

Market Tone Improves On Easing In U.S.-China Tensions

- USD mixed vs. G10 as participants focus on individual developments.
- CAD steady just above last week's low; all eyes 10:30am ET oil inventory data.
- EUR rises on stronger IP and Italian fiscal developments; neutral/bearish.
- GBP recovers from fresh low under 1.25; all eyes on party confidence vote.
- JPY tentatively extending Monday's bearish reversal; wider spreads a headwind.
- AUD consolidates around midpoint of two month range; 1Y OIS below RBA rate.
- MXN extends recent recovery on improvement in market tone; IP data 9am ET.

FX Market Update - Markets are trading with a mostly positive tone overall; global stocks are firmer and US futures are higher, nudging top major bond markets slightly lower (US 10YY up 1bps). Major commodity prices are firmer also, with crude gaining a little less than 2% on the day and gold flat to very slightly higher. The USD itself is mixed versus its G-10 peers, with the GBP and EUR leading gains on the day while the SEK is under-performing after inflation data came in below expectations for a second time in two months – just ahead of next week's Riksbank policy meeting. Some relaxation in the Huawei issue after a Canadian judge granted CFO bail and President Trump suggested he could intervene in the issue if it would help US/China trade policy helped lift risk sentiment. The CNY and MXN are marginally higher, reflecting better risk sentiment while the TRY weakened in response to news that Turkey will launch military operations in Syria "within days". President Trump also told Reuters that the Fed would be "foolish" to raise interest rates next week and that the Fed is being "far too aggressive", however. The US releases CPI data at 8.30ET, with headline price growth expected to come in flat in the month and slow to 2.2% (from 2.5%) in the year. Canada releases house prices data but the main focus for market will be on the UK Conservative party's leadership confidence vote that was announced early this morning – the outcome of which will help shape the course of the Brexit debate in the UK. The GBP's gains earlier reflect market speculation that PM May will win this face off but the margin of the victory will be an important indication of how May's Brexit policy can proceed through parliament if she does win. The outcome of the confidence vote is expected around 9pm London time today (16.00ET).

USDCAD (1.3379) • The CAD is quietly consolidating for a second consecutive session and hovering just above last week's 18 month low. Broader developments remain dominant in the absence of domestic releases and the CAD remains strongly correlated to the price of WTI, which appears range bound in the mid/lower-\$50/bbl area. Risk is elevated into the 10:30am ET EIA inventory release, following last night's sizeable API draw. Domestic rate expectations are showing signs of stabilization at muted levels with OIS pricing roughly 20bps of BoC tightening by April. U.S.-Canada yield spreads remain wide with the 2Y and 5Y holding above 70bps as the 10Y threatens fresh highs around 80bps. A high frequency fair value estimate using the 2Y and 5Y spreads as well as a Terms of Trade index currently has USDCAD in the lower 1.33s. We remain cautious on the basis of bearish seasonals, given the CAD's tendency to weaken into year end and only base around the end of January.

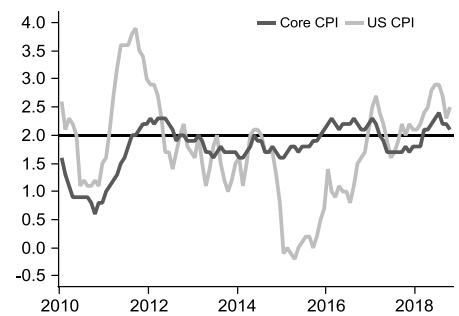
USDCAD short-term technicals: bullish-neutral—momentum indicators are bullish and the DMI's are confirming as USDCAD continues to trade within the ascending trend channel from early October. The channel floor is currently just above 1.33 and the ceiling is around 1.3520. Recent congestion has centered around the June high at levels roughly corresponding to a pair of key longer term technical levels including

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Shaun Osborne
Chief FX Strategist
416.945.4538
shaun.osborne@scotiabank.com

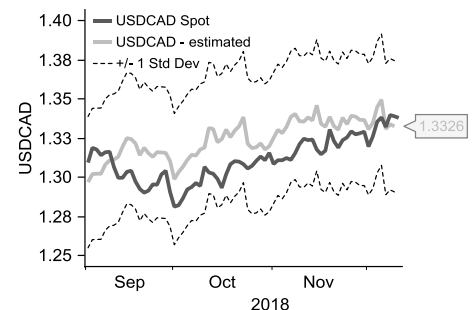
Eric Theoret, CFA, CMT
FX Strategist
416.863.7030
eric.theoret@scotiabank.com

U.S. CPI - Headline Expected At 2.2% Y/Y



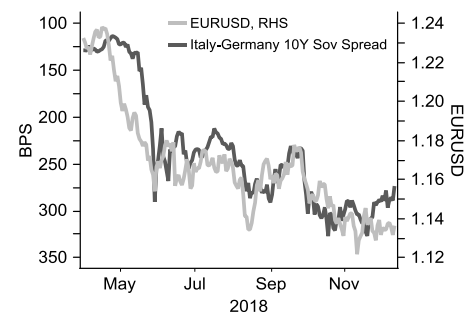
Source: Macrobond, Scotiabank FICC Strategy

USDCAD Vs. Estimated Fair Value



Source: Macrobond, Scotiabank FICC Strategy

EUR Ignoring Bund-BTP Spread



Source: Macrobond, Scotiabank FICC Strategy

the last major retracement of the May-Sep 2017 decline (1.3384) and the midpoint of the range from 2016 (1.3376). Near-term resistance is expected above 1.3420.

EURUSD (1.1326) • Eurozone Industrial Production rose a stronger than expected 0.2% in Oct but the Sep decline in output was revised to a more significant -0.6% from the preliminary -0.3% outcome. We continue to think that the Eurozone economy can rebound from some of the temporary headwinds it has encountered in H2 this year and look for above potential growth to keep the ECB on track for a modest policy adjustment later in 2019. We remain positive on the broader outlook for the EUR as a result but recognize that short term price trends are getting caught up in GBP volatility.

EURUSD short-term technicals: neutral/bearish – EURUSD's drift lower off the early week high has consolidated overnight (potential bear flag) and broader price signals remain tilted towards the negative after Monday's sharp fall from the low 1.14s (rejection of potential break out resistance). We see support at 1.1320 and at 1.1300 resistance at 1.1350/60.

GBPUSD (1.2564) • PM May will contest a leadership vote of confidence today among the parliamentary Conservative party. May needs a majority of 50% + 1 of the 315 Tory MPs (so 158) to retain the leadership position and the BBC is reporting that 158 MPs have declared they will support her. But we note that public displays of affection do not count for much in a secret vote. If she does win, the margin of the victory will be important; a crushing victory should shut down the sniping of the hard Brexit crowd while losing the support of 80-100 MPs would be a pyrrhic victory at best – and the problem of advancing her policy through parliament would remain (and perhaps become even harder). A win might increase the odds of an early election. GBP uncertainty renewed and we suspect that the pound may struggle to sustain short-term gains.

GBPUSD short-term technicals: neutral/bearish – Short-term patterns look a bit more constructive for Cable, with the pound squeezing off the overnight low after twice failing to crack under 1.2480 (now support). We see resistance at 1.2650/60 and, stronger, at 1.2700/25.

USDJPY (113.44) • JPY is slightly softer and tentatively extending Monday's bearish reversal in an environment of lingering risk aversion. The modest recovery in U.S. yields is bearish for JPY and delivering pressure via wider yield spreads. Measures of implied JPY volatility remain muted and risk reversals are range bound suggesting no meaningful change in the premium for protection against JPY strength. Core machine orders data were softer than expected and weighed modestly on the JPY. Tankan sentiment and industrial production figures are scheduled for release on Friday (Thursday NA evening).

TECHNICALS: BUY/SELL SIGNALS AND PIVOT LEVEL **Dec 12, 2018**

	30 Day Hist Vol	Spot	MACD	9 & 21- day MA	DMI	RSI	Pivot 1st Support	Pivot 1st Resist.
USDCAD	6.2	1.3379	buy	buy	buy	61	1.3357	1.3412
EURUSD	6.9	1.1326	buy	sell	buy	46	1.1288	1.1382
GBPUSD	10.0	1.2564	sell	sell	sell	37	1.2482	1.2643
USDCHF	4.7	0.9965	sell	sell	sell	50	0.9898	0.9996
USDJPY	5.2	113.44	sell	sell	sell	53	113.13	113.64
AUDUSD	8.6	0.7208	sell	sell	sell	46	0.7185	0.7230
USDMXN	11.3	20.1167	sell	sell	sell	48	20.04	20.27
DXY (USD index)	6.1	97.38	buy	na	buy	58	96.99	97.66
EURCAD	6.3	1.5153	buy	buy	buy	56	1.5103	1.5238
GBPCAD	10.8	1.6809	sell	sell	sell	45	1.6689	1.6942
AUDCAD	5.9	0.9644	sell	buy	buy	56	0.9624	0.9668
CADMXN	11.4	15.04	sell	sell	sell	42	14.99	15.13

Source: Scotiabank & Bloomberg

TODAY'S CALENDAR

Time (ET)	Country	Release	Period	Consensus	Last
08:30	US	CPI MoM	Nov	0.0%	0.3%
08:30	US	CPI YoY	Nov	2.2%	2.5%
08:30	US	CPI Ex Food and Energy MoM	Nov	0.2%	0.2%
08:30	US	CPI Ex Food and Energy YoY	Nov	2.2%	2.1%
09:00	MX	Industrial Production NSA YoY	Oct	1.8%	1.8%
14:00	US	Monthly Budget Statement	Nov	-\$198.0b	-\$100.5b
19:01	UK	RICS House Price Balance	Nov	-0.10	-0.10
02:00	GE	CPI MoM	Nov F	0.1%	0.1%
02:00	GE	CPI YoY	Nov F	2.3%	2.3%
02:45	FR	CPI MoM	Nov F	-0.2%	-0.2%
02:45	FR	CPI YoY	Nov F	1.9%	1.9%
03:30	SZ	SNB Sight Deposit Interest Rate	13-Dec	-0.75%	-0.75%
03:30	SZ	SNB 3-Month Libor Lower Target Range	13-Dec	-1.25%	-1.25%
03:30	SZ	SNB 3-Month Libor Upper Target Range	13-Dec	-0.25%	-0.25%
03:30	SW	Unemployment Rate	Nov	5.7%	5.5%
04:00	NO	Deposit Rates	13-Dec	0.75%	0.75%
04:00	SZ	SNB's Jordan speaks			
07:45	EC	ECB Main Refinancing Rate	13-Dec	0.00%	0.00%
07:45	EC	ECB Marginal Lending Facility	13-Dec	0.25%	0.25%
07:45	EC	ECB Deposit Facility Rate	13-Dec	-0.40%	-0.40%

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