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The Morning Briefing

North American Edition
Monday, May 7, 2012
6:30 am (EDT), 11:30 am (BST)
Allen Sinai, Chief Global Economist

GLOBE AT A GLANCE – Chang Liu, London / Pierre Ellis, New York

Equities: All lower. Japanese equity markets closed clearly lower. Other major Asian markets were broadly lower too. European bourses opened lower and then climbed slightly through morning trading, albeit remaining in negative territory as midday approached, as election results in France and Greece reflected public discontent over austerity measures and cast doubt over the region's ability to fix its debt problems.

Bonds: Europe mixed, Japan higher. JGB prices rose across nearly all maturities, with the yield curve steepening on the medium to long-term end. European bond prices saw continued divergences, however, with Germany and France higher, but peripheral markets all broadly lower, led by a steep drop for Greek following the election on Sunday.

Currencies: Little change. The dollar seesawed against the yen through both the Asian and morning European sessions, trading little changed around ¥/$ 79.82. Against the euro, the US currency saw broadly similar developments, moving near $/€ 1.304.

Germany: Orders rise clearly. Coming in clearly above expectations this time around, manufacturing orders rose clearly in March by 2.2% M/M.

France: Hollande wins presidency. Voters gave Socialist candidate Francois Hollande a narrow victory in the French presidential election on Sunday, defeating incumbent president Nicolas Sarkozy.

Greece: Backlash for the nation's two largest parties. Results for Sunday's general election showed a collapse in support for the nation's two largest parties, the conservative New Democracy and socialist PASOK.

Indonesia: Growth moderates further. Coming in largely in line with expectations, national accounts data showed GDP growth slowing slightly to 6.30% Y/Y in Q1.

Australia: Stronger retail sales. Surprising to the upside, March seasonally adjusted nominal retail sales rose 0.9% M/M.

U.S. ECONOMIC AND CREDIT MARKET OUTLOOK – Pierre Ellis, New York

Long Treasuries rose solidly Friday, with the ten-year yield falling five basis points while the two-year yield slipped fractionally. The market was little changed overnight but reacted sharply to a surprising April employment report, first whipsawing on apparently contradictory elements of it—a weak payroll result but also a decline in the unemployment rate—before settling into a firm uptrend reaching the closing levels by noontime, and holding them absolutely steadily.

April **payroll employment** undershot expectations, rising 115,000 (Consensus: +165,000; Decision Economics: +138,000). Private-sector employment rose a modestly healthier 130,000, following on upward-revised increases of 166,000 in March (was +121,000) and 254,000 in February (was +233,000).

The most significant slowdown in April from March was in manufacturing (+16,000 from +41,000). Private services employment, meanwhile, slowed to +116,000 from +128,000 in a very scattershot pattern, encompassing a big acceleration in retail trade (+29,000 after -21,000) offset by slowdowns in education and health (+23,000 after +45,000) and leisure and hospitality (+12,000 after +52,000).

That sort of diversity, and the appearance of solid strength in either March or April, resists any thematic interpretation—in particular, notions that results for both months were heavily depressed by a weather payback. The better explanation might be that the economy in general is confronting serious uncertainty—most notably now, regarding domestic politics—making employment gains much more closely tied to immediate needs.

The average workweek, meanwhile, held steady, as expected—suggesting that immediate labor demand and employment are in close balance—while average hourly earnings were weak, holding steady instead of rising the generally expected 0.2%.

The upshot of the results as a whole is another month of very restrained labor income growth—giving no incremental boost to consumer spending. Limited employment growth, combined with limited income growth, will keep a relatively tight lid on the sort of pent-up-demand spending that could otherwise give overall consumer spending a boost above trend.

The unemployment rate, meanwhile, fell 0.1 point, to 8.1%, as against a general expectation of no change—but, in the unhealthy pattern of -169,000 employment and -342,000 labor force.

That sort of "improvement" cannot go on indefinitely, and will certainly not placate Fed doves—who have pointed to ongoing labor-market progress as a factor restraining them from calling for easing. The other key determinant for them was avoidance of steady disinflation—and now wages have apparently gone flat.

The FOMC will surely consider whether the market slowdown can be attributed mainly to weather factors—and will see another employment report before their next meeting. Meanwhile, the general tone of demand-side numbers will probably decide the general tone of speech comments, and any impression of shifting consensus that they create.

All mainstream GDP forecasts—other than the very strong ones—remain tenable at this point, given the great swings in productivity lately, but will be feeling downward pull.

DAILY CALENDAR

Markets should not be distracted by scheduled items today, with **consumer credit** results never attracting attention, unless spectacular in some way, and Richmond Fed President **Lacker**, a voter this year, very unlikely to surprise with any shift in his longstanding hawkish views.

The Schedule Today: March consumer credit, at 15:00 EDT/19:00 GMT, and a speech by Richmond Fed President Lacker, at 19:15 EDT/23:15 GMT.

DE Forecasts:

Consumer Credit Outstanding: +$7.5 billion.

CANADA – Melissa Pumphrey, New York

(Friday) PMI unexpectedly declines. The Ivey PMI dropped 10.8 points to 52.7 (Consensus: 61.0; Decision Economics: 64.5), indicating business sentiment fell rather sharply in April. While the inventory measure showed marked improvement from 45.7 to 56.8, the price measure deteriorated 3.6 points to 60.3. Of note, the Royal Bank of Canada (RBC) offers its own PMI measure which posted a 0.9 point increase to 53.3.

Perhaps this moderation of sentiment can be interpreted as a "return to reality." The Ivey PMI approached its historic apex in February with a 66.5 print—meanwhile, most other macroeconomic indicators hinted at weakness. The RBC PMI suggests that conditions are not necessarily worsening, but rather moderating at a level that suggests slower growth.

WESTERN EUROPE – Chang Liu, London

GERMANY – Orders rise clearly. Coming in clearly above expectations this time around, manufacturing orders rose clearly in March, with the 2.2% M/M gain more than unwinding the (upwardly revised) 1.4% drop seen in January. Meanwhile, the breakdown showed the latest increase to be a reflection of improvements in both export orders and on the domestic side.

While the data continues to be prone to marked volatility, the data may be hinting at a possible uptrend returning, with the Economics Ministry commenting that the new order trend is gradually pointing north again following the winter season.

FRANCE – Hollande wins presidency. Voters gave Socialist candidate Francois Hollande a narrow victory in the French presidential election held on Sunday, defeating incumbent president Nicolas Sarkozy. Speaking after his victory, the nation's first Socialist president in 17 years said his mission was to give Europe a dimension of growth and prosperity, and that his election signaled a hope that austerity does not have to be inevitable in the region. However, the president-elect now faces a difficult six weeks ahead in which he will be faced with challenges including agreeing to a deal with Germany on the new fiscal treaty, naming a prime minister for the nation from his presidential staff and securing a parliamentary majority in elections held on 10 and 17 June.

SPAIN – Industrial production weakness continues. March (workday adjusted) industrial production dropped by 7.5% Y/Y, a seventh straight fall and a drop that was steeper than the 5.3% decline in the previous month. The clearer fall was very broadly-based. Meanwhile, unadjusted or headline production growth fell even more acutely by 10.4% Y/Y.

GREECE – Backlash for the nation's two largest parties. Results for Sunday's general election showed a collapse in support for the nation's two largest parties, the conservative New Democracy and socialist PASOK. The latter party had essentially exercised a monopoly on voters' choice since the 70's, but Sunday's result showed the two largest parties failing to get the necessary combined 151 parliamentary seats in order to form a coalition government., hence casting into doubt the nation's ability to ensure that the second € 174 bln bailout programme can be implemented. The combined 149 seats for the two parties is thus 2 short of the working parliamentary majority and mean that they will be forced to seek a third ally, which may prove difficult as the other two pro-austerity parties do not reach the 3% limit for parliamentary representation. Meanwhile, the leftist Syriza emerged in second place (ahead of PASOK) with 51 seats and will now become the main opposition party. Its leader, Alexis Tsipras, has campaigned against the austerity measures and lending agreements however and completely ruled out any cooperation with New Democracy and PASOK.

In a speech following the election, New Democracy leader Antonis Samaras vowed to do his best to form a government. The mandate will, however, pass on to the second party if he fails to get the necessary support within three days and then to the third party and so on, with it possible that a new election will be held in June if no government is formed.

OTHER WESTERN EUROPE

SWITZERLAND – Inflation still clearly negative. Coming in slightly below expectations, April consumer price inflation was stable at -1.0% Y/Y, a seventh successive negative reading but still the lowest in almost three years. In M/M terms, prices rose by 0.1%, led higher by clothing and transport costs. Meanwhile, core inflation measures were largely unchanged, with the ex-food, energy and fuel figure stuck at -1.2% Y/Y while measure also excluding administered price products rose slightly by 0.1 percentage point to -1.5%.

Modest rise in unemployment. Largely as expected, the seasonally adjusted jobless rate rose to 3.1% in April from a downwardly revised 3.0% in March. The unadjusted rate, however, fell to 3.1%.

CENTRAL EUROPE, RUSSIA AND TURKEY – Chang Liu, London

CZECH REPUBLIC – Mixed messages in retail sales. March seasonally adjusted real retail sales (excluding vehicles but including fuel sales) rose by 1.0 in M/M terms, just about offsetting the 0.9% decline seen in the previous month. In (unadjusted) Y/Y terms, however, sales rose by 0.3% in March, slowing from the 0.7% increase in February. This was a reflection of a steeper fall for food sales (-2.1% from -0.4%), outweighing a pick up in non-food sales growth to 2.8% from 2.1% in February. Meanwhile, including vehicles, seasonally adjusted retail sales also increased in March, but by 0.4% M/M following a 0.2% fall in the previous month, while the unadjusted Y/Y rate of growth actually fell by 0.3% after a 1.6% in February.

Trade surplus widens. Visible trade data for March showed seasonally adjusted exports falling by 0.6% M/M, more than unwinding the 0.1% increase seen in the previous month and the first negative reading since August 2011. Import growth, meanwhile, fell more clearly by 2.1% M/M following a 1.2% gain in February. As a result, the trade surplus widened to CZK 28.31 bln in March from CZK 24.94 bln in the previous month.

ASIA – Chang Liu, London

INDONESIA – Growth moderates further. Coming in largely in line with expectations, national accounts data showed GDP growth slowing slightly to 6.30% Y/Y in Q1 from 6.49% in the previous quarter, now a six-quarter low. In Q/Q terms, GDP rose by 1.4%. The latest slowing was a result of a fall in growth for manufacturing and hotels & restaurants, but being undermined by some improvement in utilities, transport and agriculture. On the expenditure side, meanwhile, a rise in government spending was outweighed declines elsewhere.

TAIWAN – Consumer price inflation rises further. Overshooting expectations this time around, CPI inflation rose to 1.44% Y/Y in April, accentuating the 1.01 percentage point jump to 1.25% in the previous month and now a three-month high. On a M/M basis, prices rose by 0.94%. The Y/Y breakdown revealed the latest result to be a reflection of increases in price pressures for clothing (5.92% from 2.91%) and transport (0.14% from -2.02%), outweighing a fall for food (2.11% from 3.10%).

Elsewhere, wholesale price inflation actually turned more negative to -0.55% after a 0.24% fall in March, while import price inflation plunged to 0.14% last month from 1.53% in March, all hitting new cycle-lows.

Exports weaken further. Exports fell 6.4% Y/Y in April; double the size of the drop seen in the previous month. Imports, meanwhile, actually rose by 2.1% following a 5.8% fall in the previous month. As a result, the trade surplus narrowed clearly to $ 0.69 bln last month from $ 2.96 bln in April 2011.

OCEANIA – Chang Liu, London

AUSTRALIA – Stronger retail sales. Surprising to the upside, March seasonally adjusted nominal retail sales rose 0.9% M/M, building on the 0.3% increase in the previous month and now the largest gain in the cycle. The breakdown showed the latest result to be a reflection of improvements in food (0.9% from 0.4%), apparels (1.6% from -1.2%) and cafes & restaurants (2.0% from -0.7%) sales.

More notably, quarterly seasonally adjusted real retail sales for Q1 showed sales growth more than tripling to 1.8% Q/Q from 0.5% in the previous quarter, now the largest gain in the cycle. This was a reflection of a rise in food (2.5% from 0.9%), apparels (3.2% from 1.9%) and department stores (2.6% from -0.6%) sales growth, but being undermined by a deterioration in household goods (-1.4% from 1.6%).

Deeper contraction in construction. The March Performance of Construction Index fell by 1.3 points to 34.9, more than unwinding the 0.6 point gain in the previous month and now a twenty-third-straight sub-50 reading. The latest outcome was a reflection of faster contraction in activity (dragged down by a particularly large fall in apartments) and new orders, but being undermined by a slightly slower pace of contraction for employment.

Mixed messages in business confidence. The National Australia Bank measure of business confidence rose by one point in April to 4, now a joint cycle-high. The business conditions index, however, fell by 3 points to 0, now a joint cycle-low. Notably, the breakdown revealed the latest result to be a reflection of deterioration in profitability and exports.

Rebound in building approvals. Surprising clearly to the upside, overall building approval numbers actually jumped 7.4% M/M in April, but still unable to unwind fully the downwardly revised 8.8% slump seen in the previous month. The latest recovery was a reflection of a swing into expansion for private housing, while public housing saw a much less steep fall.