



GLOBE AT A GLANCE – Andrew Wroblewski, London / M. Cary Leahey, New York

Equities: Europe lower, Asia mixed. Japanese equity markets closed higher. Other major Asian markets were mixed, however. European bourses fell through early morning trade, before then moving mostly sideways as midday approached, dragged down by weak survey data for the region and ongoing worries about Greece.

Bonds: Europe mixed, Japan lower. JGB prices fell across nearly all maturities, with the yield curve steepening on the medium to long-term end. European bond prices saw continued divergences, however, with German, French and Portuguese markets flat-to-higher, but other peripheral markets, Greece and Spain in particular, lower.

Currencies: Weaker yen. The dollar rose against the yen through both the Asian and morning European sessions, moving higher on net to around ¥/\$ 80.14. Against the euro, the US currency see-sawed through both sessions, trading little changed near \$/€ 1.33.

Eurozone: Contracting afresh? The February flash PMIs suggest that Eurozone economic activity is at best stabilizing into the current quarter but may have contracted afresh.

United Kingdom: BoE split. Surprising most, the minutes from the 8-9 February BoE MPC meeting showed the committee split over the decision to enlarge the asset purchase program a further £ 50 bln.

China: Less steep contraction in manufacturing. The February flash HSBC/Markit manufacturing PMI rose by 0.9 point to 49.7.

Taiwan: Growth slowdown revised, economy still entered recession. Updated national accounts data still showed GDP growth slowing further in Q4, but with the fall back revised slightly downwards to 1.89% Y/Y.

U.S. ECONOMIC AND CREDIT MARKET OUTLOOK – M. Cary Leahey

Treasuries The yield curve steepened with the 10-year backing up 5 bp to 2.06% while the 2-year rose 1 bp to 0.30%. The 10-year yield had been 1.8% at the beginning of the month, before the new round of promising US data started to hit the tape.

Data/event recap: There were no indicators or Fed utterances.

DAILY CALENDAR

We start today with ICSC/GS chain store sales index (07:45 EST/12:45 GMT), the Redbook chain store sales index (08:55 EST/13:55 GMT) and existing home sales (10:00 EST/15:00 GMT). We have no Fed policymakers to worry about today.

Chain store sales showed a mixed tone last week, with the Redbook firming to a 2.7% y/y comparable store sales gain from 2.5% while the ICSC/GS index faded from 3.5% y/y gain to 2.8%. The ICSC/GS index is a bit below its 3.0% to 3.5% full month target. Both indexes are in the lower end of their recent ranges. Special factors such as milder weather and the timing of Valentine's Day and the Super Bowl worked in different directions on sales making it hard to interpret recent sales trends. In fact, February is a slow (and sometimes volatile) month for sales as little of the spring merchandise has been rolled out so no strong conclusions can be drawn from the generally slower pace in the last month.

New and existing home sales have been going in different directions in this expansion. Existing home sales have risen over 15% relative to their early 2009 lows, while new home sales have fallen almost 10%. **Existing home sales** are expected to rise modestly (DE: +1.5% to 4.68M; consensus: +1.1% to 4.66M). The months supply of inventories, which has fallen steadily from 9.5 months in July to 6.2 months in December, close to historical average of 6.5 months. The visible supply may bounceback a bit, particularly if some of the shadow inventory of current foreclosures is released to the market. The Fed expects a sizeable increase in REO (real estate owned) inventory this year of as much as 1.9M units compared to 1.1M in 2011 and 0.6M in 2010, which is the single largest impediment to the recovery in the housing market.

CANADA – Melissa Pumphrey, New York

(Tuesday) Retail sales buck earlier trends and decline on autos. December retail sales fell by 0.2% (Consensus: -0.2%, Decision Economics: unch) to \$38.8 billion, following a November figure which was revised upward from +0.3% to +0.4%, on below par holiday spending on automobiles and auto parts. Ex-auto retail sales remained unchanged (Consensus: +0.1%, Decision Economics: +0.4%), as increases in supermarket and food and beverage sales were offset by disappointing sales at department and electronics stores. This month's drop follows four months of increases; however, in volume terms retail sales were unchanged. Motor vehicles fell by 1.0% m/m to \$8.69 billion, gasoline sales dropped by 1.1% m/m, and auto parts sales declined by 9.4%.

December data differed markedly from the trends in 2011. Retail sales were up 3.6% y/y, and 1.6% in volume terms, largely due to increases in motor vehicles (+6.2% y/y), gas stations (+3.9% y/y), and auto parts (+6.9% y/y). Every Canadian province posted increases in retail sales in y/y terms.

Weak retail sales suggest decelerating domestic demand. With rising unemployment and historically high household debt-to-income ratio, consumer spending may be limited in its contribution to GDP growth in 2012.

(Tuesday) Wholesale sales continue to rise on food and autos. Wholesale sales increased by a more-than-anticipated 0.9% m/m (Consensus and Decision Economics: +0.6%) to \$49.6 billion and brought the y/y gain to 7.4%. This marked the seventh increase in the last eight months and was largely based upon increases in the motor vehicle (+3.4% m/m) and food, beverage, and tobacco (+1.9% m/m) sectors. In volume terms, the index posted a 1.3% m/m gain. Wholesale sales growth was concentrated in the eastern provinces. Inventories also increased by more than anticipated, +1.4% (Decision Economics: +0.2%), on increases in agricultural supplies (+9.9% m/m).

Wholesale sales received a boost from motor vehicles as kinks in the supply chain from Japan appear to have finally been repaired.

WESTERN EUROPE – Andrew Wroblewski, London

EUROZONE – Contracting afresh? The February flash PMIs suggest that Eurozone economic activity is at best stabilizing into the current quarter but may have contracted afresh. Indeed, the aggregate PMI reading for the Eurozone softened for the first time in four months, actually slipping slightly to levels marginally consistent with contracting activity for the whole Eurozone and to a more clear-cut fall outside of France and Germany. Even so, the survey carried mixed messages.

On the less downbeat side, the manufacturing PMI rose for the third month in succession, albeit with the 0.2 point rise to 49.0 being the smallest in that sequence and much softer than the 1.9 points January jump. Notably, while the headline figure remained well below the long-term average, there were less ominous signs offered by parts of the survey break-down, including a continued but less steep fall in overall orders (including those for exports) which led to the forward-looking order/inventory ratio remaining close to the seven-month high posted in January. However, there was continued weakness on the job front.

Possibly more gloomily, the flash services PMI also undershot expectations in sliding from a five-month high and ending a run of three successive rises. Specifically, it fell 1.0 point to 49.4. However, more promisingly, service sector respondents saw new orders drop less clearly while confidence about the coming year rose for the fourth successive month and to the highest since last July.

As for price pressures, these also showed mixed messages but with overall prices charged falling for the fifth successive month, despite higher input costs.

Comment: *These PMI flashes may disappoint, but perhaps not too much should be read into them. For a start, the mixed messages in the data are too imprecise to suggest anything at this juncture but that the activity in the Eurozone overall has largely stabilized. In addition, weaker February readings should not be that much of a surprise given the very cold weather that hit Europe through the month, something that will very clearly have hit activity. As a result, it is still more likely than not that the Eurozone may be able to avoid any deeper contraction in the current quarter than the 0.3% Q/Q drop posted in Q4. Therefore, these survey data continue to suggest that while downside economic risks are still very much evident they are yet to materialize any further. Mainly this seems to be result of resilience in Germany and (to a lesser extent) France, with the German PMI readings still in conflict with more upbeat activity levels that other alternative-sourced surveys (such as Ifo) have for some time been pointing to.*

Regardless, these and other survey data continue to suggest that the rest of the Eurozone is still contracting clearly. As a result, these numbers will still be causing some consternation within the ECB, even if they (alongside further hints of an improvement in consumer confidence) can be said to be consistent with signs of a tentative stabilization in activity that the central bank has pointed to of late. Even so, it is clear that any such stabilization is still at low levels, still implying that risks of more than a mild recession remain, (particularly outside of France and Germany).

As for the causes of this stabilization, less weak global economic conditions are implicit in the survey findings as may be the dampened turmoil in Eurozone financial markets. More specifically, it seems companies are eating into backlogs in order to sustain output while also making heftier discounts to boost sales. The former (of course) cannot be sustained for ever, while the latter should add to the disinflation backdrop that has tentatively resumed in the Eurozone. Even so, these PMI data will make the ECB feel more justified in continuing its wait-and-see approach, albeit with the central bank still very aware that the fragile growth backdrop could easily see peripheral bond market turmoil intensify again.

Orders bounce back. Showing more of a bounce than many had expected, industrial new orders jumped 1.9% M/M in December, more than unwinding the little-revised 1.1% November drop, but very much leaving in place the clearly volatile pattern seen of late. Even so, the November figure was not a reflection of broad-based weakness given the clear drop back in consumer and transport orders. Even so, on a Y/Y basis, orders growth turned less negative at -1.7%.

(Tuesday) Consumer sentiment edged back up. Matching expectations, the flash consumer confidence reading for February rose to -20.2 from -20.7 in the preceding month, thereby up further from the 28-month low set in December.

GERMANY – Softer survey messages. The February flash PMI numbers revealed somewhat softer fortunes for the private sector, but still suggesting clear, positive overall rates of growth. The manufacturing PMI fell 0.9 point to 50.1 unwinding half the gain of the previous month. It was still undermined by falling orders at both home and abroad and softer output growth.

Furthermore, the services PMI was (for once) weaker than expected, slipping 1.1 points to 52.6, down from the seven-month high set in January, but with the fastest growth in new work since last July.

Construction drops afresh. December construction orders decreased by 2.9% M/M, partly unwinding the large bounce seen in the previous month (10.1%), but still being the fourth drop in the last five months of data. The latest fall was broad-based but still resulted in the Y/Y rate turning more positive at 13.7%.

FRANCE – Mixed messages. Showing somewhat mixed messages, but still consistent with the economy growing modestly, the February flash PMIs again moved in opposite directions. Most notably and very clearly undershooting expectations, the services PMI dropped for the first time in four months, easing from a five-month high of 52.3 back to 50.3. Even so, business expectation rose to a six-month high. Meanwhile, the manufacturing PMI bounced afresh, with the 1.7 points rise to 50.2 taking it to a seven month high. The data showed more an easing in output and orders weakness, the latter helped by a recovery on the export side.

Inflation falls. Undershooting expectations for once, headline CPI inflation dropped 0.2 percentage point to 2.3% Y/Y in January, easing from a cycle-high. In M/M terms, prices decreased 0.4%, a reflection of fresh food and clothing price declines.

The breakdown showed that the Y/Y rate was trimmed by the steeper fall in clothing prices, the latter helping pull back the core inflation (excluding fresh food, energy and taxes effects) by 0.3 percentage point to 1.5% Y/Y, a three-month low. Meanwhile, EU-harmonized inflation also fell last month, but only by 0.1 percentage point and to 2.6%.

ITALY – Inflation edges down. Matching preliminary numbers, final data showed that consumer price inflation slipped 0.1 percentage point to 3.2% Y/Y in February, thereby down a further notch from an October reading of 3.4% that was the highest in three years. Overall, prices rose by 0.3% in M/M terms, while the core rate also eased a notch (to 2.3% Y/Y). Meanwhile, the EU-harmonized measure dropped more clearly, by 0.3 percentage point to 3.4%.

OTHER WESTERN EUROPE

UNITED KINGDOM – BoE split. Surprising most, the minutes from the 8-9 February BoE MPC meeting showed the committee split over the decision to enlarge the asset purchase program a further £ 50 bln. However, rather than dissenting against any enlargement as some had suggested, the two votes against the decision (from MPC members Miles and Posen) were actually in favor of a larger increase (ie of £ 75 bln).

However, not too much should be read into this split. Indeed, comments from Posen in the last few days underscore that his thinking is largely consistent with the BoE outlook as evident in the Inflation Report this month. Admittedly, there was some discussion suggesting more of a split in the committee than the vote would suggest, with some members envisaging somewhat larger upside risks to inflation than in the Inflation Report, something that provided a case for no additional stimulus being provided at all. Most likely, these members may have been concerned about productivity and profit margins, issues that have clearly bothered the MPC for some time. In addition, the slightly better economic signs may have had some impact on overall thinking

More likely than not therefore the decision to enlarge the asset purchase program by a further £ 50 bln was something of a compromise, with an added rationale being that any larger increase may have surprised markets to a degree that may have led to the impression that the MPC was more concerned about the economy than it actually was.

With this in mind, these minutes offer nothing of major note to the policy outlook, certainly not providing any suggestion of a greater predilection to further stimulus than the even-handed outlook offered by the Inflation Report. Instead, the MPC reaction function remains very much data-driven. Against this backdrop, further stimulus may be on the cards but it may not arrive as soon as the current asset purchase program is completed in May.

SWEDEN – Unemployment no longer falling? Coming in slightly above expectations once again, the (unadjusted) unemployment rate still fell further in January relative to its year-before counterpart. At 8.0%, it was 0.2 percentage point below that of the same month in 2011, a less clear-cut Y/Y drop to that evident in previous readings. However, seasonally adjusted numbers confirm that underlying joblessness is no longer falling (now at a rate of 7.6%). In addition employment growth has also come to a standstill.

NORWAY – Better jobs data. The seasonally adjusted unemployment dropped a notch to 3.3% in the three months to January, suggesting an end to the slight uptrend in previous months. Regardless, there were more encouraging signs of an increase in employment as the data did show a continued rise of 0.4% in the last three months, helping to push up the Y/Y change in employment growth to 2.1%.

ASIA – Chang Liu, London

CHINA – Less steep contraction in manufacturing. The February flash HSBC/Markit manufacturing PMI rose by 0.9 point to 49.7, a seventh sub-50 reading in the past eight months, albeit now the third-strongest outcome in that cycle. The latest result reflected a swing back into expansion for employment and inventories, undermined by a swing into contraction for new export orders.

Commenting on these results, HSBC noted that the marginal improvement seen this month was led by quickened production following the New Year holidays. Looking ahead, the Bank saw no meaningful recovery in domestic demand and with external weakness becoming more evident, HSBC called on the PBoC to ease policy further after its first reserve requirement ratio cut last weekend.

MALAYSIA – Inflation falls further. Coming in slightly below expectations, consumer price inflation fell by 0.3 percentage point to 2.7% Y/Y in January, building on a same-sized drop in the previous month and now a fresh cycle-low. In M/M terms, prices picked up by 0.3%, boosted by food and education costs. The Y/Y breakdown, meanwhile, revealed the latest moderation to be a reflection of falls in price pressures for food (4.8% from 5.1%), clothing (-0.5% from 0.8%) and transport (1.6% from 1.9%), but being undermined by a slight pick up in utilities (1.8% from 1.7%).

TAIWAN – Growth slowdown revised, economy still entered recession. Updated national accounts data still showed GDP growth slowing further in Q4, but with the fall back revised slightly downwards to 1.89% Y/Y from an initial estimate of 1.90%. This revision still left growth down clearly on the Q3 gain of 3.45%, the slowest pace in over two years. On a seasonally adjusted Q/Q basis, GDP actually saw a 0.15% drop (revised up from a 0.25% fall), still a second consecutive contraction following the (also upwardly revised) 0.05% decline in the previous quarter and dragging the economy into recession.

The expenditure breakdown (all purely in Y/Y terms) showed a fairly broad based deterioration across components. Indeed, private consumption expenditure growth slowed clearly to 0.98% from 3.24% in Q3, but government spending growth actually improved to 3.17% from 2.43% (revised up clearly from the advance reading). Capex growth, meanwhile, was also revised upwards, but still showed a clear fall from the last quarter of 12.41% following the 9.13% Q3 contraction, now the largest decline in the cycle. Elsewhere, net trade continued to provide a modest boost to growth, with export growth slowing to 0.78% from 2.10% but imports turning more negative with a drop of 7.23% after a 3.72% fall in the previous quarter.

On the output side, the data showed a swing into a contraction for the secondary sector (-1.71% Y/Y from 3.12) alongside a drop in growth for the tertiary sector (1.32% from 2.82%), all outweighing improvements in the primary sector (3.45% from -0.52%).

Notably, the latest report also showed GDP growth for 2011 to be 4.04%, slightly above the preliminary estimate of 4.03%. Also notable, following today's report the Government revised down its GDP forecast for 2012 to 3.85% from 3.19% previously, but with inflation now projected to be around 1.46% this year from 1.29% previously.

Labor market conditions improve. The seasonally adjusted unemployment rate fell by 0.02 percentage point in January to 4.19%, a second successive fall and still the lowest since August 2008. The level of unemployment, meanwhile, fell for the twenty-third-straight month, this time by 8.76% Y/Y, a less steep drop than the 9.42% fall in the previous month and now the second-weakest decline in the cycle. Elsewhere, the level of employment rose by 1.75% Y/Y last month, down slightly from the 1.78% increase in December and the second-weakest gain in the cycle.

SOUTH AFRICA – Chang Liu, London

Inflation rises. Exceeding expectations, consumer price inflation rose by 0.2 percentage point to 6.3% in January, a new cycle-high. The result was the thirteenth increase in the past fifteen months, boosted by rising price pressures for food and transport. Meanwhile, on a M/M basis, prices rose by 0.6%.

It is worth noting that headline inflation exceeded the upper limit of the Bank's target range of 3-6% for a third consecutive month.

OCEANIA – Chang Liu, London

AUSTRALIA – Wage growth picks up. According to the Australian Bureau of Statistics, wages rose by 1.0% Q/Q in Q4, a larger gain than Q3's 0.7% rise, surprising to the upside and now the joint-largest increase in the cycle. This latest outcome was a reflection of faster wage growth in both the public sector (0.8% Q/Q from 0.5% in Q3) and private sector (1.0% from 0.9%). Elsewhere, on a Y/Y basis, wage pressures were stable at 3.6% last quarter from Q3, still the smallest increase since Q3 2010.

Leading index rebounds. The leading index, compiled by Westpac, rose by 0.5% M/M to 283.4 in December, more than unwinding the 0.1% drop in the previous month and now the highest since August. Meanwhile, the annualized growth rate was 2.3%, up from 1.8% in the previous month but still clearly below trend growth (of 3.0%) for a fourth straight month. The coincident index, meanwhile, rose by 0.1% to 270.6 in December, a new cycle-high but with an annualized growth rate of 2.5% also being below trend growth of 3.0%.

Meanwhile, the December Conference Board-compiled leading index rose by 0.2% M/M to 128.4, unwinding some of the 0.3% gain seen in the previous month and now the second-highest in the cycle. The coincident index, meanwhile, was unchanged at 119.4 in December, still a joint cycle-high.