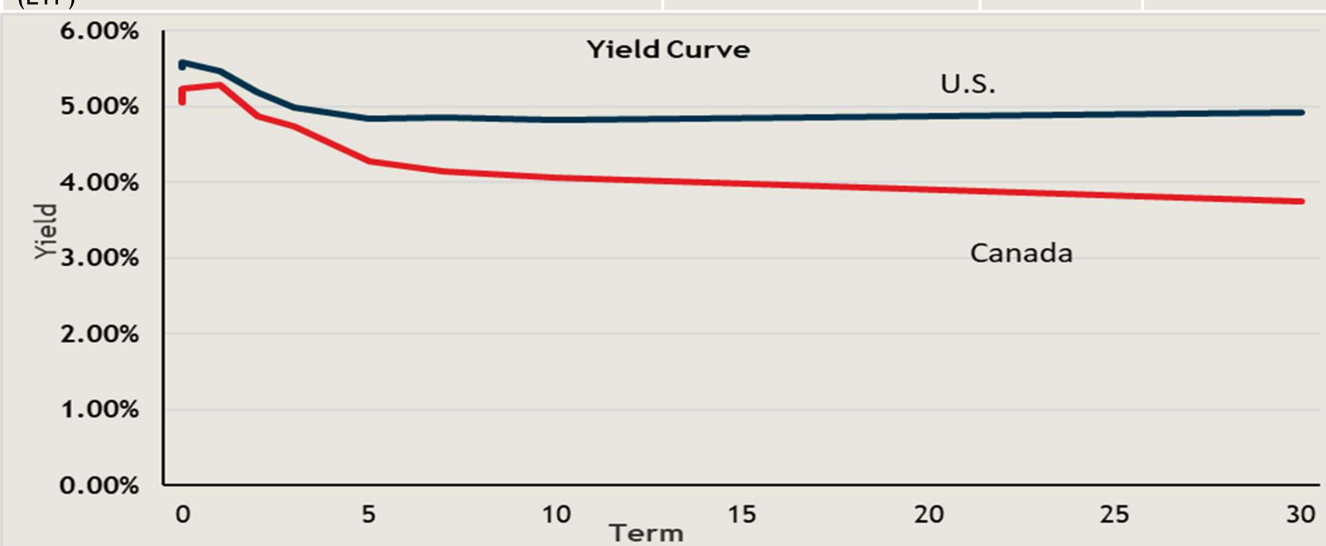
Morgan Stanley	MS	BMO	1.28
Nasdaq Inc	NDAQ	07:00	0.68
Netflix Inc	NFLX	16:00	3.49
Northern Trust Corp	NTRS	BMO	1.47
PPG Industries Inc	PPG	AMC	1.94
Procter & Gamble Co	PG	BMO	1.72
State Street Corp	STT	07:30	1.81
Steel Dynamics Inc	STLD	AMC	3.46
Tesla Inc	TSLA	AMC	0.74
Travelers Companies Inc	TRV	BMO	2.99
US Bancorp	USB	BMO	1.02
Zions Bancorporation NA	ZION	AMC	1.15

Source: Refinitiv

Top News
Fixed Income

Canadian Key Rate	Last	Change bps		Last	Change bps
CDA o/n	5.00%	0.00	CDA 5 year	4.27%	-3.8
CDA Prime	7.20%	0.00	CDA 10 year	4.05%	-2.1
CDA 3 month T-Bill	5.16%	0.0	CDA 20 year	3.96%	-1.4
CDA 6 month T-Bill	5.23%	0.0	CDA 30 year	3.74%	-1.4
CDA 1 Year	5.28%	-4.0	5YR Sovereign CDS	41.7	
CDA 2 year	4.87%	-2.4	10YR Sovereign CDS	42.77	
US Key Rate	**Last**	**Change bps**		**Last**	**Change bps**
US FED Funds	5.25-5.50%	0.00	US 5 year	4.84%	-3.6
US Prime	8.50%	0.00	US 10 year	4.82%	-3.2
US 3 month T-Bill	5.35%	-0.3	US 30 year	4.92%	-2.6
US 6 month T-Bill	5.59%	-0.8	5YR Sovereign CDS	48.43	
US 1 Year	5.47%	-2.0	10YR Sovereign CDS	58.7	
US 2 year	5.18%	-3.2			

Preferred Shares Indicators	Last	Daily %	YTD
S&P Preferred Share Index	506.27	-0.10%	-7.00%
BMO Laddered Preferred Shares (ETF)	8.48	-0.23%	-6.19%



Source: Refinitiv

Top News

Economy & Strategy

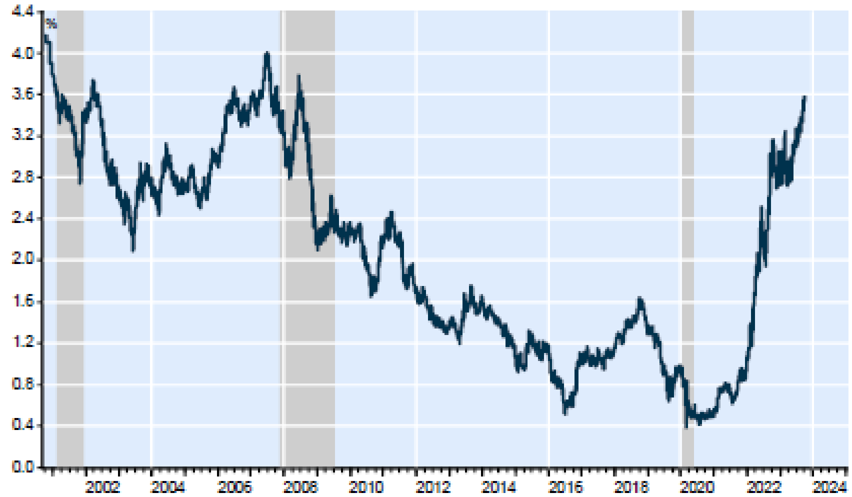
NATIONAL BANK OF CANADA FINANCIAL MARKETS

Monthly Economic Monitor - October 2023

Summary

- The last two years have seen one of the most violent recalibrations ever seen on the global bond market, with interest rates paid on sovereign bonds issued by governments around the world rising by no less than 280 basis points on average since October 2021. While it is difficult to disentangle the causes of the recent rise in bond yields, its effect on global growth will be no less significant, especially as this increase has been concentrated in the long end of the curve, which tends to have a greater impact on economic activity. And while no region of the world will be spared, the eurozone seems to us to be particularly vulnerable in this new interest-rate environment. Highly indebted emerging economies are also likely to suffer from this recalibration, especially in a context where the U.S. dollar has risen sharply, further increasing the cost of servicing debt. Weakness in the eurozone and emerging economies could be temporarily masked by solid growth in the United States, something which should enable global GDP to grow by 3.0% this year. But we continue to expect growth to slow down significantly in 2024 (+2.2%), held back by a weakening in the world's leading economy.
- Judging by its most recent economic forecasts, the Federal Reserve seems to have joined the camp of those who believe in the theory of "immaculate disinflation", which stipulates that price growth can be curbed without the process being too painful for the U.S. economy. And it has to be said that recent data releases have rekindled hopes of such a scenario becoming a reality. But progress towards the dual mandate of full employment and 2% inflation by no means guarantees a soft landing. Although we agree with the central bank that inflation should continue to decelerate in 2024, we believe this will be at the expense of economic activity. Our prognosis is guided by the fact that rate hikes tend to affect the economy with a long lag, particularly in the U.S. where most mortgages are fixed over a long period, sparing households the full impact of tighter monetary policy today. But with the cost of servicing non-mortgage debt rising all the time, consumers will likely have to exercise greater restraint going forward. We therefore expect U.S. growth to slow sharply in Q4, after having been well above potential in Q3. The extent of the slowdown, however, will depend on the duration of the auto workers' strike, which, according to our calculations, will subtract 0.1% per week from annualized quarterly growth. This subdued end to the year should not be too detrimental to annual growth, which we forecast to reach 2.4% in 2023. Looking ahead, we still expect the U.S. economy to slip into recession in the first half of 2024, a scenario that will result in an expansion of just 0.3% for the year as a whole.
- The Bank of Canada decided to keep rates unchanged at the beginning of September, but stated that it was prepared to raise rates again if necessary in the absence of progress on the underlying inflation measures. Now that this has happened, is a rate hike inevitable? Not so fast, as the bank is now faced with a dilemma. It was easy to raise rates when the economy still had momentum and was showing signs of overheating. But this is no longer the case. Inflation has been surprisingly high, but economic growth in the second and third quarters is well below its July forecasts. GDP per capita is even set to decline for a fifth consecutive quarter in Q3. What's more, there are no signs of a recovery in the months ahead, with consumer and SME confidence now at levels seen only during recessions. It would be perilous for the Bank of Canada to remain focused on inflation, given the lag in transmitting monetary policy to the economy, and even longer for inflation. According to our calculations, no less than 43% of the impact of rate hikes has yet to be felt on consumption. This is enormous, especially as households are already showing signs of running out of steam. Against this backdrop, combined with the tightening of financial conditions triggered by the global rise in long-term interest rates, we continue to anticipate economic lethargy over the next twelve months. We forecast growth of 1.0% in 2023 and 0% in 2024.

World: Violent re-pricing on the bond market over the past two years
Bloomberg global aggregate government bond yields



NBF Economics and Strategy (data via Bloomberg)

Monthly Fixed Income Monitor - October 2023

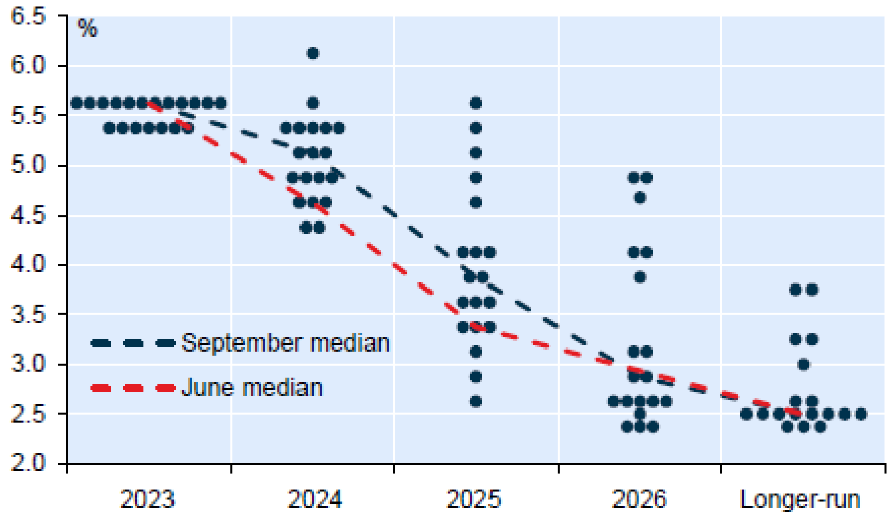
Forecast Summary

- While the situation is undeniably fluid, even the outbreak of war in the Middle East can't fully arrest (or reverse) the broad repricing of duration risk. Sentiment has swung violently relative to our last published forecast. In the U.S., a resilient economy and stubborn inflation has lent marginal credibility to the high(er)-for-long(er) school of thought, with devotees growing in number and conviction. Of note, fresh data (including core CPI, jobs and retail) suggest that (a bit) more tightening may ultimately be required to cool things off. OIS markets have less-than-full conviction as it relates to a final hike in fed funds, but we see a greater-than-50% probability of the FOMC delivering one last quarter-point hike before the year is out. As we've heard from certain FOMC members, a pronounced back-up in longer-term interest rates—and the attendant tightening of financial conditions—could well substitute for direct policy rate tightening. So we'll be closely monitoring valuations across rates, credit and equity markets as FOMC decision days approach. More than an upwardly revised policy rate path, bond investors have been troubled by the U.S. fiscal trajectory. Elevated and unrelenting government borrowing, compounded by ongoing central bank balance sheet remediation in the form of QT, has met with investor apathy, including from some high-profile corners overseas. Judging from recent price action, it's a noxious mix, propelling term premia higher and making good on a steepening bias (although not exactly in the manner we saw a steepener playing out).
- Notwithstanding lingering concerns over sticky inflation, the economic cycle should ultimately hold sway. Contracting U.S. real GDP growth, slower full-time hiring, tame(r) wage growth and tapped-out consumers will secure material inflation relief in 2024. So while it could be 'higher', it might not necessarily be for all that 'longer'. While our prevailing economic/rates narrative has been roundly challenged in recent weeks, we have resisted pushing back the timeline for FOMC rate cuts. Our more cautious U.S. growth outlook would put cutting conditions in place sooner than many believe. Having been so radically re-priced, longer-term rates (e.g., U.S. 10s topping 4.8%) appear broadly oversold. Our forecast sees 10-year Treasuries recovering ~50 bps in the coming year, an economic stumble, tamer inflation and resulting swing to less-restrictive policy hinting at a more conventional 'bull steepening' of the Treasury curve in 2024. A full dis-inversion in U.S. 2s-10s may be in reach by late 2024.
- In contrast to FOMC forecast tweaks, the Bank of Canada's official forecast revisions (via October's MPR) must acknowledge slower growth and hotter inflation than previously envisaged (in July). Stagflation? There's a hint of it, at least for time being. And it leaves the BoC in something of a bind. Acknowledged policy signposts remain worrying, wage growth too brisk and core inflation momentum hardly benign. Corporate pricing behaviour has yet to normalize and short-term inflation expectations remain elevated. Given the BoC's acknowledged tightening bias, a 25-bp hike in Q4 cannot therefore be ruled out. Complicating matters, and ultimately arguing against further policy rate tightening, is Canada's deteriorating growth trajectory, which has tilted lower even before controlling for super-sized population gains. (Aside: Sky-high immigration should be viewed as inflationary in the short-term, owing to the acute shortage of available housing supply. Taxation tweaks

and other policy interventions won't remedy housing market imbalances anytime soon, rent inflation likely to remain sticky.) As we look ahead to 2024, a deepening economic slowdown is expected to deliver real progress on inflation, allowing the BoC to turn down the level of policy rate restrictiveness. In all, as much as 100 bps of rate cuts could be on the table for next year, a 2024:Q2 policy rate pivot coming ahead of the FOMC given Canada's more interest-rate-sensitive economic model. From a cross-market perspective, more contained government borrowing needs and a still-engaged non-resident investor have supported Canadian bond yields vs. Treasuries. This has been most observable/relevant out the curve. It's a particularly compelling narrative and one that looks to have staying power.

2024 and 2025 dots adjusted higher... again

FOMC September 2023 'dot plot', with median dots from September and June



Source: NBF, FRB | Note: 2026 dots not available in June

Canada: Sigh of relief on the inflation front in September

After two consecutive months in which inflation exceeded economists' consensus expectations, the opposite occurred in September. The widespread nature of August's significant rise led many to fear the worst. September's data confirmed our view that this upsurge was temporary, as 7 of the 8 components moderated from last month's pace. The only exception was food, which rose from 0.20% m/m to 0.27%, which is still much lower than what we've seen recently. The widespread moderation in inflation can also be seen in the core inflation measures of the Bank of Canada, which rose at their lowest pace in 31 months. We think the September data will take a lot of pressure off the Bank of Canada to do more. True, core inflation measures have not improved much on a three-month annualized basis, remaining in an uncomfortable range. But the bank is now facing a dilemma. It was easy to raise rates when the economy still had momentum and was showing signs of overheating. But this is no longer the case. Inflation has surprised them on the rise, but economic growth in the second and third quarters is well below its July forecasts. What's more, there are no signs of an upturn in the months ahead, with consumer and SME confidence now at levels seen only during a recession. It would be perilous for the Bank of Canada to remain focused on sticky inflation with real policy rate the more restrictive since 2008, given the lag in transmitting monetary policy to the economy, and even longer for inflation. According to yesterday's Business Outlook survey, capacity utilization is already back to normal, and the outlook is bleak. Against this backdrop, combined with the tightening of financial conditions triggered by the global rise in long-term interest rates, we continue to anticipate economic lethargy over the next twelve months without any further BoC tightening.

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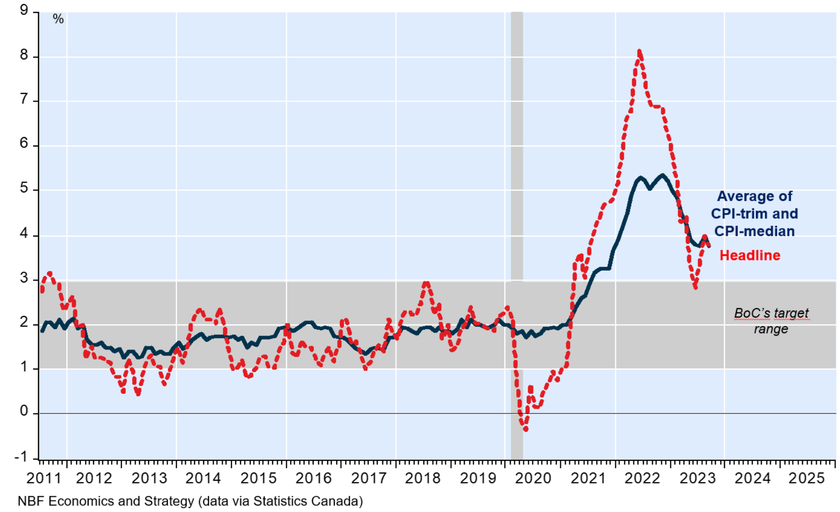


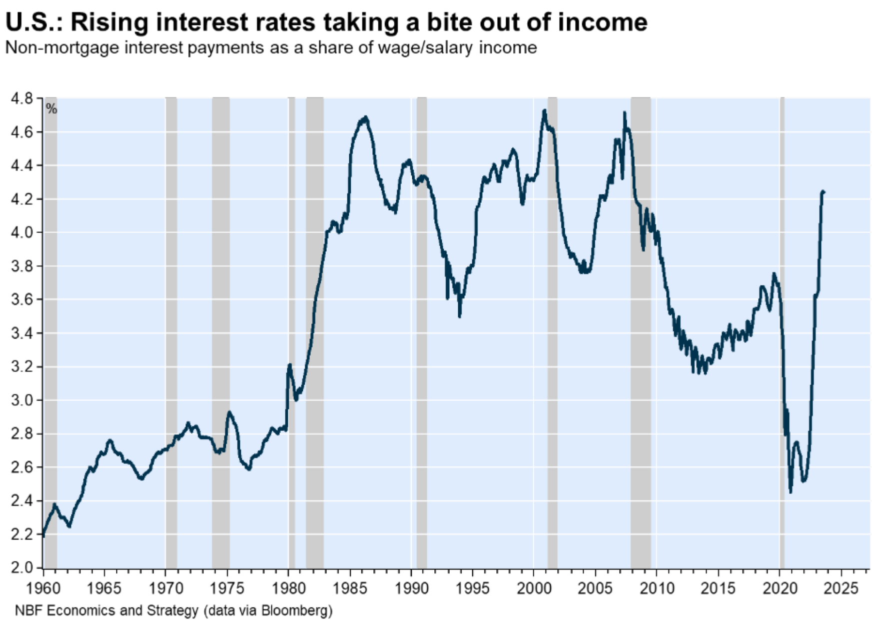
Snapshot – U.S. Retail Sales (September)

In the U.S., retail sales advanced 0.7% in September, more than the +0.3% print expected by consensus. Adding to the good news, the prior month's result was revised upwards, from +0.6% to +0.8%. Sales of motor vehicles/parts contributed positively to the headline print as they advanced 1.0% in the final month of Q3. Without autos, retail outlays rose a consensus-topping 0.6%, as gains for miscellaneous items (+3.0%), non-store retailers (+1.1%), gasoline stations (+0.9%) and health/personal care (+0.8%) were only partially offset by declines for clothing (-0.8%), electronics (-0.8%) and building materials (-0.2%). Outlays in restaurants and bars progressed 0.9% on a monthly basis. In all, sales were up in 8 of the 13 categories surveyed. Core sales (i.e., sales excluding food services, auto dealers, building materials, and gasoline stations), which are used to calculate GDP, progressed 0.6%.

Bottom line:
Once again in September, retail sales data came in stronger than expected. And unlike last month, this increase was not only due higher prices – recall that last week's CPI report showed goods prices rising only 0.1% in September. Part of the monthly gain reflected rising sales at automobile dealerships, but the strength was certainly not limited to this sole category. Outlays on miscellaneous goods bounced back after two consecutive contractions in July and August, while sales at non-store retailers continued their seemingly unstoppable progression. The continued increase in spending in bars and restaurants in September was another piece of good news in the report as it suggests spending on services (which accounts for a bigger portion of GDP than spending on goods) remained healthy in the month. A third consecutive decline in furniture sales, on the other hand, reflected a still depressed real estate market. Recall that home resales remain roughly 25% below their pre-pandemic level. Discretionary sales also came in stronger than expected and were tracking a 6.4% annualized increase in the third quarter as a whole, something that should translate into a very healthy contribution to GDP growth from goods consumption.

Although the process is obviously taking longer than we anticipated, we continue to expect a deterioration in the situation of households going forward and, therefore, a significant slowdown in consumer spending. Keep in mind that outlays have been boosted in Q3 by the concert tours of Taylor Swift and Beyonce, as well as the Hollywood blockbusters Barbie and Oppenheimer, which together generated around $8 billion in spending. Unfortunately, in a context where this rise in household spending was not accompanied by a corollary increase in disposable income, but was rather the result of a significant drop in the savings rate, we fear that the burst of vigour will be short-lived. Indeed, it seems that, in order to finance their largesse, consumers have once again had to draw heavily on the pool of excess savings accumulated during the pandemic which, according to our calculations, will be fully depleted in the early months of 2024. Our expectation of lower consumption growth is also guided by the fact that rate hikes tend to affect the economy with a long lag, particularly in the U.S. where most mortgages are fixed over a long period, sparing households the full impact of tighter monetary policy today. But sparing them the full impact is not the same as sparing them completely. While mortgages account for the lion's share of household indebtedness in the U.S., the scale of outstanding loans in other sectors remains significant. And this is where consumers are currently feeling the effects of rising interest rates. This, at least, is suggested by the marked increase in the proportion of salary/wages that has to be spent on non-mortgage interest payments. The rise in credit card interest payments is partly responsible for this increase, which is hardly surprising given the increased use of this form of payment and the explosion in rates charged on outstanding balances. The situation is similar for auto loans, a segment in which the amounts financed continue to rise despite a major tightening of credit conditions.

In our view, rising debt servicing costs in these sectors will weigh on disposable income growth - and hence household consumption - in the months ahead. This phenomenon will be reinforced by the resumption of student loan repayments. Already in September, transfers by the Department of Education to the U.S. Treasury, consisting mainly of student loan repayments, had risen to $6.97 billion, an amount similar to pre-pandemic levels and equivalent to around 0.4% of total consumer spending. In view of these factors, we expect growth to slow markedly in Q4, after having been well above potential in Q3. The extent of the slowdown, however, will depend on the duration of the United Auto Workers strike, which we calculate will subtract 0.1% per week from annualized quarterly growth.



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