

CAPITAL MARKETS RESEARCH

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Daily Points

— Tracking the Numbers

On Deck for Friday, June 29

Country	Date	Time	Indicator	Period	BNS	Consensus	Latest
CA	06/29	08:30	IPPI (m/m)	MAY	--	0.0	0.0
CA	06/29	08:30	Raw Materials Price Index (m/m)	MAY	--	-2.0	-2.0
CA	06/29	08:30	Real GDP (m/m)	APR	0.2	0.2	0.1
US	06/29	08:30	PCE Deflator (m/m)	MAY	--	-0.2	0.0
US	06/29	08:30	PCE Deflator (y/y)	MAY	1.6	1.5	1.8
US	06/29	08:30	Personal Consumption (m/m)	MAY	0.0	0.0	0.3
US	06/29	08:30	Personal Income (m/m)	MAY	0.1	0.2	0.2
US	06/29	09:45	Chicago PMI	JUN	51.5	52.3	52.7
US	06/29	09:55	U. of Michigan Consumer Sentiment	JUN F	74.0	74.1	74.1

KEY POINTS:

- * Risk on as European Summit Rumored to Result in Bank Bailout Plan
- * China industrial profits lower than at this time last year
- * Germany retail sales lower in May...
- * ...While France consumer sales are higher
- * Eurozone inflation stable in June
- * UK index of services flat
- * Japan inflation edges lower, industrial production tails off
- * Canada GDP today
- * US personal consumption data due out

INTERNATIONAL

Markets are trading with a highly positive tone on press reports that Europe's bailout fund (the EFSF/ESM) will be used to directly recapitalize European banks (no official releases have been made). Reports say that the bailout costs will be shouldered by the collective fund and not the countries whose banks are being bailed out. This means in effect that Europe collectively will pay for the recapitalization of the Spanish banking system (as opposed to Spain going it alone – which it probably could not afford). EURUSD spiked on the news, moving almost two big figures from 1.245 to 1.263 instantly (it has now settled somewhat below 1.26). European stocks are rallying hard with the biggest gains centered on financial stocks. The Spanish IBEX index's financials sector is up +3% as are financial stocks on the DAX (generally, European stocks are up by 2% or more across the board). Crude is trading positively, with Brent and WTI August contracts both higher by more than 2%. CAD is stronger against the USD and has rallied nearly a full big figure from yesterday's close. Bonds are selling off: generic German 10-year bunds were yielding more than the generic US 10-year briefly today, although they have since pared their losses and are back to trading at a slight premium to US 10's (albeit the slightest premium in some time).

Reports from the **European Summit** say that European leaders agreed in principle to enact a variety of measures to address the short term and medium term funding needs of Italy and Spain. The agreement was reached after Spanish and Italian leadership refused to endorse the pan-European EUR130bn stimulus package before the assembled European leaders addressed their short-term needs (i.e. discussed a bank bailout, etc.). As no official details have been released, we are left to go with press reports. So far, the main measures being reported are as follows:

BoC Events

BoC Overnight Lending Rate

Current Rate: 1.0%
Next Move: July 17 @ 1.0%
Bias: Hawkish

Fed Events

Fed Funds Target Rate

Current Rate: 0-0.25%
Next Move: August 1 @ 0-0.25%
Bias: Dovish

Key International Events

BoJ

Current Rate: 0.10%
Next Move: July 12 @ 0.10%
Bias: Dovish

BoE

Current Rate: 0.50%
Next Move: July 5 @ 0.50%
Bias: Dovish

ECB

Current Rate: 1.00%
Next Move: July 5 @ 1.00%
Bias: Neutral

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- 1) Comprehensive bailout of troubled banking systems the costs of which will be shouldered by the EFSF/ESM.
- 2) A banking union that would set up a common bank regulatory authority (there are conflicting reports as to who will run it, but it looks as though it will either be operated by the European Commission or ECB).
- 3) Countries that are adhering to their EU budgetary commitments will be able to borrow money directly from the EFSF/ESM with less onerous conditionality than is currently being negotiated, and the EFSF/ESM will not necessarily demand 'super senior' status.
- 4) Common deposit insurance and bank resolution could be part of the banking union.

The creation of the banking union and common oversight body will be a condition for the implementation of the bank bailouts. The plan will be for a provisional or initial version of the banking regulator to be set up by year end.

It is worth noting that the development of the EFSF/ESM into a bank bailout fund would not be dissimilar to the path that the US took with its own emergency Troubled Asset Relief Program or TARP. TARP was initially created to buy so-called 'toxic assets' but quickly evolved into an all-purpose fund to recapitalize banks and other entities. The EFSF/ESM was initially created as a 'fire-wall' to bail out Greece and potentially other countries, in effect buying their debt. Instead, it is morphing into a more targeted institution that lends directly to the troubled parts of the economy.

The immediate effect is that markets are discounting the possibility that Spain will not need to pay for its bank bailout, and the Spanish sovereign curve is trading 40-50bps lower according to Bloomberg data.

UK monthly services output was unchanged in April after a 0.6% m/m gain the prior month. Our UK economics team notes that it is going to be hard for this component to add to growth in Q2. June is likely to see a fall of around 1.2% m/m (based on what happened in April last year when there was a lost working day), so barring a miracle in May, we suspect that services output will shrink by 0.1% q/q during Q2 - compared to 0.1% q/q growth in Q1.

The harmonized 'flash' inflation number in Europe came in flat at 2.4% m/m in June (it was at 2.4% m/m in May as well). We know that inflation slowed in Germany, Spain and Belgium but increased in Italy. Lower energy prices were a factor for all of them (less so though in Italy), while colder than usual temperatures kept food prices higher.

Germany retail sales came in at -0.3% m/m in May, dragging down the national number to -1.1% y/y. The losses were fairly broad, but a -5.7% m/m change in IT sales stands out (that sector had been up by a matching 5.7% m/m in April. Car and vehicle sales were up by 1.4% m/m. French consumer spending data was stronger, however, up 0.4% m/m in May (0.6% y/y). Both annual numbers are low, highlighting the extent to which general European weakness is impacting the largest Eurozone economies.

China industrial profits data came out overnight and showed that industrial profits were 2.4% lower at month-end in May 2012 than they had been in May 2011. While there is sequential month-on-month growth (gross profits were CNY 1.8bn in May vs. CNY 1.4bn in April), the growth is slower than last year.

Japan released a host of economic data. CPI edged lower (-0.4% m/m in May) with indications that it will fall further in June (Tokyo June CPI fell by -0.6% m/m). Industrial production fell by 3.1% m/m and construction orders fell by 0.9% m/m.

CANADA

While markets are focused on Europe today and higher WTI prices should set the tone in Canadian markets, **April GDP** data will be released too. Scotia anticipates a muted gain of 0.2% m/m with high amounts of tail risk posed by volatility in commodities output during the month. On the basis of retail sales, housing starts, wholesale trade, and manufacturing output data, we would be tracking a slight contraction in GDP (approximately -0.1% m/m). Things get trickier, however, once we try to account for volatility in the natural resource sector during April. Potash and fertilizer plant that had been idled from January through March came back online in April providing a surge in output that echoed through a variety of macroeconomic aggregates (e.g., exports of fertilizers and fertilizer materials were up by 51.8% m/m). On the other hand, there were temporary maintenance-related shutdowns at oil and gas refineries resulting in lower output in the oil and gas sector. It's hard to say how the two swings will bear out in the aggregated data as oil and gas output is twice as significant as mining output — of which potash mining is a subset — but the relative magnitude of the swing in the agriculture sector was greater. We're expecting the surge in agriculture-related output to trump the oil and gas maintenance, hence our 0.2% m/m GDP call. The bottom line is that the Canadian economy is increasingly geared to commodities output, so much so that swings in fossil fuel and potash output are key factors in forecasting GDP.

UNITED STATES

Scotia expects a flat personal spending reading (0% m/m) and a slight increase in personal income (+0.1%) when PCE data are released today (8:30amEST). US consumers went on a car shopping spree during H1 2012, increasing the volume of car purchases by 12% over the 2011 average. This is somewhat of a surprise as job growth, while better than during 2011, was fairly subdued (164/k per month on average through May), while nominal personal income increased by a scant 1.3%. In part because of the spike in car purchases, personal consumption expenditure increased by 1.8% through April in nominal terms and +1.1% in real terms. The implication is that the shopping has been financed out of savings, and indeed the personal savings rate has fallen from 4.2% in December 2011 to 3.4% in April 2012. Average hourly wages were slightly higher in May (+0.1%) while retail sales, which include car sales, were lower by 0.2%. In short, it looks like there is a good chance that consumers retrenched during May.

Fixed Income	Government Yield Curves (%):											
	2-YEAR			5-YEAR			10-YEAR			30-YEAR		
	Last	1-day	1-wk	Last	1-day	1-wk	Last	1-day	1-wk	Last	1-day	1-wk
U.S.	0.31	0.30	0.30	0.71	0.69	0.76	1.62	1.58	1.68	2.73	2.68	2.76
CANADA	1.01	0.95	1.06	1.23	1.17	1.31	1.73	1.68	1.81	2.33	2.29	2.36
GERMANY	0.14	0.11	0.14	0.64	0.57	0.64	1.62	1.51	1.58	2.36	2.27	2.25
JAPAN	0.11	0.11	0.10	0.22	0.22	0.22	0.84	0.82	0.83	1.89	1.87	1.88
U.K.	0.28	0.27	0.32	0.74	0.68	0.74	1.72	1.64	1.72	3.03	2.96	2.96
	Foreign - U.S. Spreads (bps):											
CANADA	70	65	76	52	48	55	11	10	13	-40	-39	-41
GERMANY	-17	-20	-17	-7	-11	-11	-0	-6	-9	-36	-41	-51
JAPAN	-20	-19	-20	-49	-47	-53	-78	-76	-85	-84	-80	-88
U.K.	-3	-4	1	3	-0	-1	11	6	5	30	28	20

Equities			% change:			
	Last	Change	1 Day	1-wk	1-mo	1-yr
S&P/TSX	11424.70	13.76	0.1	0.1	-1.6	-13.4
Dow 30	12602.26	-24.75	-0.2	0.2	0.2	2.8
S&P 500	1329.04	-2.81	-0.2	0.3	-0.3	1.7
Nasdaq	2849.49	-25.83	-0.9	-0.3	-0.7	4.0
DAX	6308.79	158.88	2.6	0.7	-1.4	-13.5
FTSE	5573.17	80.11	1.5	1.1	3.4	-4.8
Nikkei	9006.78	132.67	1.5	2.4	4.0	-8.1
Hang Seng	19441.46	416.19	2.2	2.3	2.0	-11.9
CAC	3136.26	84.58	2.8	1.5	1.7	-20.1
Commodities			% change:			
WTI Crude	80.52	2.83	3.6	1.0	-11.3	-15.0
Natural Gas	2.78	0.06	2.2	6.0	14.5	-35.5
Gold	1558.50	-15.00	-1.0	-1.5	-1.0	4.0
Silver	27.08	0.27	1.0	1.0	-4.1	-21.3
CRB Index	271.81	-3.39	-1.2	1.7	-2.8	-19.8
Currencies			% change:			
USDCAD	1.0229	-0.0103	-1.0	-0.2	0.1	5.5
EURUSD	1.2580	0.0136	1.1	0.1	0.6	-12.9
USDJPY	79.53	0.0700	0.1	-1.1	0.1	-1.5
AUDUSD	1.0184	0.0139	1.4	1.2	3.4	-4.7
GBPUSD	1.5605	0.0086	0.6	0.1	-0.2	-2.8
USDCHF	0.9559	-0.0092	-1.0	0.1	-0.5	14.6

Source: Bloomberg. All quotes reflect Bloomberg data as at the time of publishing. While this source is believed to be reliable, Scotia Capital cannot guarantee its accuracy.