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Global Radar Screen

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DE Tactical and Strategic U.S. and Global Fixed Income Prospects: September 9, 2011			
Country/Region	**Tactical**	**Strategic**	**Comments**
United States			
Fed—Fed Funds	*Stable*	*Stable*	Fed takes the no-hike pledge to mid-2013 but could break it at any time (we hope).
2-yr. Treas.	*Neutral*	*Higher*	Obama's $450B plan may only keep growth above 2%.
10-yr. Treas.	*Neutral*	*Higher*	And 2% GDP growth and 2% inflation still supports sub 4% 10-year yields.
Eurozone			
ECB—Refi Rate	*Stable*	*Stable/lower*	Real economy softening, especially around the periphery and in regard to the consumer. Banking sector and widening sovereign debt problems even clearer, despite latest Eurozone efforts. ECB policy reversal possible-bond buying/liquidity injections.
Bund (10-year)	*Neutral*	*Stable*	Despite ECB worries to the contrary, sizeable output gap, exacerbated by increasing fiscal tightening, suggest no domestic inflation risk, especially given fragile banking system and inter-related still soft monetary data.
United Kingdom			
BoE—Bank Rate	*Stable*	*Stable*	Substantial easing in place, but lending backdrop still weak. MPC splits about inflation risks are clear. BoE on hold for some time.
Gilts (10-year)	*Neutral*	*Higher*	Economy has lost momentum as fiscal tightening starting to come through, with consumer the key downside risk.
Japan			
BOJ—Call rate	*Stable*	*Stable*	More easing coming soon but only baby steps.
JGB (10-yr.)	*Neutral*	*Higher*	Outlook is uncertain, but huge looming supply, exacerbated by quake rebuilding costs.
Tactical or "Short-Term"- 2 weeks to 2 months; Strategic or "Longer-Run" - 6 mos. to a year or more. Bold shading denotes change in view			

Overview—Scotty, Give Me More Stimulus! The 2008/09/10 Plans Aren't Enough!

Investors have a strong sense of déjà vu now that Obama announced yet another stimulus package. It is hard to forget how excited analysts (and equity investors) got talking about the 2010 plan, with growth of 4% bandied about as likely. It didn't happen, in part because most of the 2010 stimulus went into the gas pump. Now some prominent analysts estimate a 2 percentage point boost to GDP growth which could make the 4% growth target possible again. But investors won't be burned twice and are incorporating smaller changes to their GDP and earnings outlooks. Many may have already factored-in much of Obama's package into their existing forecasts, such as the extension of the employee payroll tax cut or the extension of unemployment insurance benefits. In addition, even though the proposals are familiar and enjoy bipartisan support, not all will be adopted by Congress, making the package potentially much smaller. If the package is paid for immediately with offsetting outlay cuts or tax increases, the simulative powers become very small. Finally, with expectations so depressed among households and small businesses, many forecasters will be prudent and argue Obama's plan will only solidify their existing forecasts. We would be surprised if many analysts put GDP growth above 3.5% in 2012, a pace that might be as much as 1 percentage point above where they were before the speech. But it would be hard to carry much less than 2.5% to 3% growth next year which is a lot better than 1% to 2% many worry about. Unfortunately, for Obama, who is trying to keep his own job next year, even 3% GDP growth might not lower the jobless rate very much. Even an "8" handle on the unemployment rate would normally scuttle a sitting president's reelection chances. Obama may be saved if the Republicans put up their own ideologically pure version of George McGovern, who got only 38% of the popular vote and a meager 17 electoral votes in 1972. The more the Republican candidates talk about dismantling popular programs like Social Security and Medicare, more likely the candidate who energizes the Republican "base" is less likely to become president.

- **U.S.**: A heavy data calendar may not add much to our store of knowledge. The CPI and PPI updates will be decent and retail sales should advance moderately. Investors will be more attuned to the Congressional reaction to the Obama stimulus plans and any last minute maneuvering by FOMC officials prior to the September 20/21 meeting.

- **Eurozone:** The better IP updates on tap may be at odds with the recent survey data. The jobs update may be downbeat and the HICP final estimate may show a downward revision. The ECB bulletin may provide more details on banking sector problems, while the latest ECB buying announcement and Italian/Spanish bond auctions will be noteworthy.

- **United Kingdom:** Plenty of important data arrive, headed by the CPI numbers which will be the calm before the Sept. storm when inflation picks up noticeably. Widespread weakness may be evident in labor market update and retail sales

- **Japan:** The main item this week is will be the MOF business survey tracking the post-earthquake industrial recovery, well before the more closely examined Tankan survey. Activity has not yet quite re-attained the pre-disaster peak, and there is serious question as to how strong the post-rebound trend will be. Both the tertiary industry and IP reports will give an update on the transition from disaster-rebound to medium-term growth.

- **Emerging Markets/Regions:** No major EM central bank we follow meets this week, leaving them more time to watch the bobbing and weaving of their Western European and American counterparts.

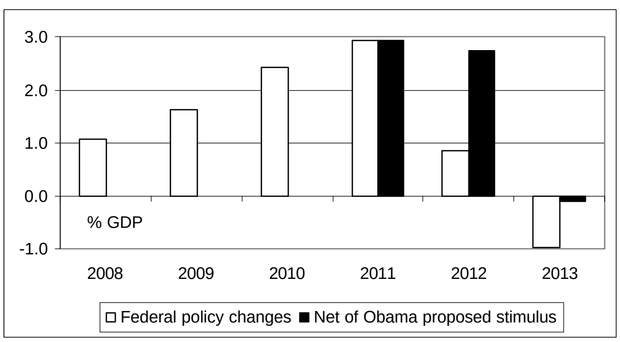
Specific Regional Themes

- **U.S.: Finally Some Data to Help Us Forget**

Fiscal policy has turned stimulative in 2011 with the passage of the compromise tax plan last December (white bar in Chart 1). We had been worried that policy would turn very restrictive in 2011 without some additional near-term stimulus as the impacts of the 2008 stimulus plan had peaked in mid-2009. This strategy to go for growth is understandable given the high unemployment rate and still sluggish recovery.

But the decision was playing with fire as the $200B in added stimulus this year was not tied to medium term fiscal consolidation. Now Obama wants to fix that problem in a more poisoned political climate post the debt ceiling debacle. Even if the White House gets all it wants from the $450B package, fiscal drag would be virtually eliminated in 2012 (black bar). This is another good reason why firms are not upbeat about 2012, as fiscal policy would be neutral after providing 1 percentage point of stimulus annually from 2008 to 2011.

Chart 1: Will Fiscal Policy Hurt Growth in 2012?



The indicator calendar is heavy, with decent inflation readings taking a back seat to the **retail sales** update. Both DE and consensus are carrying decent increase (DE: +0.5%; consensus +0.3%). The **PPI** (Wed) may actually decline in August DE: +0.1%, consensus -0.1%), while the core gain is close to trend. The **CPI** (Th) will be close to trend as weak commodity prices play a smaller role (DE: +0.3%; consensus: +0.2%.

IP is likely to fall moderately based on the jobs report (DE: _0.2%; conensus+0.1%. But there will be more interest in the timelier **empire state survey** and **Philly Fed** (all Th) for hints of some bounce from depressed levels in August.

The Reuters/Michigan **consumer sentiment index** (Fri) may be relatively steady (DE and consensus: 56.5) after the nine point slump in August. The report may come to late to get much bounce from Obama's speech.

Only a few Fed speakers are on tap again. Fed chairman **Bernanke** makes introductory remarks at a Fed academic conference in DC (Th), while St Louis president **Bullard** (voter 2013) does the same before a Fed TV event (Mon). The always entertaining Dallas Fed czar **Fisher** (dissent voter 2011) give and outlook speak (Mon), while Fed governor **Tarullo** gives a talk at the Fed conference (Fri). (M. Cary Leahey)

- **Eurozone: Better Output Numbers**

The upbeat results from Germany and France so far imply that the **Eurozone industrial production** data (Wed) should show a very clear bounce (Consensus: 1.5% M/M; DE: 2.0%), albeit with the data possibly suggesting a fresh divergence is occurring between northern and southern economies. **Italian output** data (Mon) will give a clearer picture.

Even so, the Eurozone output data may look at odds with the downbeat nature of recent business survey data. However, a more downbeat picture may emerge in regard to **Eurozone employment numbers** (Thu).

Also on Thursday, **final Eurozone HICP** data arrive, which may reveal a downward revision to the flash estimate (Consensus: 2.5% Y/Y; DE: 2.4%) as well as some further drop in core measures: a clearer picture will emerge after **Spanish and French CPI** data on Tuesday, with **Eurozone labor cost** data (Fri) underscoring the lack of domestic inflation pressures.

Otherwise, the **ECB Monthly Bulletin** may get more attention than usual, especially if it provides details regarding the problems that the Eurozone banking system is having at present. There will be the usual interest in the **ECB bond-buying announcement** on Monday as well as some key **bond auctions** in the likes of Italy (Tue) and Spain (Thu).

- **United Kingdom: Key Data Await**

There is plenty of important data in the coming week. **CPI numbers** (Tue) may be the calm before the storm as only from the data due in the next month will the much-flagged utility price rises push the Y/Y rate appreciably higher. In the interim, these next CPI data should see the Y/Y rate little changed (Consensus: 4.5% Y/Y; DE: 4.4%).

Wednesday sees the **labor market update** where more widespread weakness may be evident, ie not just in the unemployment figures (Consensus: 32K; DE: 25K), but also in employment too. **Average earnings** growth should remain soft (Consensus: 2.7% Y/Y; DE: 2.5%), still consistent with a squeeze on spending (Consensus & DE: -0.3% M/M).

Retail sales figures (Thu) should highlight this squeeze with fresh weakness expected. Otherwise, the week sees **visible trade** data and the **RICS housing market survey** on Tuesday with the latest **BoE household inflation expectations** survey on Thursday.

- **Other Europe: SNB Thinking After the FX Vow**

In **Sweden, CPI data** (Tue) may reveal a clear slowing in both headline and core numbers, while the **labor market** update (Thu) may still show clear robustness, albeit still consistent with some softening having occurred of late.

There is little of note in **Norway** in the coming week.

Switzerland has the **quarterly SNB assessment** due on Thursday morning. This has lost much potential interest now that the SNB has already revealed its hand with its decision in the last week to target the exchange rate against the euro with unlimited intervention. Even so, it will be interesting to see if the SNB acknowledges the resilience in the economy to date, while – in regard to policy – markets may be keen to find out to what extent the central bank plans to sterilize its FX intervention.

- **Oceania: RBNZ Policy Pause**

In **Australia**, a quiet week lies ahead in terms of economic data. The week sees a number of survey updates, including the **NAB business confidence** (Tue) numbers and the **Westpac consumer survey** (Wed). The only other data of note are **visible trade** numbers arriving on Monday.

In **New Zealand**, the week begins with Q2 **manufacturing activity** numbers and **QV house prices** (both Tue). But all of the attention will be on the **Reserve Bank of New Zealand policy decision** on Thursday, where rates are generally expected to remain unchanged. The **Performance of Manufacturing Index** (also Thu) then completes the week. (Andrew Wroblewski)

- **Japan: MOF Survey**

The signal item in this relatively quiet week is likely to be the quarterly **Ministry of Finance Business Outlook Survey**, arriving Monday. Governor Shirakawa has identified potential damage to business confidence as the major near-term threat from the strengthening of the yen, and the MOF Survey will give a reading weeks in advance of the Bank of Japan's own, far more massive, Tankan Survey. Monday also brings July **tertiary-industry activity** data, tracking the post-earthquake recovery of the single biggest sector in the production-side accounting of the economy. Activity has not yet quite re-attained the pre-disaster peak, and there is serious question as to how strong the post-rebound trend will be. The only other closely watched data release of the week will be the revised July **industrial production** report—giving, like the tertiary-industries data, an update on the transition from disaster-rebound to medium-term trend growth. (Pierre Ellis)

- **Emerging Markets: Central Bank Watch:**

No major EM central bank we follow meets this week. Like most of us, they are sitting back and watching developments in Western Europe and the U.S. (Andrew Husby)